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## Frank H. Knight on social values in economic consumption: an archival note

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### ABSTRACT

This note reproduces an unpublished paper on “Social Values in Economic Consumption” which Knight prepared for the Social Science Research Council (SSRC) Summer Conference, on Nantucket, Massachusetts in June 1931. This paper sheds new light on Knight in two important respects. First, it presents, in a more systematic fashion, Knight’s criticism of what he perceived to be the then standard theory of consumption. Specifically, Knight argued that an individual’s consumption is dictated more by his income in relation to others than by mere utility maximisation—a notion now commonly known as relative income hypothesis. In this connection, Knight also pointed out that a general increase in income, not only leaves the individual’s relative position in society unaltered but makes her/his situation worse off due to the peculiar characteristics of the market for “personal services.” Second, this unpublished address provides further evidence of how, in spite of some substantial differences in terms of methodology, his research interests converged in many respects with those of the institutionalists.

### KEYWORDS

Frank H. Knight; consumption; relative income; institutionalism

### JEL CODES

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## Introduction

In the opening pages of his *Income, Saving, and the Theory of Consumer’s Behaviour* (1949, 15), the work which introduced what came to be known as the “relative income hypothesis,” James Duesenberry indicated both Thorstein Veblen and Frank Knight as two authors who had made “real contributions to our understanding of consumer behavior problems.” Albeit significant, Duesenberry continued, their contribution was limited, in the sense that “they did not try to develop a positive analytical theory of consumption”—one which “would take into account the interdependence of preferences and still be useful in connection with the problems traditionally called economic.” Duesenberry’s joint reference to Veblen and Knight may appear at least ironic. Not only, in fact, Knight did not hesitate in more than an occasion to drop caustic comments on Veblen, but, more crucially, he stood for almost two decades as a staunch adversary

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of many leading institutionalists of his time, especially those of the so-called “scientific” wing of the movement.<sup>1</sup> In this connection, Knight himself made clear to Wesley C. Mitchell in 1923 that his forthcoming contribution to Rexford G. Tugwell’s institutionalist manifesto *The Trend of Economics* (Knight 1924) was intended to be “a presentation of the claims of the old-fashioned theory as against institutional economics.”<sup>2</sup>

Yet, Duesenberry is correct in calling attention to Knight’s “dissenting” views on consumption theory, although his contention that “Knight’s critiques on utility theory were written primarily in connection with a discussion of the relations of economics and ethics” (1949, 15) needs to be further qualified. The implicit reference here is to Knight’s “Ethics and the economic interpretation” (1922)—a crucial essay which marks the beginning of Knight’s lifelong crusade against the strictly “scientific” (or “behavioristic,” in the jargon of the time) conception of economics. In this, and in a series of other important essays published during the 1920s and early 1930s, Knight’s primary intent was to set in clear terms what he perceived to be “The Limitations of the Scientific Method in Economics” (1924), to cite the title of one of his most incisive works of those years. Economics, Knight held (1922, 475–476: see the discussion in Emmett 2006), can be scientific only to the extent “its subject-matter is made abstract to the point of telling us little or nothing about actual behavior.” As a science of conduct, in fact, economics can only predict that an individual will prefer larger quantities of wealth to smaller because “in the statement the term ‘wealth’ has no definite concrete meaning; it is merely an abstract term covering everything which do actually (provisionally) want.” In a similar vein, Knight continued, the law of diminishing utility merely indicates that an individual will maximise total utility at the point where the last unit of each good consumed provides equal utility, that is, where marginal utilities are equal. In the end, “[s]uch laws are unimportant because they deal with form only and say virtually nothing about content, but it is imperative to understand what they do and what they do not mean.”

Even more severe limitations apply to the behaviouristic interpretation of behaviour in terms of “stimulation and response with consciousness out of it” (460 n3). As Knight put it in a letter to Morris A. Copeland, probably the most outspoken among the proponents of behaviourism in economics:

I submit that no man, however well-educated or critical, or scientifically biased, can carry on five minutes of ordinary conversation about any topic of human interest connected with human relations, without repeatedly and distinctly recognizing: (a) that human actions are largely caused and inevitably interpreted in terms of wishes or desires, in a sense categorically different from mechanical estimation; and (b) furthermore, that they are similarly caused by and inevitably interpreted in terms of (to a lesser but important degree) value judgment in a sense categorically different from wishes or desires.<sup>3</sup>

<sup>1</sup> Knight gives us an amusing example of his typical deliberately provocative style in a 1940 letter he sent to Joseph Dorfman, Veblen’s biographer and renown institutionalist: “I would really like to know what standing Veblen has or had, if any, in the field of Archaeology, which is the foundation of his whole position. I have never happened to know of any recognized archaeologist recognizing Veblen’s existence. If I am grossly uninformed in that connection, I do wish you would give me references which would enable me to get right. Another question which is, of course, impertinent to ask, but about which I was even more puzzled, was whether your statement about Veblen’s standing among ‘the economists who count’ was meant seriously, or was intended to be funny.” Frank H. Knight to Joseph Dorfman, 18 December 1940; quoted in Asso and Fiorito (2013, 63).

<sup>2</sup> Frank H. Knight to Wesley C. Mitchell, 18 May 1923; quoted in Fiorito (2000, 290).

<sup>3</sup> Frank H. Knight to Morris A. Copeland, 25 January 1927; quoted in Asso and Fiorito (2003, 79).

91 Knight restated his position in his entry “Value and Price” for the *Encyclopaedia of*  
 92 *the Social Sciences*. Values, he argued (1935, 246–247), enter the realm of economic  
 93 behaviour in two different ways. First, he argued, “what is chosen in an economic trans-  
 94 action is generally wanted as a means to something else”—a point reminiscent of  
 95 Dewey’s denial of the means-end dichotomy (Hands 2006)—and this in turn implies “a  
 96 [value] judgment that is a means to the result in question.” Second, “what is ultimately  
 97 wanted for its own sake can rarely, if ever, finally be described in terms of physical con-  
 98 figuration, but must be defined in relation to a universe of meanings and values.”  
 99 Human conduct, Knight argued, is ultimately an exploration into this field of “meaning  
 100 and values”—a conscious striving towards new and “better” wants, rather than an exer-  
 101 cise in utility maximisation or, even worse, a mechanical sequence of conditioned acts.  
 102 The kind of scientific economic science advocated, on different grounds, by utility theo-  
 103 rists and behaviourists à la Copeland, cannot capture the value dimension of human life.  
 104 This task belongs to ethics or, as Knight wrote elsewhere (1924, 144), falls into the  
 105 domain of “the philosophy of history in the economic field, or what some of its votaries  
 106 have chosen to call ‘historical’ and other ‘institutional’ economics, studying the  
 107 ‘cumulative changes of institutions.’”

108 It is thus within the broader framework of his “antipositivism,” as Dan Hammond  
 109 (1991) defined it, that Knight developed his criticism of “standard” consumer theory,  
 110 and this explains why Knight’s discussion of the topic retained a somewhat fragmentary  
 111 and muddled character. What concerns us here is that is that Knight had the chance of  
 112 exposing his views in a more systematic fashion in a specific occasion—namely, when he  
 113 presented a paper on “Social Values in Economic Consumption” at a Social Science  
 114 Research Council (SSRC) Summer Conference, on Nantucket, Massachusetts in June  
 115 1931. Some background is necessary in this connection. Knight was acquainted with  
 116 Max Handman, an early promoter of institutionalism who later became a professor of  
 117 economics at the University of Michigan (Rutherford 2011).<sup>4</sup> Handman had chaired a  
 118 roundtable session at the December 1928 American Economic Associations meetings on  
 119 Economic History to which Frank Knight contributed (“Economic history” 1929). Then  
 120 Handman apparently invited Knight to join the newly established SSRC Committee on  
 121 Consumption and Leisure.<sup>5</sup> The committee was chaired by Handman himself and  
 122 included, in addition to Knight, Hazel Kyrk from the University of Chicago, Alvin  
 123 Hansen and Ronald S. Vaile from the University of Minnesota, Thomas D. Eliot from  
 124 Northwestern University, Carle C. Zimmerman from Harvard University, and  
 125 Hildegard Kneeland from the U. S. Bureau of Home Economics (Social Science  
 126 Research Council 1931). The group was well assorted: Hansen was an economist whose  
 127 business cycle studies had already brought him to the attention of the world profession;  
 128 Kyrk and Kneeland were among the most renown American home economists of their  
 129

130  
 131 <sup>4</sup> According to Albert B. Wolfe (1936, 192), the term “institutional economics” was invented “probably by Max  
 132 Handman in a conversation with Thorstein Veblen, about 1916.” At that time the two men were colleagues at  
 133 Missouri (Rutherford 2011, 15).

134 <sup>5</sup> The committee on Consumption and Leisure was one of the several SSRC advisory committees on Problems  
 135 and Policy established for the biennium 1931–1932. The other committees were devoted to the following fields:  
 crime, the family, personality and culture, population review, pressure groups and propaganda, public adminis-  
 tration, the seminar in culture and personality, social and economic research in agriculture, and  
 social statistics.

136 time; Zimmerman was a sociologist and social statistician who had worked extensively  
137 under Pitirim Sorokin; Vaile was a marketing expert; Thomas Dawes Eliot, T. S. Eliot's  
138 cousin, taught both sociology and anthropology.<sup>6</sup>

139 Knight's paper "Social Values in Economic Consumption" reveals a clear continuity  
140 with his previous epistemological writings, while also containing some novel elements  
141 that deserve our attention. Knight never published the paper, but a typewritten copy of  
142 the original manuscript can be found among his papers at the University of Chicago  
143 and is reproduced for the first time at the end of this brief introduction. In addition to  
144 the SSRC conference paper, Knight also drew up some "Jottings on Wants and  
145 Consumption" which further allow us to define his overall position. Knight's corres-  
146 pondence is also enlightening in many respects. Knight had in fact anticipated the  
147 main coordinates of his forthcoming contribution to the SSRC conference in a long let-  
148 ter he sent to Handman on 22 April 1931. "If we haven't talked about it,"—Knight  
149 wrote to Handman—"what I am thinking of reduces to two main ideas." The first is

151 That study of consumption in terms of particular specific commodities, as named and  
152 priced in the market cannot get anywhere, because people really use the most divergent  
153 commodities to satisfy essentially the "same" wants. To get anything in any degree  
154 general from one society or group to another or stable from one time period to another  
155 we must—fobidding as the task is—work with something less superficial, some notion  
156 of the wants themselves. In the concrete these are almost entirely social in origin and  
157 character, such things as conformity, distinction, power, prestige, etc., mixed with  
158 esthetic considerations which have more of a certain kind of objectivity, and ultimately  
159 with physical subsistence considerations which in fact play almost no role at all in  
determining what actually people do or want or consume.<sup>7</sup>

160 Accordingly, we find Knight stating in his paper that "[t]he general principle on  
161 which the argument rests is that the values or satisfactions involved in consumption  
162 are almost entirely cultural, i.e., historically created, artificial, in a sense accidental."  
163 Knight conceded that human wants can be arranged along a scale indicating in  
164 descending their level of objectivity in "physical-biological" terms. Yet, he continued,  
165 even the most objective human wants "owe their actual concrete character to social  
166 conditions historically molded," while, at the same time, "it is hard to find a need or  
167 objective want even in the most general sense corresponding to the behavior observed,  
168 the 'goods and services' consumed."

169 Moving from these premises, Knight could assert that the concrete form of what we  
170 call our "needs" as well as "the concrete means of satisfaction we connect with them"  
171 are determined by values of a "non-physical sort"—and so far he was reasoning along  
172 the path already delineated in his 1922 paper. From now on, however, Knight intro-  
173 duced some novel considerations which are not to be found in his published writings.  
174 The social values associated with consumption, he added, "may be positive or negative

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176  
177 <sup>6</sup> Unfortunately, our archival search, both at Knight papers at the University of Chicago and at the SSRC Papers  
178 at the Rockefeller Archive Center, did not allow us to trace any other contribution to the round table.  
179 Furthermore, only Zimmerman appears to have published a specific contribution on consumption shortly after  
180 the SSRC conference but the study, an empirical discussion of Engel's law (Zimmerman 1932), was related to  
the activities of Harvard Committee on Research in the Social Sciences.

<sup>7</sup> Frank H. Knight to Max S. Handman: 22 April 1931. Frank H. Knight Papers: box 4, folder 3. Special  
Collections Research Center, University of Chicago Library.



depending on the forms and terms of the association.” Knight elaborated on this point in his “Jottings” from which we quote in full length:

The valuation, or want-satisfaction situation, partakes very largely of two antithetical social forms. One, the competitive game, the other the orgy. In a game of cards, what the players immediately concretely want is cards, but of course only as symbols. But the point is that to destroy the conflict of interest is to destroy the interest itself, to chloroform the whole situation. And similarly as to applying the economic categories of efficiency of “justice,” or at least the notion of diminishing utility and distributive ethics. Similar reasoning, *mutatis mutandis*, regarding the orgy. There cannot be a conflict of interest, and economic categories are inapplicable. Obviously much consumption partakes of one character or the other (fashion perhaps fundamentally orgiastic) or, paradoxically, of both at the same time. And possibly there are other fundamental types, as well as various degrees and manifestation-forms. (I am not clear how far the urge toward power and distinction, to order others about and be served, reduces to the same principle as the competitive game.)

In this passage, cryptic as it is, two kinds of social relations involved in consumption are juxtaposed: the “competitive” game and the “orgy.” While in the former the “conflict of interest” between individuals is not only ineradicable, but constitutes the ultimate essence of the social value involved, the latter seems to apply to those dimensions in social relationship that cannot be experienced by only one individual, because they depend on the “positive” interactions with others. Interestingly, Knight appears also to be aware of the fact that competitive consumption implies some form of zero-sum game and he pointed out the importance of relative considerations where higher income brings status benefits to an individual:

But how many effectively realize, visualize, that money is only a means of getting things actually desired away from other people? How many realize that if at the same time that “I” get more money other people also get more, the results cancel out, that everyone being in the same relative position as before means that everyone is in the same absolute position as before? Of course every teacher of economics is fully aware that this fallacy is inveterate in the thinking of the public and its cure one of the first but exasperating difficult task of economic instruction.

But Knight was not satisfied with the “mere fact” that we see our income in comparison to the income of others. “That is of course a commonplace,” he stated, “but there is a deeper point.”<sup>8</sup> This brings us to the second idea Knight intended to develop in his paper. Quoting again from his letter to Handman:

The particular phase of this which seems to me to offer promise for study and development has to do with the relativity of income, specifically as the latter ties up with personal services, in contrast with commodities. Insofar as what we want and strive to get is either personal services “as such” or results which in the given state of technology can only be supplied through personal services, a general rise in incomes in a group (increase in economic efficiency) not only cancels out, but makes the situation

<sup>8</sup> A somewhat rigorous exposition, based on utility analysis, of the zero-sum nature of status competition had been proposed by the economist George P. Watkins in 1915 (Fiorito and Vatiello 2018). Watkins’ discussion caught Knight’s attention (1923, 593 n5) who commented: “Many of the ‘higher’ wants are keenly satirized in Veblen’s *Theory of the Leisure Class*. A sober discussion of the problems involved, of much greater scientific significance, is found in the later chapters of G. P. Watkins’s volume on *Welfare as an Economic Quantity* [1915].” A further analysis of economy as a zero-sum game is in Robert Lee Hale’s contributions (Vatiello 2013).

worse than before from the standpoint of satisfying these wants. It makes the classes who render such “services” more independent in all senses of the word, and their services not merely more expensive but less “reliable,” and valuable. In the form of a principle, the increase in economic efficiency in the production of commodities, if the distribution is at all comparable, essentially involves a decrease in the efficiency of personal services industries.<sup>9</sup>

Knight discussed this specific point in the second half of his SSRC paper. First, he made a distinction between “goods” and “personal services,” i.e., between “[those] forms of consumption which do not involve personal contact with the producer and those which involve such contact.” Then, he argued that a generalised rise in the income not only tends to increase the demand for personal services, as they are “complementary to commodities,” but also makes this demand less elastic with respect to income. Knight here seems to assume some form of increasing irreversibility of personal service expenditure, in the sense that when their level of income drops, individuals seek to maintain the level to which they are accustomed. At the same time, he continued, a higher level of general income reduces the supply of personal services also increases its inelasticity, because “a high commodity income frees people from the pressure to render personal services, and they do not ‘like’ to earn their living in that way.” This, it should be noted, justifies Knight’s contention that personal services become relatively “more expensive” with a general increase in the standard of living, but leaves unexplained why “personal services” should become less efficient and “reliable.”<sup>10</sup> On this ground, Knight could reassert the relativity of income in more pervasive sense than the one theorised by Duesenberry:

Insofar as what we want with income in any sense is finally the ability to command the labor of others, then a rise in the level of “real income” cancels out as between individuals in just the same way that a rise in the level of money income cancels out if not accompanied by an actual increase in the production of the items which constitute real income

not only does the individual fail to command more of the services of others if he gets a larger commodity income and the others get it in the same degree at the same time; not only that but “he” (whoever he may be) actually has much less command over others in consequence of a general uniform increase in commodity income. This principle has very wide ramifications, the nature of which depends, as does ultimately the validity of the principle itself, of certain facts if an institutional character.

As a significant example, Knight referred to the so called “servant problem”—a phrase which was then used to refer to the difficulties employers had in hiring and keeping “domestic service,” as well as to the problems servants experienced in their occupation. At the time this was a widely debated theme both in the popular and academic press. “Beyond doubt,” wrote Willystine Goodsell in the *Annals* (1932), “democracy created the domestic servant problem which has disturbed the souls of housewives from the early decades of the nineteenth century to the present.” Goodsell, as many other then-contemporary observers, pointed out that in a rapidly growing

<sup>9</sup> Frank H. Knight to Max S. Handman: 22 April 1931. Frank H. Knight Papers: box 4, folder3. Special Collections Research Center, University of Chicago Library.

<sup>10</sup> A possible (long-term) explanation could be that since the increased wages provide the means for many of the individuals supplying personal services to shift toward more agreeable occupations, the new entries are less skilled and hence less efficient.



271 industrial society domestic service retained much of a preindustrial organisation and  
 272 ethos.<sup>11</sup> The relationship between master and servant, mediated by wages “absurdly  
 273 low from a modern standpoint,” remained structured by an older sense of duty and  
 274 mutual obligation. “No wonder,” Goodsell wrote, “young women preferred the freer  
 275 life and the better pay in the factories.” Moreover, “the democratic gospel of the equal-  
 276 ity of all men was bound to make itself felt in the attitudes and the behavior of under-  
 277 paid household drudges.”

278 Knight considered the servant problem as “due to or at least associated with the  
 279 higher general level of incomes in America,” as compared to the European situation.  
 280 To Knight’s eyes the crux of the whole issue was the negatively shaped supply curve for  
 281 domestic services:

282 Here one encounters another paradox of pecuniary relations, the inverse elasticity of  
 283 supply for labor; the more money one offers to pay the less one may be able to buy.  
 284 And perhaps especially so in the long run view; the higher servants’ wages go the less  
 285 effective the tendency to “educate” people for the role in the inclusive sense of the term,  
 286 or at least, the pressure on the buyers to find some other mode of life becomes more  
 287 effective than the pressure on sellers to supply the type of service buyers require. It  
 288 needs no pointing out that high class living quarters are largely a matter of personal  
 289 service, the availability of which depends more on social traditions and tastes of the  
 people who render it than on any more tangible economic consideration.

290 Another important factor, which he just touched upon, was that domestic service  
 291 remained “preponderantly a question of woman’s work, which is another angle of the  
 292 question as between many parts of America and Europe, where women have a scarcity  
 293 value in one case and are more or less of a drug in the market in the other.” The most  
 294 interesting aspect of Knight’s discussion, however, is to be found in the solution he  
 295 offered. Here he differed from the bulk of his contemporaries who had proposed either  
 296 to make domestic work more efficient, or to treat domestic help like workers in any  
 297 other industry, with definite hours, hourly wages, work plans, and regular days off (see  
 298 Dudden 1986 for a survey of the literature of the period). In Knight’s view the only  
 299 viable solution was to be found in the new techniques and appliances which would  
 300 allow individuals to substitute “commodities” for personal services. As he put it in his  
 301 correspondence with Handman, this perspective would open new avenues for research:

302 To generalize economic well-being through efficiency, we have to find some way of  
 303 converting services into commodities. Can a “higher culture” be achieved without  
 304 domestic service? is the interesting question. “What about” a civilization which lives in  
 305 mechanical kitchenettes, and eats out of tin cans? Of course the core of the investigation  
 306 would be in the field of domestic service, but the general field of investigation extends  
 307 far beyond that—chauffeurs, musicians and actors, etc., etc. I merely suggest the  
 308 possibility of a study of the possibilities of substituting commodities for personal  
 309 services with all the consequences and ramifications involved, including a study of the  
 310 meaning of personal service in different connections, etc., etc. (Personally the humble  
 311 laundry has long seemed to me an especially inviting point of attack: how can it be that  
 312 with all the modern science and machinery applied, and no sentimental reason for

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313 <sup>11</sup> Willystine Goodsell was professor of history and philosophy at Teachers College, Columbia University. In  
 314 1928, a group called the National Council on Household Employment had brought together social scientists,  
 315 labor activists, efficiency experts, and even future First Lady Eleanor Roosevelt to try to solve the so-called  
 “servant problem.” See Dudden (1986) for a discussion.

wanting laundry done in personal contact with the beneficiary, it still seems to pay to have the Washfrau come into the home rather than send the washing out.

In more general terms, Knight identified social progress with the progressive “commodification” of personal services, so that consumers could fully exploit the increase in efficiency due to technological advance. He made the point crystal clear in a crucial passage of his SSRC paper: “[u]nquestionably we have, particularly in America, substituted commodities for services, or taken the effects of increase overwhelmingly in that form.” And, he significantly added, “if the fundamental values which have gone with capitalism and democracy in the past maintain their hold, the further and relatively complete development of this substitution is a primary task confronting economic progress.” This is an interesting feature of Knight’s own notion of liberalism which he did not fully develop in his subsequent writings.

A few words should also be spent on the relationship between Knight and the institutionalists—an aspect which has received some attention in the literature (Hodgson 2004; Rutherford 2010; Fiorito 2016). As shown by the paper reproduced below, Knight’s research agenda overlapped in some important respects with that of many leading institutionalists of the time. In this connection is significant to note that the SSRC committee on consumption and Leisure revealed a clear institutionalist orientation—with Handman, Kyrk, Kneeland, and Hansen all more or less directly affiliated to the movement. Yet, it should be made clear, Knight was by no means part of the network of individuals who promoted institutionalism during the late 1910s. His firm opposition to empiricism, pragmatism and behaviourism distanced him from institutionalism and much of his academic work during the 1920s and 1930s can be seen as a response to (what he perceived to be) the scientific pretensions of the movement (Asso and Fiorito 2008). Knight did not deny the heuristic value of neoclassical economics once its limitations are well understood.<sup>12</sup> What he advocated was a clear epistemic discontinuity between the analytical apparatus of scientific economics and the study of the changing institutional framework of societies. While people like Morris Copeland and Lawrence K. Frank, saw institutionalism as an application of the “scientific” in economics, Knight conceived it as a sort of philosophy of history in the economic field where human behaviour is seen “as the expression of conscious attitudes toward values whose content is largely an institutional product” (Knight 1923, 355; see also 1924).<sup>13</sup>

<sup>12</sup> Knight made this point crystal clear later in his life: “Hence these ‘limitations’ constitute no objection to traditional economic theory, either as science or in relation to practice – provided only they are understood, and its part in the whole project of education and of social management is understood, and is combined with the results of other disciplines whenever this is needful for handling the problem, scientific or practical, that is under consideration” (Knight 1950, 122).

<sup>13</sup> Kyrk’s *Theory of Consumption* (1923), a then much acclaimed institutionalist contribution, did not escape Knight’s critical attention. In his unpublished notes on Kyrk, Knight found her reliance on Dewey’s instrumentalism “too narrow, even self-contradictory.” To Kyrk’s eyes, Knight explained, the origin of value lies in its contribution to human adjustment and survival. This, he insisted, “is in line with Dewey’s narrow ‘biological’ pragmatism.” But how then can Kyrk justify her assertion that moral and aesthetic values “have a way of appearing as categorical absolutes and as independent values, good for nothing but good in end of themselves [Kyrk 1923, 159]”? Reconciliation under the umbrella of instrumentalism, Knight concluded, “would require a conception of ‘end’ so broad as to make the notion of instrumentality and the means-end relation meaningless.” “Notes on Miss Kyrk’s chapter on the Value Problem” (1923). Frank H. Knight Papers: box 10, folder 24. Special Collections Research Center, University of Chicago Library. On Knight’s somewhat controversial relationship with pragmatism see Hands (2006) and Fiorito (2009, 2011).


Although Knight never returned on the notion of income relativity, his interest on consumption surfaces with regularity in his subsequent works. In more than an occasion, we find him anticipating many of the critical issues that have been raised against standard choice theory. One of these, for instance, is the idea the idea of errors/mistakes in rational decision making which have been emphasised in the heuristics and biases literature in behavioural economics: “This introduction of... error as essential features of utility reasoning, making maximum utility define the goal of conduct which people try to reach, but not that which they actually realise, seems to differentiate it sharply from the sort of cause met with in the physical sciences” (Knight 1931, 60). In a similar vein, Knight advanced the notion that preferences may not exist, or may not be known, prior to the act of choice; but they are forged and formulated during the very evaluation and choice process. This is the idea of constructed preferences (Slovic 1995). In Knight’s words:

First, the end is rarely or never actually given in any strict sense of the word; it is in some degree redefined in the course of the activity directed toward realizing it, and the interest in action centered in this definition and discovery of ends, as well as in their achievement. That is, the end is always itself more or less problematic, as well as the procedure (use of means) for realizing it. (Knight, 1941, 136)

In 1944 Knight touched again upon these themes but within a different context. This time he targeted the Hicks-Slutsky ordinal approach to demand theory. The essential feature of the Hicks-Slutsky approach, he stated (1944, 289), comes down to the “replacement of the conception of ‘absolute’ diminishing incremental utility ... with a diminishing ‘coefficient of substitution’ of one good for another, assumed to be a purely behavioural principle.” Knight’s goal this time was to defend a psychology-based account of consumer’s demand still based on the “conventional” notion of cardinal utility. Intentional behaviour, he contended, always involves a process of valuation and, in turn, valuation always contains a quantitative element in it. This means that not only individuals rank outcomes in terms of utility, but that they can estimate, even if not exactly measure, the difference in the “conscious well-being” experienced in different outcomes—“Whenever our minds judge one experience to be greater, more intense, than another, it is always possible to distinguish between (approximately) equal and unequal degrees of change” (304).

This is not the place to deal in detail with these aspects of Knight’s thought (see Mirowski and Hands 1998 for a discussion). What concerns us here, and this our final notation, is that even in his attempt to rescue demand theory from behaviourism, Knight did not miss the opportunity to stress again the limitations of neoclassical analysis. These limitations become manifest when consumption is looked at as a form of social interaction and social values are taken into consideration. “Association itself has only to a limited extent the purpose assumed in economic analysis,” i.e., the attainment of given ends. Reiterating almost verbatim what we find in his 1931 address reproduced below Knight concluded: “To a very large extent it [association] is a matter of formulating the rules of a game, in which individuals do indeed pursue ends, but ends symbolic in character, set up to make activity interesting, instrumental to this purpose, and in large part effective because of their conflicting or competitive nature” (311).

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## Social values in economic consumption

Frank H. Knight Papers: box 12, folder 4. Special Collections Research Centre, University of Chicago Library

Everybody says consumption is perhaps the most important phase of economics and deplors the relative neglect of its study, but no one seems able to propose a line of effective attack on the study itself. Of course the "law of diminishing utility" tells us nothing about consumption in the concrete. These remarks pass over the question of the proper form and usefulness of this principle, and also pass over the general subject of the usefulness of a type of economic study which makes no pretence of describing or affording a basis for predicting the concrete content of economic behaviour. Nor is any "solution" of the problem of consumption offered; it is merely the hope that the suggestions offered have some value, and that they point a direction for further study.

The general principle on which the argument rests is that the values or satisfactions involved in consumption are almost entirely cultural, i.e., historically created, artificial, in a



sense accidental. As a fact they fall more or less definitely in a series along a scale in this respect, beginning with types of want and want satisfaction which are *relatively* objective, universal, physical-biological. Yet we must be clear that physical needs as such play an almost exclusively indirect role in economic life among civilised peoples. The concrete wants which motivate consumers' expenditure are wants for a particular thing or "services" more or less definable physically, and their specific character is historically and socially determined. Man as a biological specimen has extremely few specific needs and these play little part in motivating civilised economic behaviour. Water and salt are specific needs, but they become economic goods (as contrasted with free goods) chiefly through conditions imposed by the requirement of satisfying other wants of a different character. We need food, in the sense of nourishment; But our wants are for certain foods. Dietetic science has taught us much about the kinds of food we need and the limits of substitution of one kind for another; but these have little correspondence with the kinds we desire and buy. Indeed there are so many kinds in the economic sense, so many different "foods" as offered in the market, within any one kind as defined dietetically, and so many kinds in the dietetic sense which are excluded economically by social custom and standards, that the dietetic concept of food in relation to the economic foods is rather a new set of problems than a help in solving those of the student of actual consumption. But food has the greatest degree of physical definiteness and universality of any of our wants. What applies to it will apply all the more to other want categories, clothing, shelter, the comforts, conveniences, recreations, and beautifications of life and finally the mere emulations fashion and fads. Further comment on this list is not needed to bring out the fact that the different categories do, as stated at the outset, fall along a sort of scale, of which even the most objective items owe their actual concrete character to social conditions historically moulded,<sup>14</sup> while at the other extreme it is hard to find a need or objective want even in the most general sense corresponding to the behaviour observed, the "goods and services" consumed.

On the other hand, however, it must be emphasised that "man is a social animal." He most emphatically "does not live by bread alone." His purely artificial, social wants, tend to become needs in the veritable, imperative sense. People suffer pain, become unhappy, morbid, sick, mad, even die from things so intangible as lack of recreation or of tolerable social status, and in acute cases commit suicide even when in good health rather than suffer "indignities" which have no significant physical consequences and which in themselves are purely symbolic, and incapable of description in physical terms.

It is to be noted with reference to the notion of a scale of degrees of the social-historical or artificial quality in wants that it is by no means a simple, linear scale, but an intricately branched one. Wants of different kind may lie at the same distance from the ideal zero point of pure specific physical needs, or there may be room for wide difference of opinion as to the relative distance of two types. And the different kinds of want overlap and interconnect. It is not the purpose here to enter upon the construction of an analytic table of wants, developing the composition of recognised categories out of elements, but an illustration or two may be in order.

The discussion so far has shown that the concrete form of what we call our "needs" and the concrete means of satisfaction we connect with them are determined by values of a non-physical sort. Suppose we consider for a moment one of the most basic and general categories of value "above" the physiological level, namely aesthetic value, or beauty. First there are the appreciative and creative sides of beauty, theoretically opposed, but actually overlapping, and both mixed with elements of social value, pride and emulation, and communicated meaning.

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<sup>14</sup> A particularly interesting case which can only be mentioned would be that of health wants. Certain remedies are said to be "specific" for certain diseases. But there seem to be much truth in the old-fashioned view that the diseases themselves are largely the product of civilization, and certainly medical science is placing more influence all the time on general hygiene and less on specifics. Presumably no one would argue that there is actually any specific correlation between health and the things people actually buy and do at a cost "for their health."



The artistic merit of a human production may be utterly different from the “pure beauty” of a sunset. Appreciation may be largely pride of possession or pride of achievement, both of which may be sympathetic as well as personal. We “value,” admire and take pride in, both the possessions and achievements of relatives, friends, fellow-townsmen, groups and cultures to which we belong, etc., in a sense distinct from any immediate “sensuous” appeal, and the value connected with the communicative element depends on whom the communication is from as well as what is communicated. Then of course there is the eternal quarrel between art-for-art ethics or utility, regarding which it seems self-evident that utility is no more objective than either of the others and that the fields of all three are much more overlapping than contrasting. Finally, we undoubtedly have to recognise in aesthetic values a large element of pure fashion, or even faddism, itself an interesting concept to attempt to analyse.

An attempt to distinguish and define the final elements in our valuations, i.e., our real values themselves in real contrast with the varying and accidental instruments which minister to them, would lead into catalogues of “instincts” à la [William] McDougall at all or “wishes” and the like à la [William I.] Thomas et al. Nothing of the sort is contemplated here. The writer is in fact a sceptic with regard to all such lists, definitions and logical arrangements, on general grounds, confirmed by the utter inconsonance of the results of such endeavours to date. Until social psychology has made real advance, say by effectively settling the relation between work and play, elaborate or definite constructions of the sort must be highly individual. But that does not mean that we cannot refer to more general urges underlying our superficial concrete evaluations, nor even that it is possible to discuss human motives, objectives and achievements in any field without going a considerable distance in this direction. Insofar as we get down to anything at all fundamental, general or permanent in the treatment of purposive behaviour, such as economic activity is to the degree that we have any right to use the term economic itself, we clearly must do so. For it is just a plain and obvious “fact” that the actual concrete “goods and services” produced and consumed are the infinitely various, accidental and fleeting symbols of the underlying realities. The idea that these things are “objective” in the sense of the requirements of science is an illusion difficult to explain. As John B. Clark long ago insisted, utilities are not things, but the particular qualities in things, and it is equally clear that the qualities are relative to human appreciations, which in turn are local and evanescent as to the concrete and external but general and permanent in some degree when interpreted in terms of basic human nature.

It is indeed an obvious convenience to the statistics-grinders to list and measure the things for which people spend money, accepting as final the names by which they are known in the market. But anyone interested in “facts” must see at a glance that the names themselves are very frequently manufactured with the commodities, often at much greater cost, and often constitute the only distinctive thing about the commodity itself and its actual basis of appeal. The study of consumption in terms of concrete items, without endeavouring to reduce to some sort of order the more stable values which things themselves accidentally symbolise and embody is certainly foredoomed to futility. It should be an impertinence to do more than mention the obvious fact that the actual expenditures for “food” even of a family in very moderate circumstances include a fairly small fraction for actual nourishment and a fairly large fraction for taste and social values like conformity and distinction and an indefinite list besides. To be sure the economic individual does not realise this; he “thinks” he “wants” the things he buys and does not know that expenditures for food or drink and those for clothing, housing, a car, travel, culture, even donations to causes, may be all means of satisfaction for the same wants. But that does not alter the “facts” as the student must recognise them.

## II

Interest in the study of consumption, like that impelling to most studies, is of two main sorts, “theoretical” and “practical.” In the present case it is assumed that the desire to consume is the chief “cause” of or force explaining economic behaviour in its other stages or branches,

586 and it is assumed at the same time that it is the true and proper “end” of the other activities.  
587 We pass over the fact that in social science, unless the student regards himself as outside of  
588 social phenomena in a one-sided relation of understander and/or controller which has no reality  
589 in modern society, there is a logical contradiction between the two standpoints. The point  
590 to be developed here has to do both with understanding and control. It offers some explanation  
591 of certain phenomena of consumption, and of production as dependent on consumption,  
592 and points out some conditions and requisites for the direction of economic development  
593 along lines generally admitted to be desirable in view of the accepted ideals of modern western  
594 civilisation. It may be well to indicate the scope of the discussion by listing some of the problem  
595 excluded by the treatment. No question will be raised as to the fundamental assumption  
596 conventional in classical economics that the direction of causality both is and should be from  
597 the side of consumption; I merely remark in passing that there are serious limits to the truth  
598 of both the theoretical and practical phases of the assertion. Likewise accepted for the purpose  
599 of the argument is the boarder assumption of conscious purposiveness being economic activity,  
in contrast with any sort of automatism or growth through mechanical process like accidental  
variation and selective survival.

600 To the point I wish to make there are two natural lines of approach. On the one hand, as  
601 indicated in the title, it has to do with social values involved in consumption. But only with a  
602 particular form of social value, the value of direct human association, which may be positive  
603 or negative depending on the forms and terms of the association. The particular case at issue  
604 under this head involves the general distinction between “goods” and “personal services,”  
605 forms of consumption which do not involve personal contact with the producer and those  
606 which involve such contact. The question is raised as to what has happened in this field in  
607 consequence of the general increase in economic efficiency and rise in general incomes, and  
608 the further question as to what must be brought about if increased efficiency is to be reflected  
609 in a correspondingly “improved” standard of living. Unquestionably we have, particularly in  
610 America, substituted commodities for services, or taken the effects of increase overwhelmingly  
611 in that form. And it will be argued that if the fundamental values which have gone with capitalism  
and democracy in the past maintain their hold, the further and relatively complete development  
of this substitution is a primary task confronting economic progress.

612 From another angle, the argument has to do with the relativity of wealth or riches. Here I  
613 do not mean the mere fact that idea of comfort or well-being itself is relative in the two senses  
614 of being measured from some level of expectations or from that of the position of other persons.  
615 Wealth, or more properly real income, is relative in a much deeper sense, which may be  
616 brought out by beginning with the relativity of money as such as an object of pursuit.

617 The point I wish to make has to do with the relativity of the wealth or riches in a certain  
618 fundamental sense. But, negatively again, I do not mean the mere fact that the idea of comfort  
619 itself is relative insofar as the satisfactions derived are based on competitive emulation. That is  
620 of course a commonplace, but there is a deeper point. One may begin with the relativity of  
621 money itself as an object of pursuit. Of course most people who strive to get money will admit  
622 if directly asked that they do not want money as such, but the things it will buy. (Indeed they  
623 probably admit this, generally speaking, to a much greater degree than it is really true!) But  
624 how many effectively realise, visualise, that money is only a means of getting things actually  
625 desired away from other people, how many realise that if at the same time that “I” get more  
626 money other people also get more, the results cancel out, that everyone being in the same relative  
627 position as before means that everyone is in the same absolute position as before. Of  
628 course every teacher of economics is fully aware that this fallacy is inveterate in the thinking  
629 of the public and its cure one of the first but exasperating difficult task of economic  
630 instruction.

631 But that, of course is no contribution. The question I raise is that of the degree to which  
632 the same is true at bottom of “real income” in the most objective possible definition of the  
633 concept. My thesis is in a word that it is true ultimately insofar as real income consists of personal  
634 services, and that this means to a very considerable extent. Insofar as what we want with  
635 income in any sense is finally the ability to command the labour of others, then a rise in the

level of “real income” cancels out as between individuals in just the same way that a rise in the level of money income cancels out if not accompanied by an actual increase in the production of the items which constitute real income. Of course I abstract in both cases from the effects of changes in the distribution among individuals. Any one individual who gets relatively more money income *is* in the position to get and does presumably get more real income if the total is the same as before, and the same holds for the increased ability of an individual who gets relatively more real income to command more of the services of other persons who get relatively less. But, and this is the point, *not only* does the individual fail to command more of the services of others if he gets a larger *commodity* income and the others get it in the same degree at the same time; *not only* that but “he” (whoever he may be) actually has much *less* command over others in consequence of a general uniform increase in commodity income. This principle has very wide ramifications, the nature of which depends, as does ultimately the validity of the principle itself, of certain facts if an institutional character. Some of these, and the social values at issue I shall attempt very briefly to indicate, beginning with the conditions affecting the principle itself.

In technical terms, and viewing the facts of Western civilisation as facts before inquiring into reasons underlying them, a rise in the general income level greatly increases the demand for personal services (and increases the inelasticity of demand) and decreases the supply and increases its inelasticity also. Personal services are complementary to commodities; one cannot enjoy a high commodity standard of living without command over personal services, but a high commodity income frees people from the pressure to render personal services, and they do not “like” to earn their living in that way (as a surface fact of Western civilisation, consideration of reasons, underlying factors, to come later). Of course on the other hand, over wide areas and within wide limits commodities can replace personal services in the satisfaction of the “same” wants (in terms of a superficial classification of wants) and it is a question of social psychology and institutions how far wants for additional satisfactions will take one form or another. These general conceptions seem to me to set a problem study of which would yield results within unpredictable limits, worth their cost in comparison with other directions in which the effort might be expanded. In terms of the usual jargon, it is a question of the relative elasticities of demand and supply of commodities and personal services and on the demand side this is as in other cases a problem of the nature and relative importance of relations of complementarity as compared with those of substitution, both of which are partly technical or quasi-technical matters and partly matters of pure taste, like the question of the extent to which one can substitute butter for bread by spreading it thicker as against the extent to which a composite utility is dependent on fixed proportions in combination.

The general idea may be made clearer by an example. It is a common impression, both in America and in Europe, that money goes very much farther there than here. Now as everyone knows, basic commodities, particularly food and clothing materials, are not cheaper in Europe. Axiomatically (barring monopoly) nothing which enters into international trade can differ in wholesale price in different regions by (much) more than the transportation costs, and in fact these things are typically exported from America and imported into Europe, so that in fact they are appreciably higher there than here. Yet the general impression referred to is by no means a myth of unexplained origins. Thousands of people are constantly moving back and forth, and particularly as between the United States and Germany people representing nearly all classes in the population. And one commonly hears on both sides that a marc (24¢ less a fraction) goes as far there as a dollar in the US. Passing by the question of exaggeration or the actual degree of difference, it is by common consent very great. Two lines of reflection at once suggest themselves, the first relating to the manner in which people typically live, and the second to the impingement of the situation on different social classes at different income levels.

Regarding the typical manner of life, two facts strike any observer forcefully. The first is that food costs are not so very different for the same dishes, although as regards served food in home or restaurant there is a difference in favour of Europe, contrasting with the difference in favour of America for cost of the ultimate materials. The conspicuous difference is in the

676 amount of house-room on the one hand and on the other the automobile. And the economist  
677 will notice at once that the habits of the people correspond to price opportunities. When one  
678 thinks of getting out of straightened circumstances into a “comfortable” scale of living in  
679 Europe, one thinks of a larger and better living quarters, and in America one thinks of a car.  
680 But the car is of course much cheaper here and the ampler living quarters there. Europeans  
681 jump to the conclusions that this reflects a lack of culture among Americans, whose apprecia-  
682 tions run to power and fast movement (the “noise” factor here is a little ambiguous!). They  
683 tend to smile at a literate people living in kitchenettes apartments eating out of tin cans and  
684 actually spending on luxurious private transport a considerable fraction of all their living  
685 outgo, even at the lower price for the car and higher price for “decent” accommodations here.  
686 There is some truth in their point of view, much as it may go against our patriotic pride, but  
687 on the other hand there is an “explanation,” which may “explain” our behaviour without  
688 recourse to differences in taste or may on the other hand “explain” the difference in taste, or  
689 an uncertain mixture of the two. The point is that not merely it is “cheaper” to do as the  
690 American middle class does, but that the money expense is rather the smallest factor in the  
691 situation. Due to or at least associated with the higher general level of incomes in America  
692 (part also of the tradition of democracy, American brand), is the “servant problem.” Here one  
693 encounters another paradox of pecuniary relations, the inverse elasticity of supply for labour;  
694 the more money one offers to pay the less one may be able to buy. And perhaps especially so  
695 in the long run view; the higher servants’ wages go the less effective the tendency to “educate”  
696 people for the role in the inclusive sense of the term, or at least, the pressure on the buyers to  
697 find some other mode of life becomes more effective than the pressure on sellers to supply the  
698 type of service buyers require. It needs no pointing out that high class living quarters are  
699 largely a matter of personal service, the availability of which depends more on social traditions  
700 and tastes of the people who render it than on any more tangible economic consideration. Of  
701 course, it is preponderantly a question of woman’s work, which is another angle of the ques-  
702 tion as between many parts of America and Europe, where women have a scarcity value in  
703 one case and are more or less of a drug in the market in the other.

704 Other elements in the domestic living situation present other problems. The cost of build-  
705 ing is lower in Europe; though not a personal service industry it resembles the latter in the  
706 sense that its products cannot be transported and hence their price reflects differences in pre-  
707 vailing wage rates. (Which may be modified between countries by differences in the constitu-  
708 tion of the “non-competing” economic strata.) Ground rents in cities are also much lower,  
709 which is to me a mystery. Some features of municipal policy may largely affect various factors  
710 in living costs, but discussion would involve extended study of the policies and of the inci-  
711 dence of the taxation by which they are carried out. No doubt in part the apparent differences  
712 in wage levels would be found to be nominal, being really compensated by public services pro-  
713 vided out of taxation really falling upon the wage earners.

714 The other leading thought referred to is the natural question whether the advantage of liv-  
715 ing in Europe on the part of consumers of personal services is not associated with a corre-  
716 sponding disadvantage for the class which renders them. With reference to the matter at issue,  
717 living costs, this may be true to some extent for domestic servants as such, and possibly to a  
718 greater extent for other types of labour. Undoubtedly the migration to America has been pri-  
719 marily from the “lower classes” while it is the fairly comfortable classes who talk more of the  
720 lower cost of living in Europe. Yet German and other European immigrants to America are  
721 characteristically disappointed with opportunities here. They admit a higher commodity scale  
722 of living here, but find other drawbacks, which bring up the whole question of the type of  
723 social and community life as itself an item in the scale of living, but one whose valuation  
724 depends on habits as well as other differences in tastes.