

ECONOMICS FOR REAL

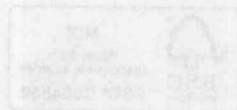
USKALI MÄKI AND THE PLACE
OF TRUTH IN ECONOMICS

Edited by
Aki Lehtinen, Jaakko Kuorikoski
and Petri Ylikoski

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economics

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First published 2012
by Routledge
2 Park Square, Milton Park, Abingdon, Oxon OX14 4RN

Simultaneously published in the USA and Canada
by Routledge
711 Third Avenue, New York, NY 10017

Routledge is an imprint of the Taylor & Francis Group, an Informa business

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British Library Cataloguing in Publication Data

A catalogue record for this book is available from the British Library

Library of Congress Cataloging in Publication Data

A catalog record has been requested for this book

ISBN: 978-0-415-68654-9 (hbk)

ISBN: 978-0-203-14840-2 (ebk)

Typeset in Times
by Wearset Ltd, Boldon, Tyne and Wear



Printed and bound in Great Britain by
TJI Digital, Padstow, Cornwall

Economics for Real

Modern economics abounds with complicated mathematical models that use a variety of unrealistic assumptions. This raises the question of whether economists are studying the economy for real. Are economists aiming at the truth at all, or are they merely playing intellectual games? Uskali Mäki, a pioneering philosopher of economics, has offered a way of understanding such modeling practices that is, perhaps surprisingly, based on the idea that some unrealistic assumptions are necessary for getting to the truth in economics.

Mäki has formulated his ideas in terms of the 'method of isolation' which is naturally related to his scientific realist approach to economic methodology. He has thus shown how economic theories may aim at the truth even though they are based on unrealistic assumptions, and how this endeavor is perfectly consistent with scientific realism. This book shows how Mäki's work on truth, unrealistic assumptions, realism, isolation, idealization, unification, explanation as redescription, commonsensibles, models, rhetoric and economics of economics springs from a comprehensive philosophical overall perspective. At the same time, in a true realist spirit, some of the essays provide amendments and criticisms of Mäki's work.

This book provides the first comprehensive and critical examination of Mäki's realist philosophy of economics.

Aki Lehtinen is a post-doctoral researcher at the University of Helsinki, Finland.

Jaakko Kuorikoski is a post-doctoral researcher at the University of Helsinki, Finland.

Petri Ylikoski is Deputy Director of Trends and Tensions in Intellectual Integration (TINT) in the Department of Social and Moral Philosophy, University of Helsinki, Finland.

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The field of economic methodology has expanded rapidly during the last few decades. This expansion has occurred in part because of changes within the discipline of economics, in part because of changes in the prevailing philosophical conception of scientific knowledge, and also because of various transformations within the wider society. Research in economic methodology now reflects not only developments in contemporary economic theory, the history of economic thought, and the philosophy of science; but it also reflects developments in science studies, historical epistemology, and social theorizing more generally. The field of economic methodology still includes the search for rules for the proper conduct of economic science, but it also covers a vast array of other subjects and accommodates a variety of different approaches to those subjects.

The objective of this series is to provide a forum for the publication of significant works in the growing field of economic methodology. Since the series defines methodology quite broadly, it will publish books on a wide range of different methodological subjects. The series is also open to a variety of different types of works, including original research monographs and edited collections, as well as the republication of significant earlier contributions to the methodological literature. The International Network for Economic Methodology (INEM) is proud to sponsor this important series of contributions to the methodological literature.

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Uskali Mäki and the place of truth in economics

Edited by Aki Lehtinen, Jaako Kuorikoski and Petri Ylikoski

Contributors

John B. Davis is Professor of History and Methodology of Economics at the Amsterdam School of Economics at the University of Amsterdam. He is also Professor of Economics in the Department of Economics at Marquette University, Milwaukee.

Till Grüne-Yanoff is Associate Professor of Philosophy in the Department of Philosophy and History of Technology at the Royal Institute of Technology, Stockholm.

Francesco Guala is Associate Professor in the Department of Economics at the University of Milan.

D. Wade Hands is Distinguished Professor of Economics in the Department of Economics at the University of Puget Sound, Tacoma, Washington.

Daniel M. Hausman is Herbert A. Simon and Hildale Professor in the Department of Philosophy at the University of Wisconsin-Madison.

Frank Hindriks is Assistant Professor in the Department of Ethics at the University of Groningen.

Kevin D. Hoover is Professor of Economics in the Department of Economics and Professor of Philosophy in the Department of Philosophy at Duke University, North Carolina.

Jaakko Kuorikoski is a Post-Doctoral Researcher in the Department of Political and Economic Studies at the University of Helsinki.

Aki Lehtinen is a Post-Doctoral Researcher in the Department of Political and Economic Studies at the University of Helsinki.

Ilkka Niiniluoto is Professor of Theoretical Philosophy in the Department of Philosophy, History, Culture and Art Studies at the University of Helsinki.

Don Ross is Professor of Economics in the School of Economics at the University of Cape Town.

Jack Vromen is Professor of Philosophy of Science and Methodology in the Faculty of Philosophy at Erasmus University Rotterdam.

Petri Ylikoski is Academy Research Fellow at the Academy of Finland and working in the Department of Philosophy, History, Culture and Art Studies at the University of Helsinki.

Jesús Zamora Bonilla is Professor in the Department of Logic, History and Philosophy of Science at the UNED, Madrid.

Preface

Economics is a curious and controversial science. More than any other field, it currently provokes questions about whether its theories have anything to do with the reality they are supposed to cover. Economics is under pressure from the general public due to its alleged failures in terms of forecasting real-world economic problems. It is also under pressure from the other sciences, which fail to see how the assumptions made in economic models can be squared with what is known about human behavior, cognition and social institutions. The situation is not helped by the nonchalant manner in which practicing economists often dismiss such charges. This criticism is undoubtedly a good thing, because no science can flourish in a state of stagnant dogmatism and insulation. However, it is all too easy to criticize this perceived lack of realism in an unconstructive way. This type of criticism reveals an ignorance of the methodological difficulties in studying complex social phenomena; it professes unrealistically high opinions of the successes of the other sciences; and it may totally fail to grasp the rationale of the mainstream way of doing economics. It may also fail through its wrongheaded philosophical presuppositions about science in general. Therefore, what constructive criticism of economics based on its alleged alienation from reality requires is a knowledge of the philosophy of science.

Perhaps the most influential philosopher of science focusing on questions of realism in the context of economics is Uskali Mäki. The purpose of this volume is to provide a broad and critical examination and overview of his philosophy of economics. Uskali Mäki is one of the pioneers of the philosophy of economics as a distinct academic discipline. Not only was he one of the first professional philosophers to build their professional identity on philosophical reflection concerning economics, he was also instrumental in creating many of the social institutions promoting independent yet rigorous methodological thinking: the International Network for Economic Method; the Journal of Economic Methodology; the Erasmus Institute for Philosophy and Economics in Rotterdam; and Trends and Tensions in Intellectual Integration in Helsinki. He also edited some of the best-known collected volumes in the philosophy of economics. A bringing together of the diverse threads of Mäki's own methodological insights is long overdue, as he has thus far published only articles and book chapters. One reason for this may be his philosophical temperament, which has always been more

inclined towards the finer details of the argument than the provision of a grand philosophical system – especially if the latter comes at the expense of the former. Mäki's body of work offers neither easily quotable slogans nor an off-the-shelf monolithic doctrine with which to attack or defend the way in which economics is practiced. What it offers are conceptual and argumentative tools with which to reason and argue about the practice of economic model building and the epistemological questions therein in a more subtle and rigorous manner.

This collection is not intended to be a blanket endorsement of Mäki's ideas. It should not be read as an exposition of what the philosophy of economics, or economics for that matter, should be like. Our aim is to offer a critical overall assessment of a series of philosophical positions and arguments concerning economics, which we feel are important and deserve to be collected together to provide easier access to philosophers, economists and anyone interested in the questions of theory, modeling and truth.

These articles were presented as papers in a special session of the International Network for Economic Method conference held in Helsinki in September 2011, organized to celebrate Mäki's 60th birthday. We would like to express our deepest gratitude to Päivi Seppälä, who took care of much of the practicalities during the final stages of producing this volume, and to Caterina Marchionni, who acted as a commentator and a source of ideas for much that has gone into this book. We would also like to thank all the reviewers along the way, whose valuable comments have helped immensely in improving the articles. Needless to say, we are grateful to Uskali for giving us the excuse to undertake this endeavor. Our final thanks go to the contributors – we were pleasantly surprised by the enthusiasm and cooperativeness of almost all of the people we contacted. This shows the high standing that Uskali Mäki has in the philosophy of economics community.

Aki Lehtinen, Jaakko Kuorikoski and Petri Ylikoski
Helsinki 31.5.2011

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Introduction

Uskali Mäki's realist philosophy of economics¹

Aki Lehtinen

1 Introduction

Mainstream economics abounds with complicated mathematical models that use a variety of unrealistic assumptions. Assumptions such as infinitely living individuals, perfectly balanced budgets, perfectly rational individuals, zero transaction costs, constant returns to scale, fixed preferences, fictional auctioneers, and societies with no government are regularly employed in economic modeling. Furthermore, some things such as institutions, habits, and changing preferences seem to lean on economic phenomena but are summarily set aside under the suspicious-sounding but omnipresent *ceteris paribus* clause. Given these features of economics, it is not surprising that other social scientists and the general public are often very critical of the whole approach.

The abundance of unrealistic assumptions raises questions concerning the nature of the enterprise: Are economists aiming at the truth at all, or are they just playing an intellectual game in which such assumptions are acceptable for some mysterious reason? Are they studying the economy for real? Are they simply uninterested in truth, or is there perhaps some other way of accounting for their modeling practices? Yet this modeling practice does constitute the mainstream, and this fact alone raises the question of why this is so. Furthermore, many economists are in a position to make major societal decisions. This raises further questions: Are the vast majority of economists simply deluded in engaging in such a weird practice? How can it be that models based on such unrealistic assumptions are assumed to be relevant to policy?

This question of unrealistic assumptions is perhaps the hottest topic in economic methodology. Milton Friedman (1953) famously argued that the realism of assumptions in economic theories did not matter as long as the predictions derived from them were correct. It is easy to see why Friedman's instrumentalist answer has been so popular among economists. If it is pointed out that an assumption is unrealistic, an instrumentally inclined economist may decline from justifying it and merely retort that 'it is of course just an assumption in a model that is not to be taken too seriously, and ... all models are false anyway'. Some economic methodologists (e.g., Boland 1979) are also perfectly happy with instrumentalism. We can at least easily explain the widespread use of false

assumptions if economic theories are not meant to be true, but are merely useful tools for predicting the future and for guiding economic policy.

There are, however, many reasons why most methodologists (and economists) have abandoned instrumentalism. Daniel Hausman's (1994) analogy with cars highlights one problem with it. If a car runs smoothly we do not need to know much about what is under the hood, but as soon as it does not function properly it may be necessary to look more closely at its internal workings. Another major issue is that economics also deals with explanation. From this perspective, it is not surprising that economists spend a considerable amount of time arguing for their assumptions and challenging their peers' assumptions in scientific conferences. It is difficult to make sense of these practices in terms of instrumentalism.

Given the deficiencies of instrumentalism and also in the Lakatosian and Popperian approaches to economic methodology, Tony Lawson and Uskali Mäki launched realism as a meta-theoretical approach more or less simultaneously at the turn of the 1990s.² They both agree that science is not just an intellectual game and that scientists should aim for truth. One of the main theses commonly associated with realism is that mature and advanced scientific theories are, by and large, true. Some versions of realism claim that science provides literally true accounts of reality. However, given the ubiquity of unrealistic assumptions, how can economics and realism be reconciled?

Mäki and Lawson part company here. Although both are waving the flag of realism, their approaches are fundamentally different. Lawson draws inspiration from Roy Bhaskar's critical realism and uses it as a platform for arguing that mainstream economics is not consistent with realism and ought to be changed accordingly. In contrast, Mäki's aim has been to show that, despite the seeming discrepancy between realism and unrealistic assumptions, scientific realism can be reconciled with many approaches in economics, both mainstream and not-so-mainstream. The starting point is that there is a difference between *realism* (a meta-theoretical doctrine) and *realisticness* (an attribute of scientific representations such as assumptions).³ Scientific realism can thus be perfectly compatible with unrealistic assumptions as long as the *function* of these assumptions is compatible with realism, and the methodologist's task is to sort out the various functions that different assumptions have. The pivotal role of unrealistic assumptions and a deep commitment to scientific realism jointly determine Mäki's research agenda. The main question is: *what does it take to formulate an account of realism and of economics such that the two are compatible?*

Monographs (Lawson 1997, 2003) and anthologies (Cruickshank 2003; Fleetwood 1999; Fullbrook 2009; Lewis 2004) in which Lawson's account of realism is discussed are readily available. Mäki is a prolific writer on economic methodology, but has mostly published in specialized journals. His views are thus not equally accessible to a more general audience of philosophers and economists. He provided an intellectual history himself (Mäki 2009e), and revealed similar information in an interview conducted by his own students (Mäki 2008d), and his views have also been compared to Lawson's realism and/or rhetoric in

various contributions.⁴ However, there is no comprehensive analysis of Mäki's philosophy of economics. This volume endeavors to correct this omission by focusing on Mäki's scientific realist account of economics.

Mäki has made contributions in various areas of the philosophy and methodology of economics, including unrealistic assumptions, the rhetoric of economics, Austrian economics, institutional as well as mainstream economics, the sociology of knowledge, economic models and the economics of economics.⁵ Aside from his realist philosophy of economics, he is perhaps best known for his analysis of the method of isolation. In more general terms, his peers have certainly learned to recognize his careful analytical style, which his under-laborer conception (Mäki 2000b: 47) of the role of philosophy legitimizes.

The purpose of this introductory chapter is to show how the different parts of Mäki's work hang together through the notion of realism and to provide a description of his vision of economic methodology. Reading everything he has written (to which I had access) has been a revealing experience. I have come to realize that his academic production constitutes a unified framework in which a few central concepts and distinctions are applied, and at times slightly modified, in different contexts. He provides not just an isolated argument but rather a full philosophical system that is, nevertheless, constructed in a piecemeal fashion. In order to illustrate this unity I will also discuss his early work starting from the beginning of the 1980s, thereby covering topics such as *explanation as redescription* and *essentialism* about which he has not written since the beginning of the 1990s. I am doing this in the hope of being able to provide a deeper understanding of other topics that he does continue to discuss, such as *truth in models* and *commonsensibles*. In the last decade he has often claimed that he has realist intuitions (Mäki 2000c: 112; 2002a: 9; 2003b: 66; 2005b: 235; 2008c: 296). Although he might no longer subscribe to all of these older ideas, I believe that discussing them here will help in articulating what such intuitions might be.⁶

Although the aim is to provide an overview of Mäki's realist philosophy of economics, I also hope to cater for experienced readers by providing some new observations and interpretations of his work. Given the clarity of Mäki's writing, I cannot hope to do better than he does with respect to some key ideas. If you have not read them already, I particularly recommend his works on realism (1989, 1990d, 1992a), on models and assumptions (2000a, 2011a), and on the method of isolation (1992c, 1994b), and a particularly characteristic contribution that combines realism and isolation (2004a).

I will also introduce the various chapters included in this volume, giving them a context within Mäki's realist philosophy of economics. In a true realist spirit, the style of the articles will be that of critical engagement rather than outright advocacy. The authors take on various aspects of Mäki's realist philosophy of economics. Collectively, they provide a lively account of the scientific realist position that has influenced the philosophy of economics through Mäki's writings. This book should be of interest not only to philosophers of economics but also to social scientists and economists reflecting on the nature of their science.

The topics covered in this introduction are discussed in roughly the same chronological historical order in which Mäki presented them. I will start in Section 2 by presenting Mäki's vision of doing the philosophy of economics. He is famous for distinguishing between various kinds of realism and realisticness. I suggest in Section 3 that he is particularly critical of ontological and referential anti-realisms, and discuss why these aspects of realism are so important to him, given his account of explanation as redescription and essentialism. My aim in Section 4 is to sort out how his notion of *commonsensibles* is related to these issues and to represent his views on constructive empiricism. Section 5 is devoted to a discussion of Mäki's account of unification, and Section 6 to an exposition of his method of isolation. I consider his contributions on realisticness and kinds of assumptions in Section 7, and discuss his most recent work on models in Section 8.

2 The vision

The very notion of a vision of what one is engaged in doing is particularly important to Mäki. This aspect of his approach is clearly evident in the papers he wrote in Finnish during the early stages of his career. I hope that laying out the main contents of these early papers in the international arena will enhance understanding of how a devotion to realist philosophy can arise from such a vision in a fairly natural way.⁷ He writes, for example:

The starting point of the [philosophical] project is the conviction that economic methodology should not be based merely on prescriptive apriorism or descriptive empiricism ... but rather at least partly on scientific results and realistic metaphysics. ... Theoretical conservatism, persuasive argumentation, the monopoly of one paradigm or the free competition of approaches ... and the strict application of predictive power have been proposed as general methodological principles. ... In economics, conditions for these should be found from the nature of the economy and from the special relationship between economists and the economy. Metaphysical considerations may then give a partial explanation of descriptive methodology: Why do economists act as they do? Because the nature of the object, the beliefs concerning it, and a certain point of view towards it are prone to provoking such action. ... Why should economists proceed in a certain way? Why would it be rational? Because the nature of the object of investigation and a certain point of view towards it require such actions in order to achieve a certain goal.

(Mäki 1981–1982: 177)⁸

Similarly:

Consider your project simultaneously as an empirical and a theoretical one. Do not, for example, borrow anything from the philosophy of science