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The Journal of  
**Socio-  
Economics**

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Journal of Socio-Economics 31 (2002) 45–57

## The individual in economic analysis: toward psychology of economic behavior

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### Abstract

“... Economics is supposed to be concerned with real people. It is hard to believe that real people could be completely unaffected by the reach of the self-examination induced by the Socratic question, ‘How should one live?’—a question that is, also a central motivating one for ethics. Can people whom economics studies really be so unaffected by this resilient question and stick exclusively to the rudimentary hard-headedness attributed to them by modern economics?” Amartya Sen, *On Ethics & Economics*.

“... Apart from a few exceptions, the international consensus view within sociology, anthropology, political science and psychology seems to be that agents are not irrational in the way that neoclassical economists presume. The orthodox economic canons of rationality are thus widely rejected elsewhere,” Geoffrey M. Hodgson, *Economics and Institutions*.

“Once we realize that the human mind is everywhere active and imaginative, then we need to understand the routes of this activity if we are to grasp how the human mind works. This is true whether the mind is trying to come to grips with painful reality, reacting to trauma, coping with the everyday or just making things up. Freud called this imaginative activity phantasy, and he argued both that it functions unconsciously and that it plays a powerful role in the organization of a person’s experience. This surely, contains the seeds of a profound insight into the human condition; it is the central insight of psychoanalysis . . . a pervasive aspect of mental life . . . Are we to see humans as having depth—as complex psychological organisms who generate layers of meaning which lie beneath the surface of their own understanding? Or are we to take ourselves as transparent to ourselves?” Jonathan Lear, *Open Minded: Working Out the Logic of the Soul*. © 2002 Published by Elsevier Science Inc.

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## 1. Introduction

This paper is about the psychology of economic choice and decision making. My goal is to point the way toward an understanding of economic behavior unfettered by the positivism of orthodox economics which holds that, “the only relevant evidence is that provided by external observation” (Loasby, p. 16). My focus is on significant insights into economic behavior to be gleaned from psychological theory, particularly the role of emotions and the unconscious in human behavior as it is portrayed in psychoanalytic theory but ignored in orthodox economic analysis.

The perspective in this paper complements criticism of conventional models of economic behavior. For example, Herbert Simon writes, “. . . the dream of thinking out everything before we act, of making certain we have all the facts and know all the consequences, is a sick Hamlet’s dream. It is the dream of someone with no appreciation of the seamless web of causation, the limits of human thinking, or the scarcity of human attention” (quoted by Loasby, pp. 140–141). Loasby cites Simon as concluding that neoclassical economists in his view too often make their problems soluble by making the solutions useless (Loasby, p. 143). Oliver E. Williamson describes transaction cost economics as becoming, “. . . more self-conscious about its behavioral assumptions” (Williamson, 1986, p. 174). Oliver North wrote recently, “individual utility functions are simply more complicated than the simple assumptions so far incorporated in neo-classical theory” (North, 1990, p. 20).

My interest is in line with a tradition of dissent going back roughly to the German historical school in Europe of the late 19th century and the American institutionalists (starting with Thorstein Veblen and John R. Commons) in our country in the first half of the century. In part, it is a product of my long-standing exploration in the psychology and philosophy of economic behavior.

The importance of exploring the pervasive role of emotion in human behavior has been voiced in other social sciences. Anthropologist Robert I. Levy, notes, “. . . interest in emotion is coming back in anthropology, particularly in the work of some younger anthropologists” (Levy, 1985, p. 215). A pioneer in psychiatry, Harry Stack Sullivan commented at mid century, that “. . . economics has developed with singularly little interest in the persons who manifest economic behavior . . .” (Sullivan, 1940). Social theorist Anthony Giddens assigns a primary role to the unconscious in human behavior (Giddens, 1984). And of course this is a primary focus of psychoanalytic theory.

Resting on its utility driven model of economic behavior, the thrust of orthodox economics, with some significant exceptions, that I shall describe shortly, has largely been a denial of the complexity of human and economic behavior. It confines itself to the effects of, not the direct roots, of economic behavior. Marshall in his seminal work, *Economic Principles*, wrote “it is essential to note that the economist does not claim to measure any affection of the mind in itself, or directly; but only indirectly through its effects” (Marshall, 1920, p. 15). He accepts the simplistic assumption that economic behavior is solely maximizing behavior. Amartya Sen characterizes orthodox behavioral model as narrow and inadequate. He refers to “. . . the indigent nature of the basic utilitarian view of the person” and asserts that “the real issue is whether there is a plurality of motivations, or whether self interest alone drives human beings” (Sen, 1987, p. 19).

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