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## Character Issues: Classic Reprint

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# The Practical Utility of Economic Science

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### [Abstract](#)

If it happened every year that the President of this Section undertook to justify his own existence, I am afraid the Section would become weary. But my four distinguished predecessors have all been drawn from the Civil Service, and though each of us may have doubts about particular branches of the Civil Service, we are most willing to allow that as a whole it is at least a necessary evil, so that we do not get apologies from the Presidents who, so to speak, represent the practice of political economy. I hope, therefore, that you will bear with me if I offer some reasons for thinking that the teaching and study of the theory of economics is not, as many people seem to suppose, a wholly unnecessary evil, but, on the contrary, a thing of very great practical utility.

I do not mean to argue that a knowledge of economic theory will enable a man to conduct his private business with success. Doubtless many of the particular subjects of study which come under the head of economics are useful in the conduct of business, but I doubt if economic theory itself

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\* Edwin Cannan. *The Practical Utility of Economic Science*. Original publication: *The Economic Journal*, Vol. 12, No. 48. Dec., 1902, pp. 459-471. Cannan was then the President of the British Association for the Advancement of Science, Section F: Economics, which later became the Royal Economic Society, and the lecture was his presidential address. The article is no longer under copyright.

is. It does not indeed in any way disable a man from successful conduct of business; I have never met a decent economist who was in a position of pecuniary embarrassment, and many good economists have died wealthy. But economic theory does not tell a man the exact moment to leave off the production of one thing and begin that of another; it does not tell him the precise moment when prices have reached the bottom or the top. It is, perhaps, rather likely to make him expect the inevitable to arrive far sooner than it actually does, and to make him underrate, not the foresight, but the want of foresight of the rest of the world.

The practical usefulness of economic theory is not in private business but in politics, and I for one regret the disappearance of the old name "political economy," in which that truth was recognized.

One of the commonest complaints of the time is that there is no text-book of economics which commands any really wide approval, and you may therefore, I think, fairly ask me to explain what I mean by the teaching and study of economic theory before I undertake to prove its practical uselessness in the discussion of legislative and administrative measures. I will therefore endeavour to sketch as shortly as possible the course of instruction which the modern teacher of economic theory, if unhampered by too close adherence to traditional standards, puts before those who come to him for instruction.

The first, or almost the first, thing he will do is try to open the eyes of his pupils to the wonderful way in which the people of the whole civilized world now co-operate in the production of wealth. He may perhaps read them Adam Smith's famous description of the making of the labourer's coat, a description which required three generations and three great writers to elaborate in the form in which we know it. Or he will ask them to consider the daily feeding of London. There are, he will point out, six millions of people in and about London, so closely packed together that they cannot grow anything for their own consumption, and yet every morning their food arrives with unfailing regularity, so that all but an infinitesimal fraction of them would be extremely surprised if they did not find their breakfast ready to hand. To prepare it they use coal which has been dug from great depths hundreds of miles away in the Midlands or Durham; in consuming it they eat and drink products which have come from Wiltshire, Jamaica, Dakota, or China, with no more thought than an infant consuming its mother's milk. It is clear that there is in existence some machinery, some organisation for production which, in spite of occasional failures here and there, does its work on the whole with extraordinary success. It is easy to be pessimistic, especially when the weather is damp,

and we are apt to concentrate our attention, and to endeavor to make others concentrate their attention, on this or that defect, and to forget that the system is not made up of defects, but on the whole works very well. Imagine the report of a really outside observer. In all civilised planets, I have no doubt, there must be an institution more or less resembling the British Association. An economist in Mars, let us say, has been favoured with a glimpse of this island through a new mammoth telescope of sufficient power to let him see us walking about, and he is reporting to Section F what he saw. Will he say that he saw a confused scramble for the scanty natural products of the earth? That most people were obviously in a state of starvation? That few had clothes? And that scarcely any were housed? No, truly; he will be much more likely to report that he saw a wonderfully orderly population, going to and from its work with amazing regularity, without a sign of compulsion or unwillingness; that it appeared to be fed and clothed and housed in way extraordinarily creditable on the whole to some mysterious organisation, the nature of which he could only guess it.

Having endeavored to make his pupils recognise that we are organised, and that the organization works, the teacher will go on to show how it works: why things that are wanted are produced in the places where they can be easiest produced and taken to the places where it is most convenient to consume them; why people go to live in large numbers in spots where it is desirable they should work, and leave great areas sparsely inhabited; why more people are brought up to follow an occupation when the desire for its products increases, and fewer when it decreases; why if the harvest is short the consumption is economised so as to spread it over the year; and so on. The answer to all these questions is of course, “self-interest” or “the hope of gain.” Durham coal, Wiltshire milk, Danish butter, Jamaica Sugar, Dakota wheat, and China tea go to London because it pays to send them there. People congregate in London or Belfast because it pays them to work there. More do not come, because it would not pay them. Young people leave agriculture and go to towns to make agricultural implements or bicycles because it pays. The consumption of grain is economised and spread over the year because it pays to hold the stock. If people with one accord left off doing what paid we should all be dead in two months.

The reasons why it pays to do the right thing—to do nearly what an omniscient and omnipotent benevolent Inca would order to be done—are to be looked for in the laws of value. This used to be regarded as a somewhat arid subject, but the discussions of recent years, especially the

contribution made by Jevons and the Austrian school, have fertilised it. Long ago economists pointed out how the much-abused corn-dealer who held out for a higher price saved the people from starvation; and we now, thanks to the theory of final utility, not only know that is a fact, but also why it is a fact, that value rises with the extent and urgency of demand, so that, when a thing is much wanted, much is offered to those who produce it, or are ready to part with it, and consequently its production is stimulated or its consumption economized, as need be.

This will naturally lead to the question of distribution—the question, that is, why much of the produce falls to the share of one individual and little to that of another; why, in a word, some are rich and others poor. The teacher will here explain that the share of each person depends on the amount and value of his contribution to production, whether that contribution be labor or the use of property. He will show how this system of distribution is essential to the existing system of production, where no man is compelled to work or to allow his property to be used by others, and where every man has legal freedom to choose his own occupation and the uses to which he will put his property. He will beware of claiming for it that it is just in the sense in which justice is understood in the nurseries where jam is given when the children are good. There is, he will explain, no claim on behalf of the system that it rewards moral excellence, but only that it rewards economic service. There is no claim that economic service is meritorious. Whether a man can and does perform valuable economic service does not by any means depend entirely on his own volition. His valuable property may have come to him by bequest or inheritance; his incapacity to do any but the least valuable work may be the result of conditions over which he had no control. The system exists not because it is just, or to reward merit, but because it is inextricably mixed up with the system of production. It has one great evil—its inequality. Moralists and statesmen have long seen the evils of great inequality of wealth, and now, thanks to modern discoveries in economic theory, the economist is able to explain that it is wasteful, that it makes a given amount of produce less useful, because each successive increment of expenditure yields, as a rule, less enjoyment to the spender. The teacher will go on to show how this organisation of production and distribution is made possible by the order enforced by the government, and how, in various ways, government supplements it or modifies it; but I shall not enlarge upon this part of the teaching of economics, as its usefulness is obvious. My theme is the usefulness of the other part, the explanation of the organisation of

production and distribution so far as it depends on separate property, free labour, and the consequent action of self-interest.

In the first place, I maintain that the widespread dissemination of such teaching would help to do away with a vast amount of most disastrous obstruction of necessary and desirable changes. Take, for example, the obstruction offered to changes in international trade. Of course every conceivable argument has been used by different writers in wholly different circumstances for obstructing the co-operation of mankind in production, as soon as it oversteps a national boundary. But what is the real support of this kind of obstruction? Obviously the fact that certain producers, or owners of certain means of production, are damaged by an increase in the importation of a particular article. Their loss, their suffering, if their loss is severe enough to deserve that name, appeals to popular compassion, and their request for "protection" is easily granted, the new trade is nipped in the bud, and things are forced to remain in their accustomed channels. The same principle is not obtained as between county and county or between province and province, simply because there is then visible to everyone an opposing interest, the interest of the new producers, within the hallowed pale of the national boundary. Adam Smith tells us when the great roads into London were improved, some of the landlords in the home counties protested on the ground that the competition of the more distant counties would reduce their rent. The home counties did not get the protection they wanted, because it was obviously to the interest of the more distant counties that they should not have it. These two interests being balanced, the interest of the consumer, London, turned the scale. So it usually happens that beneficial changes in internal trade are allowed to take their course without obstruction, because the votes of two sets of producers counteract each other, and the consumer's interest settles the question. But in international trade one of the two sets of producers is outside the country: it consists of hated foreigners; the fact that it will benefit is an argument against rather than for the threatened change in trade, and the consumers therefore feel it patriotic to sacrifice their own interest and vote for protection. But if they were properly instructed in economic theory they would see at once that such magnanimity is entirely misplaced. They would see that it would cut away all international trade, since, if there were no fallacy involved in it, the stoppage of each import taken separately would benefit home producers and damage foreign producers. Even if some of the imported commodities could not be produced at all at home, substitutes, more or less efficient, could be produced, and give all the more employment. Having acquired some notion of the advantages of co-

operation and the territorial division of labor, the consumers would regard this as a *reductio ad absurdum*, and after thinking a little further they would soon see that, after all, there is another set of producers, actual or potential, within the country who will gain—namely, the producers, present or future, who will supply the articles which are to go abroad in exchange for the new import. They will see that what they are asked to do is not to maintain the amount of national production, but merely to prevent a change in its character which will be accompanied by an increase in its amount.

Take another example of Chinese obstructiveness to desirable change. As great cities grow, it becomes convenient that their centres should be devoted to offices, warehouses, and shops, and that people who work in these places, and still more their families, should live in the outskirts. I do not know that anyone has denied this. Certainly the great majority are willing to admit it. At one time it is believed that a quarter million of people lived in the square mile comprised within the City of London; no one supposes that would be convenient now. There is no reason to suppose that further change in the same direction will not be desirable in the future. Yet, as incredible as it will appear to future generations, public opinion, The House of Commons, the London County Council, and some town councils think, or at any rate act as if they thought, that the process has now gone far enough, and ought to be stopped; as if the state of things reached about the year 1891 was to be permanent, to last for ever and ever. Private owners are indeed still allowed to pull down dwelling-houses and erect shops and offices, but they are abused for doing so, and their liberty is at least threatened. But if a new railway or a new street is made—in all probability with the intention of increasing the accessibility of the centre from the suburbs—if even a new London Board School is built, and houses inhabited by persons who have less than a certain income are pulled down in any of these processes, it is required by law or parliamentary resolution that other houses for these people must be built in the neighbourhood. So it comes about that there are in quarters of London most unsuitable for the purpose enormous and repulsive barrack dwellings, the sites of which are devoted *in secula seculorum* to the housing of the working classes; while the immense cost of devoting them to this instead of to their proper purpose is debited to the cost of improving the facilities for locomotion or to education, and is defrayed principally by the rates on London property, which chiefly consist of houses, and to some extent by the higher charges on railways consequent on the restriction of facilities for extension. Fifty pounds a head is the average loss involved to the rates of London on every man, woman, and child for whom the

dwellings are provided. Such is the wisdom of practical men uninformed by instruction in economic theory.

This palpable absurdity could never have been perpetrated if the general working of the economic organization had been understood. In that case it would have been seen at once that the extrusion of over 200,000 inhabitants from the City of London in the past, which is admitted to have been desirable, was effected by the quiet operation of the laws of value. It would have been seen that, as it became desirable to turn the City to other purposes, the ground in the City became too valuable to use as bedrooms and as living-rooms for mothers and children, and this increase of value drove out the 200,000 inhabitants. It would have been seen that the change had not come to an end, and no responsible body would have dreamt of putting themselves in opposition to it by buying sites and writing them down to 2 per cent of their actual value in order that they might be tied up for ever and ever to be the homes of a certain numbers of persons with less than a certain income. If some unusually dense individual who had failed after many attempts to pass his examination in economic theory had proposed the policy which had been adopted, he would have been asked two questions: first, "What peculiar sanctity is there about the position being occupied in the closing years of the nineteenth century? Why should this be stereotyped for all time? Why should not the position at the end of the seventeenth century have been maintained? Why should we not endeavor to restore the working classes to their old home in the City, and remove the Bank of England to Tooting?" Secondly, "Whom do you imagine you will benefit by the policy you propose?"

It is difficult to conceive of any answer to the first question. To the second the reply of the dunce would, of course, be that he thought the policy proposed would benefit the people housed on these expensive sites. This answer would at once be condemned as unsatisfactory. To build houses on land worth £100,000, and let them to the first-comers of respectable antecedents at rents which would pay if the land were worth £2,000, would be a very stupid sort of almsgiving if these respectable first-comers actually got the difference between the interest on the £100,000 and the £2,000. But no one supposes that they do get this difference, or any considerable part of it. The difference is almost entirely pure loss to the community. The chief immediate effects of the policy are, first, to retain in the centre the men, women, and children who inhabit the dwellings; secondly, to retain other workers who perform various offices for these inhabitants; and thirdly, to ensure a supply of labour for factories which would otherwise (to the advantage of every one concerned) be driven into

the country by the pressure of the high wages necessary to bring workmen to the centre or to pay their house rent if they lived there.

So much for the utility of economic theory in preventing obstruction of desirable changes. My second claim on its behalf is that it serves to hinder the adoption of specious but illusory projects. This, I think, may be illustrated by examples closely connected with those which we have already considered under the head of obstruction.

The people who are most anxious to obstruct changes in the channels of trade which are coming about of themselves because they are profitable, are often extremely anxious to promote changes which will not come about of themselves because they are not profitable. For this end one of their most favorite devices at present is a State or municipal subsidy to locomotion or transport between particular points. So we have shipping subsidies, free grants to light railways, the construction of unprofitable telegraph lines by the Post Office, and the advocacy, at any rate, of the construction of unprofitable tramways by municipalities. The practical man, uninstructed in economic theory, feels uneasy about such projects because he does not see where he is to stop, and he feels obscurely that a universal subsidisation would mean ruin. But he does not see why he should not go a little way, and he goes sufficiently far to involve a loss quite worth considering. A knowledge of economic theory would come to his assistance by showing him that, as a rule, the most profitable enterprises are those which it is most desirable to undertake first, and that the subsidisation of the less profitable does not create new enterprises, but merely changes the order from the more desirable to the less desirable. I suppose that if in 1830 Parliament had offered a sufficient subsidy a railway might have been at once made and worked from Fort William to Fort Augustus, to the great satisfaction of the inhabitants of Fort Augustus and the intermediate places. But it is obvious that it was more desirable, in the interests of the whole community, that the railway from Fort William to Fort Augustus should wait for seventy years, and that the railway from Manchester to Liverpool, and many others, be made first.

Then, too, we find people who are not quite so stupid as to think the working classes should always remain in the places where they were at the end of the nineteenth century, alleging that the way to cure overcrowding is for local authorities to enter the building trade in a general way, and build houses inside or outside their districts, wherever it seems most convenient. To the mind uninstructed in economic theory it seems obvious that the larger amount of housing there is the less overcrowding there will be, and that the more housing local authorities provide the more housing there will



be. Economic theory, with its explanation of the general working of the organisation of production, suggests two objections. First, an addition to the housing in any locality will not be effectual in diminishing overcrowding, in so far as it attracts new inhabitants to the spot; a policy which assumes that the comparative plentifulness of houses is [not]<sup>1</sup> a factor in the determination of the enormous and perpetual migration of people from place to place which is indicated in the tables of birthplaces and births and deaths in the census, is doomed to failure. Secondly, economic theory suggests the reflection that the mere fact of a local authority building some houses will not cause the whole number to be greater, if for every house built by the local authority one less is built by private enterprise, and that this is very likely to happen. Houses have been built by private enterprise in the past, and in these houses nearly the whole population is at present housed. I have seen an enthusiast for municipal housing stand in the empty streets of a town late at night, when every soul in the town was evidently housed, and say in a tone of conviction, "Private enterprise has failed." In that town four small houses had been built by municipal enterprise and more than ten thousand by private enterprise, and private enterprise was adding hundreds every year, while the housing committee of the corporation was meeting once a year to re-elect its chairman. Is it likely that private enterprise will build as much when it is competed with or supplemented by—the term does not matter—municipal enterprise? Why should it? If the municipality turned baker, would the private bakers continue to bake as much bread? Is not the attempt to stop overcrowding by inducing local authorities to build houses exactly the same thing, and just as absurd as it would be to attempt to cure underfeeding by opening municipal butchers' and bakers' shops?

In the long run, I admit, experience teaches. Protection has fallen once in this country, and I have little doubt that it will fall again if it becomes considerable. The policy of obstructing the removal of dwellings from the centre of a great city already excited opposition in the London County Council, though unanimity still reigns in those last homes of extinct superstitions, the Houses of Parliament. Chancellors of the Exchequer and finance committees may be trusted to offer a stout resistance, on what they call financial grounds, to any really great development of the system of subsidies. There is hope even that the municipal building policy may be checked by the laborious inquiries which show by statistics what everyone knows, that the poor are ill-fed and ill-clothed as well as ill-housed, and

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<sup>1</sup> *EJW ed. note:* We suspect that Cannan intended a "not" here.

therefore lead people to consider how the poor may be made more able to pay for houses, among other things, instead of simply how houses may be built in the absence of an effective demand for them. But I claim that, in matters such as these, a more widespread appreciation of economic theory, and the quickened intelligence which that would produce, would save us much painful experience, many costly experiments, and an enormous mass of tedious investigation.

Thirdly, and, at any rate on the present occasion, lastly, I claim that the teaching and study of economic theory has great practical utility in promoting peace and good will between classes and nations.

Between classes within the same nation the peacemaking influence of economic theory lies chiefly in the fact that it tends to get rid of that stupid cry for “rights” and “justice” which causes and exacerbates industrial and commercial quarrels. When demand for some commodity falls, or supply from some new quarter arises, and profits and wages shrink, the workers cry out that they are being unjustly treated, because they have the unfounded belief that reward is or ought to be proportional to moral merit, and they are not conscious of any diminution of their moral merit. They demand a living wage, or a minimum wage and employment for all who happen to have been hitherto employed in the trade, rend the air with complaints, and get subscriptions from a compassionate but ill-informed public. We cannot, of course, expect people who suffer by them to regard even the most beneficial operations of the economic organisation with enthusiasm or even satisfaction. It would be absurd to do so. But all the same, it is true that a wider apprehension of the fact that it is only by raising and lowering the advantages offered by different employments that production is at present regulated so as to meet demand would not only diminish the dissatisfaction, but also, which is more important, diminish the actual suffering by causing transitions to be less obstinately resisted. The present fashion of deploring rapid changes of trade and dwelling-place is a most unfortunate one; the ordinary forms of labour do not, as a matter of fact, require such specialised ability that there should be much difficulty in changing from one to another; and surely it is much better for a man to work at several different things at different places in the course of his life than to stick for ever in the same place, surrounded by the same objects, going through the same monotonous round of duties? Anything which will weaken the present obstructive sentiment and lead people to regard the necessity of a change of employment or residence as temporary inconvenience rather than a cruel injustice is to be warmly welcomed.

It is not, however, only the poor and the industrious who would be taught by a greater knowledge of economic theory not to kick against very necessary pricks. The rich, both industrious and idle, would be taught to be far more tolerant than they are of attempts to diminish inequality of wealth by reducing the wealth of the rich as well as increasing that of the poor. The economist may be a little more annoyed with the workman who insists that he ought to have thirty shillings a week for producing something worth fifteen shillings, or five shillings, or nothing at all, but he can only have hearty contempt for the millionaire who holds up his hands in holy horror and murmurs “confiscation,” “robbery,” “eighth commandment,” when it is proposed to relieve him of a fraction of a farthing in the pound in order to bring up destitute orphans to an occupation in which they may earn twenty-five shillings a week. The sanguine teacher of economic theory has hopes of making even such a man see that he has his wealth, not because Moses brought it down from Sinai, or because of his own super-eminent virtue, but simply because it happens to be convenient, at any rate for the present, for society to allow him to hold it, whether he obtained it by inheritance or otherwise. In other words, that private property exists for the sake of production, not for the sake of the particular kind of distribution which it causes. Some, I know, say that the rich are so few that it does not much matter whether they acquiesce in the measure meted to them or not but that is not the teaching of history; and I think you will agree with me that for the progress of the whole community it is, in practice, quite as important to secure the acquiescence of the rich as of the poor.

In regard to international relations, the first business of the teacher of economic theory is to tear to pieces and trample upon the misleading military metaphors which have been applied by sciolists to the peaceful exchange of commodities. We hear much, for example, in these days of “England’s commercial supremacy,” and of other nations “challenging” it, and how it is our duty to “repel the attack,” and so on. The economist asks “what is commercial supremacy?” and there is no answer. No one knows what it means, least of all those who talk most about it. Is it selling goods dear? Is it selling them cheap? Is it selling a large quantity of goods in proportion to the area of the country? Or in proportion to its area or population? Or absolutely, without any reference to its area or population? It seems to be a wonderful muddle of these various and often contradictory ideas rolled into one. Yet what a pile of international jealousy and ill-feeling rests on that and equally meaningless phrases! The teacher of economic theory analyzes or attempts to analyze these phrases, and they disappear, and with them go the jealousies suggested by them.

When misleading metaphors and fallacies are dismissed, we are left with the facts that foreign trade—the trade of an area under one government with areas under other governments—is merely an incident of the division of labor, and that its magnitude and increase are no measures of the wealth and prosperity of the country, but merely of the extent to which the country finds it convenient to exchange commodities of its own growth or manufacture for commodities produced elsewhere. If the city of York were made independent, and registered its imports and exports, they would come out far larger per head of population than those of the United Kingdom or any other great country. Should we be justified in concluding York to be far richer than any great country? If means were discovered of doubling the present produce of arable land with no increase of labour, much less corn would be imported to Great Britain and less of other goods would be exported to pay for it; the foreign trade of the country would consequently be diminished, but would the people be any less prosperous? What jealousies, heart-burnings, and unfounded terrors leading to hatred would be extinguished if only these elementary facts were generally understood!

To anyone who has once grasped the main drift of economic theory, it will be plain that the economic ideal is not for the nation any more than for the family that it should buy and sell the largest possible quantity of goods. The true statesman desires for his countrymen, just as the sensible parent desires for his children, that they should do the best paid work of the world. This ideal is not to be obtained by wars of tariffs, still less by that much greater abomination, real war, with all its degrading accompaniments, but by health, strength and skill, honesty, energy, and intelligence.

#### ABOUT THE AUTHOR



Edwin Cannan (1861-1935) taught at the London School of Economics from 1895 to 1926, serving a long stretch as chairman after 1907. He had a reputation as a critic of classical economics, particularly for his 1893 work, *A History of the Theories of Production and Distribution in English Political Economy from 1776 to 1848*, and yet devoted to Adam Smith, represented by his famed edition of *The Wealth of Nations* (1904), the standard edition for generations, and by his explications of Smith, such as “Adam Smith as Economist: The Gospel of

Mutual Service,” *Economica*, 1926. Ideologically, he started as a moderate “new liberal” interventionist, but around the time of his editing of Smith and the present essay (1902) moved sharply toward classical liberalism, and thereafter became a strong defender of classical liberal economic policies. Cannan realized an economics of plain language, concrete illustration, and institutional pertinence, and wrote a great deal for the general reader. Friedrich Hayek wrote of Cannan: “Many of his economic essays which he published in two volumes, *The Economic Outlook* (1912) and *An Economist’s Protest* (1927), deserve, even now, renewed and wider attention, and translation into other languages. Their simplicity, clarity and sound common sense make them models for the treatment of economic problems, and even some that were written before 1914 are still astonishingly topical. Cannan’s greatest merit, however, was the training, over many years, of a group of pupils at the London School of Economics.”