

economics, information & quality

[http://www.sims.berkeley.edu/academics/courses
/is290-10/f05/Economics&Quality.pdf](http://www.sims.berkeley.edu/academics/courses/is290-10/f05/Economics&Quality.pdf)

"my knowledge of economics is poor"

**I don't know much about
economics but I know what I like**

why economics?

the information age/economy

information rules/new rules

economic discourse

NY Times: Krugman, "economic scene"

New Yorker: Gladwell, "financial page"

why economics?

Charles Hamlin	Marriner Eccles
William Harding	Thomas McCabe
Daniel Crissinger	William McChesney
Roy Young	Martin Arthur Burns
Eugene Mayer	G. William Miller
Eugene Black	Paul Volker
	Alan Greenspan

economics & quality

"Quality is so disputable a matter,
that I look upon all information of
this kind [i.e. about quality] as
somewhat uncertain."

—Adam Smith, *Wealth of Nations*, 1776

economics & quality

"Quality has not yet been successfully
specified by economics, and this
elusiveness extends to all problems in
which it enters."

—George J. Stigler, 1961

specifying quality

"There is an incentive for sellers to
market poor quality merchandise.

... The difficulty of distinguishing good
quality from bad is inherent in the
business world

... Gresham's law has made a modified
reappearance

...An **asymmetry** in available information"

—George Akerlof

information & markets

"It is a basic tenet of our economic system that information in the hands of consumers facilitates rational purchase decisions; and, moreover is an absolute necessity for the efficient functioning of the economy."

FTC, 1979



economics & information

"'Perfect information' ... free, complete, instantaneous, and universally available ...[is] one of the defining features of the perfect market."

—James Boyle.

"At the same time, both the perfect and the *actual* market structure ... depend on information being a commodity ... costly, partial, and deliberately restricted."

alternative accounts

"Clearly there is here a problem of the Division of Knowledge which is quite analogous to, and at least as important as, the problem of the division of labour. ... instead of showing what bits of information the different persons must possess in order to bring about the result, we fall in effect back on the assumption that everybody knows everything."

—Freidrich von Hayek, "Economics & Knowledge," 1937

division of knowledge

"The 'data' from which the economic calculus starts are never for the whole society "given" to a single mind ... knowledge ... the dispersed bits of incomplete and frequently contradictory knowledge which all the separate individuals possess."

"... a problem of the utilization of knowledge not given to anyone in its totality."

F. von Hayek, 1945

the price is right

"Price dispersion is a manifestation—
and, indeed, it is the measure—of
ignorance in the market."

"The problem of quality has been ...
evaded by the assumption of
homogeneous goods."

"Let us consider these [used-car]
dealer markets."

— George J. Stigler

escaping quality?

"Tastes neither change capriciously nor differ importantly between people.

... we believe our approach better explains when behavior is stable than do approaches based on customs and traditions.

... we would welcome explanations of why some people become addicted to alcohol and others to Mozart."

– George J. Stigler & Gary S. Becker, "De Gustibus Non Est Disputandum," 1977

obfuscation?

"One should hardly have to tell academicians that information is a valuable resource: Knowledge *is* power."

– George J. Stigler

"information as that which is being communicated becomes identical with "knowledge" in the sense of that which is known."

–Fritz Machlup, *The Production and Distribution of Knowledge*, 1962



knowledge industry

"All the aspects of knowledge—its creation, its storage, its retrieval, its treatment as property, its role in the functioning of societies and organization—can be (and have been) analyzed with the tools of economics.

Knowledge has a price and a cost of production; there are markets for knowledge, with their supply and demand curves, and marginal rates of substitution between one form of knowledge and another."

—Herb Simon, "The Many Shapes of Knowledge," 1999

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knowledge concerns

tacit knowledge

"The concept of the inextricable tacitness of human knowledge forms the basis of arguments ...against ... every construction of rational decision processes as the foundation for modeling and explaining the actions of individual human agents."

– Cowans, David, & Foray

knowledge concerns

social knowledge

[any dissent from methodological individualism] "implies that the behaviour of men is directed by mysterious forces that defy analysis and description."

—Ludwig von Mises, *The Ultimate Foundation*, 1962

what's at stake?

economic imperialism

"This traditional approach of the economist offers guidance in tackling these problems – and that no other approach of remotely comparable generality and power is available."

Stigler & Becker, 1977

imperfections

imperfect information

imperfect markets

"counteracting institutions"

"the difficulty of distinguishing good quality from bad is inherent in the business world; this may indeed explain many economic institutions."

– Akerlof

quality assurance

"Nature has wisely judged that the distinction of ranks, the peace and order of society, would rest more securely upon the plain and palpable difference of birth and fortune, than upon the indivisible and often uncertain difference of wisdom and virtue. The undistinguishing eyes of the great mob of mankind can well enough perceive the former: it is with difficulty that the nice discernment of the wise and virtuous can sometimes distinguish the latter."

—Adam Smith, *Moral Sentiments*, 1759

counteracting institutions

apportioning risk brands

"New products are associated with old
brand names. This ensures the
prospective consumer of the quality
of the product."

—Akerlof

counteracting institutions

advertising

"In practice, the FTC and the courts have recognized that advertisements cannot be required to carry every relevant piece of information ... the problem, at bottom, is that there is no easy way of distinguishing deception from the larger problem of inadequate consumer information."

Beales, Craswell, Salop, "Efficient
Regulation," 1981

branding institutions

Socrates & Arrow

problems of expertise

Arrow, "Information &
Economic Behavior," 1973

"doctors, lawyers, and barbers ... the high school diploma, the baccalaureate degree, the Ph. D., even the Nobel Prize, ... education and labor markets themselves have their own 'brand names'."

—Akerlof
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