Generations of Economists

David Collard

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Generations of Economists

This book focuses on the interaction between practising economists and previous generations of economists. Because economic problems, such as crashes, tend to recur and are only partially understood, it may be profitable to read the work of previous generations in a collaborative spirit. Sometimes this can offer a different perspective on current preoccupations and cause us to reconsider the scope of our much criticised subject. The book gathers together earlier work by the author which appeared in various academic books and journals, with the addition of six new chapters.

The book is divided into five parts. Part One is concerned with Pigou and the Economics Tripos at Cambridge. The author is recognised internationally as an expert on Pigou, and this section contains a new essay on him together with previously published papers on his treatment of the business cycle. The theme of Part Two is utilitarianism, focusing on Bentham, Mill, Sidgwick and Pigou, and assesses its present position in economics. Part Three is about general equilibrium theory and includes a newly written chapter on the 'founding fathers', Edgeworth and Walras, in addition to one focusing on John Hicks. Part Four is mainly concerned with two writers, each neglected in his own way: John Tozer, an early mathematical economist, and Alfred Russel Wallace, the famous evolutionary biologist. Finally, Part Five deals with inter-generational economics, including a paper on the 'Cambridge Tradition' in generational economics and two new essays, by Ramsey on saving and Samuelson on overlapping generations.

Overall, this collection makes for a lively, informative and thought-provoking collection. It will interest anyone with an interest in the history of economics and of economic thought.

David Collard is Emeritus Professor of Economics at the University of Bath.

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Introduction

1 Generations of economists and the economics of generations

Newton, famously and possibly tongue-in-cheek, declared that if he saw far it was because he stood on the shoulders of giants. Something of the sort must be true of all sciences, including economics, no matter what we think of the stature of our forebears. Our subject is where it is largely because of its history. It is difficult to see, for example, how modern general equilibrium theory could have come about without the 'founding fathers' (Chapter 10) or modern welfare economics without utilitarianism (Chapter 7).

The very best economists have closely engaged with the history of their subject. One thinks of Schumpeter, of course. But also of Samuelson (1966, 1986) who analysed all the major economists, making Samuelsonian mathematical versions of them all, of Hicks who wrote on everything (Chapter 15), of Sraffa whose theoretical structure (Chapter 14) was intimately bound up with his own interpretation of Ricardo. One must even include Keynes (whose account of his 'predecessors' on effective demand was, admittedly, tendentious) for his magnificent essays on Edgeworth and Marshall (and, indeed, Newton). None of these writers was primarily or solely an historian of economic thought. Their engagement with the subject suggests a symbiotic relationship between 'doing' economics and studying its history. The past was (is) grist to their (our) intellectual mill.

This is not to say that modern economists have much to learn from the past in terms of technique and measurement. One has only to glance at the journal literature for confirmation that the level of theoretical and econometric sophistication is vastly higher than it was even a generation ago. Economists learn their latest techniques from previous generations of mathematicians, statisticians and engineers, not from previous generations of economists. For the modern economist the history of the subject might figure briefly in the customary 'literature search' undertaken by PhD students, or as a useful source of quotations and embellishments, but for everyday work it is sufficient to use convenient shorthands like 'Ricardian Equivalence' or 'Walrasian Equilibrium' without enquiring too closely into what Ricardo or Walras meant. A detailed examination of their writings may safely be left to specialist intellectual historians or to antiquarians. (This applies *a fortiori* to 'neglected' economists, Chapter 16). Nevertheless, economic analysis is not a matter of technique alone and there are some aspects of economics, concerning scope and perspective, on which a 'conversation'[1] with older generations

of economists might be productive. I am using the term 'conversation' not literally but to indicate an open-minded examination of former generations' work and possibly its use as an intellectual sounding board.[2] Pursuing the notion of a symbiotic relationship between the practice of economics and a study of its history I shall take 'perspective' as the main theme of this chapter.

Perspective

In some subjects a theory emerges that 'explains' a great number of previously poorly understood phenomena and is almost universally accepted. A good example is the theory of tectonic plates which explains continental movement, earthquakes, volcanoes and biological diversity. Another example is natural selection, which provides a powerful and beautiful hypothesis to explain the mechanism of evolution (Chapter 18). These theories, the theory of tectonic plates and the theory of natural selection, 'explain' phenomena and enable us to better understand them. Even though earthquakes and species variation occur in different forms and in different places, there is a sense in which the intellectual problem is 'solved'.[3] We do not need a new theory for each earthquake or tsunami: in economics it sometimes appears as though we do. This is because some economic problems recur from generation to generation but in a different guise and in a different context. For example, the free trade versus protection debate has taken the form of Smith versus the Mercantilists, the Anti-Corn Law League versus the Corn Laws, Free Trade versus Imperial Preference and the GATT versus trading blocs. For each generation the problem is more or less resolved, but the caravan moves on and the problem reappears in a somewhat different guise a generation or two later. Theoretical progress does take place, so we do not have to begin again each time, but economics is a social science and as yet lacks an all-powerful hypothesis such as a tectonic plate theory or a theory of natural selection. The closest we have got to such a theory is the harmony doctrine associated with Adam Smith's 'invisible hand' but this hardly commands universal assent. Indeed, the pursuit of a 'grand hypothesis' in economics is a chimera and to proceed as though we had one is an error. To do so would be to ignore the perspective that can be brought by having a 'conversation' with those who have grappled with similar problems in the past.

Historical perspective is, however, only part of the story. There is perspective in depth; there is also perspective in width. Mainstream economics is subject to various critiques for being too narrow and too orthodox. They include the feminist critique, the socialist critique, the environmentalist critique, the behavioural critique, the communitarian critique, the developmental critique and, no doubt, several others. It is not that economists have ignored these topics. Quite the opposite. The criticism is that of economics imperialism: that economics does indeed look at all these issues, for example, the analysis of marriage and divorce, of income redistribution, of choice over lotteries, of voluntary work, of rural poverty, but narrowly applies the tools of orthodox analysis. A related criticism is that in applying economics to these areas economists ignore the insights provided by sociology, anthropology, psychology and even politics. This would not much

matter if the 'predictions' provided by economists were superior but, alas, this is not always the case.

The remainder of this chapter illustrates the supposition that a study of the history of economic thought brings both perspective in depth and perspective in width.

Cycles and crises

The economic crisis of 2008 has done the reputation of economists, together with that of bankers and accountants, little good. It was not meant to happen,[4] but it has had the interesting effect of forcing the New Macroeconomics into a dialogue with Old Keynesians. Policymakers across the globe seemed to dust off their copies of Keynes and apply demand stimulation packages as if the New Macroeconomics had never happened. Keynes's 'liquidity trap' even became a hot search on the Internet.[5] This, probably short-lived, rehabilitation of Keynesianism is the most striking and obvious intellectual consequence of the crisis. However, historical perspective should also stimulate a re-examination of our theories of the business cycle. The contrasting treatments of the cycle by Pigou and modern theorists are discussed in chapters 3 and 4. I am not, of course, suggesting that Pigou was in some sense 'right': only that it is hubristic to claim that his and other inter-war approaches have nothing to say to us.

After the Keynesian Revolution economists rather lost interest in the cycle, and the models that emerged were mechanical in nature such as Hicks's (1950) combination of the multiplier and accelerator with real floors and ceilings (see Chapter 15). By the late 1960s (Friedman 1968; Phelps 1968) it had become accepted that inflation was determined by the rate of increase in the money supply and that in the long run unemployment would settle at its 'natural' rate. Demand management policies could work only in the short term. The rational expectations 'revolution' went much further. If markets were rational and wellinformed, the effects of changes in monetary or fiscal policy would be fully anticipated.[6] Hence, only unanticipated or random changes would have any effect and these could hardly count as policies. Demand management would therefore be ineffective even in the short run. The best policy would be to set a credible inflation target (with the nominal interest rate being its instrument) and leave unemployment to settle at the natural rate. With governments pursuing the sorts of policy just described, any 'policy-induced' cycle should disappear.[7]

But there could, nevertheless, be 'equilibrium' cycles, the essence of which is that cycles are a working through of shocks to which the system has to adjust. There is then little point in 'interfering' with this process: to do so would be to prolong the adjustment. One such model is the 'real business cycle' model in which a (favourable) productivity 'shock'[8] is applied to an economy growing along a trend path. The shock increases real wage and interest rates relative to the future and increases current labour supply and employment. Combined with some persistence in the shock, inter-temporal substitution is enough to produce plausible[9] business cycles so that any perturbations will be Pareto-optimal (see,

for example, Long and Plosser 1983). At the same time, 'New Keynesian' models began to appear, in which nominal demand shocks could have real effects on employment. Most of these models assumed price or wage rigidity, often in the context of imperfect markets: for example, the so-called 'menu costs' of changing prices (Caplin and Spulber 1987) could generate price-rigidity,[10] or 'efficiency wages' (Shapiro and Stiglitz 1984) or 'insider power' (Shaked and Sutton 1984) could produce wage rates above the market clearing wage. All of these approaches amount to throwing some grit into the machine so that an adverse demand shock could lead to quantity adjustment rather than price adjustment. The remedy suggested was usually to try to reduce rigidities, particularly by labour market interventions (Layard *et al.* 1991). No one, as far as I am aware, has recently attempted anything like a synthesis of theory and measurement.

Pigou (Chapters 3 and 4) attempted such a synthesis, rejecting equilibrium business cycles as merely a theoretical possibility. Though not elegant it was comprehensive, allowing several sorts of impulse, real, monetary and psychological (particularly expectations), to trigger a cycle. He was obviously influenced by Dennis Robertson (1915) on the importance of the gestation period, Moore (1914) on leads and lags, and Mitchell (1913) on the possibility of a self-generating cycle. A difficulty with modern theory on the business cycle is that we are presented with a number of nicely honed, very specialised models. A new synthesis of business cycle theory, combining modern theoretical rigour and econometric skill with the scope and 'thickness' of more old-fashioned approaches is an obvious topic for a 'conversation'.

Altruism and giving

My second illustration is from an area in which I have previously taken some interest (Collard 1978), the roles of benevolence and altruism in economics (see also Chapters 13 and 21). Here my contention is that a symbiotic relation between modern developments and the history of economic thought is ongoing and is still working itself through. My own work, for example, was stimulated by Edgeworth's excellent discussion (see Chapter 13). Technically, Edgeworth had much to offer and his convenient separation of market and extra-market behaviour has remained a central feature of modern economics.

Technical contributions aside, a discussion of much wider scope is to be found in the eighteenth-century literature, which is recapitulated here since the classical and neo-classical positions are better known. Scepticism towards 'benevolence' had an established history, well before Adam Smith's famous remark that 'it is not to the benevolence of the butcher, the brewer or the baker that we expect our dinner but from their regard to their own interest' (Smith 1776, book 1, chapter 2). Mandeville, in his allegory *The Fable of the Bees* (1724), had been even more critical of a reliance on benevolence: 'pride and vanity have built more hospitals than all the Virtues put together'. But parallel with a powerful scepticism about benevolence went a complementary, almost equally strong tradition. Some, like the Earl of Shaftesbury (1669), believed that

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