

Alternative Microeconomics

Four Chapter Individual and Community

I INDIVIDUALS AND COMMUNITY

A community is a group of individuals with a set of shared values and objectives.

Social institutions are the result of human behavior.

Social Institutions also influence human behavior.

Institutions, such as markets can be misused.

The interests of all individuals and groups are not the same and may be in conflict..

A community is made up of a group of individuals. One of the characteristics of a community is that there is an intersection of a set of shared values and objectives held by the individuals. Social institutions (embedded patterns of behavior within a society) represent these shared values. Only under rare circumstances would a group of individuals have the same set of shared objectives. Because they are individuals, it is probable that some of their objectives will be different and conflict or compete. It is necessary for the community to have a set of social institutions to coordinate competing values and ends.

Social institutions both arise from human behavior and influence their behavior. Traditions, mores, customs and more formal institutions (such as laws), define the range of choices. Markets are also a social institution. A voluntary contract between two individuals is a social mechanism to coordinate activities. Markets require a social infrastructure. Trust, expectations about buyers and sellers providing information (no fraud, deceit or duress), obligation to fulfill contracts and expectations that individuals will do no harm to others, facilitates the operation of markets. Adam Smith (1723-1790) points out that markets are subject to abuse:

People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices. It is impossible indeed to prevent such meetings, by any law which either could be executed, or would be consistent with liberty and justice. But though the law cannot hinder people of the same trade from sometimes assembling together, it ought to do nothing to facilitate such assemblies, much less to render them necessary. (Smith WN, p 128)

Participants in markets may also use formal institutions (law, regulations) to benefit themselves:

The interest of the dealers, however, in any particular branch of trade or manufactures, is always in some respects different from, and even opposite to, that of the public. To widen the market and to narrow the competition, is always the interest of the dealers. To widen the market may frequently be agreeable enough to the interest of the public; but to narrow the competition must always be against it, and can serve only to enable the dealers, by raising their profits above what they naturally would be, to levy, for their own benefit, an absurd tax upon the rest of their fellow-citizens.

The proposal of any new law or regulation of commerce which comes from this order ought always to be listened to with great precaution, and ought never to be adopted till after having been long and carefully examined, not only with the most scrupulous, but with the most suspicious attention. It comes from an order of men whose interest is never exactly the same with that of the public, who have generally an interest to deceive and even to oppress the public, and who accordingly have, upon many occasions, both deceived and oppressed it. (Smith WN, p 250)

II INSTITUTIONS

Douglass North argues that

Institutions are the rules of the game. They structure human behavior (an "exchange" or interrelationships.

Institutions are the rules of the game in a society or, more formally, are the humanly devised constraints that shape human interaction. In consequence they structure incentives in human exchange, whether political, social, or economic. Institutional change shapes the way societies evolve through time and hence is the key to understanding historical change. (North, 1990, p 3)

North expands "human exchange" to include human interactions that include "political, social or economic" phenomenon. Human exchange is interpreted as "human interaction on social, political and economic levels." North's broader definition will be used in this chapter even though the term "exchange" is quite specific:

In North's quote, exchange refers to human interaction. Exchange may be more narrowly used to describe a contractual relationship based on quid pro quo.

Exchange involves a quid pro quo, i.e. an exchange of private property rights between individual agents. The terms of the exchange are clearly specified: "I will give you this if you will give me that." The goods to be exchanged are clearly specified, as are the terms of the exchange. (Chapter 2, p 15)

North identifies the roles of these institutions;

Institutions;
 1) Reduce uncertainty
 2) Are constraints
 3) May be formal or informal
 4) Are both positive and negative
 5) Are different from organizations

- *"Institutions reduce uncertainty by providing structure to everyday life." (North, p 3)*
- *"Institutions include any form of constraint that human beings devise to shape human interaction. Are institutions formal or informal? They can be either, and I am interested both in formal constraints – such as rules that humans beings devise – and informal constraints – such as conventions and codes of behavior." (North, p 4)*
- *"Institutional constraints include both what individuals are prohibited from doing and, sometimes, under what conditions some individuals are permitted to undertake certain activities." (North p 4)*
- *"A crucial distinction in this study is made between institutions and organizations. Like institutions, organizations provide a structure to human interaction. (North, pp 4-5; North points out that organizations are considered as one of the players or actors while institutions are the underlying rules of the game.)*

Institutions are created by humans and evolve over time

"Institutions are a creation of human beings. They evolve and are altered by human beings; . . . Integrating individual choices with the constraints institutions impose on choice sets is a major step toward unifying social science research." (North, p 5)

North refers to some institutions as "conventions and codes of conduct." Traditions, customs, mores, rules of thumb are other examples of implicit

Institutions act as short cuts to solving problems.

institutions that are part of the rules of the game. These habitual patterns of behavior or embedded rules may arise spontaneously. Individuals seek solutions to problems. When they find something that works (or provides a reasonable solution), they learn to try the same approach when the same or new problems arise. These institutions become short cuts to analyzing and devising new solutions for every new problem.

Implicit institutions are communicated through tradition, custom, religion and the like.

These implicit institutions may be transmitted to others in a variety of ways. Custom and traditions are the most obvious. It is possible to create codes of conduct that may be communicated through religious beliefs. Religious law and jurisprudence are common to almost all societies. In societies that depend on interpersonal relationships, these implicit institutions may be dominant in influencing behavior patterns.

Where implicit institutions are weakened, explicit institutions may emerge.

In cases where the community becomes complex, the effects of social values on individual choices may be weakened. If implicit social institutions are weakened, force of law (formal explicit institutions) may be used to encourage some behavioral patterns and discourage others. Adam Smith had a manuscript on jurisprudence destroyed at the time of his death (1790). Copies of students' notes on Smith's lectures on jurisprudence (1762-63, 1766) were found and published as *Lectures on Jurisprudence (LJ)*. In these notes, Smith describes the role of law within a society.

There are two major approaches to jurisprudence; Common law and the Napoleonic code.

The two traditions of common law and the Napoleonic code provide the framework for the legal systems in most Western industrial countries. Common law is based on *stare decisis*; i.e. laws emerge over time on the basis of precedence. As society, technology, relationships, environment and other features of society change, laws are modified. The Napoleonic code (dates from 1804) is based on Roman Law. It establishes a clear legal framework on issues of property, inheritance, the family and individual freedom. Both approaches provide formal rules of the game and may be considered as an explicit, formal institution.

The relationship between the legal and economic system is well established. John R. Commons (*Legal Foundations of Capitalism*, 1924) and Richard Posner (*The Economic Analysis of the Law*, 1973, sixth edition 2003) are foundations for two traditional approaches to law and economics.

Institutions and Costs

Transaction costs are the costs involved with the transfer (exchange) of ownership.

The provisioning process and the allocation process both involve the ownership of resources and goods as well as the mechanisms by which the rights of ownership are transferred. Within a society, the transfer of ownership of goods is not without costs. In the case of eminent domain, there are costs (opportunity costs) to the authority that defines and enforces the transfer of ownership of goods (property rights). Individuals who are affected by eminent domain incur costs as well. There are also costs of using exchange. These costs are the effort (sacrifice) of individuals to obtain information about goods, other individuals who are willing to enter a contract and the effort to negotiate the contract or terms of exchange.

Social institutions and organizations emerge to reduce transaction costs.

Social institutions and organizations are a social response to reduce the costs of exchange and eminent domain. Social institutions also facilitate and enforce reciprocity. The costs of using exchange are referred to as "transaction costs." (see Coase, "Nature of the Firm". 1937)

The institutions define the rules of the game; provide individuals with

information and some degree of certainty in their social interactions. This reduces the time and effort (transaction costs) that individuals devote to the allocation problem.

Institutions and organizations are human creations that are intended to solve problems. It should be noted that these human creations might be intentional and explicit or unintentional and implicit. As in all human endeavors, some attempts are more successful than others; i.e. some institutions are more successful at achieving objectives than others.

While social institutions evolve as short cuts to problem solving, the vested interests may try to prevent changes in institutions

Institutions arise as solutions to a given set of problems. Should the elements of the problem change (the actors, agents, technology, information, other institutions), the institutions may need to adapt. However, any set of institutions is correlated with the interests of particular individuals. Some of these individuals benefit from the particular structure while others are not. Those who benefit from a particular institutional structure have a vested interest in preventing changes in the institutions. These vested interests may use their positions and power to prevent institutional change and to work to alter institutions (particularly explicit institutions such as law) in their interests. Consequently, the institutions that are prevalent at any point in time may lag behind environmental, technological and social changes.

Patents, copyrights, regulations of communication industries (radio, television, newspapers, internet and the like) determine the behavior of the agents and firms in those industries. George Stigler (1911-1991) described a "capture theory of regulation." (Stigler, 1971, Published first in 1962 with Claire Friedland) He argues that when an industry is regulated, it is in the interests of that industry to capture the regulatory agency and influence its policies. The communication industries have a greater incentive to influence the policies of the Federal Communications Commission (FCC) than the average person. Recent actions by the FCC have allowed greater concentration of news media. Companies that publish music have more interest in the laws regarding the ownership (copyrights) and royalties to music than the public; the "Napster" incident on downloading music files from the Internet is an example.

The insurance, pharmaceutical, hospital and medical industries have more interest in the social institutions that influence the delivery of health care than individuals. Health insurance emerged in the mid 1930's as a solution to the problems of random, catastrophic health care costs and how hospitals and doctors would receive financial payment. The insurance and health care providers (doctors, pharmaceutical, hospitals and insurance industries and firms) have a vested interest in maintaining the system that maintains their sources of revenue.

The vested interests have an incentive to shape the formal and informal institutions that relate to their activities.

Morality, Justice and a Stable Society

Institutions also exist to promote social values of justice, morality, peace, etc.

Institutions reduce the costs of the allocation process. Additionally, justice, an orderly society, tranquility, security, peace are objectives that are commonly held in many societies. Adam Smith (1723-1790) is used to express these ideas here since he is generally regarded as one of the first writers to advocate a system based on morality, markets and law. He wrote

the *Theory of Moral Sentiments* in 1759 to describe his view of the role of sympathy and empathy in human behavior. He argues that justice is essential for an orderly society. On the first page of *Theory of Moral Sentiments*, Smith writes;

*How selfish man may be supposed, there are evidently some principles in his nature, which interest him in the fortune of others, and render their happiness necessary to him, though he derives nothing from it, except the pleasure of seeing it. Of this kind is pity or compassion, the emotion which we feel for the misery of others, when we see it, or are made to conceive it in a very lively manner. That we often derive sorrow from the sorrow of others, is a matter of fact too obvious to require any instances to prove it; for this sentiment, like all the other original passions of human nature, is by no means confined to the virtuous and humane, though they perhaps may feel it with the most exquisite sensibility. The greatest ruffian, the most hardened violator of the laws of society is not altogether without it. (Smith, *TMS*, p 47)*

Smith continues on the role of society in the formation of individual values;

Society provides the context for human values and morality.

*Were it possible that a human creature could grow up to manhood (sic) in some solitary place, without communication with his (sic) own species, he could no more think of his own character, of the propriety or demerit of his own sentiments and conduct, of the beauty or deformity of his (sic) own mind, than of the beauty or deformity of his (sic) own face. All these are objects which he cannot easily see, which naturally he does not look at, and with regard to which he is provided with no mirror which can present them to his view. Bring him into society, and he is immediately provided with the mirror which he wanted before. It is placed in the countenance and behavior of those he lives with, which always mark when they entered into, and when they disapprove of his sentiments; and it is here that he first views the propriety and impropriety of his own passions, the beauty and deformity of his own mind. (Smith, *TMS*, p 204)*

Smith continues;

Individuals need the assistance of others. If morality and beneficence does not provide the assistance that is needed, mercenary self interest (exchange) may be used.

It is thus that man, who can subsist only in society, was fitted by nature to that situation for which he was made. All the members of human society stand in need of each other's assistance, and are likewise exposed to mutual injuries, Where the necessary assistance is reciprocally afforded from love, from gratitude, from friendship, and esteem, the society flourishes and is happy. All the different members of it are bound together by the agreeable bands of love and affection, and are, as it were, drawn to one common centre of mutual good offices.

But though the necessary assistance should not be afforded from such generous and disinterested motives, though among the different members of society there should be no mutual love and affection, the society, though less happy and agreeable, will not necessarily be dissolved. Society may subsist among different men, as among different merchants, from a sense of its utility, without any mutual love or affection; and though no man in it should owe any obligation, or be bound in gratitude to any other, it may still be

upheld by a mercenary exchange of good offices according to an agreed valuation.

Society, however, cannot subsist among those who are at all times ready to hurt and injure one another. (Smith TMS, p 166)

Justice is a necessary element of any society

. . . Society may subsist, though not in the most comfortable state, without beneficence; but the prevalence of injustice must utterly destroy it. . . . Justice, on the contrary, is the main pillar that upholds the whole edifice. If it is removed, the great, the immense fabric of human society, that fabric, if I may say so, to have been the peculiar and darling care of nature, must in a moment crumble into atoms. (Smith TMS, p 167)

As society cannot subsist unless the laws of justice are tolerably observed, as no social intercourse can take place among men (sic) who do not generally abstain from injuring one another; the consideration of this necessity, it has been thought, was the ground upon which we approved the enforcement of the laws of justice, by

Smith recognizes that beneficence and morality cannot be the only mechanism that creates order in society. He argues that;

Morality may be corrupted by the tendency of humans to admire wealth rather than wisdom.

This disposition to admire, almost to worship, the rich and the powerful, and to despise, or, at least, to neglect persons of poor and mean condition, though necessary both to establish and maintain the distinction of ranks and the order of society, is, at the same time, the great and most universal cause of the corruption of our moral sentiments. That wealth and greatness are often regarded with the respect and admiration which are due only to wisdom and virtue; and that the contempt, of which vice and folly are the only proper objects, is often mostly unjustly bestowed upon poverty and weakness, has been the complaint of moralists of all ages. (Smith TMS, p 126)

Smith is not the only writer to argue the importance of justice and morality in the proper functioning of society. Plato, Aristotle, St Thomas, and a host of writers argue the role of justice. At the same time, most recognize that beneficence and cannot be the only motivating force in society.

The need for morality is based on biology and ecology; Joan Robinson argues:

Common feelings in a society are expressed in ideology.

A society cannot exist unless its members have common feelings about what is the proper way of conducting its affairs, and these common feelings are expressed in ideology. (Robinson, p 3)

Both self interest (ego) and compassion for others.

The biological necessity for morality arises because, for the species to survive, any animal must have, on the one hand some egoism—a strong urge to get food for himself (sic) and to defend his means of livelihood; also—extending egoism from the individual to the family—to fight for the interests of his mate and young. On the other hand, social life is impossible unless the pursuit of self-interest is mitigated by respect and compassion for others. A society of unmitigated egoists would knock itself to pieces; a perfectly altruistic individual would soon starve. There is a conflict between contrary tendencies, each of which is necessary to existence, and there must be a set of rules to reconcile them. Moreover, there

Justice and concern for others is crucial for civil society.

must be some mechanism to make an individual keep the rules when they conflict with his immediate advantage. (Robinson, p 4) . .

Since the egotistic impulses are stronger than the altruistic, the claims of other have to be imposed upon us. The mechanism by which they are imposed is the moral sense or conscience of the individual. (Robinson, p 5) . . .

But observe, it is the honesty of other people that is necessary for my comfort. (Robinson, p 6)

Justice and concern for others is an important objective that is often reflected in the golden rule: "Do unto others as you would have them do unto you." Or to quote Ivan Hill,

Men of many ages have considered the Golden Rule to be the fundamental moral imperative. Confucius once was asked, 'Is there one word which may serve as a rule of practice for all of one's life?' He answered, 'Is not reciprocity such a word? What you do not want done to yourself, do not do to others.'" (Hill, p 4)

A just and moral society where humans can live in a peaceful environment is an objective held by many philosophers through the ages. Perhaps for some, the history of conflict and war casts doubt on a human objective of justice. Alternatively, perhaps conflicts and wars occur because of feelings or injustice.

Creativity, family, relationships and respect are important objectives for individuals.

Tradition, customs, mores, and other social institutions are mechanisms through which individuals acquire common values. The size of one's family, forms of marriage, responsibility for children or parents, expectations about disposal of wastes, use of resources, obligations to care for less fortunate people, trust, theft, voting, creativity, duty to family (country, etc) attitudes about stewardship, are examples of values that may be generally held by the members of a community. These values influence the choices that individuals make.

III AGENTS

An agent has the authority to select and act on alternatives to achieve ends.

A decision also implies the existence of an agent. An agent is an individual who has the authority to evaluate, select, and act on alternatives to achieve an end. The agent may act for themselves or on the behalf of a principal. Agents choices may be based on intuition, habits (rules of thumb, institutions), explicit rules or reason.

Competing ends can be coordinated by exchange, reciprocity, eminent domain, and philanthropy

Any decision implies that there is an end, objective, or goal that an agent wishes to achieve. Humans seek means to achieve ends. As suggested above, decisions based on reason must have an objective. Intuition as a method for making decisions also implies that a result is desired. Rules and habits (or social institutions) arise because there is some desired end to be accomplished. The question is what is the origin and nature of the objectives.

Both the ends and means may be influenced or constrained by resource endowment, technology, or social institutions (such as customs, traditions, markets and law).

In the case of an agent or agents representing a principal, there may be a conflict or incompatibility among their objectives. This is referred to as the

The principal/agent problem is the result of conflicting goals and lack of information.

principal/agent problem. The agent has a conflict of interest. A stockbroker acts as an agent for an investor; a doctor may act as the agent for a patient. The lawyer acts as an agent for her client, the principal. The goal or end of the investor may be to maximize earnings on their assets. The end or objective of the stockbroker may be to maximize their commission. In the short run, the broker may sacrifice the earnings of the investor to maximize commissions. Hopefully, in the long run the broker will recognize that the short term strategy will result in the loss of the investor as a client. The principal must have some knowledge and information regarding the agent's behavior. In a complex world, this does not always happen. Enron is an example of the principal/agent problem. The interests (ends) of the CEO and management (the agents) were inconsistent and had priority over the goals of the stockholders (principals).

A code of ethics helps to ameliorate the principal/agent problem in some cases.

In a complex world where it is difficult for principals to have information to evaluate all the action of the agents, a code of conduct or code of ethics may be important as a means to get the agent to act for the principal. The Hippocratic oath is a social institution to insure the physician acts in the principals interests. Accountants and lawyers are other examples of professions that rely heavily on codes of ethics to resolve conflicts between the principal and agent.

Organizations and Agents

Organizations are human creations that are different from social institutions.

Organizations are another way that the cost of economic activities. North distinguishes between institutions and organizations. Both provide structure to human interactions. Ronald Coase (1910-) sees both as mechanisms to reduce the costs of transferring ownership. (Coase, 1937)

The crucial difference is that institutions are part of the rules of the game and organizations are participants in the game. The firm (or any organization) arises because there are costs to using the "pricing mechanism."

Coase's idea of transaction cost is crucial to explaining the existence of firms and organizations.

What the prices are have to be discovered. There are negotiations to be undertaken, contracts to be drawn up, inspections to be made, arrangements to settle disputes, and so on. These costs have come to be known as transaction costs. Their existence implies that methods of co-ordination alternative to the market, which are themselves costly and in various ways imperfect, may nonetheless be preferable to relying on the pricing mechanism (market? Author's question), the only method of co-ordination normally analyzed by economists. It was the avoidance of the costs of carrying transactions out through the market that could explain the existence of the firm, in which the allocation of factors came about as the result of administrative decisions.

In the "Nature of the Firm" I argued that in a competitive system there would be an optimum of planning since a firm, that little planned society, could only continue to exist if it performed its co-ordination function at a lower cost than would be incurred if co-ordination were achieved by means of market transactions and at a lower cost than this same function could be performed by another firm. . . .

I argued in "The Nature of the Firm" that the existence of transaction cost leads to the emergence of the firm. (Coase 1995,

p 8-9)

A firm is a small planned society that uses administrative decisions rather than exchange (or reciprocity).

The firm (or any organization) comes into existence to create a small “planned society” and to use administrative decisions to allocate resources because it would be more costly to use market exchange. Firms (or organizations) may be for profit, not-for-profit, cooperatives, sole proprietorships, partnerships or corporations. There are many ways of categorizing organizations.

Within a firm the CEO, Board of Directors, shareholders, Vice-President of Marketing, Vice-President of Production and the assembly line workers may have competing objectives that will be resolved by authority, contract, or some other social institution. There are managerial techniques that might be used to coordinate the activities of the diverse groups in a firm.

In a family, the parents may have different ends than the children. There are parental “instincts,” love and social expectations as well as laws that insure the parents act in the child’s interests.

The principal/agent problem is a major problem within a firm or organization.

Within an organization, the principal/agent problem becomes important. Usually a manager (CEO) makes administrative decisions that affect many other groups. Their administrative decisions may be guided by general policies and guidelines established by a Board of Directors who in turn is constrained by the shareholders (or owners). The objectives of the shareholders may or may not be reflected by the decisions of the manager. The manager may have a different set of objective and the shareholders may or may not have information (or control) over the decisions of the manager. Kenneth Lay and the management of Enron is an example of the principal/agent problem.

IV OBJECTIVES

The alternative chosen to achieve and end is called the means

An objective, goal or end is something that an individual or group of individuals hopes to achieve. There may be many alternatives that will potentially achieve the end or goal. Some alternatives have a higher probability of success. The alternative that is selected, through reason, rules, habits or intuition, is the means.

Both the means and the ends may be influenced by the individual’s environment

It is not always clear how humans create their objectives or ends. One hypothesis is that they are capable of thought and can imagine alternative states or conditions. If the alternative state is perceived as preferable to the existing state, the alternative state becomes an end. This process necessarily requires a subjective valuation or ranking of alternative states or conditions. I am hungry. I can perceive or imagine myself not being hungry. Not being hungry is preferable to being hungry so the objective or end is to reach the preferred state. The mind is capable of recognizing an incongruity between what is and what I imagine can be. I may seek the means to satisfy my hunger through reason. Intuition, rules or habitual patterns of behavior may also suggest means of satisfying my hunger.

Social forces may influence individuals objectives.

Many substances will satisfy hunger. Geographic differences and resource endowment may alter what people choose to eat. Inuit people eat whale and sea lion. In the southwestern United States pinto beans, corn and chili peppers are favorites. In France, escargot is a delicacy. Individuals often develop a “taste” or preference for a food they ate as a child. As a result, we often think of foods as representing different social or ethnic groups. Italian, Chinese, Mexican, Indian are examples of ethnic foods that

represent different social groups from different locations.

The means and ends can become confused.

Hunger is a physiological stimulus so it is easy to recognize the incongruity between being hungry and not being hungry. Other events are more complex. I have shelter that is adequate (a 700 square foot shelter that has plumbing and heat) but can imagine a larger house (3000 square foot with a den and multiple bathrooms) that I would prefer. If the 700 square foot house is adequate, why is the larger house preferred? Is it because I perceive that my neighbors (the community) associate the bigger house with status? Do the values of the community influence my preferences? If my objective or end was to acquire status, the large house was the means to achieve that end. If my objective was to have enough room for a large family, the large house may be the means to achieve that end. To the casual observer the acquisition of a large house may incorrectly be seen as the desired end.

Economics is a study that is based on scarcity of the means to achieve objectives. As a result, choices must be made on the relative values that are placed on the competing objectives. To repeat from above, Warren Samuels argues that the *"economy is a process of valuation... That to behave and to choose is to engage in valuation and thereby to participate in the social, or socioeconomic, valuation process."* [Samuels p ix] He goes on to point out that, *"the economy encompasses more than the market..."* and *"that other nonmarket valuational processes exist."* These valuational processes are used to choose among competing ends, or objectives.

ECONOMIC OBJECTIVES

There may be tradeoffs between quantifiable and non-quantifiable objectives.

Justice, respect from others and creativity are not easily measured. Income, quantities of goods and prices are more easily measured. There are many complexities in measuring incomes, quantities of goods and prices. In spite of measurement problems, individuals tend to focus on phenomena that can be ranked or associated with a magnitude (or number). This is particularly a problem when quantifiable objectives are to be traded off for non-quantifiable objectives. Examples include an individual who sacrifices a larger salary for a job with more activities that are creative or to remain near a personal relationship. The appreciation of environment or wildlife may be sacrificed for jobs or timber production.

There are also tradeoffs between personal objective and economic objectives.

Economic objectives are complex linkages. Utilitarianism is the philosophical foundation of modern economics. The perceived objective is to maximize the utility or welfare of the members of society. In a simplistic world, the welfare or utility of the community is the sum of the utilities of each member of that society. Therefore, if each individual maximizes their utility it will maximize the utility of the group. The maximization of each individual's utility is consistent with the maximization of the utility of society. This view requires a social mechanism or institution to coordinate or constrain the behavior of individuals. The constraints may be social institutions such as moral rules, mores, customs, laws, or the market.

In a simplistic world the maximization of individual utility is consistent with the maximization of social utility.

Social institutions constrain and guide individual behavior.

Since it is not possible to measure utility, welfare or happiness, utility is connected to variables that can be measured. In orthodox economics, a person's utility is a function of (or determined by) the quantity of goods and services they consume. Since utility can't be measured and is a function of the quantity of goods, an increase in the quantity of goods consumed is assumed to increase utility or welfare: *more goods are preferred to fewer*

Since utility can't be measured, the quantity of goods serves as a proxy for utility.

goods. As a result, economic growth, producing more goods (as measured by gross domestic product) becomes a perceived objective.

The desire to measure may result in the use of misleading information.

The inability to measure utility also leads to the use of price as a proxy. The price of a good is perceived as an indicator of its value. Relative prices are seen as information that can be used to rank the worth or value of goods.

The inability to measure utility directly leads to a focus on quantities of goods and their relative prices as a substitute. This process often leads to ignoring or minimizing the importance of non-market objectives. If prices are distorted by lack of information or imperfections in the social institutions, the rankings based on relative prices may be misleading.

In the modern world our objectives and behavior may be altered by advertising. Fashion and fads popularized in the media also shape our objective and the means we choose to achieve them.