DOES ADVERTISING CREATE PREFERENCES? A MODERN EXAMINATION OF JOHN KENNETH GALBRAITH'S "DEPENDENCE EFFECT"

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1. Introduction

Love them or hate them, advertisements are everywhere. From the billboards drivers pass on the highway to the commercials families watch in between segments of their favorite television show to targeted online advertisements that bombard college students as they shop on Amazon for textbooks, advertisements play a very visible role in all aspects of modern society. What economic function, however, do advertisements serve? Are they simply a marketing tool designed to convince consumers to purchase goods they do not *actually* need just so greedy capitalists can make a few extra dollars? John Kenneth Galbraith seems to think so. In his 1958 book entitled *The Affluent Society*, Galbraith (158) argues that advertising is a tool used by producers to manufacture individual preferences that are then satisfied by the products they created—a process Galbraith terms the "dependence effect."

This paper, however, aims to prove that Galbraith's dependence effect does *not* hold true for privately produced goods due primarily to the existence of 1) individual sovereignty, 2) the entrepreneur, and 3) the mechanism of profit and loss but may perhaps hold true for publicly produced goods due to the lack of these three aspects. As such, rather than view advertising as a tool employed by greedy capitalists to lead consumers astray and into an overconsumption of unnecessary goods that would require the government's corrective action as Galbraith (1958) suggests, advertising is better understood—through the lens of praxeology—as simply another form of action that aids market participants in their decision-making process.

2. Galbraith's Argument

At the outset, it is important to rehearse Galbraith's argument more specifically. He is taking the position not that advertising shapes but that it actually *creates* individual preferences. He coins the term dependence effect to describe this process and defines it as "the way wants depend on the process by which they are satisfied" (Galbraith 1958, 158). In other words, production through advertising creates the wants and preferences of individual people. Unfortunately, Galbraith does not specifically define what he means by "creating" preferences. For the sake of the argument in this paper, it will be defined as the ability to control another's actions. In other words, the use of advertising creates (or controls the demonstrated) preferences of others. The terminology is being defined in this manner precisely because preferences are *demonstrated*. One cannot assume to know the preferences of another apart from action. Thus, in order to analyze the ability to control preference, it must be measured with a proxy, and that proxy is an assumed ability to control action.

In continuing with Galbraith's argument, he believes that "the institutions of modern advertising and salesmanship… cannot be reconciled with the notion of independently determined desires, for their central function is to create desires—to bring into being wants that previously did not exist" (1958, 155). He even provides empirical support for this claim by finding that:

> A broad empirical relationship exists between what is spent on production of consumers' goods and what is spent in synthesizing the desires for that production. A new consumer product must be introduced with a suitable advertising campaign to arouse an interest in it. The path for an expansion of

> output must be paved by a suitable expansion in the advertising budget. Outlays for the manufacturing of a product are not more important in the strategy of modern business enterprise than outlays for the manufacturing of demand for the product. None of this is novel. All would be regarded as elementary by the most retarded student in the nation's most primitive school of business administration. The cost of this want formation is formidable. (Galbraith 1958, 155-156)

For Galbraith (1958, 156), all this evidence serves as proof for his recognition that "production, not only passively through emulation, but actively through advertising and related activities, creates the wants it seeks to satisfy." As such, the purpose of advertising according to Galbraith is to form wants and create preferences.

Galbraith (1958, 155) further clarifies in a footnote that "the competitive manipulation of consumer desire is only possible, at least on any appreciable scale, when such need is not strongly felt." In other words, want creation from advertising is only possible in *affluent* societies. In such societies, Galbraith finds that the most basic needs of human existence have already been met, which leaves producers with no choice but to manufacture *new* needs, *new* desires, and *new* preferences. This, as understood by Galbraith's term dependence effect, is the purpose of advertising. Therefore, it is important to note that it is *only* because the need or preference is not strongly or urgently felt that it can be created and/or manipulated by advertising. Galbraith explains that:

> The fact that wants can be synthesized by advertising, catalyzed by salesmanship, and shaped by the discreet manipulations of the persuaders shows that they are not very urgent. A man who is hungry need never be told of his need for food. If he is inspired by his appetite, he is immune to the influence of Messrs. Batten, Barton, Durstine & Osborn. The latter are effective only with those who are so far removed from physical want that they do not already know what they want. In this state alone men are open to persuasion. (1958, 158)

In other words, if an individual's preference is something basic and/or urgent (like the need for food and shelter), then advertising cannot create and/or manipulate those wants.

Instead, the needs and preferences must be something extraneous or even unnecessary for them to be created by advertising. Galbraith (1958, 158), therefore, reveals that “[a]s a society becomes increasingly affluent, wants are increasingly created by the process by which they are satisfied.” As such, the extent of this paper is limited to a consideration and evaluation of only first world countries. Because Galbraith’s argument focuses specifically on these richer, more affluent areas, this paper also proceeds under the same constraints.

Overall, Galbraith (1958) uses his term dependence effect to conclude that the government must intervene in the market and protect consumers from overconsuming on unnecessary and exorbitant goods. He believes that gluttonous overconsumption in the private sector starves the public sector of adequate funding. Public provision of goods (which includes categories such as education, protective services, roadways, etc.) are drastically *underfunded* while private provision of lavish, unnecessary goods are considerably *overfunded*. Therefore, Galbraith believes that the use of advertising harms society, and so its existence serves as a call for government intervention. This paper, however, asserts that the existence of individual sovereignty, the entrepreneur, and the mechanism of profit and loss work together in unraveling Galbraith’s dependence effect argument in the private production of goods.

3. Refuting Galbraith: Private Provision of Goods

3.1 Individual Sovereignty

Sovereignty is a topic of debate in the economics literature. Francis Munier and Zhao Wang highlight how Galbraith's:

> analysis was suggested in an economy in construction and strong growth, [and it was] applied especially to a mass consumer society, where the urgency of the needs was no longer the important problem to solve. Today, the consumer is confronted with an infinity of products and consumption is no longer urgent. Thus, in a globalized economy, interactive and knowledge-based, the question of the dependence effect and the relevance of the sovereign consumer must be discussed in other contexts. In this way, the real question is, in fact, who exercises the power? Is it the producer or the consumer? Or is it perhaps both? (2005, 67)

In other words, who has the sovereignty, or underlying power and influence, in a free market economy? Is it the producer? Is it the consumer? Or is it perhaps both, as suggested by Munier and Wang?

Some, such as Ludwig von Mises, have argued in favor of *consumer* sovereignty, a term scholars typically trace back to William Hutt and his 1936 book entitled *Economists and the Public: A Study of Competition and Opinion* (Murphy 2003; Persky 1993, 183-194). In his work *Bureaucracy*, Mises writes that:

> The captain [of the economic ship] is the consumer… They, by their buying and by their abstention from buying, decide who should own the capital and run the plants. They determine what should be produced and in what quantity and quality. Their attitudes result either in profit or in loss for the enterpriser. They make poor men rich and rich men poor. They are no easy bosses. They are full of whims and facies, changeable and unpredictable. They do not care a whit for past merit. As soon as something is offered to them that they like better or that is cheaper, they desert their old purveyors. (1944, 2021)

In other words, consumers are "merciless" bosses (Murphy 2003). Producers work to satisfy *consumer* preference and consumer preference alone. Mises further "liken[s] the operation of a market to a… [situation] in which every penny spent is a vote by the consumer indicating those products and services to which society's resources should be devoted" (Murphy 2003). Producers, therefore, earn profits based on how well they satisfy consumer preference, and they earn losses if they fail to do so adequately.

This notion of consumer sovereignty *alone* starts to unravel Galbraith's perceived dependence effect in the production of private goods. According to consumer sovereignty, it is the preferences of the *consumer* that drives production and advertising expenditures. Producers earn profits or accrue losses in accordance with how well they satisfy or do not satisfy consumer preferences. Thus, the consumer sovereignty position asserts that "[a]ny eccentric producer who flouted the wishes of his customers and" produced goods that did not align with consumer desire "would soon go out of business" (Murphy 2003).

Munier and Wang, however, do not so quickly discount the role and importance of the *producer* on the market. They agree, at least in part, with consumer sovereignty supporters in recognizing that "consumers demand that the producer take into account their dynamic and uncertain preferences. In this logic, consumers keep a part of sovereignty" (Munier and Wang 2005, 78). The authors also, however, recognize the importance and influence of external stimuli which is something F.A. Hayek discusses in his 1961 response to Galbraith called "The Non Sequitur of the 'Dependence Effect.'" Hayek states that:

> Most needs which make us act are needs for things which only civilization teaches us to exist at all, and these things are wanted by us because they produce feelings or emotions which we would not know if it were not for our cultural inheritance… It would scarcely be an exaggeration to say that contemporary man, in all fields where he has not yet formed firm habits, tends to find out what he wants by looking at what his neighbors do and at various displays of goods

> (physical or in catalogues or advertisements) and then choosing what he likes best. (1961, 346-347)

Essentially, no human being lives, acts, or operates in a vacuum. Everyone, at least at some point, interacts with the groups, culture, and institutions around them. The preferences people have and the goods they possess *influence* the preferences that other people have and the goods that other people purchase. The economy is a complex, integrated, and *social* system. It is nearly impossible *not* to be influenced, at least in part, by others. Hayek (1961, 347), therefore, concludes that influence from culture and other people "would clearly not justify the contention that particular producers can deliberately determine the wants of particular consumers." In other words, external stimuli (such as advertising) may influence preferences, but they cannot "'determine' them" (Hayek 1961, 347).

In returning to Munier and Wang's argument, they conclude that sovereignty is *shared* by producers and consumers. Consumers make choices from a set of options that already exist, and producers are the ones in charge of making those options exist (Munier and Wang 2005, 79). The authors, therefore, assert that the "dependence effect is no longer relevant in a modern economy based on knowledge. The direction of the [sovereignty] relationship is no longer important" because both producers and consumers influence each other (Munier and Wang 2005, 79).

While the notion of consumer sovereignty provides some worthwhile critiques on Galbraith's dependence effect, the concept of sovereignty is best understood, however, in terms of Murray Rothbard's (2009) notion of *individual* sovereignty. This terminology properly recognizes the notable role and position of both producer and consumer by rooting the analysis more firmly in human action and avoids potential economic downfalls that stem from a “consumer only” type of sovereignty. Rothbard explains that:

> in the free market economy people will tend to produce those goods most demanded by the consumers. Some economists have termed this system ‘consumers’ sovereignty.’ Yet there is no compulsion about this. The choice is purely an independent one by the producer; his dependence on the consumer is purely voluntary, the result of his own choice for the ‘maximization’ of utility, and it is a choice that he is free to revoke at any time. (2009, 629)

Basically, the consumer is not and cannot force the producer to make the goods that he desires. Instead, the notion that producers conform to or satisfy consumer preference comes largely from the idea that producers will gain monetary rewards (i.e. profit) for doing so.

All this, however, is assuming that utility and profit maximization is the preference most desired by producers. What producers prefer can and does, in fact, vary from person to person. Rothbard (2009, 629) rationalizes that a “producer’s psychic valuations” can “counteract monetary influences.” This means that a person’s motivation for producing may be something other than a maximized monetary reward achieved by satisfying consumer preference. Rothbard (2009, 629-630) lists enjoyment of work as an example of an alternative preference for producing. As such, “[t]o earn a monetary return, the individual producer must satisfy consumer demand, but the extent to which he obeys this expected monetary return, and the extent to which he pursues other, nonmonetary factors, is entirely a matter of his own free choice” (Rothbard 2009, 630). Rothbard (2009, 630), therefore, asserts that “[i]n a purely free society, each individual is sovereign over his own person and property… No one is ‘sovereign’ over anyone else’s actions or exchanges. Since the consumers do not have the power to coerce producers into various occupations and work, the former are not ‘sovereign’ over the latter.” Overall, these statements show that neither the producer nor the consumer can claim sovereignty over the other. They have sovereignty over themselves (over their own individual person), but they do not have the ability to control another.

As such, the notion of *individual* sovereignty begins the process of crippling the validity of Galbraith’s dependence effect in the private production of goods. It is simply *not* the case that producers can use advertising to control the preferences and actions of consumers. The existence of individual sovereignty on the free market means consumers have free will over their own choices. They do, therefore, choose what goods to buy and what goods not to buy based on their *own* volition. This volition, moreover, does not have to be formed independent from external stimuli. In fact, it will *never* be formed independently, for culture and institutions along with the preferences, decisions, and actions of others will—in some manner and to some extent—influence the decision-making process of others.

3.2 The Entrepreneur

Next is a discussion on how the existence of the entrepreneur further disproves Galbraith’s dependence effect in the private production of goods. Israel Kirzner provides key insights about the role of the entrepreneur in his 1973 book called *Competition and Entrepreneurship*. According to Kirzner (1973, 135), “[e]ntrepreneurs compete with one another… by seeking to offer *better opportunities* [emphasis added] to the market…. [that] offer[ ] buyers something they seek *more eagerly* [emphasis added].” In doing so, “costs are incurred by the entrepreneur as he attempts to offer opportunities which market participants will consider *more attractive* [emphasis added] than those available elsewhere” (Kirzner 1973, 126). Kirzner (1973, 138) highlights further that “[e]ntrepreneurs… buy up the resources and put them to work in producing the *more valuable* [emphasis added] product.” Thus, “[i]n the decision about which quality of product is to be produced the really significant aspect is not how to economize with given resources in attaining given ends, but the alertness with which the producer recognizes the kinds of goods consumers are *eager* [emphasis added] to buy” (1973, 139). These statements describe the entrepreneur as someone who brings something *more* valuable to the market than before. The entrepreneur is satisfying preferences that are *more* highly desired than the preferences currently satisfied. He is finding what the consumer wants and then is delivering a solution to *those* wants.

The role of the entrepreneur as explained by Kirzner represents the complete opposite of what Galbraith suggests. In fact, Galbraith hardly even mentions the entrepreneur in his work at all. What he does claim, however, is that in the affluent society, the most important preferences have already been satisfied. It is precisely because these most basic and most urgent needs have already been met that Galbraith finds cause for the dependence effect. The entrepreneur, therefore, (if he even exists at all according to Galbraith) can only seek to satisfy preferences that are lower and lower on an individual’s value scale. The lower he goes on the value scale, the more the entrepreneur must "create" new preferences through advertising. As such, Galbraith's understanding is a complete inversion of the role of the entrepreneur. In fact, the role of the entrepreneur proves that he does not function to create *new* preferences but works to satisfy the preferences that *already* exist.

Kirzner adds that:

> As part of his *entrepreneurial* role, it is the function of the producer to go beyond the mere fabrication and delivery of a commodity to be available for the consumer. He must also *alert* the consumer to the availability of the product, and sometimes he must even alert the consumer to the *desirability* of an already known product. As we shall discover, this latter role cannot be understood merely as that of 'producing knowledge' for the consumer concerning prospective or existing opportunities. Rather, it consists in *relieving the consumer of the necessity to be his own entrepreneur*. (1973, 136)

Advertising *is* alerting the consumer to the availability and desirability of a product. Contrary to Galbraith, this does not mean that advertising creates or determines preferences and/or action. Instead, it relieves the consumer of having to be his *own* entrepreneur. In other words, it relieves the consumer of having to search for information concerning the availability and desirability of a good on his own. Advertising communicates a message. It is informing consumers, but it does not determine the preferences and/or actions of those receiving that message.

3.3 Profit and Loss

Lastly, the market mechanism of profit and loss provides empirical evidence against the dependence effect's applicability to the private production of goods. Rothbard (2008) reminds that advertising claims are always tested by consumers on the market. If those claims fail, then "the product will soon fade into oblivion" (Rothbard 2008). This means that empirically speaking, the dependence effect could only be true if and only if products never failed or "flopped" on the market following an advertising campaign. The test cases of New Coke, Colgate Frozen Dinners, EZ Squirt Ketchup, and Keurig Kold prove otherwise.

First is the case of New Coke. At the time, the Coca-Cola company was not known for making big changes (Zmuda 2011). Natalie Zmuda (2011) explains how many people "inside the company [actually] fought the launch of Diet Coke, the first trademark extension because 'they believed that Coke was one thing, one sound, one size, one taste'… But Diet Coke's successful launch gave the company a new mind-set, and three years later,… it prepared to launch New Coke." As the name of the product suggests, New Coke was a *new* recipe, a *new* flavor, and a *new* taste. It was a major change for the company. Zmuda (2011) notes that "[i]n the advance of New Coke, Mr. Zyman [Coca-Cola's chief marketing officer at the time] says the company ramped up ad spending, doubled price promotion and employed deep discounts—[but it was all] to no avail." New Coke appeared for only 77 days in 1985 before it was removed from shelves (Zmuda 2011). It was launched on April 23, 1985, and Coca-Cola reversed the launch on July 10, 1985 (Zmuda 2011). Excerpts from an interview with Mr. Zyman explain it best:

> We eventually got to the point where management and everybody decided we needed to bring back [the original formula] to appease those people who weren't happy… It was very exciting at the beginning, because all of a sudden we had almost a rebirth, a renaissance of the brand. Consumers were looking at it and business was booming. Consumers wanted the brand; they appreciated the brand; they knew what the brand was all about. (Zmuda 2011)

Despite Coca-Cola's extensive advertising campaign, consumers did not want New Coke, and they made their preferences known. They wanted the original recipe, the original taste. The Coca-Cola company listened to its consumer and brought back the original Coke formula appropriately called "Coca-Cola Classic" (Zmuda 2011).

The second market test is the case of Colgate's Frozen Dinners. One of the exhibits in The Museum of Failure, is a Colgate Beef Lasagna packaging, but "Colgate refutes the existence of their 1980s line of microwaveable cuisine. In fact, the company's legal representation contacted the museum after it began receiving international attention, stating '[Colgate] has no recollection of a Colgate Lasagna'" (Ripley's Believe It or Not! 2021). The Museum of Failure's curator, Dr West, explains that "he reconstructed what Colgate's so-called lasagna frozen dinner looked like… from reputable online sources… [believing] that Colgate remains too embarrassed to let the cat out of the bag when it comes to their failed line of frozen entrees" (Ripley's Believe It or Not! 2021). The product's existence was almost a mystery, but two sources provided concrete evidence that the dinners did, in fact, exist. The first source is a 1966 version of the *Television Age Magazine*. In this magazine, there is:

> a profile of the Colgate-Palmolive Company mentioning George Henry Lesch. In 1961, Lesch became the new chairman and the president of the company, and he aggressively sought new ways to expand the brand's reach. According to the article, this included, 'A line of dried chicken and crabmeat entrees under a Colgate Kitchen label… introduced and quickly withdrawn.' (Ripley's Believe It or Not! 2021)

The second source is the American Institute of Food Distribution's "Weekly Digest," Volumes 72-73, produced in 1966. This edition of the "Weekly Digest" "also reported on

Colgate's foray into crabmeat and chicken entrees in 1966. The article claimed Colgate created a range of five products test-marketed in 1964. But according to the report, Madison, Wisconsin, represented the only place these products ever got marketed" (Ripley's Believe It or Not! 2021). Overall, "[w]hile the descriptive language 'chicken and crab meat' rules out the existence of Colgate *Beef* [emphasis added] Lasagna, it's clear the company did try to wade into the food market" (Ripley's Believe It or Not! 2021). Colgate had supposedly "hoped to entice people into eating their frozen meals and then brushing their teeth with the company's toothpaste" (Ripley's Believe It or Not! 2021).

The third case is EZ Squirt Ketchup produced by Heinz. Starting in 2000, the Heinz ketchup brand rolled out:

> vibrant, crazy-colored ketchup in purple, pink, orange, teal, and blue varieties. Heinz EZ Squirt's first color entry was 'Blastin' Green' and was created as a promotional ketchup in support of the first Shrek movie, and moms and kids came running. Each new color resulted in incremental sales volume. In fact, more than 25 million bottles of colored ketchup were sold, helping Heinz capture an all-time high of 60% of the U.S. ketchup market, before softening sales resulted in the EZ Squirt brand being pulled from the shelves by January 2006. (Glass 2011)

Sandie Glass (2011) notes that there are two main reasons for why EZ Squirt Ketchup eventually disappeared from the market despite the Heinz company's advertising efforts. The first reason concerns the target audience. According to Glass (2011), the product's appeal to kids was attached to the movie, and "[k]ids have short attention spans." Eventually, moms just went back to normal ketchup (Glass 2011). The second reason involves the product itself. Glass reveals that:

> The vibrant color hues [of the ketchup]… were achieved by stripping the red color from traditional Heinz ketchup and adding food coloring. And because the flavor had to be tweaked to taste just like traditional ketchup, it could no longer be called 'tomato ketchup' like the original red. We believe that Heinz compensated for this by fortifying it with Vitamin C to win the approval of Moms. But most parents are pretty health-conscious when it comes to feeding their kids, and EZ Squirt came along at a time when parents were becoming more and more cautious of artificial food colorings and its effects on kids' behavior and allergies. (2011)

One key takeaway from this example is how the general rise in health-conscious eating conflicted with the Heinz company's crazy colored ketchups. Once the product's initial appeal had dried up, moms desired a return to the healthier and more natural option of regular ketchup. Like New Coke, consumers wanted the original formula back. EZ Squirt Ketchup is thus another great example of a product that did not—despite advertising efforts—satisfy consumer preferences and was, therefore, removed from shelves.

The final market test is the case of the Keurig Kold. The Keurig company wanted to extend the brand beyond coffee products via an at-home soda machine (Peterson 2016). Unfortunately, after only nine months, the company discontinued the product (Peterson 2016). Why did the Keurig Kold fail despite its advertising campaign? There are three main reasons. First, according to Hayley Peterson (2016), "the machine was too expensive." The Keurig Kold cost a massive $369 whereas a cheap SodaStream was only $79 (Peterson 2016). Peterson (2016) breaks the figure down to cost per soda such that "every soda from Kold machine cost $0.99 to $1.29. By comparison, SodaStream drinks cost between $0.08 to $0.20 per serving." For the second reason, Peterson (2016) notes that "[s]oda consumption… [had] been falling in the US for decades." Peterson wrote her article in 2016, and in it, she states that "[p]er capita soda consumption last year [2015] was 41.4 gallons, down from 52.4 gallons in 2004, according to date from Beverage Digest, a trade publication."

The final reason concerns how "[t]he machine was too big, loud, inconvenient, and unreliable, according to customer reviews," and it is from these customer reviews that consumer preference reveals itself (Peterson 2016). Although the advertisements for Keurig Kold claimed it would cool after only two hours, one customer review reported that it actually took five hours to cool (Peterson 2016). Another review mentioned a continual humming sound "as long as it's plugged in" (Peterson 2016). The serving size of each soda was also limited; syrup pods could only produce a certain, specified quantity, so consumers could not alter the drink sizes (Peterson 2016). Peterson (2016) also highlights that the "Coca-Cola soda pods… [were] being sold in packs of four for $4.99. That means every pod… [was] about $1.25. Meanwhile, 2-liter bottles of soda sell for under $2 in grocery stores." Not only did the advertising claims for the Keurig Kold fail to hold up when tested on the market, but consumers also conveyed their lack of preference for the product in their abstention from buying it. Overall, these examples provide empirical evidence against the existence Galbraith's dependence effect in the private production of goods. In these four cases, producers were not able to control the actions and preferences of consumers. In fact, by not buying these products, consumers did the exact opposite of what producers had hoped.

<u>4. Refuting Galbraith: Public Provision of Goods</u>

Given the preceding analysis for how Galbraith's dependence effect does not hold true in the private provision of goods, it is time to evaluate how and why it may, in fact, hold true in the public provision of goods. Rothbard (2008) remarks that "[a]pparently, Galbraith has never heard of, or refuses to acknowledge the existence of, *governmental* propaganda. He makes no mention whatever of the hordes of press agents, publicists, and propagandist working for government agencies, bombarding the taxpayers with propaganda which the latter have been *forced* to support." Robert Batemarco adds that:

> Where Galbraith is right [regarding the dependence effect] is that such salesmanship does indeed get people to demand things that are not in their best interests. Where he goes terribly wrong is in finding producers in the marketplace as the primary perpetrators of this effect. In fact, it is the *state* [emphasis added] that makes greatest use of salesmanship to obtain the consent of people for things that… not only make them … [worse] off, but usually do them harm. What makes the State's behavior even worse is that when the State's salesmanship fails, the State can fall back on the use of force to get people to satisfy the wants 'that production creates.' Private firms, unless they are in league with the State, do not have that ability. (2014)

Batemarco (2014) provides several examples of what he means by the state using advertising, salesmanship, and propaganda to control the preferences and actions of consumers, one of which being the "US entry into World War I."

Batemarco (2014) claims that most Americans, at least initially, did not want the US to join WWI and cites two main pieces of evidence. The first reason "can be inferred from the fact[ ] that they [Americas] re-elected a president who ran under the slogan, 'He kept us out of war'" (Batemarco 2014). While most politicians run for office on a platform of wide-ranging policy positions, the brewing world war was likely a topic of common concern among many Americans. There can be no doubt, therefore, that the issue of war played a major role in the election. As such, voting for a president who “kept us out of war” represents a free expression of preference as evidence by the action of voting. Many politicians run extensive advertising campaigns to convince voters to favor them, but, ultimately, no one forces anyone’s hand in the voting box. The decision is of the voter’s own free will and volition.

As for the second reason, Batemarco (2014) states “that the number of volunteers was not sufficient for the US to commit large armies to that conflict without conscription.” Volunteering to serve in the military is also a free expression of individual preference as evidenced by the action of volunteering. Conscription, on the other hand, forces individual action to conform to the preferences designed and laid out by the government. It is not a *free* expression of preference and action but a *forced* expression of conformity.

As such, the dependence effect may in fact exist for the public provision of goods due to the lack of 1) individual sovereignty, 2) the entrepreneur, and 3) the market mechanism of profit and loss. First is the lack of individual sovereignty. Rothbard (2009, 630) defines sovereignty as “the quality of ultimate political power; it is the power resting on the use of violence.” State sovereignty, therefore, means the government holds the ultimate political power and possesses ultimate control on the use of violence. The existence of state sovereignty in a mixed economy, therefore, interferes with the individual sovereignty in a free market. As stated before, “[i]n a purely free society, each individual is sovereign over his own person and property” (Rothbard 2009, 630).

Government interference, however, compromises individual sovereignty. The cost of not conforming to the goals of an advertising campaign in a free market is $0.00, but the cost of not conforming to a government-sponsored propaganda campaign is greater than $0.00. This altered cost structure exists due to the state's ability to use force. As such, it incentivizes greater conformity and thus demonstrates an ability to "control" action and therefore determine preferences.

Second is the lack of the entrepreneur. In the public sector, the role of the entrepreneur is extremely diminished—if not eliminated. While there are always margins of adjustment that can be made due to government interference, people are rewarded *less* for being entrepreneurial and *more* for following the rules of the bureaucrats, for staying in-line and not asking questions, and for doing what they are told. As such, there is a lowered incentive to innovate. There is also less motivation to satisfy those more highly desired preferences (or the same preferences in a better way) because the reward for doing so is lacking.

The absence of a reward for innovation leads into the third item—the absence of profit and loss. Simply put, the government does not operate via profit and loss. They, therefore, *cannot* engage in economic calculation. As such, government propaganda is *not* subject to a market test the way private advertising *is*. Batemarco provides several noteworthy examples of publicly provided goods and services that are not subject to a market test. They include:

> The TSA and its privacy-violating "security theater," NSA spying on law-abiding citizens, subsidized artwork of dubious value, a War on Poverty that generated

> numerous behaviors that perpetuated poverty, and a food pyramid that, when followed, seems to lead to more obesity rather than less, are just a few on a list that seems endless. In every one of these cases, people came to accept such programs that were not satisfying needs that were intrinsic due to the hype generated by court economists or court historians, or failing that, had them shoved down their throats by force. Thus, the Dependence Effect is alive and well. Only its presence is most strongly felt in the government sector. (Batemarco 2014)

In the absence of individual sovereignty, consumers *and* producers face incentives that push them towards compliance, and without the entrepreneur, the government faces less competition, and so, there are fewer alternatives. Yet, even if individual sovereignty and the entrepreneur did exist in the public provision of goods, the lack of economic calculation means the government is *not* subject to a market test. The government can, therefore, ensure that its publicly provided goods are bought (i.e. conformed to) by consumers precisely because they hold the ultimate power of violence. Consumers are not as free to express their preferences through their actions because they face a higher cost in doing so if the action does not conform to the government's intervention and/or mandate.

5. A Better Way to Understand Advertising

While Galbraith paints a picture of advertising as a harmful tool used by capitalists to lead consumers into an overconsumption of unnecessary goods, this paper proposes that advertising is best understood through the lens of praxeology. As such, advertising is simply another form of communication with a two-fold nature. This means that advertising is both informative *and* persuasive in nature. In addition, advertising aids market participants in numerous ways. One example of this is the way in which advertisements serve as both a credible commitment and signal when information is costly to acquire, which thus eliminates Galbraith's perceived dependence on the government to "correct" the market.

5.1 The Praxeology of Language

Daniel W. Hieber (2017) discusses how language is merely a subset of praxeology. He states that speech is a form of action because "[s]peakers use language to accomplish goals in the social world" (Hieber 2017). This is not new and was actually first suggested by Austrian economists such as Mises. Hieber (2017) emphasizes that "[t]o the Austrians… the study of language is simply one subfield within a broader field of study that encompasses all the social sciences: *praxeology*, or the science of human action." Linguistics and economics, therefore, are both value-free. Linguists like economists take ends as given and only evaluate the means (Hieber 2017). While "Mises believes that only certain types of speech are action," Hieber (2017) believes that "[a]ll speech is action." This paper affirms the latter view.

Furthermore, it is common knowledge for the economist that all means are scarce. This also holds true in speech and language. Hieber (2017) explains that "[a] person cannot physically produce more than one utterance at once. They must always choose which of the things they wish to say first. They must in the most literal sense *economize* on their speech, thereby making the act of speaking subject to various laws of praxeology and economics." Individual actors also showcase time preference in their speech. Hieber states the following:

> speakers always try to accomplish their communicative goals using the fewest expressions, articulatory gestures, and cognitive resources possible. In linguistics,

> this is known as the principle of economy or *principle of least effort*… other things being equal, speakers generally place the most newsworthy information first, thereby conveying the maximal amount of information in the shortest possible time. (2017)

The art of linguistics also follows the law of diminishing marginal utility. According to Hieber (2017), "words lose their pragmatic utility with increased use over time. The very utility of a novel construction is exactly what incentivizes speakers to use it more frequently. As its frequency increases, it becomes routinized, losing some of its original utility and semantic distinctiveness." An example of the diminishing marginal utility in speech is the use of cliché. Authors sometimes include a cliché in their writing due to its novel construction and common understanding among audience members. The more a cliché is used, however, it becomes *over*used and later avoided in writing altogether.

Hieber (2017) also notes the presence of opportunity costs associated with speech such that "the opportunity cost of what is said is everything that is not said." People also economize on their speech which is not to say that individual actors always speak quickly and bluntly or only share very limited information, but people do speak in a way that will convey their point in an efficient, if not the *most* efficient, manner (Hieber 2017). Hieber (2017), therefore, contends that "[t]o hedge or to speak indirectly is every bit as purposeful and motivated as speaking in simple, terse, declarative sentences." Meaning, the goal in speaking, writing, etc. is to communicate efficiently *and* effectively, but the method or means of doing so can vary. Lastly, Hieber describes speech as a mutually beneficial form of exchange. According to Hieber:

> Participants in discourse choose to give their time to engaging in that discourse in lieu of the various other activities they could be doing… Discourse and

> conversation are [also] coordinative and cooperative rather than violent and hegemonic. Even the most… hateful speech, speech meant to anger and incite, is at its core an attempt to accomplish a communicative exchange. The opposite of a cooperative speech exchange is not uncooperative speech exchange, it is physical violence or the threat thereof. (2017)

As such, advertising—as a written, verbal, and visual form of speech and language—is best understood through a praxeological lens.

5.2 Advertising's Informative and Persuasive Nature

With this praxeological lens in mind, the nature or function of advertising is to both inform and to persuade. In noting this dual nature of advertising, Kirzner (1973, 154) discusses articles and arguments from both Chamberlin and Hicks. According to Kirzner (1973, 154), the article by Chamberlin shows that "just as we are prepared to ascribe social utility to strictly informational advertising because consumers desire information, so must we concede that 'appeals to emotions' fill an equally strong demand." Essentially, Chamberlin ascribes that for some people, what matters most to them is *who* is using the good in question. For some people, knowing which celebrities use which products matters more to them than the actual use of the product itself (Kirzner 1973, 153).

This, in turn, exemplifies the subjective nature of preferences (Kirzner 1973, 143). Hayek (1961, 346) elaborates that "there are some desires which aim, not as a satisfaction derived directly from the use of an object, but only from the *status* [emphasis added] which its consumption is expected to confer." In other words, consumers prefer goods not only for their use but also their status. Goods, therefore, incorporate a bundle of attributes, and people value goods for different reasons. Some value things for the use it has in completing a task. Some value a good for its low price. Others value a good because it represents the latest and greatest technology, and some people value a good because it is a name brand, etc.

Returning to Kirzner's analysis, he explains how "Hicks, too, has criticized those who have judged the social function of advertising to be confined to its strictly informational aspect… Hicks, like Chamberlin, denies the existence of a clear line separating information from persuasion" (Kirzner 1973, 154). Rothbard (2008) adds that "[a]dvertising is… used as a means of [both] (a) conveying information to the consumers that the product is now available and telling them what the product will do; and (b) specifically, trying to convince the consumers that this product will satisfy their given want." As such, it is very clear and apparent that advertising functions to both inform and persuade the intended audience.

This element of persuasion, however, is very different from Galbraith's notion of want creation. Hayek (1961, 347) highlights that "[t]hough the range of choice open to the consumers is the joint result of, among other things, the efforts of all producers who vie with each other in making their respective products appear more attractive than those of their competitors, every particular consumer still has the *choice* [emphasis added] between all those different offers." As such, it is the notion of individual sovereignty that differentiates advertising's persuasive nature from Galbraith's want creation, and as mentioned before, choices are never made in a vacuum. In other words, advertising is one such "external stimuli" that can help inform and *shape* preferences, but it never *determines* them. The notion of individual sovereignty upholds that ultimate choice and volition remains in the individual acting and not in the persuasion of the message.

5.3 Advertising as both a Credible Commitment and a Signal

Lastly, it is important to note a few ways in which advertisements actually aid market participants in their decision-making process. In brief, I. P. L. Png and David Reitman (1995) suggest that advertising, at least in part, serves as an example of a credible commitment. They note that “branding [which just *is* another form of advertising] is a way by which a seller can commit to product attributes that are difficult for third parties, such as courts to verify” (Png and Reitman 1995, 207-208). So, “[w]hen consumers pay a premium price for a branded product, they are paying for an implicit guarantee of superior quality” (Png and Reitman 1995, 208). In other words, credible commitments indicate to consumers that the company offering the commitment is trustworthy. To make the commitment *credible,* the producer typically retains a large sunk cost (i.e. a large, expensive advertising budget) that can only be recouped through continual or repetitive purchases. If a producer lies about his product offering and commits fraud, then customers will eventually take their money else, leaving the producer with a huge cost he cannot cover. On the other hand, if a producer acts with integrity and honors his commitment by *not* deceiving his customers, then he will be rewarded with continued operation and can, therefore, eventually cover the cost of his initial sunk cost.

Complementary to Png and Reitman's article, Benjamin Klein and Keith Leffler (1981) suggest that advertising, at least in part, also performs the role of a signal. They describe that:

> Luxurious storefronts and ornate displays or signs may be supplied by a firm even if yielding no direct consumer service flows. Such firm-specific assets inform consumers of the magnitude of sunk capital costs and thereby supply information about the quasi-rent price-premium stream being earned by the firm and hence the opportunity cost to the firm if it cheats… [and, so,] [a] sufficient investment in advertising implies that a firm will not engage in short-run quality deception since the advertising indicates a nonsalvageable cost gap between price and production costs, that is, the existence of a price premium. (Klein and Leffler 1981, 630).

In other words, credible commitments and signals go together. The existence of a credible commitment on the market *signals* to consumers that a company is trustworthy because if that company deceives the consumer, the company will suffer in the long run due to the existence of sunk costs. Advertising is one such sunk cost. Contracting a celebrity for a commercial, for example, can be very costly for a company. What this celebrity-endorsed advertisement does in part, however, is signal to consumers that the company is an honest, reputable company. The company (most likely) is not looking to scam its consumer but actually wants to offer the product it claims to possess (Klein and Leffler 1981, 631).

Overall, the existence of credible commitments and signals are especially helpful when information about the goods or company in question are costly for the consumer to acquire information. Klein and Leffler summarize nicely that:

> This analysis of advertising implies that consumers necessarily receive something when they pay a higher price for an advertised brand. An expensive name brand aspirin, for example, is likely to be better than unadvertised aspirin because it is expensive. The advertising of the name brand product indicates the presence of a

> current and future price premium. This premium on future sales is the firm's brand name capital which will be lost if the firm supplies lower than anticipated quality. Therefore, the firms selling more highly advertised, higher priced products will necessarily take more precautions in production. (1981, 632)

As such, one way in which advertising aids market participants is through its dual function as both a credible commitment and a signal.

6. Conclusion

In conclusion, advertising is not a tool used to manipulate consumers into buying unnecessary goods just so greedy capitalists can make a few extra dollars as suggested by Galbraith. Instead, advertising is better understood through the lens of praxeology. It has a dual nature that seeks to both inform and persuade its audience. Persuasion, however, does not mean that advertising determines preferences. On the contrary, advertising (like other forms of external stimuli) can *influence* individuals in their preference-forming and decision-making processes, but it is the individual who retains sovereignty over their own actions and decisions. Thus, the dependence effect does not hold true in the private provision of goods due to the existence of individual sovereignty, the entrepreneur, and the market mechanism of profit and loss. The dependence effect may, however, hold true in the public provision of goods due to the lack of these three categories.

As such, the public sector is not "poverty stricken" as Galbraith suggests (Rothbard 2008). Moreover, government action is not needed to correct the perceived market failure of overconsumption due to advertising campaigns. In fact, advertising actually *aids* market participants. When information is costly to acquire, for example, advertising can and does often serve as both a credible commitment and signal, proving to consumers that a company is trustworthy. Advertising, therefore, is a product of human action, and it helps facilitate trade. As such, it is not in need of regulation but in need of a round of applause.

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