ISSN 2049-3274

Volume 6, Issue 5

October 2016

World Economics Association Newsletter

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.

Inside this issue:

WEA Online Conference
Food and Justice: Ideas for a new global food agenda? 5th November – 5th December 2016

WEA young economists Facebook group
(now 6000+ members)

Past Newsletters available at:
http://www.worldeconomicsassociation.org/newsletters/

WEA Pedagogy Blog

...welcomes posts about your experiences and suggestions on teaching and learning economics, with a strong focus on methods leading to deep understanding of current real world economic issues.

World Economics Association

Voluntary annual membership fees:

http://www.worldeconomicsassociation.org/membership/annualfees

Crash and learn?

By David Ruccio

[Reproduced from here on the RWER Blog]

The case for changing the way we teach economics is—or should be—obvious.

It certainly is apparent to the students of Manchester University's Post-Crash Economics Society and to the other 44 student groups, members of Rethinking Economics, pressing for pedagogical changes on campuses from Canada to Italy and from Brazil to Uganda.

But as anyone who teaches or studies economics these days knows full well, the mainstream that has long dominated economics (especially at research universities, in the United States and elsewhere) is not even beginning to let go of their almost-total control over the curriculum of undergraduate and graduate programs.

That's clear from a recent article in the *Financial Times*, in which David Pilling asks the question, "should we change the way we teach economics?"

Me, I've heard the excuses not to change economics for decades now. But it still jars to see them in print, especially after the spectacular failure of mainstream economics before, during, and after the worst economic crisis since the first Great Depression.

Here's one—the idea that heterodox economics is like creationism, in disputing the "immutable laws" captured by mainstream theory:

> Pontus Rendahl teaches macroeconomic theory at Cambridge. He doesn't disagree that students should be exposed to economic history and to ideas that challenge neoclassical thinking. (He prefers the word "mainstream", since neoclassical, like neoliberal, has become a term of near-abuse.) He is wary, however, of moving to a pluralist curriculum in which different schools of thought are given similar weight.
>
> "Pluralism is a nicely chosen word," he says. "But it's the same argument as the creationists in the US who say that natural selection is just a theory." Since mainstream economics has "immutable laws", he argues, it would be wrong to teach heterodox theories as though they had equal validity. "In the same way, I don't think heterodox engineering or alternative medicine should be taught."

Rendahl also argues that students are too critical of the models they encounter as undergraduates:

> When we start teaching economics, we have to teach the nuts and bolts." He introduces first-year students to the Robinson Crusoe model, in which there is only one "representative agent". Later on, Friday is brought on the scene so the two can start trading, although no money changes hands since transactions are solely by barter. (Money and credit are strangely absent from most economic curricula.)

Somehow, the "simplification" involved in presenting a theory of capitalism without money and credit—and therefore without the mechanisms that, from the start, invalidate Say's Law—is presumed to be innocent.

Then, of course, there's the ever-present worry about banishing mathematical modeling, which is taken to be the necessary condition for intellectual rigor:

> Angus Deaton, who won the Nobel Prize in economics and teaches at Princeton, says economics is a broad church, but one that needs to be kept rigorous.
>
> He gives the example of Daron Acemoğlu, a "young superstar" at the Massachusetts Institute of Technology, whose research includes the study of how institutions foster or inhibit growth. "He's a very good example of the way things ought to be going, which is you do history but you know enough mathematics to be able to model it too. Banishing mathematics is not the solution," he says. "The model is the cross-check on whether you actually know what you're talking about."

For economists like Deaton, rigor is identified with mathematics, not with knowing the assumptions of a theory or being acquainted with various theories.

And, finally, there's the idea that part of economics is broken but the rest is just fine:

> In Manchester, Diane Coyle also defends the basic methodology of economics. She says there is confusion among critics between microeconomics, the study of the behaviour of individuals and firms, and macroeconomics, the study of whole economies. Macroeconomics, she admits, "is broken". But microeconomics is both robust and often verifiable with real-world data. What, she asks, can heterodox economists contribute to typical concerns of microeconomics, such as discovering the right mix of policy incentives to discourage obesity?

In Coyle's case, the assumption is that there's a set of theory-independent, "real-world data," against which neoclassical microeconomics has been compared and ultimately verified. That, of course, is news to other economists, who use different theoretical lenses, and see very different data.

The assumptions built into each and every one of these defenses of mainstream economics and attacks on heterodox economic theories as well as any hint of pluralism in the teaching of economics are, at best, outdated—the leftovers from positivism and other forms of post-Enlightenment scientism. They comprise the "spontaneous philosophy" of mainstream economists who have exercised hegemony in the practice and teaching of economics throughout the postwar period.

And, yes, Pilling is right, when that hegemony is challenged, as it has been by economics students and many economists in recent years, "the clash of ideas gets nasty."

Blind leading the blind

By Peter Radford

[Reproduced from here on the RWER Blog]

A few days ago David Ruccio posted an article titled "Crash and Learn" on the state of economics education. I want to elaborate a little further, although my usual skepticism on this subject does bridle a tad at the concept of economics education. Is that the same as "military intelligence"?

Anyway, in that article is this quote:

In Manchester, Diane Coyle also defends the basic methodology of economics. She says there is confusion among critics between microeconomics, the study of the behaviour of individuals and firms, and macroeconomics, the study of whole economies. Macroeconomics, she admits, "is broken". But microeconomics is both robust and often verifiable with real-world data. What, she asks, can heterodox economists contribute to typical concerns of microeconomics, such as discovering the right mix of policy incentives to discourage obesity?

Therein, as someone once said, lies the tale.

Macroeconomics is "broken". I quite agree. It's nice to see an august member of the trade admitting that snake oil is snake oil no matter how clever the mathematics looks. Not that I blame the math. You can't make something silly into something smart simply by expressing it in the formal language of math. If the root is rotten so is the formal outcome.

But that part I like more is that she goes on to laud the robust nature of microeconomics.

Wrong.

Micro, if anything, is worse than macro. It is so utterly disconnected from reality that it is incapable of anything other than talking about itself. Which it does loudly and proudly.

Let's begin with a broad observation: one of the problems with the mess that is macro is that for decades we have been told to build on micro foundations. Not only does this deny the existence of any phenomenon that might emerge from higher level interactions between lower level phenomena, it assumes that micro has anything useful to say. Yet it is at the level of micro that much of the absurdity of modern economics has festered. Rational behaviour in all its ridiculous glory is a tenet of micro. So is all the nonsense about perfection of information. To pick up a microeconomics text is to enter an alternative universe where real people have been replaced by packets of data especially created by economists so that their incentive models, constrained optimization methods, and other paraphernalia all work smoothly.

These packets of data, we call them 'agents', have no choice even in the artificial domain of rational choice. Why? Because the rationality impose upon them is uniform. It conforms to special rules. Those rules dictate the response an agent gives in any situation. Those responses are thus entirely determined, not by the agent, but by the combination of rules and circumstances. So much for freedom of choice. No one, in this setting, makes a whimsical choice. Indeed they never change their mind. Ever. Instead they plod on under the tyranny of a rule-laden simplicity obeying the orders of their economist experimental overlords.

This is not human behaviour, the essence of which is the variety of response and the diversity of interpretation of identical circumstances. It is exactly that diversity that promotes robust and sustainable growth. It provides alternatives. It opens spaces for argument and thus learning. Most importantly, it is the groundwork for survival in the face of the endemic uncertainty that permeates life. The basis of all problem solving is the possibility of alternatives.

Microeconomics in its mainstream versions falls far short of talking about this kind of real world problem solving; the kind that takes place in unconstrained open systems; the kind that is influenced by higher level pressures like social power structures bearing down on the agent; the kind that real people have to make when faced with limited or asymmetrical information; and certainly not the kind that deals with complex and manifold solutions.

No, microeconomics is deeply deficient and is thus the root error in economics. It is a badly misshapen replica of a small aspect of the totality of human behaviour. But it is what economists play with. Dabbling, as some do, with institutional or incentive structures can only partly mask the error. The same goes for tricks like the introduction of transaction costs. It is relatively easy to use the techniques of economics as it is now taught to advise on the construction of contracts, incentives and so on. All you have to do is to limit the responses of your agents, give them a limited palette of possibilities, and to presume that they all behave the way they do in the utopia of the textbooks. All you need to do, in other words, is shackle them far from reality.

One more thing: the typical concerns of microeconomics have wandered so far afield from the core of economic behaviour and into distant fields such as obesity precisely because of the failure to create a microeconomics that could deal with, explain, or predict that care behaviour. All micro has become is a sophisticated technique. It is a technology or a method. It has no explanatory power in real world economies so it has been exported to deal with problems elsewhere.

Perhaps it has value out there. I do not know. But it is certainly not the robust portion of economics.

As for the aspect of microeconomics that purports to be the study of business firms. The less said the better. The entire purpose of business is to create and then exploit asymmetries of information. This is accomplished by the conversion of learning into routine and replicable activity so that cost can be driven out and profit enhanced. It has nothing to do with maximization or any of the other oddities that prowl about in the economics textbooks. But it does have a lot to do with the existence and history of social structures and networks, power relationships, culture, technology, geography, and the institutions that govern our lives.

No. Micro is just as big a bust as macro.

Models and measurement in economics 4—consumption

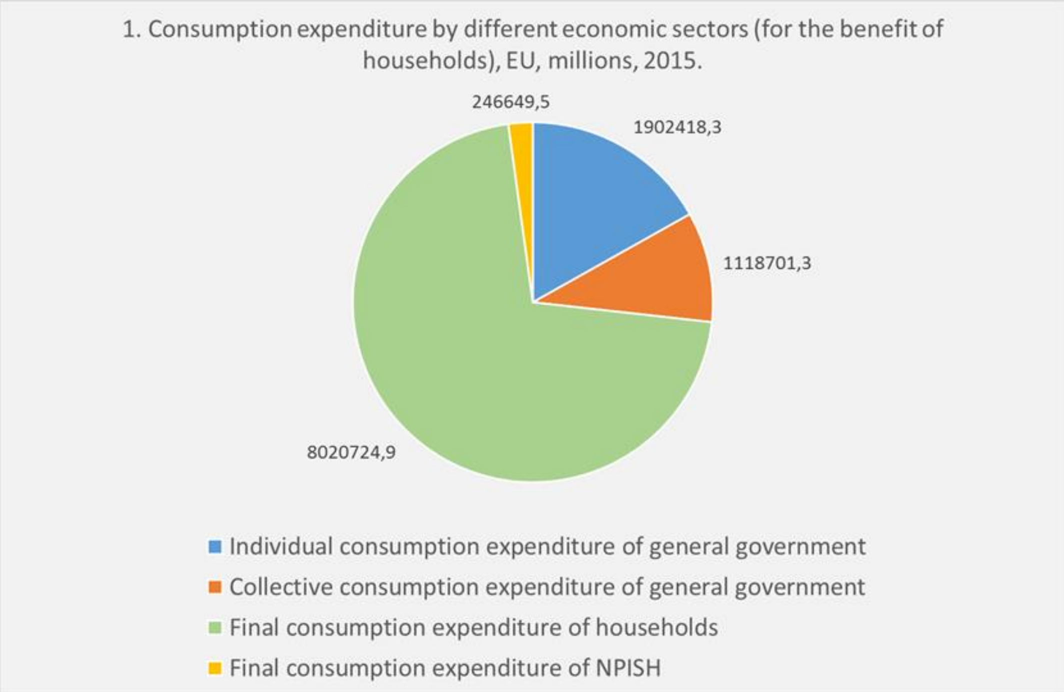
By Merijn Knibbe

This piece benefited from remarks by Dian Coyle and Josh Mason

Introduction.

This is the fourth piece in a series which investigates the large and sometimes fundamental differences between macro-economic concepts as used by economic statisticians in the national accounts and as used by (neoclassical) macro-modelers in the so called DSGE (dynamic stochastic general equilibrium) models. The first three pieces (here, here and here) were an introduction, a general overview of the accounts and a piece about the concept of capital. This piece is about the concept of the most important expenditure category of the national accounts and the DSGE models: consumption. I will investigate the different concepts which are used to define 'consumption', paying especial attention to the question whether public goods and services are included and to the question whether consumption is about acquiring goods and services or about using them.

- What is consumption? The national accounts have a well-defined and estimated concept of consumption which encompasses purchases by households but also includes public goods provided by the government to households as well as by 'NPISH' (Non Profit Institutions Serving Households, like unions and churches). By doing this the national accounts extend the concept of consumption beyond market exchange and into the realm of gift exchange as well as 'tax exchange'. DSGE models follow another track. Public goods and NPISH are excluded from household consumption and only market exchange is taken into account. This difference is remarkable. The inclusion of public goods within the consumption boundary has a long history in economics and can be traced back to at least Adam Smith (Smith, 1776). Smith did not call it 'consumption' but in the *Wealth of Nations* the entire fifth and last part of the book is devoted to the necessity of public goods and services and, with a sterling emphasis on evolving institutions, the changing and growing importance of what nowadays is called 'government consumption' (i.e. household use of goods and services purchased or produced and distributed by the government). Graph 1 shows that at present both 'individual government consumption' (education!) as well as 'collective government expenditure' (building and maintaining roads!) are non-trivial. So, why the difference between the statistics and the models?



I do not have a satisfying answer to this question. Since the days of Smith the realm of household but also of government consumption has greatly increased. Nowadays we use sewer systems, health care has changed beyond recognition, motorized ships, trains, bicycles, cars and planes have, together with a total rebuilding of our roads and canals and other transport systems, totally revolutionized the way we travel, and education has become compulsory and largely a government service. Next to this, the economic concept of consumption has widened too, as is often stated in economic textbooks. After the 'marginal revolution' in economics in the nineteenth century work considered unproductive by Smith, like personal services, is considered productive and therewith by definition also included in our definition of consumption. The Eurostat database even contains data on the turnover and price level of prostitution (COICOP code cp 122). But – less often stated in textbooks - the economic concept of consumption, or at least the neoclassical one, became more restrictive, too. Unlike Smith, Alfred Marshall, one of the marginalist economists, included personal services in his concept of consumption, but also unlike Smith he excluded individual and collective consumption expenditure by the government (Marshall, 1890), an exclusion which still is a characteristic of the modern 'marginalist' DSGE models. This despite the classic (7900 google citations!) 1954 Samuelson article which (without mentioning Smith but with a profound use of the metaphor of 'the invisible hand') introduced the Smithian concept of public provision of goods and services into neoclassical economics (Samuelson 1954). It is important to note that Samuelson, a cunning writer if ever there was one, explicitly used and connected the phrases 'public expenditure' and 'collective consumption'.[1] But though 'public expenditure' is included in the DSGE models it is, ignoring the work of Samuelson, not supposed to add to 'utility' and is therewith considered to be wasteful by definition (see for instance formula 55 and 56 of a paper which elaborates the benchmark DSGE model of the ECB, Bokan e.a. (2016)). Aside of this, DSGE models also exclude consumption of goods and services provided by NPISH.

- The DSGE concept of consumption not only excludes government provision of goods and services, it also only recognizes market transactions and has a fundamental forward looking, intertemporal character.[2] The totally forward looking character is related to the reformulation of General Equilibrium by Arrow and Debreu to include all transactions until the end of time (really…), as, in the parlance of DSGE models, 'the models look at a complete set of Arrow-Debreu commodities', including, to push this point, an apple bought in Rome in 2023. A trade-off between present and future transactions is obtained by the interest rate or, one should state, 'an' interest rate as it is not entirely clear to me which interest rate households are supposed to use (the classical formulation of this is Samuelson (1937) who was however quite critical of this idea). Goods and services in these models are generally non-durable, which means that there is no stock of durable goods like cars – the model is in the end about purchasing goods and services, not about using them. Bokan e.a. (2016) however introduce a housing sector (houses are the durable good par excellence) which rents houses to households. As the models only recognize market transactions and do not recognize non-market production of housing services by households living in their own house this is the only way they can model this. Bokan e.a. do not include the price and volume estimates of housing services of the national accounts – or any other estimate of this whatsoever – into their model.
- A forthright consequence of treating government consumption as wasteful by definition is that using DSGE models to gauge, for instance, the consequences of cuts to the provision of public goods in Greece will not show any decline of 'utility' in the models, noting also that, in the models, 'unemployment is leisure' which means that unemployment actually increases 'utility'. In contrast, using national accounts to map the consequences of such a decline of government expenditure will show a decline of production and employment, a post World War II record decline of minus 25%, as it happened. This is along with a matching increase of unemployment and (not measured by the accounts) misery and (measured by the accounts) a decline in for instance medical services. Concepts of production, prosperity and consumption as well as the choice of the consumption boundaries do matter! Remarkably, the assumed wasteful nature of government spending is not a *necessary* element of the models. DSGE models with non-wasteful government spending are possible, as indicated by the title of a 2012 working paper by Yasuhara Iwate, '*Non-wasteful government spending in an open economy estimated DSGE model: two fiscal policy puzzles revisited*' (Iwata 2012). For the geeks: one can either include government consumption directly into the utility function or use the concept of Edgeworth complementarity, i.e. the idea that a car is useless without (public) roads. But such DSGE articles are black swans. To return to the questions posed above (why the differences between the statistics and the models): we can at least state that excluding government consumption from the models is, considering Smith (1796), Samuelson (1954) and Iwate (2012), a conscious, rational choice and not a unavoidable necessity. And a choice which is pretty convenient for economists who defend brutal austerity.
- There are not just differences between the statistics and the models. A common aspect of both of them is that they are transaction based. Consumption, as defined in the national accounts, is a monetary flow concept based upon a restricted period of time. It is not about the use of goods but about acquiring goods and services. There are also notable imputations of non-monetary, non-market transactions like imputed rent of owner occupied dwellings as well as the imputation of 'Fisim', which tries to divide net interest paid by households into a fee for financial services and 'pure' interest. See Coyle, 2014, for a brief and not very affectionate investigation of this last concept. These imputations are not without consequences for understanding the national accounts. Recently, the ONS has stripped national accounts household income from all kinds of imputations to estimate a monetary concept which is closer to the actual experience of monetary income by households (Curtis, Davies and Weston, 2016). This stricter monetary concept of income, which better matches income in all kinds of income surveys and is closer to the experience of households, showed in 2008-2009 *a much stronger increase* in the monetary savings rate of households than the national accounts concept. This means that the crisis was for a much larger part

caused by balance sheet effects than indicated by the national accounts income concept. As far as I'm concerned, this totally underscores the need for monetary macro-economic variables which do not estimate welfare or prosperity but the circular flow of monetary expenditure, income and production.[3]

- Restricting consumption to acquiring instead of using goods is questionable. Purchasing potatoes is not the same thing as cooking and eating homemade Belgian fries (a recipe here), buying a Dacia Logan is not the same thing as driving it. A convincing case can be made that to estimate welfare or prosperity an estimate of real consumption, like driving your car and eating homemade meals is more important than an estimate of the acquisition of goods and services. But we're living in a monetary world. And, as explained in the second of these posts, national accounts do not try to estimate prosperity but try to estimate the circular flow of monetary income, expenditure and production. The Greek example however clearly shows that a clear relation between (changes in) these flows and (changes in) prosperity exists. Which is one reason why, guided by the ideas and person of John Maynard Keynes and against the background of high unemployment during the Great Depression and the war effort of World War II, much emphasis was placed upon the difference between present monetary flows and their maximum. This is an emphasis which, considering contemporary discussions about the level of potential income, never disappeared. Despite this, it is clear that at any given moment the stock of cars and roads is more important to consumers than the flow of new cars and the building of new roads. An analysis of this surely worthwhile and economists should probably pay more attention to this. This is however not what the national accounts intend to estimate – these were established to estimate the circular monetary flows of production, income and expenditure (and have been extended to include information about assets, debts, employment and money as well as granular data on sub-sectoral flows).
- In the text above, I deliberately often used the phrase 'acquiring goods and services'. The flow of national accounts consumption is not just about the purchase of goods and services by households. As the ESA 2010 states: "*final consumption expenditure consists of expenditure incurred by resident institutional units on goods or services that are used for the direct satisfaction of individual needs or wants or the collective needs of members of the community … actual final consumption consists of the goods or services that are acquired by resi-dent institutional units for the direct satisfaction of human needs, whether individual or collective.* Below, a snapshot from table 3.2 from the ESA 2010 explains this definition in a little more detail, note that actual final consumption is considered to be consumption *by households,* of services like education but also of defense. Some might not see this last kind of consumption as 'optimizing utility'. But that's not the point. Households do pay for it and therewith do consume it, by definition.

Table 3.2 — Sector making expenditure

	Government	NPISHs	Households	Total acquisitions
Individual consumption	X (= Social transfers in kind	X (= Social transfers in kind)	X	Households actual individual final consumption
Collective consumption	X	0	0	Government's actual collective final consumption
Total	Government's final consumption expenditure	NPISHs final consumption expenditure	Households' final consumption expenditure	Actual final consumption = Total final consumption expenditure

X: applicable
0: not applicable

To give an idea of the granular nature of the national accounts it is useful to give some detail about the national accounts definition of government consumption (ESA 2010):

"Alternatively, individual consumption expenditure of general government corresponds to division 14 of the classification of individual consumption by purpose (Coicop), which includes the following groups:

14.1 Housing (equivalent to COFOG group 10.6)
14.2 Health (equivalent to COFOG groups 7.1 to 7.4)
14.3 Recreation and culture (equivalent to COFOG groups 8.1 and 8.2)
14.4 Education (equivalent to COFOG groups 9.1 to 9.6)
14.5 Social protection (equivalent to COFOG groups 10.1 to 10.5 and group 10.7).

***3.106** Collective consumption expenditure is the remainder of the government final consumption expenditure. It consists of the following COFOG groups:*

(a) general public services (division 1);
(b) defence (division 2);
(c) public order and safety (division 3);
(d) economic affairs (division 4);
(e) environmental protection (division 5);
(f) housing and community amenities (division 6);
(g) general administration, regulation, dissemina-tion of general information and statistics (all divisions);
(h) research and development (all divisions)."

Household purchases are defined and estimated in an even more granular way. Consumption includes some but not all household production for own use. A clear example is production from vegetable gardens (insignificant in rich countries but crucial in some African ones) and imputed rents for owner occupied dwellings. Unpaid housework is excluded. If possible, equivalent market rental prices are used to value the service of owner occupied houses (kept clean and comfy by unpaid household labor). Considering the existence of a market alternative (renting a house) a case can be made to do this. There are however reasons why people do not use the market alternative and a case can also be made that a production costs or a 'hedonic' alternative should be used.
Summarizing: the accounts have a broad, detailed, well defined and estimated and backward looking monetary flow concept of consumption which includes non-market transactions. The DSGE models use a restricted, non-empirical and totally forward looking concept of consumption which only looks at market transactions. Neither the accounts nor the models look at the use of (durable) consumer goods. The accounts might however be a good idea to keep the use of all kind of imputations to the accounts as limited as possible and to show purely monetary income and expenditure next to concepts of income an expenditure which include all kind of non-monetary production.

Literature

Bokan, Nikola, Andrea Gerali, Sandra Gomes, Pascal Jacquinot and Massimiliano Pisani (2016). 'EAGLE-FLI. A macroeconomic model of banking and financial interdependence in the euro area', *European Central Bank working paper series no. 1923*. Available here.

Coyle, Diana (2014). *GDP: a brief but affectionate history.* Princeton, Princeton university press.

Eurostat/European Commission (2013). *European system of accounts ESA 2010*, available here.

Marshall, Alfred (1890). *Principles of economics. An introductory volume.* MacMillan and Co: London. Online version available here.

Samuelson, Paul (1937). 'A note on the measurement of utility' in *The Review of economic studies 4(2):*155-161.

Samuelson, Paul (1954). 'The pure theory of public expenditure' in *The Review of Economics and Statistics* 36(4): 387-389.

Knibbe, Merijn (2007). 'De hoofdelijke beschikbaarheid van voedsel en de levensstandaard in Nederland, 1807-1913' in *Tijdschrift voor Sociale en Economische Geschiedenis 4(4):71-107.*

Sekera, June (2016). *The public economy in crisis. A call for a new public economics.* Heidelberg: Springer.

Smith, Adam (1776). *An inquiry into the nature and causes of the wealth of nations.* Methuen & co.: London. Online version of the fifth edition, available here.

Davies, Phillip, Nicola Curtis and Luke Weston, 'Alternative Measures of Real Households Disposable Income and the Saving Ratio: June 2016'. Available here.

1. See Sekera, 2016, for a criticism of the rational, neoclassical nature of Samuelson's consumer of public goods.
2. Samuelson was well aware that including public consumption into neoclassical economics also required a widening of the scope of transactions beyond market transactions, considering the last sentence of his 1954 article: "*Political economy (i.e. market oriented neoclassical economics, M.K.) can be regarded as one special sector of this general domain (i.e. all transactions, M.K.), and it may turn out to be pure luck that within the general domain there happened to be a subsector with the "simple" properties of traditional economics*".
3. Which does not mean that non-monetary variables are not important. See Knibbe, 2007, for an estimate of per capita availability of food in the Netherlands, 1807-1950.

Economic growth is not "natural": re-thinking current economic challenges

By Maria Alejandra Madi
[Reproduced from the here on the WEA Pedagogy Blog]

Since the late 1980s, the World Bank has been defending a policy agenda that reinforces the free market model of endogenous economic growth. In this model human capital plays an outstanding role since the acquisition of abilities would increase productivity levels and, as a result, income levels. This is because level of product *per worker* depends on the increase of productivity. Regarding the human capital model, long run growth in each country is analysed considering the particular features of infrastructure and human capital. The divergences verified in the levels of product *per worker* among different countries can be attributed to the abilities accumulated by labour and to the infrastructure of the economies. The emergence and diffusion of the model of endogenous growth reflected the intellectual victory of ideas about the supremacy of the competitive economic order and the rejection of interventionism to promote economic growth and social justice. Considering the relevant economic outcomes of this intellectual victory, the main question that arises in the context of economics education is: *What is at stake in the economic discourse that privileges the economic competitive order as the pillar of economic growth?*

The competitive order, as a necessary one, is the central pillar of Hayek's theoretical construction. Hayek's economic discourse "naturalizes" the competitive market as a superior arrangement. However, the "naturalization" of the competitive market – by considering it a "natural" arrangement – is in reality undermined by political interests that play a crucial role in economic and political decision procedures, and in the institutional management of such issues.

Taking into account a real-world approach to economic growth, it is relevant to highlight the ideas of Keynes, Minsky, Kalecki, Rifkin in order to re-think current economic growth challenges

1. Uncertainty

John Maynard Keynes enhanced a more fruitful comprehension of the real-world where the outcomes of the entrepreneurs' decisions do not behave stochastically, that is to say, they are not predictable. In his opinion, the process of decision making is based on conventions. As uncertainty is inherent to all entrepreneurs' decisions, Keynes relied on the concepts of credibility and degree of confidence in a conventional judgment that is historically built within the markets. In a specific historical setting, the average opinion of entrepreneurs on future scenarios shapes a convention based on a precarious set of expectations about the behaviour of aggregate demand (consumption, investment, net exports, for example). Keynes focused the analysis on the expectations associated with investment decisions in a business environment where uncertainty about the future pervades the decision-making process. The very nature of wealth management under uncertainty in a monetary economy is the cause of business instability. In this sense, due to uncertainty about the future, entrepreneurs could postpone spending decisions and search for alternative forms of wealth management. One of the main theses in his contributions to policy making, as opposed to the classical economists that defend the free-market system, is that government policies and actions could play a fundamental role in shaping a business environment that could reduce uncertainty and favour investment decisions.

2. Finance and business cycles

Hyman Minsky considered the role of finance in the business cycle and developed the financial instability hypothesis which states that financial crises are inherent in the capitalist economy. From the Keynesian tradition, Minsky considered the capitalist economy as a set of interrelated balance sheets and cash flows among income-producing companies, households and banks. Minsky adds to our understanding that banks play a crucial role in determining the path of sustainable economic growth since investment decisions are affected by available finance. Through the period of boom, entrepreneurs borrow from banks and accumulate debts. A sentiment of euphoria takes over and entrepreneurs begin to be over-optimistic in their short-term expectations while financial innovations impact upon banks' assets and liabilities.

During the expansionary period of the business cycle, investment demand increases, and so does the demand for finance and funding. However, as financial fragility grows, lower levels of loans increase uncertainty and pessimism in the economy. Banks become unwilling to lend money because of higher credit risk since income flows turn out to fall short of debt repayment plans. As the investment decisions collapse, through the multiplier process, employment, income and consumption fall leading to a recession. If the financial crisis also leads to a sharp decline in prices, this can result in debt deflation where asset prices fall. In short, while considering the relevance of investment as the unstable component of aggregate demand, the Minskyan approach also points out how banks' strategies and weak financial regulation tend to induce financial fragility.

3. Income distribution

Michael Kalecki's theoretical contribution elucidates how profits grow throughout cyclical fluctuations and economic crises when the capitalist class strengthens its power relative to workers. Besides, the Polish economist shows how the evolution of income distribution affects the evolution of aggregate income. The dynamics of income and employment mainly depends on the level of spending of the capitalist class. Given the income distribution in each economic sector, "*the capitalists earn what they spend*". However, the aggregate level of the workers' consumption is subordinated to the consumption and investment decisions of the capitalist class. That is why Kalecki states "*the workers spend what they earn"*. In addition, his analysis of the oligopolistic trends in contemporary capitalism sheds light on important distributive issues at the micro level. The analysis of the *role of the markup* over prices introduces distributive challenges – not just between capitalists competing for market shares but also between capitalists and workers. Indeed, the evolution of prices depends both on the market power of firms and on the trade union struggles to win higher nominal and real wages.

4. Technology and labour conditions

Technology transforms the labour scenario as the result of the diffusion of new practices at the micro-level. More recently, the technological impact on the future of work was analysed in depth by Jeremy Rifkin. According to him, we are facing a new phase of history – a Third Industrial Revolution – that is characterized by the steady and inevitable decline of jobs in the production and marketing of goods and services. Today, the Third Industrial Revolution is a convergence of internet and renewable energy. The internet technology and renewable energies are currently starting to merge in order to build a new infrastructure for a Third Industrial Revolution (TIR) that will change the distribution of economic power in the 21st century. Indeed, changes in power will provoke a fundamental reordering of human relationships – from hierarchical to lateral power – that will impact the way we conduct economic and social activities. The intelligent TIR infrastructure—the Internet of Things—will virtually connect every aspect of economic and social life via sensors and software to the TIR platform. The connections will feed Big Data to every node—businesses, homes, vehicles, etc. — in real time. In turn, the Big Data will be analysed with advanced analytics, transformed into predictive algorithms, and programmed into automated systems. On behalf of this high-technology revolution, the number of people underemployed or without work will rise sharply since computers, robotics, telecommunications, and other cutting-edge technologies are replacing human beings in manufacturing, retail, and financial services, transportation, agriculture, and the government sector. In truth, in an increasingly automated world, workers are being polarized into two forces: on one side, an elite that controls and manages the high-tech global economy; and on the other side, a growing number of displaced workers who have few prospects for meaningful job opportunities.

***

In contemporary Western societies, most people experience a feeling of uneasiness about the current model of growth that reveals an unsustainable path. For many, the outstanding feeling is that, in current societies, the outcomes of so called "progress" have been economic instability, deleterious working conditions and inequality.

Our critical gaze is fixated on the mainstream mode of thinking about economic growth that obscures current real-world challenges. In this attempt, rethinking relevant theoretical issues about economic growth indicates the need for a deep reformulation in the economics curriculum.

References

Kalecki, M. (1954) *Theory of Economic Dynamics*. London: Allen, Unwin.

Keynes, J. M. (2010 [1936]) *The General Theory of Employment, Interest, and Money*.Mansfield Center, Connecticut: Martino Publishing.

Minsky, H. P. (2008) *Stabilizing an Unstable Economy.* New York: McGraw Hill.

Rifkin, J. (2011) *The Third Industrial Revolution: How Lateral Power Is Transforming Energy, the Economy, and the World*. Palgrave Macmillan

World Bank (2004) Making Services Work for Poor People, World Development Report Copublication of the World Bank and Oxford University Press.

Economic Depression: A commentary on Paul Romer's *The Trouble With Macroeconomics*

By David Orrell

In a previous article for this newsletter, I wrote about the rather long and withdrawn grief process that the economics profession is working through, as it comes to terms with its role in what has become known as the Great Financial Crisis. Initial denial was followed by anger towards critics, which in turn was followed by a bargaining stage. The latter (I used Dani Rodrik's book *Economics Rules* as an example) involved claims that there is nothing seriously wrong with economic models, it was just that the wrong ones were used. According to this view, critics are just attacking a simplified straw man. (We will stop attacking the straw man when it stops threatening to blow up the world financial system.)

Signs that we may be proceeding to the next stage of the grief process, depression, are evident in the recent working paper (available online) by Paul Romer, *The Trouble With Macroeconomics*. The first sentence of the abstract announces that "For more than three decades, macroeconomics has gone backwards." It goes on to describe the author's "pessimistic assessment of regression into pseudoscience." It mentions the "serious failure" of economists such as Robert Lucas, who announced in 2003, a little prematurely, that the "central problem of depression prevention has been solved." Decidedly non-upbeat section titles include "Post-Real Models", "Loyalty Can Corrode The Norms of Science", "Back to Square One", and "The Trouble Ahead For All of Economics".

The paper is based on a lecture given in January 2016, and is forthcoming in *The American Economist*. Just to be clear, this is not a magazine bent on overthrowing the status quo; indeed its web site has an entire section devoted to "Articles from Nobel Laureate Authors". Typical paper titles are more like "My Life Philosophy" (Paul Samuelson) and "How I Work" (Paul Krugman) and "Some Gleanings From My Mind" (I made that up). So this appears to represent a significant stylistic departure. And as Paul Mason observed in *The Guardian*, Romer's paper is important exactly because he is not an outsider or a rebel, but "a doyen of the profession, and from the heart of the US academic mainstream."

The paper's title is modelled on that of Lee Smolin's 2006 book *The Trouble With Physics*. In the same way that elegant but unfalsifiable string theory has taken over high-energy physics, so mainstream economics has increasingly emphasised elegant but unfalsifiable mathematical models over experimental reality. Romer for example notes that many economic models suffer from the problem that they have more parameters than can be determined from the data. Economists therefore resort to making up imaginary inputs which give the desired answers. In string theory these are called supersymmetric particles, and have names like selectrons, squarks, and winos; Romer gives the equivalent economics versions names such as phlogiston, trolls, gremlins, aether, and caloric.

However the problems are as much sociological as they are mathematical. Just as string theory is characterised by what Smolin described as "groupthink" about the correct way to approach problems, so some economists see it as "an extremely serious violation of some honor code for anyone to criticize openly a revered authority figure ... neither facts that are false, nor predictions that are wrong, nor models that make no sense matter enough to worry about."

(It is interesting to compare that with the self-image that many economists enjoy of being open to criticism. As one wrote, while commenting on one of my books: "Economists welcome criticism. In the academy, we are well-known, if not infamous, for being direct, abrupt, and rude in criticizing each other (and others). There is a very healthy discussion about methodology. Bring it on.")

Striving for acceptance

The paper is written with commendable honesty, along with a good dose of sarcasm, and an obvious concern for the state of economics. As Romer writes: "science and the spirit of the enlightenment are the most important human accomplishments. They matter more than the feelings of any of us." And it makes a nice change from the usual, rather self-congratulatory commentary that "celebrates steady progress" as Romer describes.

However, while readers of *The American Economist* may be shocked by the paper's content, it will be less surprising to those people who never bought into the orthodoxy in the first place, or have found themselves on the other side of groupthink. The comparison with string theory (to which I would add a shared fascination with a certain type of aesthetics) is apt, but it would have been nice to supplement quotes from dissident physicists with something from the dissident economists who have been saying the same things for decades. Instead, the focus is on spats between various Nobel-winners and other leading insiders.

For example, one of Romer's main criticisms of mainstream theory is that it ignores or downplays the role of money. Models typically say (or assume) that the money supply plays only an incremental role in the economy. But as Romer points out, citing some Volcker-era data: "If the Fed can cause a 500 basis point change in interest rates, it is absurd to wonder if monetary policy is important."

It is certainly refreshing to read this, since the discussion of money as anything other than a passive medium of exchange seems to be almost taboo in proper economics circles (see my review of Rodrik's book). But again, there is no acknowledgement that these issues have long been debated outside of the mainstream.

The reason this is important is not just to give credit where credit is due (we're well past that point); it is because this deafness to other voices is at the root of the "trouble with economics."

Of course, depression is a state of mind that involves turning inwards. But for an area as insular as mainstream economics, the final stage of the grief process – acceptance – will only come when it finally opens up to new ideas – or even the old ideas that have been there all along.

The oddity of a Brexit odyssey

By Jamie Morgan

Globalizations is a leading inter-disciplinary journal with an interest in political economy. It has notably published on exploitative work practices, the Arab Spring, land grabs, climate change, and the power asymmetries and future prospects of governance processes. The journal recently organized a special forum on Brexit. The forum includes contributions from many points of view: British history, the history of European integration, the role of class, the rise of the Global City, the influence of economic theory on the scope of labour practices, and the prospects for inequality, crises, and dissolution. Contributors include well-known post-Keynesians, political economists, Marxists, and European public intellectuals (James Galbraith, Bob Jessop, Ann Pettifor, Heikki Patomäki, Peter Wahl, Boris Kagarlitsky and more).

In editing these essays, it became clear to Heikki and I that Brexit is an extremely odd event. It was all too predictable at the same time as appearing unlikely, right up until the vote was counted. Nigel Farage of UKIP had already conceded and the senior Leave proponents were visibly shocked (and not a little afraid), when they realised they had won. The context of the vote and the consequences from it also seem to involve varieties of change without change. Brexit seems likely to result in serious social and economic consequences for Britain, but involves also basic degrees of continuity of policy frames within neoliberalism and its governance practices.

There is, for example, a clear narrative shift from the pre-referendum Treasury Budget Report, March 2016. In the Report, on the basis that EU members are Britain's most proximate trading partners, and comprise 44% of its exports, membership of the EU was positioned as a powerful force encouraging a more open, cosmopolitan British trading economy. However, the Leave campaign and the post-referendum government have repositioned EU membership as a constraint on a globally progressive open Britain (free to now flourish in a 'post-geography trading world'). Again, this is odd (and for more than the obvious reason that Britain looks set to create barriers to trade with its nearest neighbours, whilst seeking to develop trade treaties - a notoriously contingent and protracted process - with far flung nations). It is odd because it is an argument ostensibly focused on economics but dominated by other political concerns. The argument from the Right of the Conservatives was dominated by old concerns with the sovereignty implications of the European Commission's Social Europe agenda of integration, rather than the realities of the Single Market. For the Left, by contrast, the EU has been captured by the Single Market agenda and is overly neoliberal, and thus increasingly divisive as a source of generalized exploitation and limited democratic accountability. For the Right, the EU has been insufficiently neoliberal, but the economic argument has been *coloured* by other issues.

Ultimately, British post-referendum policy seems conditioned by choices between varieties of neoliberalism. And yet there has been no simple mapping of influence and interest along economic lines. This too is odd. If one were to begin from a simple unified concept of 'capital' and then translate this into overwhelming influence based on interests, then leaving the EU would seem an unlikely event. So unlikely that the very idea of a referendum ought to have been suppressed by the 'powerful'. It jeopardizes the status and influence of the City of London as a premier finance centre, it creates uncertainty and dislocation for multinationals and influential corporations of all kinds (risking investment projects, affecting profits via currency instability, threatening inflationary pressures on costs that affect pricing, and creating the need for decisions firms would rather avoid). Brexit is a short-term headache for 'capital' and a long-term threat to some fractions within it. It seems like a defeat, a defeat articulated and orchestrated by a Right wing party that nominally represents 'capital'. Again, this is odd. It is less odd when one considers that the referendum was a response to nationalist populism by a Conservative government aiming to undercut its own (anti-Social Europe) Right wing, as well as the electoral threat it perceived from UKIP. The leadership simply did not believe they could lose. It is also less odd when one considers the campaign was partly bankrolled by a hedge fund billionaire who made millions shorting the markets.

In any case, Brexit has very quickly become an exercise in damage limitation, posed as opportunity, and without any clear sense of what the Government is in a position to do. This is being represented as necessary secrecy as a form of negotiating strategy. But there is also something odd here. A person who campaigned for Britain to remain in the EU, not leave heads the new Government. Theresa May is not an enthusiastic Brexiteer, she was simply astute enough to say little and wait for the other major figures in her party to damage each other. She has also been astute enough to place several of the main Leave campaigners in her Cabinet -- not because she has great confidence in them, but rather because they will then own any disasters that follow. This makes for good personal politics (self-preservation of the PM), but not necessarily coherent and effective policy. Britain now has 3 people directly delegated to plan and negotiate Brexit. David Davis, heads the Department for Exiting the EU, Liam Fox, is responsible for international trade outside the EU, and Boris Johnson is foreign secretary. However, though delegated none of the 3 are yet institutionally empowered. Davis cannot negotiate with individual EU members until the EU has collectively agreed a position in response to Article 50. The UK is still an EU member and the EU is collectively responsible for trade treaty negotiations beyond its borders, so Fox has no clear institutional mandate. Johnson's position sits between these two, as simply a diplomatic voice intended to enhance Britain's presence and gravitas in the world (and, yes, everything about that statement seems like self-refuting parody even as I write it).

Moreover, these 3 are ultimately answerable to the Treasury and the Chancellor, who must incorporate any new institutional arrangements into Britain's emerging economic structure. Furthermore, all 3 must come to terms with the Home Secretary, who controls immigration policy (and so is where any special pleading regarding treatment of groups heavily dependent on foreign labour must take place -- notably for the finance sector, the health service, and agriculture). The situation is, therefore, already one involving 5 different groupings, each with their own concerns and personnel. The simple mantra that 'Brexit means Brexit' is already about as meaningful as any stanza from the Jabberwocky.

Still, the immigration issue looms large and introduces a further oddity. Immigration dominated the media coverage that led up to the referendum. However, actual voting patterns have been interpreted along several different lines, each emphasizing some particular primary cause of the vote. Did people vote Leave as the 'left behind' or economically disadvantaged, simply to hurt the establishment, did they vote based on moral panic regarding ethnicity, immigration and fears over social cohesion and cultural change (perhaps involving nostalgia for some imagined past), or did they vote based on differing ideas of governance -- an autocratic 'us versus them' mentality of control and of strong borders? Perhaps it was some combination of all of these, creating contradictory impulses and schizoid confusions -- exacerbated by the stark absence of reasoned argument in public discourse (and more worrying, an active hostility to reasoned argument -- strongly held belief was considered at least as important as evidence).

In the end though, it seems less significant what combination motivated the vote, and more significant that the consequences of the vote seem unlikely to be compatible with meeting *all* motives and expectations. More control over migration requires quite different approaches to regulation and an increasingly closed economy. This pits two core aspects of neoliberalism against each other, free flows of labour and free flows of goods and capital. This too seems odd, an internal division of policy within a set of principles that we have grown accustomed to thinking of as ideologically dominant in combination. The conflict, however, seems to be creating constraints and choices that are unlikely to satisfy any of those who voted Leave, at least as long as the framework remains neoliberal. This, of course, is the big question that waits to be answered. It is a question about the future prospects for democracy and for economies.

Are protectionism and retrenchment going to be 'solutions' to the negative aspects of globalization? There are currently many centripetal and centrifugal forces in play that could dissolve the current terms of globalization, and that could, for example, bind or dissolve the EU. Brexit as a problem posed only for Britain tells one little about this directly. However, perhaps the state of democracy in Britain tells one something. In the last 9 years Britain has only had 1 year in which (even by first past the post majoritarian standards) it has had a leadership that the electorate thought it had voted for. And it isn't now (it was David Cameron, from 2015 to 2016). All other power transitions since 2007 have been internal to parties or compromises between parties. This too is odd. It seems unique, but the issue of accountability and sense of enfranchisement is a far more generalised problem. It is one that only greater participation on different terms than today can rectify.

Odysseus required 10 years to travel home to Ithaca from Troy. Brexit seems more of an interminable journey to nowhere. Sir Thomas More's work traded on this lack of place to imagine something better, and so 'no-place' has become synonymous with an ideal place, Utopia. The Britain and Europe of ten years from now seem unimaginable to me. Fortunately, others have more foresight and much of that is signposted in the contributions set out in *Globalizations.* These can be found at:

http://www.tandfonline.com/action/showAxaArticles?journalCode=rglo20

Deglobalization? Or just an end to globalization?

By Salvatore Babones

From Global Asia Newsletter #007

The GFC marked the end of the globalization era. A fully globalized but no longer globalizing economic order is now taking shape.

Most people think globalization started in the 1990s. But if you look at the data, global trade and investment started to rise rapidly right after the 1972 collapse of the Bretton Woods system of managed exchange rates. Both merchandise trade and foreign investment peaked in 2007-2008. Growth has continued in currency exchange markets but at a slower pace than in the early 2000s. It took 25 years for the world's major markets in raw materials (oil, etc.) and manufactured goods to stabilize at a market equilibrium. Bracket the "globalization era" with the dates 1973-2008, RIP:
Al Jazeera | China: The Most Visible Victim of Deglobalization

Some of the first major beneficiaries of currency and trade liberalization were the Gulf oil exporters. Opec may be a cartel but it has never been a successful monopolist. The massive redistribution of the world's income towards oil (and other commodities) exporters in the 1970s was the result of prices rising to a market equilibrium level. A second move to market equilibrium was China's reindustrialization of the 1980s through the 2000s. The reorientation of the world's manufacturing base to China was inevitable, though that hasn't made it any more popular than high oil prices:
Al Jazeera | Hillary Clinton, Donald Trump, and China

The crisis of 2008 can be understood as the end of a period of massive redistribution caused by the breaking of the dams that held back global markets in the post-war period. The sub-prime mortgage bubble and the Euro fiasco were directly caused by gross economic mismanagement, and good (bad) policies could have made them much smaller (bigger), but the dramatic break in global economic time series is on a different scale entirely. The global integration of the world's economy is now complete. The next few centuries (yes, centuries) will clarify its direction. Personally I expect that the United States will be its biggest beneficiary.

Subscribe to the Global Asia Newsletter

Latest issue of WEA ejournal *Economic Thought*

The editors are pleased to announce the publication of the latest issue (5.2) of Economic Thought – the WEA's open access, open peer review, online journal. It is available to download at: http://et.worldeconomicsassociation.org/

It includes articles by:

Jorge Buzaglo, 'Expanding Human Capabilities: Lange's "Observations" Updated for the 21st Century'

Paul Auerbach, 'Commentary on Jorge Buzaglo "Expanding Human Capabilities: Lange's 'Observations' Updated for the 21st Century"'

David Orrell, 'A Quantum Theory of Money and Value'

Bruna Bruno, Marisa Faggini, and Anna Parziale, 'Complexity Modelling in Economics: the State of the Art'

David Ellerman, 'Reply to Commentaries on "The Labour Theory of Property and Marginal Productivity Theory"'

ANNOUNCEMENT: *THE SRAFFA PAPERS*

Piero Sraffa's papers and correspondence, held in the Wren Library of Trinity College, Cambridge, are to be made available online in their entirety.

The contents of the Sraffa Archive are being released sequentially. The first instalment, Sraffa's diaries from 1927 to 1977, and the journal of his visit to the People's Republic of China in October 1954, are now available for consultation at:

http://trin.cam.ac.uk/Piero_Sraffa

As the work of digitisation proceeds, more of the material will appear online.

Under the direction of Giancarlo de Vivo and Murray Milgate, with the collaboration of Jonathan Smith (Archivist and Modern Manuscripts Cataloguer at Trinity College) and the staff of the Wren Library, the project is planned for completion in 2017.

The project would not have been possible without the endorsement and encouragement of Sraffa's Literary Executor, Lord Eatwell. Generous support from Trinity College and the Cambridge Political Economy Society Trust is gratefully acknowledged.

Cambridge, October 2016

The WEA - journalism and communications support needed

The WEA needs to build up its public profile. So we are looking for names (and ideally email addresses) of journalists in various countries around the world who might be sympathetic to and interested in writing about or at least referring to the WEA. So please give a thought to possibilities and send suggestions to:

wea@btinternet.com

We also could use someone to act as the WEA's communications director.

World Economics Association eBook Library—try it!

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

Newsletter editor: Stuart Birks kstuartbirks@gmail.com

The World Economics Association Newsletter is published in the UK by the World Economics Association.