

MANKIW'S TEN PRINCIPLES OF ECONOMICS 1: PEOPLE FACE TRADE-OFFS

The introduction to this series is here.

The first of the Ten Principles of Economics laid down by N. Gregory Mankiw is "People Face Trade-Offs". Principles of Macroeconomics, 6th Ed. 2012, p. 4. In language more suited to a high school textbook than a best-selling college textbook, he provides several examples. If you study economics for five hours, then you can't spend that time studying something useful, like welding or English Literature. If parents have a certain amount of money, every dollar they spend on rent can't be saved, or used to buy food. Then, as if society were a person, and faced trade-offs in exactly the same way (government is just like a household) he gives two macro examples. First:

The more a society spends on national defense (guns) to protect its shores from foreign aggressors, the less it can spend on consumer goods (butter) to raise the standard of living at home.

There is also a trade-off between a clean environment and a high level of income. If companies have to pay for environmental contamination, they make smaller profits, pay lower wages, or raise prices or some combination. This is the last example:

Another trade-off society faces is between efficiency and equality. **Efficiency** means that society is getting the maximum benefits from its scarce resources. **Equality** means that those benefits are distributed uniformly among society's members. Emphasis in original.

Mankiw explains this by saying that government policies that help those in need, like unemployment insurance or welfare reduce efficiency, because, and I quote because otherwise you'll think I'm being snarky:

When the government redistributes income from the rich to the poor, it reduces the reward for working hard; as a result, people work less and produce fewer goods and services. In other words, when the government tries to cut the economic pie into more equal slices, the pie gets smaller.

The statement that individuals face trade-offs in consumption of goods and services as well as every other human activity is vacuously true. We get one life, and at any point in time can only do one thing. If we do one thing we cannot do another. So what's the point of this principle? I think it's not the principle itself, but the examples. Each supports the principles of neoliberalism, as described by Philip Mirowski in this article.

Mankiw's first two examples are folksy and disarming. Let's try a similar version:

Angela has a problem: should she summer with her mom on Martha's Vineyard, or should she summer with her dad on their ranch in Montana? Jane has a problem: should she pay her utility bill, or should she buy the drugs she needs to control her Parkinson's Disease? Since these are two individuals, you can see that the problems they face are identical. Both will suffer if they make the wrong decision, and both will suffer anyway because of the knowledge they could have chosen otherwise. The rich and the poor are just the same: people struggling with trade-offs. Or, from Mirowski on neoliberalism: [9] Thou Shalt Know That Inequality Is Natural.

Things get more complicated at the macro level. The third example, guns or butter, is as abstract as the first two are concrete. Mankiw

makes it seem that “defense” is a consumer good, like Hummel Figurines or orange marmalade. The government just goes down to the defense store and buys as much as it wants. He doesn’t talk about how those decisions get made at the social level, and doesn’t talk about who gets the benefits of those guns and who pays the costs of the foregone butter, or whether there are better ways to keep aggressors away than bombing their countries. He turns the example into a concrete fact, with no context. The choices made in the US and other countries about how much “defense” to “buy” would make a really interesting case study in macroeconomic behavior, and just defining terms would be really helpful to public discourse. That’s certainly not the point of the Mankiw textbook.

One of the goals of neoliberalism, Mirowski’s Number 5, is to change the idea of democracy from one of participation by citizens in determination of social policy to one of consuming state services, like defense. Guns v. butter shows how that notion gets into people’s heads. Given the level of corruption in the system, in the broad sense of Zephyr Teachout in her excellent book, *Corruption in America*, it’s also an example of crony capitalism, part of Number 8. There’s a lot more to unpack in the guns and butter example, but let’s move on.

The environmental example is fascinating. From the very beginning of this country, companies polluted lakes, rivers and the air, to keep costs low and prices down. No one did anything. Then when citizens started complaining about their ability to breathe the air and drink the water, and the rich people and their corporations act all outraged, like they have a right to pollute. Mankiw ignores this history, and ignores the obvious fact that dumping pollutants everywhere hurts everyone in general, and some people dramatically; and profits only a few. Again, the entire issue of pollution and environmental destruction would make fascinating case studies in economics. Mankiw’s discussion supports Mirowski number 10: Thou Shalt Not

Blame Monopolies and Corporations.

Finally, there is the trade-off between equality and efficiency. Mankiw's explanation about the negative effects of a progressive income tax on economic efficiency is flatly wrong. For my explanation, see [this](#) and [this](#) and [this](#). For a short view, does Mankiw think the economy in the 50s was less efficient strictly because of high income and estate taxes on the rich? I'd love to see a paper showing how that happened. Piketty and Saez suggest a top tax rate of 80%. Here's a short article explaining their thinking, and here's an impenetrable paper that lies below it.

I assume Mankiw was referencing Arthur Okun's 1975 book *Equality and Efficiency: The Big Trade-Off*. Okun postulated that there was a trade-off between equality and economic efficiency from his armchair, and he discusses the implications for policy in this excellent piece. By 1995, it was clear that the facts did not support his speculation. This paper is a review of literature and discussion of exactly how wrong Okun was: Lars Osburg, *The Equity/Efficiency Trade-off in Retrospect*. Subsequent work has made this even more clear. Mankiw ignores all the evidence and new theory to the contrary, choosing to continue to support an unmeasured armchair theory Mirowski number 9: Thou Shalt know that Inequality is Natural.

The point of this discussion is that textbooks have an outsized influence on people, particularly on non-specialists. They may not recall the argument, but they will recall the examples and the general approach, especially when those are common in discourse, and not contravened by other authorities. I know this from my own college education. It has taken years for me to shed the parts that don't conform to the reality of life as I have lived it and seen it.