Volume 7, Issue 6

December 2017

ISSN 2515-2602

WEA Commentaries*

A publication of the World Economics Association.

To *plurality*. The Association will encourage the free exploration of economic reality from any perspective that adds to the sum of our understanding. To this end it advocates plurality of thought, method and philosophy.

* Formerly the World Economics Association Newsletter

Inside this issue:

A Philosophical Framework for Rethinking Theoretical Economics and Philosophy of Economics

By Gustavo Marqués

Here Gustavo Marqués discusses the main tenets of his book with the above title, published by the World Economics Association.

1. Bookish Economics

In his paper *Credible Worlds: the status of theoretical models in economics* Robert Sugden called attention to the difference between "real" and "model" worlds. In fact, Sugden conceives the model world as a "parallel" world, which triggers questions about whether a connection among them exists and in that case how should it be characterized. Other authors have considered the possibility that economic models are autonomous from both theories and the facts of real market economies, which opens the door for claiming that they could be described as completely *imaginary* worlds. Is it possible that a good part of economics consists of theoretical developments that have no connection to actual market economies? The history of some branches of science shows that this possibility cannot be readily dismissed. Consider the history of anatomy during the XIV century in Europe. It was taught at universities, and the classes consisted of two different simultaneous activities. From his desk the teacher delivered a speech about the subject of the day. He was the academic authority in his classes. The content of the speech was taken from classical texts, some of them written during the III century before Christ (particularly by Galeno). Given the impossibility of dissecting cadavers (this practice was impeded by a legal disposition that prevailed during a good part of the Middle Ages) the teacher had not had contact with the organs of real human bodies and literally repeated what Galeno wrote. The problem is that Galeno had not had access to human bodies either, and in some cases he attributed to humans what he observed in pigs and monkeys. Meanwhile at the center of the room a butcher and an auxiliary of the teacher were dissecting a cadaver to illustrate to the audience the main points of the lecture. But to their surprise what they saw was sometimes very different from what was taught. They were inhabitants of the *real* world but the teacher was living inside what may be called a *bookish world*.

In this book I argue that a good part of mainstream (and maybe some non-mainstream) economics is in a situation that is similar to that of middle age anatomy: it is trapped within the "model world", solving theoretical problems suggested by previous texts. Even if finding solutions to bookish oriented problems may be found exciting by the members of the community, they may be irrelevant for approaching the main economic problems of market economies.

2. Bookish Economics inspired conventional theoretical practice

From the very beginning, the construction of economic theory as a scientific discipline deliberately assumed a sharp break with the main features that characterize real economies. Mill, Senior, Menger, Walras and many other classical economists have stated explicitly that the results of economic science are dissociated from their applications. Lucas has been even more explicit about this issue and recognized that denying uncertainty is a condition for economics to be scientific. As a result, most of mainstream theoretical economic practice involves making up imaginary worlds inhabited by truly rational agents, where regularities governed by calculable risk can be found, and has focused on the examination of the properties of these representations. Such models are built on the following set of ontological and epistemological assumptions:

1) Specific economies "contain" laws, mechanisms or some kind of regularities arising from ex – ante rational agents´ decisions. They are invariant (stable) features of the economic processes, lying below the surface of economic phenomena.
2) One of the main roles of theoretical practice is to discover these invariants.
3) This invariant knowledge also applies to the future and is obtainable ex-ante (mainly by models).

To these ontological and epistemological assumptions conventional economics usually adds a practical one:

4) Without having the invariant knowledge mentioned in (2) and (3) it is not legitimate to implement economic policies (and whatever intended policy lacking such a foundation is doomed to failure).

From this perspective it is natural to stress that the role of social or economic theory is to investigate the unwanted (and unexpected) consequences of agents' decisions. And it is also clear why those theorists need not consider incorporating uncertainty and common sense and expert knowledge into their approach. Besides, lobbying activity has no place when agents are able to take ex-ante rational decisions.

3. Mainstream Philosophy of Economics (MPE): a history of submission and failure

Standard epistemology and philosophy of economics, which assumes a *naturalized* view of science, has capitulated to the standard way of doing economics. This orientation is usually referred to as "recovering the practice" of economic theory, which means to describe as legitimate *any* contribution of standard Bookish economics. However, MPE has failed in its many attempts to solve the so called *external validity* problem. So, it couldn't justify the explanatory capability of Bookish Economics and its practical value for the implementation of economic policies. It leaves Maki's question without a clear and well founded response: "Fact or fiction? Is economics a respectable and useful reality-oriented discipline or just an intellectual game that economists play in their sandbox filled with imaginary toy models?"

Focusing its attention on Bookish Economics and taking an a-critical stance regarding standard models' results, mainstream philosophy of economics seems to be in the same weak position as the "Teachers" of Anatomy who were overcome by the rough practice of the butcher!

4. Some suggestions for reorienting Economics and Philosophy of economics

If it is assumed that (a) both agents and theorists are aware they are facing an uncertain context, and (b) they hold epistemic and ontological beliefs consistent with this state of affairs, the proper way to approach economic phenomena should be very different from those that guide current modeling practice. Particularly, instead of mechanisms or economic regularities that keep running independently of agents' expectations, the decisive role of lobbyists within open-ended and uncertain processes based on expectations should be incorporated into the analysis. The following assumptions could be the philosophical core of a new conceptual framework for economics:

instead of mechanisms or economic regularities that keep running independently of agents' expectations, the decisive role of lobbyists within open-ended and uncertain processes based on expectations should be incorporated into the analysis

1) There are economic processes based on expectations and characterized by radical uncertainty. Agents involved in such processes act in two different ways (as decision-makers or as lobbyists).
2) Ex-ante knowledge of invariant sequences of events is generally not possible (because there are few if any sequences of this kind); more importantly, such knowledge is unnecessary as support and justification for the implementation of economic policies.
3) The role of theoretical practice is to identify the many feasible "branches" of a "tree of plausible outcomes" as well as the restrictions that each sequence of events faces.
4) It is not known (and it is not possible to know) ex-ante what "branches" of the tree (what sequences of feasible alternative events) will prevail. Science cannot help us with this.
5) Other types of knowledge (common and practical knowledge as well as practical skills) are crucial for shaping those processes. It is a sort of know-how knowledge, closer to management and administration than to scientific economics.
6) Although – as was shown in point (3) – theoretical practice has an important role to play in shaping processes, what is crucial in this endeavor is another practice, which we denote as lobbying (interventional) practice, which is performed by a wide range of economic players (mostly different kind of interest groups who are able to operate on the relevant context and agents' expectations).

The whole concept of *theoretical practice* should be rethought if economic processes consistent with the above assumptions are the target. Chapter Eight argues that there are some mechanisms of economic transmission at macro level which represent *feasible* (or *credible*) sequences of economic events. I insist on the concepts of "feasibility" and "credibility". Feasible sequences *can* happen (they are attainable in our world), although it all depends on the interventions of many different lobbyists along the process. Correctly interpreted – as open ended sequences, not as mechanisms – feasible models could be useful. Consequently, when I speak of an alternative theoretical practice I am not demanding the invention of a new way of doing economic theory (a demand that would be rather foggy). Part of the required theory is already available (I mean, the *feasible* one): it offers sequences of stages which in principle could be reached and provides points of intervention for governmental administration and the several interested lobbyers.

Philosophy of economics could also be reoriented. To go beyond mainstream philosophy of economics the usual ontological and epistemological assumptions of conventional modeling practice should be critically examined and philosophical support to the above mentioned assumptions should be provided. It means to incorporate into the agenda an analysis of the ontological features of economic processes, like uncertainty, and to call attention to the decisive role of the practice of lobbing, Such problems as what kind of rationality, learning and useful theoretical practice can be achieved under uncertainty should be addressed.

5. Philosophical Problems posed by assuming open ended, uncertain and intervenable processes

Assuming open ended processes subject to interventions and pervaded by radical uncertainty means that some problems should be rethought anew and put into the philosophers' agenda. These are some of them:

Rationality

There are two basic notions of individual rationality. First, there is a subjectivist and coherentist notion which conceives "rationality" as consistency among agents' beliefs, preferences and actions. This is the one involved in Expected Utility Theory. Second, rationality is seen as a sort of calculation driving decisions that precedes the realization of their future consequences. I call it *well-grounded ex-ante rationality*. "Well grounded" because it is supposed to be founded on a calculation that takes into account the best available evidence (where "best" is that which is more determinant for the expected results). "Ex-ante" because the rational character of the decision can be recognized *before* its results are manifest. This is the kind of rationality that Keynes had in mind.

Following Keynes' remarks some scholars maintain that under radical uncertainty there is room for rational action in this second (stronger) sense. They offer three different arguments in support of this claim: (a) agents can employ induction in order to form "rational beliefs" about future events; (b) agents can perform some kind of rational economic calculation; (c) agents are able to decide rationally following a number of "techniques" or conventions. These three strategies find some support in Keynes' work. The first is developed in his *A Treatise on probability*, the second is described in Chapter 11 of his General Theory, and the latest is also suggested in his General Theory but it is made fully explicit in his article "The general theory of employment" published in 1937. In Chapter Five I contest the validity of these arguments. I claim that agents cannot behave rationally under uncertainty assuming rationality is of the well-grounded ex-ante type.

Could agents facing uncertainty behave rationally if rationality is understood in a *subjectivist and coherentist* sense? The answer to this question is vital for my distinction between "complexity" and "uncertainty". I concede that rational behavior of this type is possible in a complex world, but I deny that possibility if uncertainty prevails. However, it has been claimed that even in these circumstances agents might nonetheless be rational. Contrary to this view, I claim that if some reasonable ontological and epistemic *beliefs* are attributed to economic agents, to be coherent they *cannot* behave rationally in this sense.

To get this result it must be realized that *all* agents' beliefs should be taken into account (not only agents' subjective probabilities regarding expected results, but their epistemic and ontological beliefs too). Radical uncertainty means that they do not have vital information about those future events which are going to influence the results of their present days' decisions, *and they know that*. Besides, they also know that the influential impact of these causal events is more relevant the more they are close to the time in which the consequences of their present decisions will be revealed. This is so because the nearer in time is a causal event from its consequence, the less is the opportunity for intervening if a corrective action were needed.

Agents' ontological and epistemic beliefs should be considered as a key part of their uncertainty, which means that they know that the most relevant causal factors affecting the results of their actual decisions cannot be grasped when their decisions are taken. These philosophical convictions show them that no ex-ante rational decision is available under true uncertainty.

What sort of behavior, if any, would be "rational" then? My answer is that provided economics cannot surrender rational terminology, being rational is to intervene *a posteriori* of the original decisions for the purpose of validating them. Agents who believe in the uncertain nature of the world are driven to become lobbyists.

What about theorists' behavior? If *theorists* believe, like agents do, that the scenario is uncertain, their theoretical practice would have to be consistent with this belief, as long as their models take into account the special nature of their intended target. If the purpose of economic theory were to render account of the behavior of subjects that know (or think they know) they suffer uncertainty, their theoretical practice should assume that agents behave consistently both with respect to their set of preferences and expectations (which is the usual requirement) *and* regarding their *epistemological and ontological beliefs*. Agents should be represented as behaving consistently with respect to *all* their beliefs. Theoretical models in which agents are modeled as lobbyists should be seen not as mechanisms but as feasible (credible) sequences.

Testing and learning

The use of such essential concepts in economics, like *testing* and *learning*, are not conceptually problematic in conditions in which certainty or risk is assumed. They are not problematic given complexity (in my sense) either. But conceiving open ended economic processes in which uncertainty reigns, where consequently there are "no laws", nor "invariants" or "mechanisms" to discover, both experimental practice and learning require particular justification. Certainly, we can gather precise information, restricted in space and time. The problem is that taking uncertainty seriously puts in question the relevance these data have for future situations. (See Chapter Seven)

Pluralism and Realism

A richer taxonomy of economic models, which leaves room for distinguishing among Bookish models and Open ended feasible sequences, may be of concern for the current discussions concerning pluralism and realism. Models that at first sight seem to be mutually inconsistent, may belong to different (incommensurable) categories: one may pertain to the world of intellectual exercises and the other refer to possible courses of real world markets. As long as they belong to different categories incompatibility is out of the point, because their purpose or intended target is different. Both models may be retained without paying the price of endorsing inconsistence as a virtue (or, at least, pretending not to see a sin in it).

On the other hand, those economists who are realists can readily pay no attention to the whole Bookish Economics. But, I suggest, they can benefit from the set of plausible sequences approaching an open ended, uncertain and intervenable world, all of them realizable. Even if many of these sequences seem not to be compatible accounts of economic laws or markets mechanisms when they are understood as mechanisms, they are all realizable and compatible views as long as they are seen as future possible paths to perhaps different ends. Feasible economic sequences are not incompatible descriptions or accounts of the same target, even if they are rival sequences and may inspire different policies. Realist and pluralists' may consistently have a positive appraisal of all those views.

6. Interventionist view of Economics

The Hayekean and Popperian programs for social sciences considered that their main task was to find out those not deliberately pursued (and often not wished) consequences of our actual decisions. This is the main program of Bookish Economics, which presupposes that there are laws or mechanisms acting on the back of individuals' consciousness and commanding economic phenomena in an independent and inexorable way. To back such approach is the main task of mainstream philosophy of economics. To this project I oppose a different one in which given open-ended and intervenable economic processes based on expectations lobbyers strive (often successfully) to attain wished results. In fact, this is the whole point for the existence of lobby!

Against the view that sees Economics as just conceiving how reality works I promote an active view of Economics. However, I hold no commitment with voluntarism. Even if a lobbyist tries to impose a particular feasible sequence to get some definite results, he may be unable to attain it simply because he does not manage to gather enough strength to impose on the set of institutions and bring about the required measures.

Therefore the sequence of events that ultimately prevails does not express some sort of pre-established order. Rather it has been socially constituted, and it might not have happened at all. The temptation to naturalize the prevailing social relations is huge and history is full of examples of this class. It has been shown that presumed natural laws, like the incapacity of women to assume government responsibilities, were just social constructions. Economic feasible sequences have the same status and can be successfully implemented and managed.

A conventional economic view asserts that all the implemented policies designed to increase the income of the lower-wage people via fuelling aggregate demand will be a failure. Conventional economists say so because they assume some kind of law or mechanism which determines that fuelling the aggregate demand will result in inflation (not in more income and employment). Supposedly they know this result *ex–ante* and by *scientific* means. Other heterodox economists, on the contrary, think that the way to reach an increase in employment starts with an increase in aggregate demand. Supposedly they have discovered an alternative mechanism opposed to the conventional one! I invite economists and philosophers of economics to pay less attention to the search of automatic mechanisms able to take us (necessarily) to a success or a failure are available, and consider that political decisions and practical measures will be crucial in the resulting events. The final outcome is open (and there is some room for a sound administration on the part of the government).

Our approach emphasizes the *deliberate* aspect of the interventionist behavior and the possibility that such strategy may be successful. That is to say, we find it feasible to enforce some desired results by altering the relevant context or influencing the present decisions of other agents. If we are right, it is better to perceive social and economic events less as commanded by laws or spontaneous mechanisms than like open ended and intervenable processes constructed by the joint actions of the many mutually conflicting relevant agents.

The shift proposed means that a *scientific* approach like the one assumed by the usual way of modeling can be of little use either for analyzing market operations or as a guide for implementing efficient policies. The nature of economic processes suggests that it would be far more useful to apply a *political* analysis able to reveal their open-ended nature and the diversity of economic interests at play than a supposedly scientific analysis which aspires to find invariant laws, mechanisms or regularities.

Interview on *The Fascist Nature of Neoliberalism*

Editor's Note: In this interview, Flavia di Mario answers questions about the book she co-authored with Andrea Micocci, recently published by Routledge. Sadly Andrea Micocci (pictured) passed away a month ago. We at the WEA wish to convey our condolences to his family, friends and colleagues.

1. You refer to the fascism of capitalism and, in particular, of neoliberalism. On what basis do you make that association?

In our book we argue that contemporary capitalism is similar to, in its fundamental nature, fascist ideas and practices about politics and the economy. Our argument is based on the consideration that fascism and capitalism entail an organic view of society that characterizes by manifestations of metaphysical and mythical language the construction and affirmation of a "*pensiero unico*" (*pensee unique*, or single thought). Take "the regulating power of the market" locution as a specific instance and the demand for balance in the state budget. The practices of the "*pensiero unico*" are also particularly evident in the societal structure and organizations as in the case of managerialism of firms. We refer to managerialism as the ideology and force originated and used by managers to propose and to eventually affirm their superiority in organizing the factors of production, unquestionably imposing their practice to all industries and to all fields of society. The managerial caste does not need a democratic framework, much as the neoliberal technocracy, rather it self-legitimizes, acting in a 'military-equals-management' style. This ruthless attitude and oppressive character can equally apply to the nation-state administration, private airlines or a national electrical company. We offer historical and contemporary events that emphasize how the "*pensiero unico*" applies to the role of managers; the conceptualization of ethics and other horrific and repressive actions against forms of sociality that are not based on the standard capitalist state. In other words, our book emphasizes the relevant economic and political features of fascism in general in order to see its relation with neoliberal capitalism and managerialism.

2. Why do you say that metaphysics and myth have replaced sound ideas?

This question allows me to address two core arguments in the book: the metaphysic of capitalism as maintained in Andrea Micocci's previous works (2009/2010, 2016) and the "myth" in the contribution of Cassirer (1962). The theoretical basis at the origin of what we argue is based on the work of Micocci and contends that capitalism is based upon a metaphysic, an intellectual organization of reality that fits, and corresponds to, its own flawed intellectual mechanisms. The metaphysics of capitalism is an intellectual construction that reduces everything to a "capitalistic thing"; it pretends to provide "an ultimate system of meaning to reality" (Micocci, 2016, p.1) and to correspond to some natural tendencies. With Cassirer (1962), we agree that "myth" has survived in modern times. A "mythical" language spreads through the communication of concepts, ideas, hopes and collective feelings that would otherwise have neither rational nor factual origins. Drawing from this, we identify the foundation and functioning of neoliberal capitalism in the metaphysics and myth as describe above. Indeed, the metaphysics[1] and myth replace sound ideas by the multiplication of vague capitalistic concepts. Concrete facts are restored by metaphysical and mythical language and narratives, evocation is practiced in place of definition.

3. State intervention has been seen as a counter to the failings of capitalism, but you seem to be suggesting that it is an aspect of fascism. Have I understood, and if so, are there any alternatives?

Yes, State intervention has shown to be historically and presently a pillar of fascist ideas and practices. Historically, Paul Einzig (1933), recognizes in Hegel's doctrine of the state the ideological grounding of fascism and imperialism. Presently we experience the fact that all State regimes call themselves liberal, whereas they carry out corporatism, a set of laws and controls. The practical implication is that, despite the new media communication in present day capitalism, most individuals and groups still have as their main reference the nation state; the masses are fully integrated in the political life of an organized, centralized, authoritarian democracy and its corporatism.

The alternatives can be constructed only outside capitalism as we know it against its homogenizing, corporative and repressive logic. In the book, a CEO's speech is given as an example of the way in which the disrespect for human nature is an open, ordinary and fascist practice of corporate neoliberalism. To build alternatives, we must criticize the flawed intellectual reasoning behind the metaphysics of capitalism, and in particular in managerialism, which downgrades everything, including nature and human beings, to a price-market function. Here we express a belief in an alternative to contemporary capitalist metaphysics and mythical language, that is the hope to recover the material inside and outside ourselves. This means freeing ourselves of the metaphysics through a process of individual emancipation, which should consist of recovering the nature of our sentiments from the prevailing domination of the intellectuality of capitalism. The alternatives are constituted by radical arguments and practices, i.e., of theorizing and making revolutions and actions against the violence and prevarication of managerialism. See, for example, how the students and workers struggle in solidarity against the brutalities of corporate managers despite institutional and corporate forms of downgrading, retaliation and blacklisting. While we are talking, individuals are trying to construct relationships of solidarity outside the logic of capitalism, out of the State and the market. Take for example the communication outside the mainstream and "social" media systems. Other examples are the collective attempts for the re- appropriation of the lands, water, natural resources and public spaces, the creative and performing arts openly and freely displayed in the cities, the natural ways of farming, experimentations to switch from market-oriented production to socially oriented consumption.

4. How do you see developments into the future? Are there any positive changes likely?

Our book proposes to regard neoliberalism in its fascist nature to see beyond the academic and intellectual understanding that this view implies. Despite all the formal deprecations of the fascist ideology and practices in European democracies and elsewhere, the recent elections sought the rising and affirmation of fascist and Nazi groups that confirmed that they are not only compatible but synergic to neoliberalism. Populist and fascist groups are likely to continue the extensive use of mythical language and its absurd, nebulous and evocative concepts of community, nation, economic value, and patriotism. In our contemporary capitalism, the legalized forms of oppression operating in a fascist, and capitalistically banal manner will persist, eventually increasing by means of new technologies, especially when we come across the role and function of managerialism.

As said above, alternatives exist. Through an (inconceivable) uprising of people, new initiatives will be proposed. Their development depends much on the radical nature of these alternatives equally with the efforts to free ourselves and denounce the banalities and atrocities of neoliberalism, whether these are made by verbal or practical acts. People are reacting and denouncing the forms of control and repression, yet it is not enough. Positive changes are likely to happen in the future outside capitalism through the emancipation of people, the spontaneity of their sentiments and actions that must link the efforts to share aims instinctively from different generations.

Cassirer, E. (1962), The Myth of the State, Yale University Press, New Heaven

Einzig, P. (1933), The Economic Foundations of Fascism, MacMillan, London

Micocci, A. (2016), A Historical Political Economy of Capitalism: After Metaphysics, Routledge, London

Micocci, A. (2009/2010), The Metaphysics of Capitalism, Lexington, Lanham

1. "an intellectual construction that aims to provide an ultimate system of meaning to reality" (Micocci, 2016, p.1). Things are reduced to capitalist things, whence their limited and limiting role, and nature itself is perfectly out of touch.

Doomed to Repeat?

By Peter Radford

[Editor's note: This version taken from http://www.radfordfreepress.com/?p=2977 on 2nd January 2018.]

One of the great pleasures of living here in southern Vermont is that we have a terrific local bookshop. I go there simply to absorb that book shop vibe unattainable in the bits and bytes of Amazon. And like all good bookshops this one throws up surprises. About three weeks ago I was browsing the small business and economics section and found a book by Heinz Kurz. It's his "Economic Thought, A Brief History" I recommend it for all of you who want to understand the predicament of modern economics.

Now I admit I am a sucker for reading about the history of economics. It's a great parallel story to the broader social history of the past few centuries. Economics as it weaves back and forth from one emphasis to another is a much more humble adventure than the arrogance of the overly formal neo-mathematics that is has become nowadays. There was a time when it attempted to explore reality, when it included lumpy and vague concepts, when it allowed for collective action, and when it related to experience: how different from today's pseudoscientific axiomatically self-determining oddity.

Many of you, of course, will be completely familiar with such a history. Most of you will have your own heroes and villains as the story unfolds. Reading the Kurz book reminds me of mine.

I love the early stories.

The physiocrats for instance. They reflect their time perfectly. Agriculture reigns supreme. Industry is dismissed as a sterile sidebar. Landowner interests dominate. That was the reality of the age. No one can criticize their effort, no one can undermine their achievement. French society was teetering on the brink and was about to fall behind its industrial rivals — except, of course, those rivals were only just beginning the industrial adventure and didn't understand it themselves. In any case, Quesnay's "Tableau Economique" is one for the ages. None of our contemporary economists could or would attempt such an effort.

Then there's Smith. We've been chasing his tail, and his tale, ever since. He is a cornucopia of observations that echo on through to today. Everyone knows about the invisible hand. If ever there was a metaphor that needs explanation this is it. What did he mean by this? We really don't know. He only mentioned it once in "The Wealth of Nations" and probably didn't mean it the way we commonly think of it nowadays. Subsequent economists adopted the phrase as their own. That twist in meaning is a later part of our story. Quesnay was all about flows, Smith observed a different kind of order. But is it order? Or is it the illusion of order? Your answer will depend on your point of view.

Smith's other ideas are more interesting. The division of labor sits at the heart of modern economic society. His understanding of this makes him the first to see underneath the surface of industrialization, although I am not convinced he realized just how the revolution he was within would shake our world. Then again he understood the prominence of knowledge in spurring growth. He called it the quantity of science. Even now economics doesn't accommodate knowledge well. The weirdness of Total Factor Productivity is a testimony to just how difficult it is to squeeze a public phenomenon like science into modern models that are simply homages to individual effort and reasoning.

Let me fast forward.

Where do the wheels start to come off? The early writers, those we call the "classical theorists" talked about economics very differently from the way we do today. We lost a lot when the change occurred. Frankly I blame the "marginalists" but that's just me.

Between Smith and the so-called marginal revolution sits Marx and his critique of capitalism. The problem with Marx is that he is spot on: circa 1848 his observations made a ton of sense, and post-1848 the staid and the wealthy were terrified he might be right. They needed a new narrative to counter him. They needed to change the conversation.

And the marginal revolution was the response from economics.

The classical theorists thought in social terms. They observed and thought about social, political, and economic interconnections. Their vision of economics was rooted in a larger social context. It was obvious for all to see that the early years of industrialization were not altogether happy ones for a large portion, if not the majority, of society. Sure incomes were rising, but health and living standards were deteriorating. Urban squalor replaced the older rural idyll that the romantics imagined as reality prior to the rise of factory life. Marx was the ultimate critic of this squalor and his stories of the horrors characterizing the industrial interlude between that past idyll and his imagined future utopia unnerved high society.

History is a devil sometimes. Right when those in power needed to fend off their own queasiness about the effects of industrialization, and needed to arm themselves against a rising tide of worker unrest, economists could reach into the physical sciences and pull out miraculous concepts to defeat all that Marxist nonsense.

Back to the fore came the invisible hand, but now it was altered and updated with lots of mathematics and the notion of marginal productivity. There was, the economists of the time taught, no point in pushing back against the tide. Workers earned exactly — precisely and unequivocally — what they, well, earned. Productivity entered the lexicon. Efficiency was borrowed from physics. Inputs and outputs were tied inexorably together. And the economy was conceived, in distant echoes of Quesnay and Smith, as a great big equilibrating machine. There was no room in this scientific interpretation of the economy for romanticism or recourse to narratives. Society was only ever better off if we leave the machine to run by itself. Don't meddle or interfere became the mantra of the age. Which, for some, it still is.

That cautionary note against interference was bulked up because of arguments going on outside economics.

The journey from ancient tyranny to modern democracy had, inevitably, to pass through its own middle ages. That was when the modern notions of liberty emerged. A problem that still haunts us today is that no single definition of liberty was passed forward to us.

There is liberty as individual freedom that motivates capitalism — the freedom to own and dispose of private property is the result of the development of this notion. And there is liberty as citizenship and equality that motivated democracy — the idea of one-person-one-vote flows from here. What happens when the two liberties conflict? Well, the answers are manifold. And our current political battlefield is littered with the debris of the consequence of our inability to balance the two very well all the time.

What we can say, is that when Hayek distorted history to tell his story about the "Road to Serfdom" he deliberately set economics along an anti-democratic path. He valued personal liberty above all else. Democracy is, he thought and his heirs still think, a perversion of the purity of the great economic machine. It allows politics to act as a distributional mechanism alongside economics. And surrendering to the democratic wishes of the majority will inevitably doom liberty.

The taint of Hayek's anti-democratic convictions still sullies economics. Keynes tried to find a middle path, but the trajectory of modern economics and its obsession with the unobservable phenomenon of equilibrium, and its equally opaque partner of efficiency, has led it, inevitably, to become an ideological rather than a scientific enterprise.

There is, for instance, a straight line from Hayek to the notion of shareholder value, which is nothing more than weaponized neoclassical economics. And from shareholder value there is a straight line to the modern workplace replete with tales of woe, depressed wages, household insecurity, and tenuous employment all living in the shadow of record profits. To libertarians like Hayek undermining the futures of millions of workers is a mere nothing alongside the desire to preserve individual liberty. It makes me wonder whether such liberty is worth preserving.

Economics always has, its history teaches us, been a child of its context. What is, and is not, considered appropriate subject matter is a function of the moment. There are signs that the choice of subject matter is changing. Maybe the whole marginal era will be looked back upon as a curious misadventure. Perhaps equilibrium will be seen, at last, as an illusion. And maybe efficiency will be viewed as the chimera it is.

Hayek was right about one thing: information is paramount. Economics is the study of information: who has it? What do they do with it? How does it shape exchange? And so on. He was wrong to jump to the conclusion that he did. He argued that if the totality of information is inscrutable to any one person or group of persons, then we can conclude that it is pointless to interfere in the economy. The government, he said, ought stay well away. The price mechanism of the private market will, he went on, coordinate all that information and produce the "right" answer for us.

But how do we know?

If information is that inscrutable? How does anyone know? Prices might be wrong. How would we know otherwise?

We wouldn't. We couldn't.

There's more to this history yet.

The Invisible Hand in Context

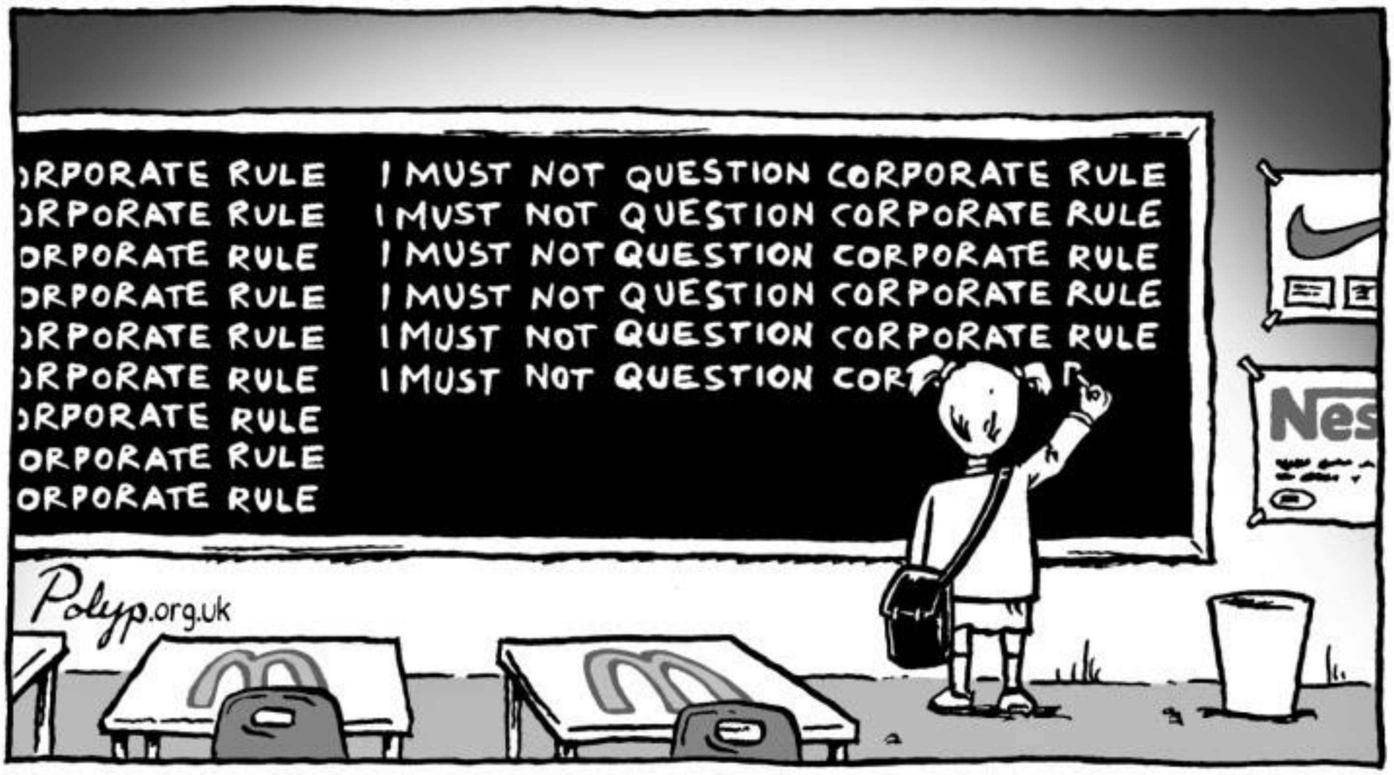
This is the one mention of the invisible hand in *Wealth of Nations*:

He generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it. ***By preferring the support of domestic to that of foreign industry****, he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain; and he is in this, as in many other cases,* ***led by an invisible hand*** *to promote an end which was no part of his intention.*

Smith, Adam. *An Inquiry into the Nature and Causes of the Wealth of Nations* (Kindle Locations 6799-6802). University Of Chicago Press. Kindle Edition.

Global Rentier Capitalism

By David F Ruccio

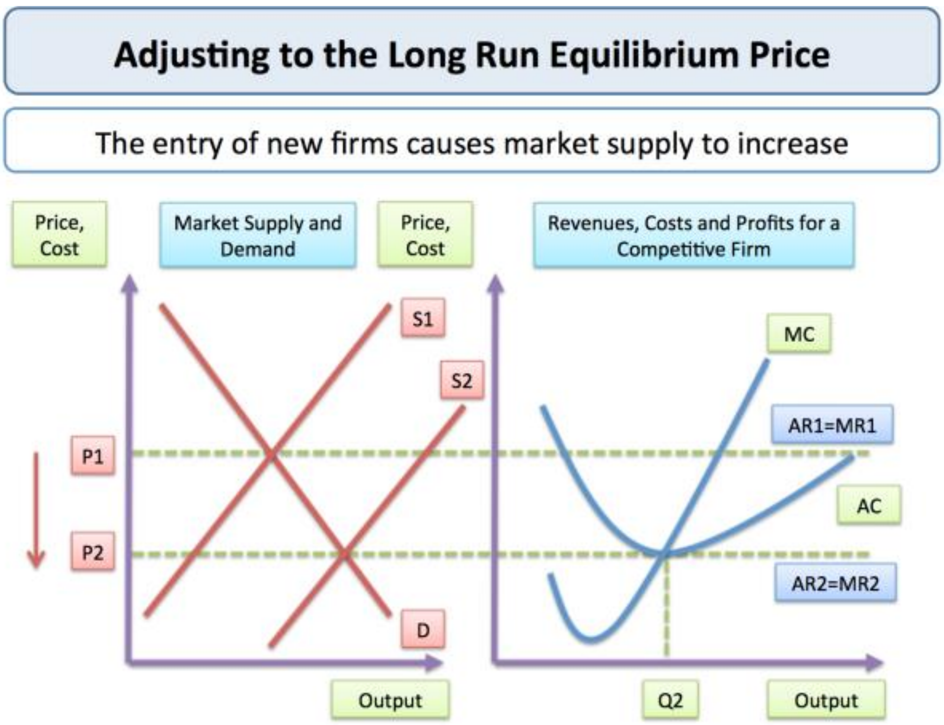


'DETENTION'

Mainstream economics lies in tatters. Certainly, the crash of 2007-08 and the Second Great Depression called into question mainstream macroeconomics, which has failed to provide a convincing explanation of either the causes or consequences of the most severe crisis of capitalism since the Great Depression of the 1930s.

But mainstream microeconomics, too, increasingly appears to be a fantasy—especially when it comes to issues of corporate power.

Neoclassical microeconomics is based on a set of models that assume perfect competition. What that means, as my students learned the other day, is that, while in the short run firms may capture super-profits (because price is greater than average total cost, at P1 in the adjacent chart), in the "long run," with free entry and exit, all those extra-normal profits are competed away (since price is driven down to P2, equal to minimum average total cost). That's why the long run is such an important concept in neoclassical economic theory. The idea is that, starting with perfect competition, neoclassical economists always end up with. . .perfect competition.[1]



Except, of course, in the real world, where exactly the opposite has been occurring for the past few decades. Thus, as the authors of the new report from the United Nations Conference on Trade and Development have explained, there is a growing concern that

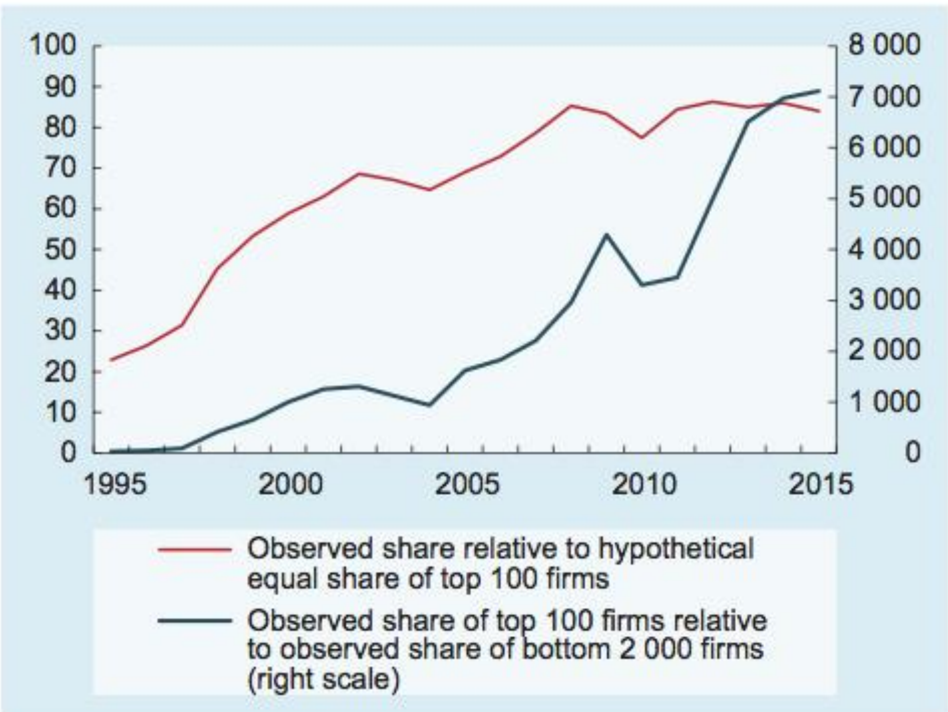
> *increasing market concentration in leading sectors of the global economy and the growing market and lobbying powers of dominant corporations are creating a new form of global rentier capitalism to the detriment of balanced and inclusive growth for the many.*

And they're not just talking about financial rentier incomes, which has been the focus of attention since the global meltdown provoked by Wall Street nine years ago. Their argument is that a defining feature of "hyperglobalization" is the proliferation of rent-seeking strategies, from technological innovations to mergers and acquisitions, within the non-financial corporate sector. The result is the growth of corporate rents or "surplus profits."[2]

FIGURE 6.1 Share of surplus profits in total profits, 1995–2015
(Per cent)

Source: UNCTAD secretariat calculations, based on *CFS* database, derived from Thomson Reuters *Worldscope Database*.

FIGURE 6.2 Ratios of market capitalization of the top 100 non-financial firms, 1995–2015



Source: UNCTAD secretariat calculations, based on *CFS* database, derived from Thomson Reuters *Worldscope Database*.

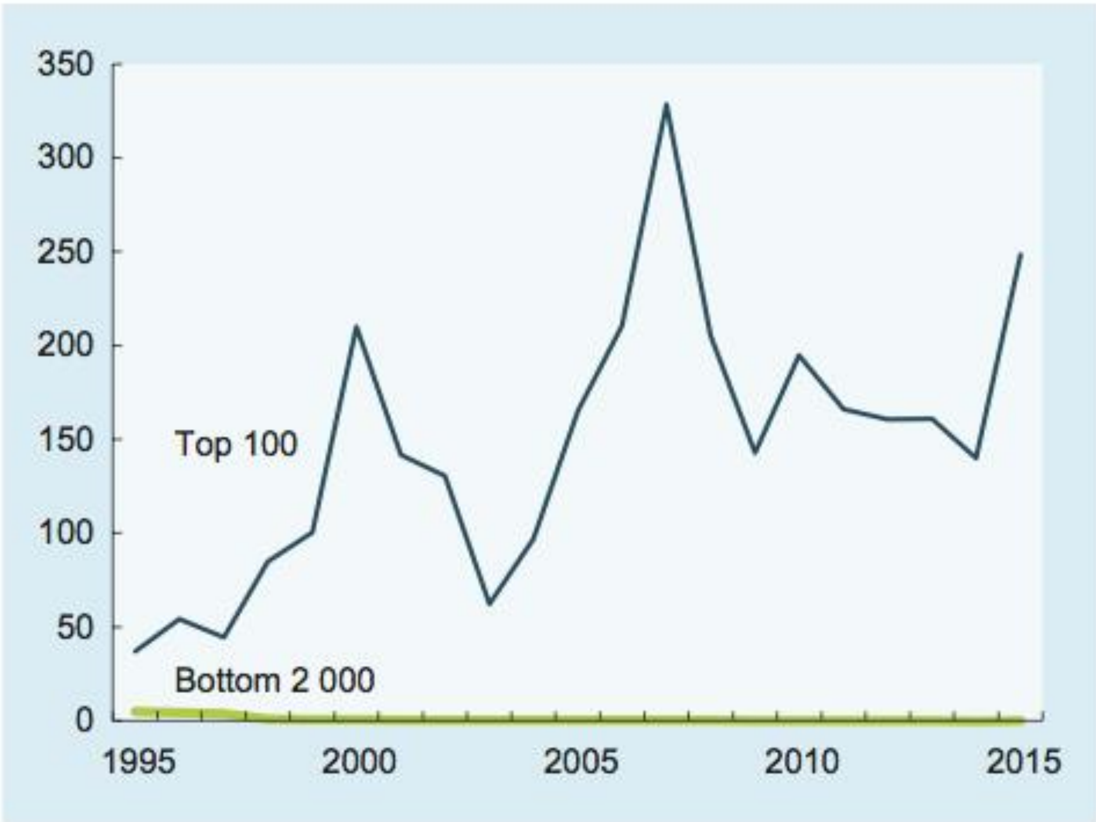
As Figure 6.1 shows, the share of surplus profits in total profits grew significantly for all firms both before and after the global financial crisis—from 4 percent during the 1995-2000 period to 19 percent in 2001-2008 and even higher, to 23 percent, in 2009-2015. The top 100 firms (ranked by market capitalization) also saw the growth of their surplus profits, from 16 percent to 30 percent and then, most recently, to 40 percent.[3]

The analysis suggests both that surplus profits for all firms have grown over time and that there is an ongoing process of bipolarization, with a growing gap between a few high-performing firms and a growing number of low-performing firms.

That conclusion is confirmed by their analysis of market concentration, which is presented in Figure 6.2 in terms of the market capitalization of the top 100 nonfinancial firms between 1995 and 2015. The red line shows the actual share of the top 100 firms relative to their hypothetical equal share, assuming that total market capitalization was distributed equally over all firms. The blue line shows the observed share of the top 100 firms relative to the observed share of the bottom 2,000 firms in the sample.

Both measures indicate that the market power of the top companies increased substantially over the 1995-2015 period. For example, the combined share of market capitalization of the top 100 firms was 23 times higher than the share these firms would have held had market capitalization been distributed equally across all firms. By 2015, this gap had increased nearly fourfold, to 84 times. This overall upward surge in concentration, measured by market capitalization since 1995, experienced brief interruptions in 2002–03 after the bursting of the dotcom bubble, and in 2009–2010 in the aftermath of the global financial crisis, and it stabilized at high levels thereafter.[4]

FIGURE 6.5 Mergers and acquisitions, total net assets, 1995–2015
(Billions of constant 2010 dollars)



Source: UNCTAD secretariat calculations, based on *CFS* database, derived from Thomson Reuters *Worldscope Database*.

So, what is causing this growth in market concentration? One reason is because of the nature of the underlying technologies, which involve costs of production that do not rise proportionally to the quantities produced. Instead, after initial high sunk costs (e.g., in the form of expenditures on research and development), the variable costs of producing additional units of output are negligible.[5] And then, of course, growing firms can use intellectual property rights and lobbying powers to protect themselves against actual or potential competitors.

Giant firms can also use their super-profits to merge with and to acquire other firms, a process that has accelerated because—as both a consequence and cause—of the weakening of antitrust legislation and enforcement.

What we're seeing, then, is a "vicious cycle of underregulation and regulatory capture, on the one hand, and further rampant growth of corporate market power on the other."

The models of mainstream economics turn out to be a shield, hiding and protecting this strengthening of corporate rule.

What the rest of us, including the folks at UNCTAD, have been witnessing in the real world is the emergence and consolidation of global rentier capitalism.

---

1. There's another reason why the long run is so important for neoclassical economists. All incomes are presumed to be returns to "factors of production" (e.g., land, labor, and capital), equal to their "marginal products." But short-run super-profits are a theoretical embarrassment. They represent a return not to any factor of production but to something else: serendipity or Fortuna. Oops! That's another reason it's important, within a neoclassical world, for short-run super-profits to be competed away in the long run—to eliminate the existence of returns to the decidedly non-productive factor of luck.

2. UNCTAD defines surplus profits as the difference between the estimate of total typical profits and the total of actually observed profits of all firms in the sample in that year. Thus, they end up with a *lower* estimate of surplus or super-profits than if they'd used a strictly neoclassical definition, which would compare actual profits to a zero-rent (or long-run equilibrium) benchmark.

3. The authors note that

> *these results need to be interpreted with caution. More important than the absolute size of surplus profits for firms in the database in any given sub-period, is their increase over time, in particular the surplus profits of the top 100 firms.*

4. The authors of the study focus particular attention on the so-called high-tech sector, in which they show "a growing predominance of 'winner takes most' superstar firms."

5. Thus, as Piero Sraffa argued long ago, the standard neoclassical model of perfect competition, with U-shaped marginal and average cost curves (i.e., "diminishing returns"), is called into question by increasing returns, with declining marginal and average cost curves.

Perfect Competition and Counterfactuals

By Stuart Birks

From: P.17 of Birks, S. (2015). *Rethinking economics: from analogies to the real world*. Singapore: Springer.

Market failure is defined in comparison to the ideal of perfect competition. An alternative is needed for comparison, and value judgments must be applied to justify one situation being considered superior to another. This raises two questions:

(i) Is perfect competition the right 'ideal'?
(ii) If it is, then given that the counterfactual is an important aspect of any policy analysis, should economic analyses compare a real situation with an unattainable ideal such as perfect competition?

Theory is, in essence, an intellectual exercise, whereby structures are presented and implications drawn. There is no a priori reason to assume that they in any way accurately reflect, or even closely approximate, the real world. At a most basic level, considering the distinction between ontology and epistemology, any description relies on the classifications afforded by the mode of expression, as with the use of language. There is not a one-to-one correspondence between words in different languages. Even if there were, the link from language to the phenomena that the words describe is not precise, if only because of the aggregation and discrete distinctions implicit in language. Consequently, descriptions cannot precisely reflect the real world.

Sen summarised the situation in his paper on 'Rational Fools' (Sen 1977). In it he described Edgeworth's analysis on the possibility of egoistic behaviour achieving general good as an abstract query, not intended to reflect reality. **Economists have taken something that was intended as an intellectual exercise, paradoxically extending it to become a combined answer to questions of 'how people actually behave' and 'how people should behave'.**

This is a serious paradox. Is no education required to improve people's economic decision making? If so, why is it accepted that education is required to increase understanding in other areas of activity? In any event, can economic decisions be considered in isolation?

Sen, A. K. (1977). Rational Fools: A Critique of the Behavioral Foundations of Economic Theory. *Philosophy and Public Affairs, 6*(4), 317-344.

Keynes was right about Quantitative Easing (QE)

By Merijn Knibbe

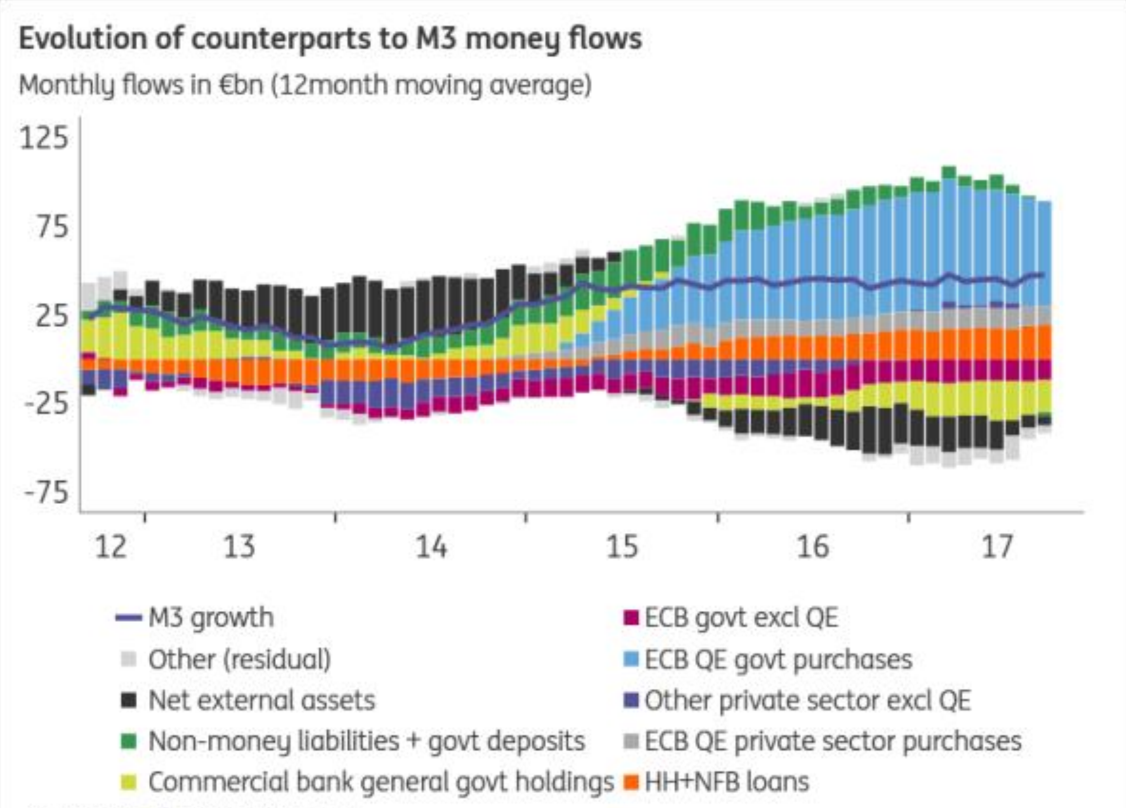
Did the growth of money caused by QE in the Eurozone (graph) stimulate economic activity? Not enough. According to John Maynard Keynes, in 'The general theory' (1936),

"*The relation of changes in M (money) to Y (income) and r (the interest rate) depends, in the first instance, on the way in which changes in M come about*."

Put differently: credit and not money makes the world go round. Money creating lending to enable household purchases of existing homes has a quite different effect on the economy than money creating lending to exiting new companies which hire lots of labor to produce live saving medical equipment (or the latest craze, L.O.L. balls, works too). Quantitative easing by central banks is a nice albeit dismal empirical example which shows that the amount of money did grow thanks to QE – but that the wrong sectors obtained the money. QE consists of a central bank buying bonds from for instance banks, pension funds and insurance companies. The graph shows that contributed quite a bit to money growth as we measure it. The money obtained by banks selling bonds (the light green bars) is not assumed to be part of 'social money' (i.e. money going around in the economy or M-3 money). The QE money paid to pension funds and insurance companies and the like (the light blue bars minus the light green bars) is however assumed to be part of M-3. But pension funds do not spend it in a useful way. They only buy other bonds and financial assets with the money. It would have been nice when pension funds, in a concerted effort with governments, had used QE money to invest in new houses, for instance in Amsterdam or London. But they generally don't. Keynes was right – just looking at M is not enough. And QE was wrong – at least the kind of QE we've seen until today. QE as we know it can be defined as the unique way to expand the amount of money in a way that influences Y the least. Even buying bad debts from banks (and writing them down) would have been a better idea.

About the graph:

The thin blue line indicates the growth of M-3 money. The light blue bars stand for the amount of QE money going to pension funds and insurance companies and the like, to pay for existing bonds. The light green bars are bonds sold by banks (money flowing into banks is not considered to be part of M-3). The net contribution of the 'MFI' sector (monetary financial institutions, i.e. banks plus the ECB) to Eurozone moneygrowth is the light blue bars minus the light green bars and the purple bars. Interestingly, the net contribution of the ECB was, until the onset of QE, negative! 'Net external assets' can be understood as money flowing to Switzerland and comparable countries.



Courtesy of Teunis Brosens

[Editor's note: originally from: https://rwer.wordpress.com/2017/11/13/keynes-was-right-about-quantitative-easing-qe/*. Follow link to see further comments and discussion.]*

How UBER Money Dominates and Distorts Economic Research on Ride–Hailing Platforms

By Norbert Häring

[Editor's Note: originally published at: http://norberthaering.de/en/32-english/news/920-uber-research]

Ride-hailing platform operator Uber is often accused of undermining labour market regulations and of overpricing at times of peak demand by "surge pricing". Uber defends itself against such accusations not only by using high-profile lobbyists, but also with the help of top-notch economists, who cooperate in exchange for exclusive data and lucrative consultancy assignments. Even reputable journals publish such sponsored analysis as if it were scholarly research.

A recent paper by renowned MIT professor Joshua Angrist with Sydnee Caldwell and Uber Research Director Jonathan V. Hall comes to the favourable conclusion that drivers benefit greatly from the fact that Uber exists. Also Princeton economist Alan B. Krueger, former chairman of the Council of Economic Advisors of the US president, wrote a paper on Uber, under contract from Uber, together with Uber's Mr Hall: an essay entitled "An Analysis of the Labor Market for Uber's Driver Partners in the United States", which makes the company appear to be a very good employer.

The survey of "Uber driver partners" on which they heavily rely, was done by a firm hired by Uber for the purpose of producing a PR-brochure. The way the research was done, and used by Kruger and Hall, is highly problematic. A potential bias, which is probably quite severe in the case of Uber with its high rate of churn, is not addressed: the survivorship bias. Dissatisfied drivers are likely to have left Uber before this satisfaction survey was taken.

Kruger and Hall do not mention that Uber cut driver compensation in many markets after the end of the investigation period. Kruger, when asked to comment, said that there was no data on that (at the time).

Uber used to publish regular earnings evaluations for New York drivers. However, despite inquiry, it has offered evaluations only up to 2015, the year in which the pay cuts started.

Krueger says he assumes that the drivers would not earn less because of such cuts. In fact, a paper exists which delivers precisely this convenient result. It is co-written by John Horton of New York University and – you guessed it – Uber economists Jonathan Hall and Daniel Knoepfle.

Data from interested parties

Krueger wrote a second paper on Uber (this time not under contract with Uber) with his Princeton colleague Judd Cramer and placed it in the May 2016 issue of American Economic Review. The main takeaway: Uber "driver partners" are used much more than normal taxi drivers. The data on Uber drivers was collected by the company, which could be considered problematic. Uber has a strong interest in the outcome, which finds that rival taxi firms are outperformed by higher efficiency rather than dumping prices, as might be inferred from the billions in losses that Uber posts every year.

In a literature survey called The Ridesharing Revolution: Economic Survey and Synthesis on Uber research for the book More Equal by Design, Robert Hahn and Robert Metcalfe from the Universities of Oxford and Chicago conclude that Uber probably has positive effects overall. As evidence they cite the study Cohen et al (2016). According to this study, Uber users realised a huge consumer surplus, which would be lost if such services were prevented by regulatory means. Only a footnote mentions that Cohen works for Uber, but readers of Hahn's and Metcalfe's chapter would not have learned, that Hahn and Metcalfe themselves are co-authors of Cohen et al, together with Uber-economist Hall and Steven Levitt, the author of the best seller Freakonomics. Asked for a comment on this, Hahn said that he would take care of the disclosure aspects the inquiry had pointed out, when working on the galley proofs for his chapter of the book.

Uber is also busy commissioning research to be published in non-US academic journals. For example, the former head of the German Monopolies Commission, Justus Haucap, co-authored a survey on mobility markets with co-authors from Uber and under contract with Uber, which was published in 2015, among other places, in the journal List Forum, which conveniently is edited by Haucap. In Wirtschaftsdienst 2/2015, a contribution from Haucap appeared that was very positive about Uber and other companies in the sharing economy. There was no reference to Haucap's contract work for Uber. When questioned about this Haucap said the disclosure had inadvertently been omitted.

Neither I nor an Uber spokesman could find a paper with Uber involvement that did not result in convenient conclusions, which Uber could use to defend itself against public criticism. This shows how problematic it is that Uber, with its financial power, dominates economic research on ride-hailing platforms.

Economic Journals play along

It is not uncommon for a company blessed with many billions of dollars of investors' money to use commissioned "scholarly" studies for its public relation goals. Unlike most such commissioned studies, however, the studies commissioned by Uber are disseminated through renowned scientific publication channels – to which the prominent and well-connected editors and authors have access. In this way, texts that border on company PR are dressed up as objective scholarly findings. After all, they appear in the prestigious series "NBER Working Papers", or reputable journals such as Industrial & Labor Relations Review (ILRR) or in the American Economic Review. Even if the results are unassailable, which is not always the case, it is Uber who is deciding who receives which exclusive data for what purpose. When the results of these papers are cited by other researchers, quite often the important fact of Uber involvement, which might have been mentioned in the original, is omitted.

Chicago economist Levitt said in a podcast, in which he talked about his Uber-related research: "I love Uber," and waxed lyrical that Uber had created an ideal market from the perspective of economists. It was clear that Uber did not have to worry about overly critical interpretation of exclusive data when Levitt approached them to gain access to it for his research. Nevertheless, Levitt reports, the company did one year refuse to provide the data, because he denied Uber a right of veto on the publication of the results. "In this case, everything was completely kosher," he concludes. That is, however, only one way of looking at it. After all, two Uber economists did act as his co-authors. They had a whole year to check and select the data that Levitt would eventually see, and ensure that it led to the desired result.

The head of the National Bureau of Economic Research (NBER), James Poterba, acknowledged that, when companies pay for studies or control access to data, it does raise difficult issues. The NBER makes sure that conflicts of interest are revealed and relies on the integrity of the associated researchers. Alan Krueger seems to see less of a danger that Uber might be able to bias research in their own favor if they are collecting and providing the data and their employees participate in the analysis. In response to my critical questions, Prof. Krueger starts by stating: "I am glad you are writing on this topic since many important studies by Joshua Angrist (professor at MIT), Steven Levitt (Clark Prize winner and professor at University of Chicago), John List (University of Chicago) and other scholars would not be possible without Uber's involvement. It would be good if you could point out that other companies should also follow Uber's example and make data available to researchers."

Krueger, who has always correctly disclosed his financial relationship with Uber, emphasises that he had contractually full control over what he writes. However, there is no such statement by his co-author Hall, who is an Uber employee and shareholder. Krueger explains that he could have cut out Hall as a co-author at any time if they had disagreed about something. Whether removing the name of the co-author of a scientific text is compatible with scientific ethics is questionable, though. Lawrence Kahn, the editor of the ILRR Review, in which the text of Hall and Krueger was published, was also invited to comment on this issue. He had no answer, apart from inviting me to write a comment for ILRR, which would then be examined by reviewers for publication.

Contact the Association

Journal editors:
RWER: Edward Fullbrook fullbrook@worldeconomicsassociation.org
Economic Thought: ETEditor@worldeconomicsassociation.org
World Economic Review: wereitor@worldeconomicsassociation.org

Conferences: Chair of Conference Organizing Committee:
conferences@worldeconomicsassociation.org

WEA Commentaries editor: Stuart Birks kstuartbirks@gmail.com

WEA Commentaries
(formerly The World Economics Association Newsletter)
is published in the UK by the World Economics Association.