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The Economist's Fallacy

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The definition of cost in the economic literature is highly standardized: the cost of X is defined as the value of the most valuable alternative that had to be forsaken in order to obtain X.[1] Let us suppose that to get X you had to abandon the alternatives Y, Z, and W. To decide which of these is the most valuable, you must of course calculate the benefits they each involve, and presumably these must be *net* benefits—you would hardly want to say that the value of alternative Z was a million dollars if it costs $999,000 to get it. To calculate net benefits, you must be able to calculate not only the actual benefits but the actual costs involved in getting them. In other words, this definition of costs essentially involves understanding the concept of cost, so the definition is circular, a fatal logical flaw.[2]

The second problem is even more fundamental. This definition of *cost* equates cost with (the maximum) *opportunity cost*; but the two concepts are not identical, although related. The key difference is that some costs are not opportunity costs at all. To understand this, it is helpful to consider a commonsensical case where the difference is more obvious than in the typical case economists consider in their professional role. In the practical problem of when to recommend surgery for an elderly patient with prostate cancer, one has to weigh the life expectancy with and without the operation, and the quality of life during those periods, plus the direct costs of the operation, which include not only the money cost but the pre-operative anxiety and the post-operative pain, and of course the pain involved as the cancer develops if it is not removed.

Now, what do we mean by saying that one of the costs of the operation is the pain it involves? The commonsensical answer is that we all know what a pain is, slight or severe, just as we know what a pleasure is—by direct experience. That is, some costs (and some benefits) are a simple matter of direct experience, like colors or affection. But the economist's definition of cost in this case would lead to the view that the cost of pain is the value of the most valuable alternative to it that was forsaken; which in this case is the state of absence of pain. That is, pain cost = value of being free of pain. Now, what is the difference between the cost of slight pain and the cost of extremely severe pain? The left hand side of the equality is obviously very different, but the right hand side is the same, because you don't forsake a different alternative in the two cases. So the cost of slight pain is the same, on this definition, as the cost of severe pain, which is clearly absurd. The economist's definition of cost is totally insensitive to major differences in true cost.

We need to remind ourselves here of the commonsensical notion of cost, according to which costs are simply the bad (i.e., disvalued)

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[1] For example, see Levin, H. & McEwan, J. (2001). *Cost-effectiveness analysis* (2nd ed., pp. 43-45). Thousand Oaks, CA: Sage. (Levin is an economist by training.).

[2] For more details on this point, see my essay "Costs in evaluation: Concept and practice" in Alkin & Solomon (Eds.). (1983). *Evaluation costs: Concept and theory*. Thousand Oaks, CA: Sage.

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things that go along with acquiring or changing things or having things happen to you. They are the negative accompaniments of changes in the situation or condition of the agent, just as benefits are the good (i.e., valued) accompaniments. And 'opportunity costs' are the other changes that could have occurred or been achieved with about the same bad concomitants. The two are thus essentially distinct—one being a set of disvalues, the other being a set of choices or changes.

Now definitions are claims about the *identity* of two things. But costs and opportunity costs are two completely different kinds of things. There is only a *metaphorical* sense in which opportunity costs are a kind of cost—because they are foregone options (in some cases), there is a metaphorical sense in which they are like money spent and some other costs that involve giving up things you previously had, like leisure time. But the sense in which you *have* options is not the same as the sense in which you *have* money or a pain-free life; so the sense in which you *lose* options is not the same as the sense in which you *lose* a pain-free life. Is *experience* pain. It's true that we sometimes talk of costs as the sacrifices we make in order to get something we want, and sacrifices include lost options. But those costs, all those other options we forego, are extremely unlike pain and some other directly experienced costs, so they cannot possibly be treated as the true meaning of costs.

Opportunity costs are an entirely different breed of cat from literal costs. Economists realize this when they take care not to add opportunity costs to other costs in order to get total costs; they forget it when they define one in terms of the other. Of course, the truth also emerges when one reflects that in truth *all* the opportunity costs are foregone when something is selected, hence—if opportunity costs were even additive in their own domain—the opportunity costs of any decision is always infinite. This oddity is avoided by defining cost as *the* most valuable of the missed opportunities; but that move runs into the circularity problem already identified. Perhaps the best way of thinking about opportunity costs is as set of perspectives on the true cost of something, as ways of seeing what that cost really means to you. As such, they are often very important in appraising true value or worth; but, like alternative perspectives on the benefits of an evaluand, they are not one of the costs or benefits.

It may be that the cause of this confusion is partly the difference between *things we choose, or plan to do*, and their costs; and *things that happen to us, us, or are done to us* and their costs to us. Things that happen to us, like tsunamis or surgical operations, are likely to have directly experienced costs such as the loss of our homes or family, and pain, which are not lost options but simply bad outcomes or tolls taken on us. Things that we consider or might consider doing, the sort of thing that economists are called in to cost, do have opportunity costs, and make it seem plausible to define all costs as opportunity costs. But they are only half of the world of costs, and that definition is absurd in the other half of experience.

Could one not argue that the economist is simply defining a construct that is useful in the science of economics, not the one in everyday language? Sure, as long as the economist explicitly abandons any claim to be analyzing the real costs that we have to consider in making decisions that affect real people. But economists don't want to do that; they want to eat their cake and have it too. That's intellectually greedy, and it's misleading advertising that seriously misleads those hoping for advice with real-world problems; especially since the economist has a perfectly good term already for dealing with what they are analyzing, namely 'opportunity costs.'

Evaluators should not follow the economists here, or they will end up in a swamp of misleading conclusions about program costs, e.g., by underweighting the directly experienced costs of loss of habitat to native people of the forests, tundra, or plains. No technician's

definition can magically equate those losses to the money they may (or may not) have agreed to accept in exchange. You may sell your soul for money, but that does not make a soul the same kind of thing as money, except (perhaps) to an economist.