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What's wrong with Economics?

I.
Hubris might well head the list

Samuelson 1973: “The spectre of the repetition of the depression of the 1930s has been reduced to a negligible probability”.

Lucas 2003: “Macroeconomics in this original sense has succeeded: its central problem of depression has been solved, for all practical purposes”.

Both statements came shortly before the crises of the economic policy regimes they championed.

Samuelson thought: we would have no more depressions because governments had the tools to prevent them. These tools were called Keynesian economics.

Lucas 30 years later: we would have no more depressions because governments no longer used the Keynesian tools to prevent them.

Samuelson was hubristic about what governments could do; Lucas about what markets could do.

Who was right? Keynesian policy seemed to work for 25 years before succumbing to the crisis of stagflation. New classical economic policy - monetarism for short - seemed to work for about 15 years then fell victim to the Great Recession of 2008.

Hubris is the belief you are right, whatever the evidence. Economists are particularly prone to hubris because of the extremism of their method and the difficulty of applying to their theories Popper's falsification principle.

II.
The collapse of the two hubristic schools has left the theory of macroeconomic policy in a mess. In fact there is no settled theory of macroeconomic policy at all.

This was brought home to me recently when I attended a debate in London on austerity policy

The issue was: was fiscal austerity the right response to the crash? Two economists said yes, the other two said no.

Simon Wren Lewis, opening the batting for the anti-austerians, produced data to show that fiscal tightening since 2010 had left the British economy between 5% and

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15% smaller than it would have been. Moreover, because austerity had stifled the growth of the economy, it had made the task of reducing the budget deficit and national debt as share of GDP much more difficult.

This was straightforward Keynesian stuff. But then something odd happened: Roger Bootle for the austerity side took exactly the opposite line, while announcing that he too was a Keynesian. How could this be? He agreed that on its own, cutting the budget deficit in a slump would make things worse. But this, he said, ignored the effect of fiscal policy on expectations. Policy was a balance of risks. If people believed that cutting the deficit was the right policy, then any failure by the government to commit to doing so would cancel any expansionary effects expansionary policy might be expected to have.

Expecting higher taxes, households and companies would increase their saving; fearing a government default on the debt, bond markets would charge the government punitive rates of interest for its money.

And here was Bootle's clincher: by committing himself to fiscal consolidation, George Osborne had given himself some room for fiscal loosening. In other words, the only way Keynesian policy might be made to work in a world of non-Keynesian expectations is by creating fiscal delusion. Proclaim your allegiance to Say's Law, and you may be able to get away with a bit of fiscal sin.

I think this is an extremely unsatisfactory position, intellectually and politically, but this is the mess macroeconomics has got itself into. Once you introduce beliefs and expectations into economics, as is surely reasonable to do, macroeconomics is all over the place, and macro policy becomes indeterminate. To use a phrase of Paul Krugman’s, it all depends on whether a good or bad confidence fairy graces your feast.

III.
For Post-Crash students the main charge against economics is its methodological authoritarianism.

Here is Jean Tirole, French Nobel Prize Winner in Economics 2014:

“As you know, I have always advocated for our country to adopt the norms of research assessment that are in use in the rest of the world. It is especially important for the community of academic teachers-researchers to be endowed with a single scientific assessment standard, based on the ranking of the journals of the discipline and on and on an external assessment by internationally prominent peers. It seems inconceivable to me that France would recognise two communities within the same discipline....Self-proclaimed 'heterodox' economists have to comply with the fundamental principles of science.”
The underlying position taken in here is that economics is a science and there is only one way to do science. A good car has been built: students must learn how to drive it.

Now, the demand to teach alternative theories of physics and chemistry makes little sense. (After all, chemistry students are no longer taught phlogiston theory as a valid alternative theory of combustion).

However, economics is not a science in this sense at all. For one thing, it is axiomatic; very little testing of models goes on. Secondly, economics is not progressive, in the sense of, say, physics. Progress in economics consists mainly of increased formalisation, rather than the discovery of fresh truths. No truth in economics, once proclaimed, has been refuted. This argues very strongly for not consigning alternatives to the current mainstream to the rubbish bin of exploded fallacies.

Thirdly, economics is not a natural science, but a social science (Keynes called it a moral science). In physics, the interaction of bodies is fixed by physical laws, but in economics it is fixed by context, values, and societal norms, which are shifting parameters. Because economics has no universal truths, it is no more entitled than sociology or history to claim an uber-theory or meta-methodology, with catechistic teaching.

Yet this is what mainstream theory claims to be. It claims that its method of analysis alone is ‘scientific’, that all alternative approaches are ‘unscientific’ or even ‘pre-scientific’.

This methodological authoritarianism has a deadening effect on the way students are taught the subject.

It closes off young minds to curiosity and enquiry just at the point at which the teacher should be opening them up. The highly depressing results are to be seen in the exams set and answered by 3rd year students.

IV.
The next flaw to which I would draw your attention is methodological individualism, the habit of treating individuals, their choices and decisions, as the sole units of analysis; an economic world made up of rational Crusoes, all maximising their utilities and expunged of all ethical, social, biological, psychological, anthropological attributes. Robert Lucas sees himself as constructing "a mechanical, artificial world, populated by...interacting robots...that is capable of exhibiting behaviour the gross features of which resemble those of the actual world...." This is quite an accurate
description of how most economists do economics; whether such a world exhibits 'the gross features...of the actual world' is exactly the point in question. It’s interesting how early in his life Keynes understood that society was not a collection of interacting robots, but an 'organic unity', a view derived from G.E. Moore via Hegel.

A crucial implication of the Keynes view is that economics should have started with aggregates, or collectives, not with individuals. In fact, this was an important part of the economics of Adam Smith and Ricardo, and only with marginalism and Lionel Robbins did it narrow down to a study of the logic of individual choice under scarcity. From the macro perspective, economics is simply a specialised branch of the management of human affairs, and should never have been sundered from the other social studies.

V.
Symbolic of this sundering is economics' stress on formalisation, or mathematics. I would call this the fallacy of misplaced precision.

I think we have to accept that mathematical formalism is a huge barrier to the integration of economics with other social sciences; it constitutes in fact economics' claim to uniqueness and superiority. It is also the main tool for selecting economists, excluding from the profession any who either by choice or incapacity do not do the maths. I agree that one can have powerful mathematical intuitions; equally one can have powerful non-mathematical intuitions.

What is the appropriate level of mathematics? This is much less frequently discussed. Maths as a check on one’s logic certainly has its place. But maths as key to the riddle of the universe is grossly oversold. Yet this is what students are led to believe. Those that can do the maths get good degrees, the ones that can’t don’t, and go off and do something else. Economics imposes much stronger barriers to entry than any other social science.

VI.
If I had more time I would point to the profoundly distorting effect on our understanding of social phenomena of the use of the equilibrium method, with its abolition of history - another unfortunate legacy of 18th century economics' engagement with physics. But I have said enough for the time being. All my criticisms are inter-related and to my mind raise serious questions about the utility of economics as currently practised.