

# The Impact of Cultural Economics on Economic Theory\*

MICHAEL HUTTER

*Department of Economics, Witten/Herdecke University, Alfred-Herrhausen-Str. 50, 58448 Witten, Germany*

**Abstract.** The paper asks what kind of impact cultural economics has had on the development of economic theory. Six research areas are discussed: productivity differentials between artistic and non-artistic labor, variations of the public good concept, particularly in relation to environmental goods, endogenous changes in preferences, long-term rates of return on paintings, impact of new media technologies and the autonomy of artistic valuation.

It is shown that these topics have relevance beyond their applications in the cultural field, and that the theoretical issues involved challenge standard assumptions and standard modelling procedures in economic theory.

**Key words:** cultural economics, development of economic theory

## 1. Introduction

To define the beginning of a discipline, one might use the moment in time at which the first classic text of the discipline has appeared. Economic science, for instance, has identified *The Wealth of Nations* as its first classic text, thus placing its beginning in the year 1776.<sup>1</sup> Cultural economics, as a discipline, has attributed that status to *Performing Arts: The Economic Dilemma*, published in 1966. Thirty years should be a long enough time span to reflect on the performance of a new discipline. One might ask, therefore, what kind of impact on the study of economics and economic behavior cultural economics has made up to now.

There are, no doubt, a number of ways of determining that impact. I will limit my answer to one subset of all the relevant contributions that have appeared since 1966. I will leave out empirical contributions even though I am aware that much of the financial support for work in the field of cultural economics has come from such applications. The demand for aid in making decisions on cultural policy issues is still increasing, and along with that demand, the statistical data base has improved significantly in many countries. In consequence, we have gained considerable factual knowledge of that sector of the economy.

---

\* Presidential address delivered at the 9th international conference of the Association for Cultural Economics, held in Boston, May 8–11, 1996.

I will also leave out those contributions that apply established tools of economic theory to a new subject. I acknowledge that the systematic use of standard analysis has made it possible to observe art markets in a dispassionate manner, and that it has identified structures of self-interest previously hidden by “culture-talk”. Such texts contain new applications of existing theory, and they broaden the scope of application. But we are looking for impact, and the application of standard tools has not changed the existing body of theory.

I want to focus on contributions that have changed, and are still changing, economic theory. There is reason to believe that observations in the cultural field have a profound heuristic advantage: Economic phenomena in the art world exhibit unusual conditions of production, exchange and demand. By observing those phenomena, properties of goods and institutional conditions can be studied which are present in all economic goods and institutions, but which are rarely as obvious and prominent as in the case of sound performances, text reproductions and image diffusion.

## 2. Six Construction Sites

To make my point, I will briefly sketch the situation in six research areas. In all of them, work is still going on. To recognize that condition, I will label them “construction sites”. I want to emphasize that this sketch is not intended as a survey. It is a *tour d’horizon*, where horizon indicates the limit of what one is able to see from a particular standpoint. The texts cited are chosen because they exemplify that horizon.

The first construction site was opened by Baumol and Bowen’s discovery that artistic and non-artistic labor differ in their ability to benefit from technical productivity gains. “Baumol’s cost disease” is still an area of active research. As the contributions to the latest issue of the *Journal of Cultural Economics* (Volume 20, issue 3) demonstrate, the observation has been extended – first by the original authors, then by many others – to other kinds of labor which are difficult to substitute or complement through technical devices. Communicative and administrative skills, teaching, education, health care and other forms of literally embodied capital have been identified as “non-progressive”. The hypothesis has also been helpful in recognizing long-term changes in factor combinations. It is indeed observed that large choirs and symphony orchestras are being substituted by smaller ensembles and by performances involving electronic reproduction. Similar trends are found in administration and in healthcare institutions, and in all other sectors that depend on embodied know-how.

The second site is by now so extensive that we have to break it down into particular issues. I am referring to work which uses the notion of public goods. The standard criteria for public goods, non-excludability and non-rivalry in consumption, are very intricate in the case of artistic goods. A certain degree of publicness is even conducive to the popularity and thus raises the exchange value of a tune, an

image or a text. Moreover, artistic and cultural activities exhibit spill-over effects for other sectors. The effects may be diffuse and vague, but they are real enough to secure financial support for the arts through a wide range of coalitions. Spill-over effects and effects for future generations due to the arts have been being discussed since the 1960s,<sup>2</sup> long before they became an issue in environmental economics.

A further project on the same site deals with the question of what constitutes the distinctiveness of the public good effect in the cultural sector, as opposed to all other sectors with such effects. Although many suggestions have been discussed, the literature does single out one primary effect: the power to define the identity of some collectivity, be it local or national, for itself. Throsby and Withers developed the argument in the late 1970s.<sup>3</sup> More recent studies on the economics of cultural heritage strengthen the validity of the argument.<sup>4</sup> Such a sense of identity is experienced in a wide variety of collectivities, be they communities, nations or organisations. It develops through knowing the same artifacts, using the same symbols and going collectively through the same performance experiences. Esteemed works of art become part of the social infrastructure. This brings into focus the fact that all kinds of environment, all kinds of context permitting an efficient production of private goods, have to have the characteristics of a public good.

The public good issue in cultural economics has fostered the insight that there is a strong resemblance, analytically speaking, between cultural and environmental goods. That insight has led to a fruitful transfer of concepts and methods in recent years. One example are studies of contingent valuation in communities and regions. Such studies attempt to determine the option value, existence value and bequest value of cultural goods. One object of study has been the Royal Danish Opera.<sup>5</sup> Another example of transfer is the frequent use of the notion of sustainability of a given or desired cultural environment.<sup>6</sup> Still, the potential of such comparative analysis has not yet been exhausted.

The public aspects of cultural goods have been part of a discussion that has altered our understanding of the production and the financing of an “adequate” supply of public and collective goods in general. But that is not all. As we turn to the third construction site, market demand, we find contributions that tackle other fundamental issues. To begin with, the standard assumption of stable preference structures is particularly inadequate in the cultural sector. Tastes are obviously socially shaped. Terms like “acquired taste” demonstrate that this fact is well known. The conditions for preference changes have been the object of extended research, as in the work of McCain on the cultivation of taste.<sup>7</sup> Another standard assumption is stability of the demand that leads to a specific price paid and volume sold. However, in the “thin” markets for art objects, that assumption does not hold – demand at a particular auction is highly unpredictable. The impact of such conditions on optimizing behavior in “tertiary” auction markets has been studied by Singer and Lynch.<sup>8</sup> A third peculiarity of demand for the arts is the star phenomenon. Again, the observation that demand concentrates on a very few performers or products for a certain period can be made in other sectors as well.<sup>9</sup>

But rarely can it be studied in as much detail as in the case of pop music charts, or blockbuster films, or bestselling books. Finally, I want to mention the issue of certification. Because of the social nature of art appreciation, the identification of certain product qualities has to be left to specialized experts. They certify objective properties, such as authorship by particular artists, and they make judgments about the artistic value of specific artist through their interpretations.<sup>10</sup> The capacity for interpretation is part of the production process, but it is also a basic skill for art appreciation, and thus for the formation of art demand.

The fourth construction site deals with a much narrower problem. The issue in question is the long-term rate of return on investments in paintings. Baumol started this debate 10 years ago.<sup>11</sup> So far, it is unclear whether the returns follow a random walk pattern, whether they stay consistently below rates in comparable markets, or whether observers are commingling two rather distinct markets, namely the market for dealers and the market for collectors.<sup>12</sup> In any case, the debate has led to a much more careful analysis of markets with thin and unstable supply and/or demand, where objects of heterogeneous quality are traded. A fine distinction is made between the "psychic income" of collectors, and the expected financial returns of a resale.<sup>13</sup> There has also been a noteworthy development of econometric methods adequate to the study of such heterogeneous samples.

The fifth item is not really a site where much work is done but rather a problem area in dire need of analytical and empirical attention. I am referring to the impact of new technologies and media on production and consumption patterns. Again, the issue does not only concern the diffusion of music and film performances, although the explosion of the entertainment industry is a remarkable phenomenon in itself. The issue is one of dealing with communication and its media in general. Therefore, the impact concerns the composition of total production value. At present, it seems as if only one sub-topic of this rapidly expanding issue is getting wider attention, namely the problem of property rights protection. The expansion of allocation dimensions by means of electronic recording and satellite transmission continues, but the currently existing institutions for the definition and the protection of intellectual property rights do not function well in such a changed technical and economic environment.<sup>14</sup> The challenge of the problem is that it forces economists to consider property right regimes that are far more complex than the traditional exclusive rights associated with material commodities.

Finally, I come to a construction site that is very old. In fact, the site has the look of an old abandoned coal mine. I am referring to the theory of value. This is forbidden territory since the epistemological restoration of neoclassical economics, beginning with J. N. Keynes and completed by Hicks and Robbins. But value plays at least as important a role in the art world as it does outside of it. In the process of making and appreciating art, there is a form of valuation at work that is distinct from valuation in terms of monetary exchange value. This is a recurring theme, as is shown in Throsby's survey article of 1994: most of the studies cited there point to artistic quality as a major explanatory variable. Apparently, artistic quality

cannot be broken down into more elementary characteristics. Despite occasional anecdotes to the contrary, there is fairly high consensus among participants in the various genres about which pieces have quality and which do not. This kind of valuation is distinct from traditional individual use value. It is a social kind of valuation, just like exchange valuation, and yet it operates differently. I have already mentioned that artistic valuation involves a complicated scheme of certification and reputation building. The same is the case for monetary evaluation. The argument, therefore, is not that artistic and cultural goods are somehow exempt from monetary valuation. Rather, it is claimed that such goods are subject to yet another, equally autonomous valuation, and that this other valuation determines exchange value to a significant extent.<sup>15</sup>

### 3. Summary

The impact of cultural economics on the development of economic theory begins to show only in a very few instances, as in the case of the “Cost disease”. Most of the contributions discussed are rather recent, and their more general relevance is rarely recognized. But the brief tour around the research construction sites has shown how varied the ways are in which standard assumptions and standard modelling procedures are being challenged, and it has shown how basic some of these challenges are. The horizon of cultural economics is wide. The discipline may be exotic with respect to the items which constitute the markets studied. But it is at the center of the issues that economic theory has to be able to deal with in order to be relevant to the problems of post-industrialist economies in the information age.

### Notes

1. The identification of a text as being “classic” is a semantic attribution which is accomplished by the circle of those who contribute to the discipline. There are, of course, always earlier texts, but those are then categorized as precursory.
2. See Peacock, 1969.
3. See Throsby and Withers, 1979.
4. See Hutter and Rizzo, 1997.
5. See Bille-Hansen, 1995.
6. See Throsby, 1994 and Peacock, 1997.
7. See McCain, 1986 and 1995.
8. See Singer, 1990, and Singer and Lynch, 1994.
9. Rosen, 1981, the starting point for most theoretical treatments, uses examples from sports.
10. See Mossetto, 1993.
11. Baumol, 1986.
12. The recently published research note by Guerzoni (1995) presents supporting evidence for the latter claim. The paper also contains an overview of the major contributions to the issue.
13. See Frey and Eichenberger, 1995.
14. See, however, the special issue of the JCE (19:2, 1995) on “The Economics of Intellectual Property Rights”.
15. On this issue see Hutter, 1997.

## References

- Baumol, William J. (1986) "Unnatural Value: or Art Investment as a Floating Crap Game", *American Economic Review* 76: 10–14.
- Baumol, William J. and Bowen, William W. (1966) *Performing Arts: The Economic Dilemma*. Twentieth Century Fund, New York.
- Bille-Hansen, Trine (1995) "A CV Study of Willingness-to-pay for the Royal Theatre in Copenhagen", Mimeo, AKF, Copenhagen.
- Frey, Bruno and Eichenberger, Rainer (1995) "On the Return of Art Investment Return Analyses", *Journal of Cultural Economics* 19 (3): 207–220.
- Guerzoni, Guido (1995) "Reflections on Historical Series of Art Prices: Reitlinger's Data Revisited", *Journal of Cultural Economics* 19 (3): 251–260.
- Hutter, Michael (1997) "The Value of Play" in A. Klammer (ed.), *The Value of Culture*. Michigan University Press, Ann Arbor.
- Hutter, Michael and Rizzo, Ilde (eds.) (1997) *Economic Perspectives on Cultural Heritage*. Macmillan Press, London.
- McCain, Roger (1986) "Game Theory and the Cultivation of Taste", *Journal of Cultural Economics* 10: 1–15.
- McCain, Roger (1995) "Cultivation of Taste and Bounded Rationality: Some Computer Simulations", *Journal of Cultural Economics* 19 (1): 1–15.
- Mossetto, Gianfranco (1993) *Aesthetics and Economics*. Kluwer, Dordrecht.
- Peacock, Alan (1969) "Welfare Economics and Public Subsidies to the Arts", *Manchester School of Economics and Social Studies*. pp. 323–335. (Reprinted in *Journal of Cultural Economics* 18: 151–161.)
- Peacock, Alan (1997) "Some Economics of Heritage Policies", in M. Hutter and I. Rizzo (eds.), *Economic Perspectives on Cultural Heritage*. Macmillan Press, London.
- Rosen, Sherwin (1981) "The Economics of Superstars", *American Economic Review* 71: 845–858.
- Singer, Leslie (1990) "The Utility of Art vs. Fair Bets in the Investment Market", *Journal of Cultural Economics* 14: 1–15.
- Singer, Leslie and Lynch, Gary (1994) "Public Choice in the Tertiary Art Market", *Journal of Cultural Economics* 18: 199–216.
- Throsby, David (1994) "The Production and Consumption of the Arts: A View of Cultural Economics", *Journal of Economic Literature* 32: 1–29.
- Throsby, David and Withers, Glenn (1979) *The Economics of the Performing Arts*. St. Martin's Press, New York.