



The Economics of Economics

Why Economists Aren't as Important as Garbagemen (but They Might Be)

Dan Šťastný

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 **CEVROINSTITUT**
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To Ivanka

CONTENTS

Foreword	IX
Acknowledgments	XII
Introduction	XIII
1 Frustration	1
1.1 The Theory-Policy Gap.	4
1.1.1 First Approach: Consensus Literature and Actual Policy	6
1.1.1.1 Consensus Literature	6
Kearl et al., 1979	7
Frey et al., 1984	8
Block and Walker, 1988	9
Ricketts and Shoesmith, 1990	9
Geach and Reekie, 1991	10
Alston et al., 1992	10
Fuller and Geide-Stevenson, 2003	11
1.1.1.2 What Economists Think	12
Trade Protectionism	13
Rent Control	16
Minimum Wage	17
Agricultural Support	18
1.1.1.3 What the Policy-makers Do	20
Trade Protectionism	21
Rent Control	22
Minimum Wage	23
Agriculture Subsidies	23
1.1.1.4 Comparison	24
1.1.2 Second Approach: Policy Change Consensus	25
1.1.2.1 Sample Survey Among Czech Economists	28
Consensus	31
Theory-Policy Gap: Existence	36
Theory-Policy Gap: Pattern	39
Sample Survey Conclusion	42

1.2 The Frustrated Economist	43
2 Theory-Policy Relationship: The Market for Economic Ideas	49
2.1 Supply of Economic Ideas	50
2.1.1 Economists' Objectives	57
2.1.2 Evolution of Supply	62
2.1.2.1 Growing Policy Irrelevance	66
2.1.2.2 Growing Interventionism	72
Search for Failures	85
Shifting Definitions	87
2.2 Demand for Economic Ideas	90
2.2.1 Policy-makers' Objectives	91
2.2.2 Evolution of Demand	96
2.2.2.1 Policy Sieve	97
Ignoring Theory	98
Twisting Theory	98
2.2.2.2 Science Interventionism	101
Employment	102
Research Support	106
Economic Education	109
2.3 Summary: The Market for Economic Ideas	110
3 Lessons For Economists	113
3.1 Economic Literacy	114
3.2 Economist-educator	117
3.3 The Economics Factory	121
4 Epilogue	124
Appendix	126
Reference	131
Index	143

FOREWORD

Once again, we are living through a major economic crisis and as always such a dramatic social shake up brings a longing by the public for government to “do something”, “do more”, “do a better job”, “try new things”, “protect us”. And governments all around the world gladly respond to these new demands. This is not surprising as this pattern has repeated itself for centuries. After every crisis and after every war the government ended up stronger. With good reason Randolph Bourne famously states that “war is the health of the state”. Through a series of events of this sort, we ended up living under powerful governments that redistribute – roughly speaking – half of what we make. (And as many argue – and many disagree – this huge expansion of governmental activities can be held responsible for our current debt crises and the financial crisis itself as well.) What is not well known, however, is the role of economics, or, rather, economists in this story. *The Economics of Economics* shows a glorious past and a gloomy presence of political economy. Early political economists used to be “pourers of cold water” as they opposed well sounding but mediocre political short-cuts for delivering prosperity, but slowly they turned into pro-active interventionist reformers. How and why this happened is a story to be told.

Economic science has long applied its tools to better understand our past (economic history), our current systems of law (economics of the law or economics of crime), political systems (economics of politics), family life (economics of family) etc. In all these endeavors into formerly unexplored fields, economics has provided us with extremely valuable insights which scholars focusing exclusively on other

disciplines are simply not able to see. For some reason, though, it has avoided looking into itself. Yet this is precisely how we can understand the dramatic change within the profession and, consequently, within society at large. And here comes professor Štátný with his contribution – *The Economics of Economics*!

Why do some theoretical insights of economists never make it into public policy debates and hence myths survive for centuries and are believed as undisputable truths by the public and policy-makers? It is as if people, contrary to the scientific knowledge, still believed that the Earth is flat. Why is it often the case with economic laws? Well, supply of and demand for economic knowledge can lead to an explanation. Yet, at the same time, some theories (such as market-failure theories) are a part of the policy debates. How do they manage to be taken seriously by policy-makers whereas other theories remain neglected? This is even more surprising because theoretical economists, the originators of those market-failure theories, did not themselves always see a practical use for them. Again, understanding supplies and demands in the process of translation of theoretical knowledge into actual policies is necessary, and for that *The Economics of Economics* is needed.

A change in semantics can have a dramatic impact in policy debates. We do need government to watch competition (antitrust laws) and give us sound money (central bank), right? To believe this requires a twisted understanding of what monopoly and inflation are. The original meanings of these concepts would dispel the need for a central bank and antitrust laws. Common sense would refute the “therapeutic state”.

We can see from time to time in politics how fast some people change their stands in accordance with what is currently popular. Communists turned into defenders of capitalism after the Velvet Revolution in my country, the Czech Republic, MPs switch party affiliations in the middle of the “game”, etc. Readers might be surprised to hear that

Professor Šťastný documents the same phenomenon in the field of economic theorizing, too – the era around the Great Depression being a nice case study, and our present crisis would offer us some empirical support surely as well. As shocking as the evidence of politicization of science may be, he does not present it as surprising news. That is because he has his economics of economics that can elegantly provide an explanation. Believe it or not, once again supply and demand do their wonders.

The Economics of Economics is well written, insightful and enjoyable for anybody who wants to understand the changes in our society. Economists are no doubt themselves at least partly responsible for being less relevant than garbage-men; but it does not have to be that way, as Professor Šťastný suggests, if they only used a different strategy to proselytize their cause.

Economic challenges must be addressed with economically intelligent responses. If not, our economically clueless “solutions” would lead to social disasters and we will neither know the way out, nor understand their roots and true causes. Hopefully, Professor Šťastný’s book will open our eyes as it carefully explains the logic behind politicization of science and gives us hope for the future. All that – and much more – in his enlightening work *The Economics of Economics*.

prof. Josef Šíma, Ph.D.
CEVRO Institute, president

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An attempt to list other people who had their, if only inspirational, share in shaping my ideas below runs the risk of unwittingly omitting some of them. With this in mind, I would hate to exclude (in alphabetical order): Richard Ebeling, Bob Higgs, and Michael Volny.

Finally, my thanks and gratitude must go to my closest collaborators, Josef Šíma and David Lipka for what by now qualifies as almost a lifelong friendship and cooperation. Last but not least, a world of thanks is bound to go to my family, for which this text provides a rare materialization of all the endless and late hours at the screen or amidst papers and books. Hopefully, this evidence will be accepted.

INTRODUCTION

George Stigler in his remarkable essays on the history of economic thought asserts that all great economists were moved to economics by the desire for social reform.¹ Assuming this to be true, *economists must then be some of the most frustrated scientific professionals*. If all of them were wiped out at once and there was not a single economist left in the world, the chances are that nobody would notice the difference. If this happened to garbagemen, to use David Colander's witty metaphor (Colander, 1991), there would surely be hardly anyone who would *not* notice.

What is the ground for such a bold claim? In what is to come I hope to show that far from having a marked influence upon the world, economists – all their institutionalized positions within government notwithstanding – are largely inconsequential and generally rather on the verge of being irrelevant. And such a state of affairs is likely, given their aspirations to shape the world, to result in their *frustration*.

It is admittedly doubtful that *all* economists actually feel this way. My personal experience – which is very close to such sentiments – makes me believe, however, that looking into the

1 Stigler claims it is generally the social reform, not the quest for pure scientific truth itself, which is the motivator and goal of economists:

Economics has seldom attracted to its ranks the detached and unemotional intellectual who finds the posing and solving of difficult problems satisfying even in the absence of immediate or perhaps even eventual usefulness of the solution. On the contrary, individuals have chosen this field because they wished to solve live economic problems and felt a need to master the weapons provided by the science which deals with these problems.

The policy orientation of classical economists does not need to be argued. [...] The story has not been greatly different since the study of economics became an academic discipline. (Stigler, 1959, p. 526).

See also quotes of Robbins to a similar effect below, p. 2.

relationship between academic economics (a product of economists' theorizing intended to shape the world) on the one hand and the economic policy (a product of political process actually shaping the world) on the other is a project worth pursuing.

Thus, in a truly *economic* fashion, I will be focusing on a means-ends relationship, except in this case the subject of such inquiry will be the economists themselves, their community and their product: the science of economics. Hence, the somewhat pretentious but fitting term, *the economics of economics*.

ECONOMICS OF ECONOMICS

At first, the economics of economics may appear as just another application of economic analysis to a particular field and an additional piece in the economists' 'economics-of-something' collection (i.e. on par with economics of labor, economics of agriculture, economics of sports, economics of arts, etc.). However, it may also be viewed as an important step in broadening the application of economics and reducing the extent of areas of thought whose truths are not subject to analysis but rather taken for granted.

This already happened in economics once with the introduction of public choice theory, which, in line with previous nomenclature, should perhaps be called *economics of politics*.² Before public choice theory, governments were largely seen as universal solutions to all problems (failures) discovered by economists in the workings of the private sphere (market). This was because governments – apart from the private individuals (consumers, producers etc.) – were not subject to economic analysis. Instead, it was *assumed* they would fix the problem once economists articulate it.

² Many authors indeed use this term. See, for instance, Tullock, 1976, or Buchanan, 1978.

The public choice theory showed this to be naïve and wrong. It explicitly recognized the fact that decisions regarding policy selection and application are just as economic in nature as decisions on the market, and may therefore be subject to economic analysis. The practical benefit of including the behavior of public decision-makers (politicians and bureaucrats) in the inquiry was that the policy-making no longer appeared as automatically fixing the failures. Just as the working of the market may result in a failure to live up to ideals postulated by economists, so may the policy-making fail to live up to proper remedies suggested by economists.

In such a context, the economics of economics takes the next – perhaps the ultimate – step beyond where public choice theory left off. It goes on to include the last component of the whole story, which so far has been left outside of the realm of economic analysis: the *economists themselves*. It therefore explicitly recognizes the fact that economists as scientists make decisions as well (what to inquire into, how to do so, etc.), and as such may be subject to the same scrutinizing eye of the economic science as all other decision-makers, even if it implies a self-analysis.³ Furthermore, doing so is not only legitimate but may actually prove quite useful. Just as the public choice theory proved instrumental in dispelling the naïve concept of politics and policy-making, so can the economics of economics shed some more realistic light on the processes in which economic theories and their policy implications emerge. Specifically, just as public choice eradicated the concept of governments as automatic benefactors, so can the economics of economics help to eradicate the idea of economics being nothing but a science practiced by unprejudiced discoverers of pure truth.

Although this third stage of economic focusing may sound quite novel and undeveloped, I claim no primacy or pioneering it. First, for decades there has been a specific scientific analysis of the scientific community that looks into

³ After all, we do not find it at all strange that medical doctors go to check-ups, and we do not think it inconceivable that even one medical doctor should examine himself.

its organization and the processes through which it develops, which is called the sociology of science.⁴ Second, not only sociologists, but economists too occasionally in the past analyzed the organization and development of science.⁵ And lastly, not only have economists tackled the sciences in general, but some of them focused specifically on economics, thus coming all the way to my present purport.⁶

And, yet, in spite of no claim to originality, I hope I am contributing here with something not altogether indispensable, and that is the policy context, as indicated by the subtitle of this work, to which my *economics of economics* is set. As expressed so succinctly by Robert Nelson:

Most economists hope that their work will have an impact on public policy. Yet, few economists devote much time or effort to studying the mechanisms by which economic writings and research are translated into public policy results. (Nelson, 1987, p. 49)

With the following text, I try to join those few economists who do try to fill this important gap.

⁴ The classics in this field include Robert K. Merton (see e.g. Merton, 1979), interestingly, the father of the economist, Nobel laureate, Robert C. Merton. On the importance of sociology of science, he (i.e. Robert K. Merton) commented:

Social scientists have been so busy examining the behavior of others that they have largely neglected the study of their own situation, problems and behavior. [...] The hobo and the saleslady have been singled out for close study, but not the social science expert. [...] Yet it would seem that clarity might well begin at home. (Merton, 1949, p. 161)

⁵ Such analysis was pioneered by Michael Polanyi (Polanyi, 1962), and by Gordon Tullock shortly after with even more explicit economic focus (Tullock, 1966).

⁶ This is especially the case of Will Hutt (see Hutt, 1936). Recently, this agenda was taken up by David Colander, Alfred Coats, Bruno Frey, Gebhard Kirchgässner, Arjo Klamer, or Charles Wyploz, to name a few. In fact, Frey actually uses explicitly the term 'economics of economics' (e.g. Frey and Eichenberger, 1997, p. 15, or Frey, 2000). Before them, Alec Cairncross alludes to "economics of economics", but does not "embark on so ambitious a task as [its] exposition" (Cairncross, 1985, p. 1).

PLAN OF THE WORK

The whole project I am embarking upon can be broken down into three main parts.

First, I would like to substantiate my starting point about there being a major divide between policy conclusions of economic theory, and the way the theory is transformed into actual economic policy. This will be done in several steps: first, I will identify the policy issues where there is a sufficient degree of consensus among economists that could enable me to consider it a scientific opinion; second, I will take a look at the ways these issues are handled by policy makers in the real world; and last, by juxtaposing the first and second, one should be able to see the impact of economists on the policy.

After having defined and shown the puzzle, I will engage in a thorough analysis of the mutual relationship between economic theory and economic policy in the effort to illuminate the way in which one impacts – both allegedly and actually – on the other. In the course of doing so, I will point out two important tendencies that may constitute the basis of the explanation of the puzzle.

Lastly, as behooves every constructive criticism, I will suggest possible implications for the work of economists that would aim at increasing their policy impact and thus at reducing their frustration at their real-world irrelevance.

1

FRUSTRATION

Economic science has a long history with roots no shorter than other sciences. Despite its formal grounding officially in the eighteenth century, scholarly thinking and theorizing about issues we call today *economic* has always been a part of the knowledge heritage of mankind. And this is of no surprise, as economics, its current caricatures notwithstanding, is ultimately a very real-worldly science, from a certain perspective even more so than natural sciences.

As evidence of the real-worldliness of economics, I venture to say that what all economic thought throughout the millennia has had in common is their proximity and relevance to questions of public policy decision-making and conduct.^{7, 8} From Chinese and Greek philosophers to medieval schoolmen to classical economists to the bulk of today's economists, one can trace their preoccupation with questions of *what* is to be

⁷ This is perhaps true of all social sciences. As Stanislaw Andreski, a British sociologist, claims:

Many of the most important insights into the nature of human society came from speculations and discussions about how it might be improved. [...] Broadly speaking, the social sciences have developed as an offshoot of reformist strivings [...]. (Andreski, 1973, p. 144)

⁸ Admittedly, some of these thoughts evolved round *private* decision-making. Most famously, the oft-cited ancient economic primer – Xenophon's household economics – was a series of precepts for running a household well. Similarly, a good part of modern microeconomics has useful business applications. Yet, as will be shown, the reformist aspirations of economic thinkers were aimed at bringing about the reform through institutional change by addressing the ruling class, not as much through educating people directly. Adam Smith's *Wealth of Nations* was, after all, his contribution to "the science of a statesman and legislator." (Smith, 1976, p. 428)

Thus, it was the rulers and legislators rather than the public who were the primary audience of an economist-reformer. Interestingly, this may well be, as I will suggest in the last chapter, a reason of their ultimate failure in doing so!

done, *how* is it to be done and *why*.⁹ With their what's, how's and why's, they were taking up the issues of their time in the comprehensible effort to change – typically, at least as they believed, to *improve* – the current state of affairs. This is plainly acknowledged by no lesser authority in the history of economic thought as George Stigler (mentioned above) or Lionel Robbins. As the latter says:

There can be no doubt that throughout history economists of all schools have conceived their work as having the most intimate bearing on politics, both in the sense of the theory of political action and of the actual practice of affairs. (Robbins, 1963, p. 5)

Robbins's insistence on this point is crystal-clear from his discussion of classical economists in particular:

[Classical economists] were critics of some contemporary institutions and some contemporary habits, and they had definite proposals for what they deemed to be improvement, which they advocated with more or less energy. (Robbins, 1952, p. 170)

[That] the classical economists are to be classified [...] as reformers, in this aspect, is a proposition which, although it is often forgotten, *should not be open to serious question*. (Robbins, 1952, p. 171, emphasis added)¹⁰

Such a reform-orientedness of economists – the fact that social reform not only moves them to study their subject and is their prime and ultimate professional goal as well – is

⁹ To this day, it still counts as a major motivation behind studying economics. As Arjo Klamer and David Colander found out, “only 17 percent [of students entering graduate schools] consider [a desire to engage in policy formation] unimportant” (Colander, 1987, p. 97) and “[c]ontrary to our expectation, the majority of students at the elite schools are motivated not by technical fascination but by the desire to understand and improve the world.” (Klamer, 1992, p. 49)
See also Klamer and Colander, 1990.

¹⁰ A virtually identical idea – though in a somewhat concise manner – is advanced e.g. by Arthur Smithies:

Economics has always been concerned with policy. Most economists have been motivated by the desire to promote what they considered to be social improvement [...]. (Smithies, 1955, p. 1)

a peculiarity of social scientists, not easily found in natural sciences.¹¹ This, however, has its consequences: it exposes economists' work to a different – and from the scientist's personal point-of-view, much more demanding – standard of success and failure in their scientific undertakings.

For, say, a physicist, establishing certain facts is typically an end in itself, and doing so implies his success and, presumably, personal satisfaction. Even if he aspires for his discovery to be of practical use, it takes little effort on his part – as long as his invention indeed is potentially useful – to put it into use.

An economist, on the other hand, aims farther than that. Discovering useful laws, regularities, or principles is to him typically only a means to his ultimate end, which, as I have argued above, is seeing them put into use. However, it is precisely this step from useful theory to its application that does not come about as easily – almost automatically, it seems – as it does in the case of natural sciences.¹² Not being able to see this step taken and thus their ultimate goals achieved, economists must often appear as *unsuccessful* in their professional efforts, despite all their – often impressive – successes in theorizing proper. Hence, the *frustration* – the title of this chapter.

¹¹ Robbins argues that

few became economists from mere curiosity; considered as pure knowledge, our subject [i.e. economics], although not without its Faustian moments, has far less attraction than many others. And although, as life goes on, a man becomes habituated to what he is doing and no longer asks himself so frequently as he did when he was young what is its further purpose, yet few, I fancy, of those whom we would regard as worth while, are not sustained in their general attitude by the belief that somehow or other what they are doing is useful and may contribute to the common weal. (Robbins, 1963, p. 7)

¹² Gordon Tullock has the following explanation for this:

[Every] new idea must be such as to attract considerable support before it has been tried, or it will never be tried. In the case of physical invention, support must also be attracted, but only a very tiny amount compared with what must be attained for application for some idea for social change. Further, if some government adopts a proposal or social change, its prestige is likely to be involved, and it will be reluctant to admit that it was wrong. As a consequence, errors may persist. In the physical sciences the man who guesses wrong also loses prestige if he must admit his error, but he will lose much more if he does not change quickly. (Tullock, 1966, pp. 189-190)

Before embarking upon analysis of the roadblocks preventing the last step from being taken, let me first document the gap between the theory and its policy prescriptions and the actual policy and, second, the feeling of frustration on the part of economists.

1.1 THE THEORY-POLICY GAP

Pointing out the existence of a gap between theory and policy is easier said than done. Actual showing and proving this existence requires some kind of standard of correspondence between economists' prescription and the policy conduct. Yet, no such standard is readily available in a useful form.

For several reasons it is complicated to devise one because it cannot be a mere comparison of an *idea* (i.e. the prescription) on one hand to the *reality* (i.e. its application as the policy) on the other. First, the idea itself is a complex matter as one is not considering an opinion of a single economist, but one of the economic profession as a whole. Clearly, no two economists are likely to have absolutely identical opinions, and such an identity among millions of professional economists is simply out of the question. Thus, identifying what 'economists think' necessitates some approximation of the consensus among the economic profession. Second, even if the prescription is known, reality may appear so complex as to render the comparison to the prescription a difficult thing to do. To wit, while a particular prescription typically addresses a narrow field of a policy problem, reality – almost by definition – encompasses the given state of affairs as a whole. To provide both a simple and a practical example, it may be possible to establish that economists agree on the benefits of disposing with trade tariffs. Now looking at what policy makers do and finding out they indeed engage in removing all tariffs from books does not yet imply there is a perfect correspondence between theory and policy.¹³ On the other hand, seeing policy

makers removing all tariffs but one does not necessarily imply that there is no correspondence at all. Thus, identifying the gap will require some kind of *standard* of correspondence.

To address the first of the problems, I will make use of published studies on the opinion consensus among economists and my own research of opinion and reform oriented works of economists. Based on both, I will make a list of propositions that I take to be the closest approximate of economic theory, i.e. of what 'economists think'.

To address the second problem, one will need to show that there is less of a correspondence between theory and policy in economics than in other sciences; that of all sciences the theory-policy gap is most remarkable precisely in economics.

The lack of consensus among economists is routinely the subject of ridicule, which, on its face, makes my task almost intractable.¹⁴ Luckily, I think there are two reasons why it makes sense for me to engage in searching for propositions economist very much agree upon.

First, the discord among economists is grossly exaggerated just by looking at seemingly endless discussions of various points in economic literature. There is much more agreement among them than meets the eye, simply because economists – valuing their own scarce time – tend to discuss only issues they disagree upon, while leaving the agreed upon conclusions out. It might be in the nature of social science that its scholarly journals create more of an impression of disagreement than the journals in natural science.¹⁵

¹³ This is because the effect of a tariff may be obtained through other policy measures that the economists did not take into account when giving their prescription.

¹⁴ There are cases where the presence of consensus among economists is subject of ridicule, too. Consider Steven Kelman, a non-economist:

The near-unanimity of the answers economists give to public policy questions, highly controversial among the run of intelligent observers, but which share the characteristics of being able to be analyzed in terms of microeconomic theory, reminds one of the unanimity characterizing bodies such as politburo of the Soviet Communist Party. (quoted in Caplan, 2007, p. 53)

¹⁵ This may be due to easier experimenting in natural sciences that may give greater credibility to, and generate less of a discussion about, individual hypotheses. Also,

Second, as the task is to judge the correspondence between economists' policy recommendations and actual policy, it is only the agreement upon issues *relevant* to public policy that is important for my purpose. Now economists may hold widely divergent views on technical and fine points of theory, but the bulk of such issues has absolutely no bearing on policy whatsoever. Thus, the degree of disagreement on policy-relevant issues is lower compared to the overall picture of discord economists impress upon outsiders. Moreover, if one further limits the scope of relevant issues to policy recommendations themselves, I suggest we will witness an even higher degree of consensus.¹⁶

On this optimistic note, let me now turn to the possible ways of exploring what economists think about policy and how that squares with the reality. First, I consider making use of existing consensus surveys, and then I consider my own type of survey specifically suited for the purpose.

1.1.1 FIRST APPROACH: CONSENSUS LITERATURE AND ACTUAL POLICY

1.1.1.1 CONSENSUS LITERATURE

Fueled perhaps by the notorious jibes about economists' disagreement, there are several studies looking into just what economists agree and disagree upon. The credit for pioneering this area goes first to Samuel Brittan (Brittan, 1972) and then to James Kearl (Kearl et al., 1979).¹⁷ It was the latter's work's

the scientific agenda in natural sciences may be composed more of original and new hypotheses rather than numerous testing and correcting the previous ones, which, again, tends to generate less polemic.

¹⁶ This is, essentially, why I am putting forth my own consensus survey, see chapter 1.1.2 and Appendix.

¹⁷ There were some prior studies inquiring about economists' opinion. For example, there is work done by J. W. Bell on the direction of the post-war US policy (Bell, 1945). It is remarkable for evidence of the post-war interventionism inertia among economists, and also for the shortcomings – almost naiveté – of the way the survey was executed (on the latter point, see e.g. Lansing, 1946).

threads that were then picked up by various authors who focused on consensus among economists in particular regions: by a group of gentlemen headed by Bruno Frey for Europe (Frey et al., 1984), by Martin Ricketts and Edward Shoemith for the UK (Ricketts and Shoemith, 1990), Walter Block and Michael Walker for Canada (Block, Walker, 1988) and then follow-ups on previous US studies: first, by a group around James Kearl (Alston et al., 1992), and lastly by Dan Fuller and Doris Geide-Stevenson (Fuller and Geide-Stevenson, 2003).

Here, I will focus on a brief description of each survey, while in the following section, I will draw conclusions as for what can be considered the economists' opinion.

KEARL ET AL., 1979

As hinted at above, this is the first survey of its kind, motivated explicitly by the alleged disagreement among economists. It consisted of 30 propositions, to which six hundred randomly selected members of the American Economic Association, stratified into four groups (elite academics, academics, government and business) were invited to respond to by choosing from the following: 'generally agree', 'agree with provisions' and 'generally disagree'.¹⁸ The results were drawn from only 211 questionnaires returned.

The degree, and rank, of consensus is based on an index of relative entropy.¹⁹ Besides the consensus itself, the authors

There is a host of other consensus studies I do not take into account here as they focus on specific policy measures or particular groups of respondents. These include e.g. DiLorenzo and High, 1988, on anti-trust policy, or Rustici, 1989, on a support of minimum wage laws. Pope and Hallam, 1986 (and others), look into consensus among agricultural economists on agricultural issues, Whaples, 1995 and 1996, respectively, on economic history among economic historians and on labor issues among labor economists, or Fuchs, 1996 on health care issues.

Finally, some authors focused on the consensus on economic issues among non-economists as well: e.g. Fuller, Alston and Vaughan, 1995, look into politicians' opinion, while Leet and Lang, 2006, map the economic educators' views.

¹⁸ A fourth possible option was 'no answer'. Though not explicitly displayed in the data, it was used to calculate the relative entropy (see below).

¹⁹ An index of relative entropy is a non-linear index between 0 (perfect consensus) and 1 (perfect dissention). It is calculated as a ratio of actual absolute entropy to

also tested, and showed the data to support, the hypotheses that there is greater consensus on micro than on macro, and on positive than on normative issues. In addition, they analyzed the variation of responses across different economists' occupations.

FREY ET AL., 1984

The proposition and responses set from Kearn et al., 1979, became a standard for further country specific studies: Austria (Pommerehne et al., 1983), France (Bobe and Etchegoyen, 1981), Germany (Schneider et al., 1983) and Switzerland (Frey et al., 1982).²⁰ In Frey et al., 1984, a familiar group of economists headed by Bruno Frey compounded the above studies mainly in order to compare the opinion across countries. What they did first, though, was a merge of all the data into one dataset of 932 respondents (out of a total of 2072 economists invited), which is of greatest interest to me as it permits to judge the overall consensus.²¹

Besides that, this study reveals interesting facts: major – almost stunning – differences on some issues across countries, and, what is really its corollary, a smaller degree of consensus in the complete dataset as compared to national datasets.

maximum possible absolute entropy. The absolute entropy is a sum of products of frequency of particular response (p_i) and its log (base 2): $\sum p_i \log_2 p_i$. The maximum possible entropy exists if the responses frequencies are evenly distributed across all options.

The same measure has been employed in all studies I take into account, although some studies use natural log in the equation. This, however, leaves the ranking unaffected.

²⁰ The number of propositions was cut from 30 to 27 by omitting the overtly USA-pertaining statements. In addition, a minor rewording was done in some cases to adjust the meaning to refer to national economy and the different time in which the particular survey was conducted.

²¹ When interpreting the complete dataset, one should keep in mind the weights of national components are a bit disproportional: 91 respondents for Austria, 162 for France, 273 for Germany, 199 for Switzerland, and the familiar 211 respondents for the USA.

BLOCK AND WALKER, 1988

The explicit purpose of the study conducted another half a decade later was to replicate the survey of Frey et al., 1984, in the Canadian environment. The questionnaire was sent out to all 1443 members of the Canadian Economic Association at that time, out of which the authors were able to receive a sample size of 443 – the largest sample size in this type of survey so far.

Walter Block and Michael Walker also went beyond the expected comparison of Canada to other countries. They also tested the Canadian responses for dependency on age, gender, and level of education of respondents, and found all of them significant, in inverted order.

RICKETTS AND SHOESMITH, 1990

This opinion survey, focusing solely on economists in the UK, was different in two aspects. First, it consisted of more propositions (35 instead of 27, or 30 respectively) with less of an overlap with the previous ones (some 20 propositions). Second, it employed a different, five-option response roster: 'strongly agree', 'generally agree', 'neither agree nor disagree', 'generally disagree', and 'strongly disagree'.²² The results were based on a questionnaire received from almost a thousand of economists, more than double the sample size of Block and Walker, 1988.

As became the norm by that time, Ricketts and Shoesmith test the influence of occupation on responses and also the degree of consensus on micro, as opposed to macro, and positive, as opposed to negative, issues. On the latter, they found a corroboration of the thesis in Kearn et al., 1979.²³ The authors further focus on determinants of policy: whether the

²² Ricketts and Shoesmith, 1990, present data on the mean response and the relative entropy. The distribution of particular answers is not published.

²³ In contrast, the surveys in between – Frey et al., 1984, and Block and Walker, 1988 – were not able to reject the hypothesis of no difference in consensus on micro and macro, and positive and normative propositions.

difference can be explained by differences in scientific predictions (an idea associated with Milton Friedman²⁴) or rather differences in normative judgment (an idea associated with Paul Samuelson²⁵). Data in this survey support the thesis that both factors are relevant, but even combined they explain the attitude to policy only to a small extent.

GEACH AND REEKIE, 1991

Further replication of the above studies came from South Africa. Perhaps inspired by then the most recent of the studies, it too contained 35, largely overlapping questions each with 5 response options (although with a different numerical coding going from 5 to 1).²⁶ The questionnaire was sent to all members of the South African Economics Society, out of whom 381 responded.

Besides agreement and the factors determining its degree, the authors compare the results with data of previous studies. As expected, they show the South African economists' opinion is closer to English speaking countries and Germany than to Austria, France or Switzerland.

ALSTON ET AL., 1992

A follow-up on the original Kearn et al., 1979 consisted of a 40-question questionnaire with the same response roster sent to 1350 economists in the US: the stratified random sample included a) elite AEA, b) other AEA, c) government, d) business, e) principles-teachers, and f) evolutionary economists.

²⁴ Says Friedman:

[I]n the Western world, and especially in the United States, differences about economic policy among disinterested citizens derive predominantly from different predictions about the economic consequences of taking action – differences that in principle can be eliminated by the progress of positive economics – rather than from fundamental differences in basic values, differences about which men can ultimately only fight. (Friedman, 1953, p. 4)

²⁵ These ideas are expressed in his textbooks, co-authored with William Nordhaus (see Colander, 1992, p. 197).

²⁶ The wording of the answers was almost identical with Ricketts and Shoesmith, except for the second response option where Geach and Reekie use 'Agree with Reservations'.

The results from 464 responses were used for purposes of comparison in time (1977 and 1990), and further for analysis of the influence of 'vintage of degree'²⁷ on responses. In both cases, some significant differences were revealed.

FULLER AND GEIDE-STEVENSON, 2003

The most recent opinion survey, run in 2000, was the largest set of questions of all (44) sent out to a random sample of 1000 members of AEA. All questions allowed for 3 standard answers: 'Agree' (A), 'Agree with provisos' (A/P) and 'Disagree' (D). The 308 returned questionnaires were analyzed in order to determine the degree of consensus. The authors constructed their own index of consensus based on 3 different measures of consensus, one of them being the relative entropy. The reported responses are contrasted to responses from Alston et al., 1992, and the degree of consensus is compared across these two surveys in order to find out the tendency of consensus in time.

*

To sum up, all of these studies are sets of propositions which stratified groups of economists were invited to respond to by choosing out of three (or five) possible answers. The authors not only derive measures of consensus, but go beyond my current interest: they compare answers of different strata of respondents (occupation, age, gender, degree vintage) and test different hypotheses about consensus (e.g. that there is better agreement in micro than in macro, and in positive, rather than in normative issues). My focus, on the other hand, was just the consensus and the mean answer (weight) in order to derive a set of policy propositions that could be taken to represent the economists' opinion.

The number of propositions ranged from 27 to 44, with some 20 (in no or only negligible modifications) appearing in all of them. The proposition set in each study is quite

²⁷ 'Vintage of degree' means the year, in which the respondents attained their highest degrees.

heterogeneous, with propositions varying both in their focus (micro, macro and even non-economic propositions) and their prescriptiveness (from strictly positive to very normative). In order to assess the impact of economists on policy, I was looking in each study for propositions that would best meet the following criteria:

- a) exhibit a fair degree of consensus;
- b) be malleable to policy interpretation;
- c) be based on economic science.

The first requirement is quite straightforward: the more consensual, the more legitimate it is for me to talk of economists as a group rather than different individuals. So is the second criterion that is essential for juxtaposition of given opinion and actual policy. The last condition is made explicit here because there may be – and, in the surveys, in fact are – issues that fulfill both a) and b) but at the same time do not follow from economics: economists as scientists have no expertise in judging whether a particular proposition is true or not.²⁸

1.1.1.2 WHAT ECONOMISTS THINK

From a fairly brief analysis of all these surveys, one can identify a small group of propositions that not only satisfactorily met the criteria but also appeared quite consistently in all, or most, of surveys. The propositions refer to four issues in public policy, and though none of them says so explicitly, I submit they can be understood as indicating that economists *oppose* the following policies:

- 1) Trade protectionism
- 2) Rent control
- 3) Minimum wage
- 4) Agriculture support

²⁸ For example, surveys typically include proposition that distribution of income should be more equal. Whatever the economist's answer may be, it cannot be derived from economics, and her opinion is therefore just as qualified as the one of a physicist or a high-school drop-out.

In order to substantiate this selection and interpretation, I present the actual survey data for each of these issues.

TRADE PROTECTIONISM

All of the surveys include almost identical statement about the effects of tariffs and import quotas; some of them have additional statements referring to international trade. I recognize that 'trade protectionism' is somewhat wider a term than just tariffs and quotas. The possible explanation why the surveys generally mentioned just tariffs and quotas is that the very statement dates back to 1977 (Kearl et al., 1979) when tariffs and quotas and protectionism were used almost synonymously, and later authors, perhaps in the effort to serve the comparability with previous studies, just followed suit.

Either way, I maintain that economists' stand on tariffs and quotas can be readily extended to include all forms of protectionism: it is well established that substitutes for tariffs and quotas are at least as harmful as their older equivalents. This is supported by the one statement in Ricketts and Shoemith, 1990, comparing the effect of non-tariff and tariff barriers, and one in Alston et al., 1992, referring to dumping and subsidies in international trade (see below).

In the following table (1.1), I present all the protectionism-related statements from all studies in their exact wording along with the distributions of answers, mean answers, the degree of consensus – the relative entropy, and its rank on the survey.

Table 1.1 Protectionism-related survey statements

Survey	Statement in exact wording	Response		Mean weight	Relative entropy [%]	Consensus rank in each survey
		Score	%			
Kearl et al., 1979	Tariffs and import quotas reduce general economic welfare.	3	81	2.8	47	2
		2	16			
		1	3			
Frey et al., 1984	Tariffs and import quotas reduce general economic welfare.	3	57.0	2.43	72	3
		2	30.8			
		1	10.3			
Block and Walker, 1988	Tariffs and import quotas reduce general economic welfare.	3	70.2	2.66	54	2
		2	25.7			
		1	3.8			
Ricketts and Shoemith, 1990	Non-tariff barriers have a more significant effect on trade flows than tariff barriers.	2	N/P	0.6	75	5
		1				
		0				
		-1				
		-2				
	Tariffs and import quotas reduce general economic welfare.	2	N/P	0.8	79	8
		1				
		0				
		-1				
		-2				
Geach and Reekie, 1991	Tariffs and import quotas reduce general economic welfare.	1	27.44	2.15	81	7
		2	47.23			
		3	10.55			
		4	12.14			
		5	2.64			
Alston et al., 1992	Tariffs and import quotas usually reduce general economic welfare.	3	71.3	2.63	57	3
		2	21.3			
		1	6.5			
	The U.S. government should retaliate against dumping and subsidies in international trade.	3	15.1	1.67	78	17-18
		2	35.1			
		1	47.6			
Fuller and Geide-Stevenson, 2003	Tariffs and import quotas usually reduce general welfare of society.	A (3)	72.5	2.67	66	2
		A/P (2)	20.1			
		D (1)	6.0			
	Increasing globalization of the economy, facilitated by the WTO, threatens national sovereignty in the areas of environmental and labor standards.	A (3)	10.7	1.43	77	4
		A/P (2)	21.1			
		D (1)	66.1			
	The U.S. trade deficit is primarily due to nontariff barriers erected by other nations.	A (3)	1.3	1.10	31	1
		A/P (2)	7.4			
		D (1)	87.6			

In all surveys, protectionism-related questions appeared among the most consensual, with the exception of anti-dumping policy question in Alston et al., 1992. All of the mean answers tend to agree with the statement, even though this agreement seems to weaken over time. (After all, the Fuller and Geide-Stevenson, 2003 survey does show – in contrast to Kearl et al., 1979 – *less* consensus, *lower* degree of the mean agreement with the statement and all that despite a *weaker* version of the statement.)^{29, 30}

The latest survey includes two original but equally consensual trade-related statements. Both express popular public sentiments, one in relation to globalization and one in relation to foreign protectionism as a cause of the US trade deficit. Economists largely disagree with both of them, which suggests itself as a disagreement with practicing protectionism.

This is even more explicit in the one statement that runs through all surveys: the effect of protectionism on economic welfare (or welfare of society respectively). If economists generally find trade protectionism incompatible with the general economic welfare, it seems reasonable to draw the conclusion that trade protectionism is a policy economists generally oppose. While it is conceivable that any particular economist finds other ends supreme to economic welfare, the plain fact is that protectionist policy is usually put forth avowedly as a means to secure general economic welfare. In such a setting, the economists' proposition that protectionism in fact *reduces* economic welfare can be interpreted as disagreement with practicing protectionism.

²⁹ While originally the statement read strictly as "Tariffs and import quotas reduce general economic welfare", in Alston et al., 1992, and later this was qualified by the term 'usually', allowing for possible anomalies or exceptions.

³⁰ Such shift may well be a consequence of greater impact of theories purporting justification for protectionism, if only on a theoretical plane. This idea is a subject of chapter 2.1.2.2.

RENT CONTROL

The effects of a price ceiling for rents on quantity and quality of housing are similarly part of every single survey, all of them using in fact the identical statement. In contrast to protectionism, rent control is a much younger type of policy whose means have hardly changed in the course of the century of its practice. I, therefore, proceed directly to the overview of survey data.

Table 1.2 Rent-control-related survey statements

Survey	Statement in exact wording	Response		Mean weight	Relative entropy [%]	Consensus rank in each survey
		Score	%			
Kearl et al., 1979	A ceiling on rents reduces the quantity and quality of housing available.	3	78	2.8	46	1
		2	20			
		1	2			
Frey et al., 1984	A ceiling on rents reduces the quantity and quality of housing available.	3	56.1	2.38	74	5
		2	27.2			
		1	15.0			
Block and Walker, 1988	A ceiling on rents reduces the quantity and quality of housing available.	3	80.4	2.75	45	1
		2	14.4			
		1	4.7			
Ricketts and Shoemith, 1990	A ceiling on rents reduces the quantity and quality of housing available.	2	N/P	1.0	80	9-11
		1				
		0				
		-1				
		-2				
Geach and Reekie, 1991	A ceiling on rents reduces the quantity and quality of housing available.	1	50.79	1.76	72	3
		2	33.68			
		3	6.58			
		4	6.84			
		5	2.11			
Alston et al., 1992	A ceiling on rents reduces the quantity and quality of housing available.	3	76.3	2.7	52	1
		2	16.6			
		1	6.5			

Generally, the question of rent control drew a somewhat greater degree of consensus than protectionism, in terms of its rank, being the most consensual in three out of six surveys. With some regional differences or differences in time, the mean answer again suggests that there is a consensus in opposition to practicing the policy of rent control as long as

the implicit policy goal is assumed to be better quality and higher quantity of housing.³¹

MINIMUM WAGE

Besides the statement on rent control, another common denominator of all surveys under scrutiny was an identical statement on the effect of the minimum wage law on unemployment.

Table 1.3 Minimum-wage-related survey statements

Survey	Statement in exact wording	Response		Mean weight	Relative entropy [%]	Consensus rank in each survey
		Score	%			
Kearl et al., 1979	A minimum wage increases unemployment among young and unskilled workers.	3	68	2.6	75	5-6
		2	22			
		1	10			
Frey et al., 1984	A minimum wage increases unemployment among young and unskilled workers.	3	41.3	2.06	83	14-16
		2	25.5			
		1	31.5			
Block and Walker, 1988	A minimum wage increases unemployment among young and unskilled workers.	3	68.2	2.53	62	4
		2	16.9			
		1	14.7			
Ricketts and Shoemith, 1990	A minimum wage increases unemployment among young and unskilled workers.	2	N/P	0.6	84	14-16
		1				
		0				
		-1				
		-2				
Geach and Reekie, 1991	A minimum wage increases unemployment among the young, the black and the unskilled sections of the population.	1	42.77	1.84	70	2
		2	44.09			
		3	4.20			
		4	5.51			
		5	3.41			
Alston et al., 1992	A minimum wage increases unemployment among young and unskilled workers.	3	56.5	2.36	74	12-13
		2	22.4			
		1	20.5			
Fuller and Geide-Stevenson, 2003	Minimum wages increase unemployment among young and unskilled workers.	A (3)	45.6	2.19	97	28-32
		A/P (2)	27.9			
		D (1)	26.5			

³¹ For a survey of articles on rent control, see Jenkins, 2009.

Eyeballing the above data suggests a lower degree of consensus within all groups, i.e. even within the US and Canadian cohort which in previous cases looked more homogenous. Second, in all surveys it shows a lower degree of agreement with the statement. Particularly interesting is the difference between the two sides of the Atlantic, both in terms of the mean answer and the rank of consensus. Both of these gaps, however, seems to narrow in time: between 1979 and 2003, the question of minimum wage among the American economists apparently came in the direction towards the situation in Europe in 1984.

Yet, all the mean answers lie closer to agreement than disagreement, so if there is anything like the economists' position on the influence of minimum wage on unemployment, it is that it leads to unemployment in those segments rather than the opposite. Interpreting this as opposition towards instituting and enforcing minimum wage laws isn't as easy: the wording of the statement does not imply it as strongly as in the previous cases. Thus, it is conceivable that an economist absolutely agrees with the statement, and yet would not oppose (or, would even favor) minimum wage on some other grounds.

AGRICULTURAL SUPPORT

The last issue is more complex than any one above. The agriculture issues are included in only two surveys that happen to be the most recent ones. This is perhaps because it was not of much interest in the 70's and early 80's when the first surveys were undertaken.

Moreover, the statements in those surveys all vary and refer to different kinds of agriculture interventions, from price regulation to subsidies to the resource allocation.

Table 1.4 Agricultural-support-related survey statements

Survey	Statement in exact wording	Response		Mean weight	Relative entropy [%]	Consensus rank in each survey			
		Score	%						
Ricketts and Shoesmith, 1990	Regulating the price of agricultural products above competitive market levels results in surpluses.	2	N/P	1.5	53	1			
		1							
		0							
		-1							
	Deficiency payments are more efficient instruments of agricultural support than intervention buying.	-2	N/P				0.6	78	7
		2							
		1							
		0							
Geach and Reekie, 1991	The agricultural control boards ensure that prices to the final consumer are lower than they would have been in their absence.	-1	3.16	3.99	81	10			
		2	10.26						
		3	10.26						
		4	36.58						
		5	39.74						
Alston et al., 1992	Economic evidence suggests there are too many resources in American agriculture.	3	48.7	2.29	85	33-37			
		2	23.9						
		1	21.3						
Fuller and Geide-Stevenson, 2003	Economic evidence suggests there are too many resources in American agriculture.	A (3)	33.9	2.09	99	37-42			
		A/P (2)	32.2						
		D (1)	25.5						

Perhaps the only reason for considering this issue as consensual at all is the high consensus ranking of two agriculture questions in Ricketts and Shoesmith, 1990. One of them – the consequence of a price floor in agriculture – ranked no worse than first, with the mean answer right between agreeing ‘generally’ and ‘strongly’. Unfortunately, the policy interpretation of this agreement is almost impossible. The statement refers to a situation whose existence one – even the most ardent proponent of price interventions in agriculture – can hardly deny. Thus, the agreement cannot be taken to imply opposition to price control of farm products.

The second statement from Ricketts and Shoesmith, 1990 seems more malleable to policy interpretation as it uses efficiency as a standard for comparing different ways of agriculture support. Unfortunately, the mean answer is only

half way between the neutral position ('neither agree nor disagree') and 'generally agree'. Reading this as outright opposition (or backing) on the part of economists to the price floors (or deficiency payments) seems a bit irresponsible. So is the interpretation of the effect of agricultural control boards in South Africa.

Finally, the question that lends itself best to policy rendition is the one found in Alston et al., 1992, and Fuller and Geide-Stevenson, 2003. Agreement here would surely be possible to understand as meaning that agriculture is supported too much, and, consequently, that economists would recommend curtailing the extent of farm support. Unfortunately again, despite the relatively high mean answer (between 'agree with provisions' and 'generally agree'), the degree of consensus is very low for such a judgment.

Even though agriculture policy, anecdotally, is very often a subject of economists' criticism, the above surveys cannot do more than indicate a likely presumption that economists do not altogether support the current farm policy, and perhaps, would recommend less government involvement.

*

The above four policies were picked to represent issues economists were asked about and best fitted the three criteria of being consensual, policy-relevant and economic.

What all four issues have roughly in common is the opposition of economists towards such policies. In order to see how these policy recommendations translate into policy, I now propose to confront them with actual government policies.

1.1.1.3 WHAT THE POLICY-MAKERS DO

In the last chapter, I created the set of propositions reflecting, as I tried to show, as closely as possible what economists think should be the economic policy. To find out to what extent this most consensual view is heeded in actual policy, let me now take a look at the latter. For each of the policy issues I provide

a cursory overview of the policy as followed by various governments.

TRADE PROTECTIONISM

One can safely claim economists have now been pushing for removal of trade protectionism, although with sporadic pauses, for centuries. To a certain degree and at least at the beginning, the free trade position was almost synonymous with being an economist. We would think it outrageous to assert that economists have had no impact at all. Even if one skips the spectacular 19th century free trade movement and the resulting trade liberalization, the post-WWII history bears enough of a testimony to the influence economists.

Yet, all that said notwithstanding, the international trade flows still remain firmly managed under the control of government, or super-government, bureaucracy. The extent to which governments today divert flows of goods from the pattern they would have otherwise taken is roughly just as large as 50 or 100 years ago. It is true that after WWII, mainly as a result of GATT/WTO-coordinated effort, the magnitude of tariffs and then even the number and restrictiveness of quotas on imports of individual countries were substantially reduced to numbers that in aggregate appear almost negligible. However, the picture of a radical trade liberalization and unbridled world commerce some are trying to paint suffers from two major flaws.

First, this process was carefully manipulated so as to avoid whole sectors of the economies. Generally, all products that are being made in one country at a *substantially* lower cost than they are being made elsewhere, are to this day subject to major conventional barriers to trade: customs duties combined with quantitative restrictions. Thus, it is precisely these sectors where the benefits of trade would be the greatest, that have been exempted from the trade liberalization process through extra agreements and clauses. The most notorious examples of these 'sensitive' articles are the farm produce and products of metallurgy or textile industries, not to mention the trade in services.

Second, and perhaps even more importantly, even where the conventional tariffs and quotas were reduced or even removed altogether, one cannot conclude it is in line with what economists recommend. This is because the conventional barriers, as they were being removed, were gradually being replaced by a more subtle set of barriers that does not strike the naked eye as protectionism at all, but is just as destructive. This is of course the endless myriad of regulations concerning the imported product. There may be low or no tariffs on the books, but they are still often invoked once the imported good fails to comply with rules of origin or does not meet the right minimum price, or even if the country of the export ceases to maintain reciprocity towards the country of import. Besides that, there are now products that instead of being subject to tariffs and quotas are effectively *banned* from certain markets for various reasons: for not complying with domestic standards of quality, for not being produced in a way the domestic legislation requires. This form of protectionism is less visible because it tends to coincide with ubiquitous domestic regulation.

What can also provide evidence of the deaf ears turned to economists when it comes to trade policy is the justification for having protection in place. Political discussion about trade issues are marred with the same myths that economists exploded centuries ago: it is, for instance, somewhat ironic that the argument tackled by Cantillon, Hume, or Smith – the balance-of-trade argument – finds its way in serious debates on trade policy. Other economists' antidotes to myths about protectionism have not fared any better.

RENT CONTROL

As opposed to trade protectionism, rent control is a much younger form of intervention, emerging only in 20th century as emergency measures. It is usually combined with other types of regulation, namely limits of contractual freedom with regard to a landlord's services and a possibility of eviction.

Economists may be said to have opposed rent control early on, if only on a more general level as having opposed price controls. A classic economic case against rent control was penned by Friedman and Stigler (Friedman and Stigler, 1946), in response to war-time controls.

It is a regulation typically (though not exclusively) administered by local governments which explains the many different arrangements and forms in which rent control is practiced within any country. It also explains why in some cities the rent was successfully decontrolled while in others it stayed.

Notorious for its rent control and rent stabilization record is New York City where it has been practiced under different jurisdictions since 1943 and widely recognized as a cause of poor maintenance and abandoned housing.

MINIMUM WAGE

Minimum wage legislation is a product of labor movements at the end of 19th century. The place of its first enactment is unusual: Australia. Many countries soon followed suit, and today 9 out of 10 countries in the world have legislation of this type. The levels are typically adjusted for inflation and rise in real wages, and – apart from all the other types of intervention I am considering here – there is *no talk whatsoever* in policy-making circles about abolishing it.

AGRICULTURE SUBSIDIES

Intervention in agriculture business reflects the age of this industry, and precedes both rent control and minimum wage. General farm subsidies are, however, a 20th-century phenomenon. In the US, it started again during the Great Depression, in the EU, it was part of the Treaty of Rome.

Despite economists' opinion, farm subsidies continue to exist in almost all developed countries to this day with very weak chances for being dismantled. They also present one of the major blocks on the way to further removal of trade barriers. The agriculture budget in the EU was over 50 billion

for 2005, almost half of the total EU budget (European Commission, 2006, p. 48). In the US, the direct farm subsidies doubled within the last decade, and in 2005 totaled more than \$24 billion (Covey et al., 2006, p. 8).

1.1.1.4 COMPARISON

My first approach to substantiating the idea of a gap between theory and policy was the comparison of what economists think (chapter 1.1.1.2) to what the policy-makers do (chapter 1.1.1.3). My findings do suggest a great deal of difference.³² However, there are certain aspects of this approach that make it deficient in what I want to use it for.

All the above studies I made use of in this first approach were primarily aiming at discerning the degrees and areas of consensus, and at finding possible explanations for variation in time and place or within each group. None of them aimed at what I look for: finding consensus for what policy should or should not be adopted. Thus, in order to use the survey data for the theory-policy gap analysis, one has to deal with a two-fold barrier.

First, even the most agreed upon statements may still appear to some observers so disputable as to cast doubts at the intention to take them as representing the opinion of the whole profession. Second, in trying to use it for the theory-policy gap analysis, one has to further interpret particular statements as supporting or opposing the related policy.

To illustrate both, take, for example, the statement on rent control: *A ceiling on rents reduces the quantity and quality of housing available*. First, although it is the most consensual statement of all, it is barely just 3/4 of all economists who 'generally agreed', while approximately 1 in 5 felt they 'agreed with provisions' and 1 in 20 'generally disagreed' with it. Thus

³² A very similar approach would be the comparison of what economists think to what the policy-makers *think*. This is partly done in Fuller et al., 1995. They found substantial disagreement, but as they limited themselves to the U. S. and did not analyze these differences further, the study is hardly more persuasive than my approaches.

it may be objected that 3 out of 4 is not consensual *enough* to proclaim it an opinion of the whole profession. Second, even if there was a perfect consensus, the statement is couched in positive terms with no explicit or direct policy implications. It may be pointed out then that if this positive statement is to be interpreted as (in fact, turned into) a policy statement, one must take something – in this case, what suggests itself, the ‘general economic welfare’ – to be the implicit norm *shared* by economists. Only then can one proceed to claiming this statement to say that economists think *ceilings on rent should not exist*. But then again, it may be objected that this is question-begging: that economists may agree with the statement, but still be in favor of rent-control.

1.1.2 SECOND APPROACH: POLICY CHANGE CONSENSUS

I try to argue below that the shortcomings of the existing surveys (with respect to the theory-policy gap investigation) I point out above can be alleviated by an alternative type of survey. Such a survey aspires to solve both problems *at once*: a) it is likely to generate greater degrees of consensus, and b) the responses can readily be used to test the theory-policy gap.³³

The essence of the alternative survey lies in changing the thrust of the survey propositions in two ways: a) the propositions focus explicitly on economic policy; b) the propositions invite respondents to express opinion on the *course of change the policy should take*.

The first adjustment is so straightforward – given the goal of theory-policy gap investigation – as to require no further comments.

The second line of adjustment is more subtle. If one desires to identify deviations of policy (reality) from theory (prescription), there is in fact no need for knowing the absolute

³³ Robert Whaples’s recent articles are attempts at something very similar (Whaples, 2006 and 2009).

states of policy economists would prescribe: it is enough to know whether economists find the policy deviating from their prescriptions and if so, in which direction. Thus, instead of asking about *absolute states* of affairs (economic policy) economists consider desirable, the proposition will refer to *direction of changes* of policy economists feel necessary and urge to be undertaken. Namely, the respondent would be invited to choose among three options regarding a given policy measure: a) the policy is too weak, i.e. it should be 'tightened', practiced more vigorously etc.; b) the policy is fine, no need for changes; and c) the policy is too strong, i.e. it should be relaxed. To give an example, instead of inviting to (dis)agree with a statement that "tariffs and import quotas reduce general economic welfare", one will only indicate whether "the extent to which the trade barriers (tariffs, quotas, etc.) are used" should be a) higher, b) unchanged, or c) lower.

Rephrasing the survey propositions in such a way would likely overcome both problems one runs into when trying to use data from past consensus surveys. First, it may draw a more consensual picture of economic profession regarding the policy questions, i.e. about what should actually be done.³⁴ It would not be splitting their opinions through technical considerations, contingent moreover on subjective individual understanding of premises used in propositions.³⁵ Second, the normative part would already be included in the statement and there would then be no need to engage in any interpretation of positive as normative. To give an example

³⁴ As Alec Cairncross, prophetically, noted:

I wonder whether the disagreement between economic theorists, even now, go as deep as their solidarity when confronted with the heresies which so often shape the policies of governments. [...] It can sometimes be easier to reach agreement between economists on what should be done than on matters of theory. (Cairncross, 1985, pp. 6-7)

³⁵ Assessing the statements used in all the surveys is of course critically dependent on the meaning of the words 'generally' or 'provisions' (or any other qualifiers) assigned to it by particular respondents. This vagueness, necessary as it may be for drawing any answers at all, presents no problem for the traditional consensus studies: they primarily compare the *relative* consensus on different issues and there is no reason to assume that different understanding of these words would systematically differ from one statement to another and thus distort the consensus order.

again, economists may have their disagreements about the precise – *absolute* – extent to which the trade barriers should be used, but when asked about how the current extent of trade barriers should *change*, there is likely to be a substantial consensus that trade barriers should be lower than they are.

Technically, one of course has to eliminate possible sources of obscurity and noise. First, the policy the propositions relate to must be specified as a *single-dimensional* policy measure to allow for the higher/unchanged/lower options. One can ask whether the income tax *rate* should be higher/unchanged/lower, but cannot ask (within one question) about the preferred changes in a tax *structure*. In cases where the policy cannot be reduced to one dimension (typically a structure of rates or a set of measures lumped as ‘regulation’), it seems desirable to advise the respondents explicitly to assume that their choices in the surveys refer to all other dimensions simultaneously. For example, when asked about the extent of anti-trust regulation, the respondents should know the options refer to the whole package of measures and assume it is impossible to change its constituent parts. ‘Higher’ then means that the anti-trust regulation should rather be enforced more vigorously or be made more restrictive; ‘lower’ means the opposite; and ‘unchanged’ means that it is either approximately what it should be or it is impossible to make it work better without changing its structure.

One may apply a similar solution to the other source of fuzziness: the *current state of policy* the respondents are asked to suggest adjustments to. Some policy measures may be of such local nature (e.g. rent-control, subsidies, regulation) that respondents may feel that their choice would vary across different areas. Here again, then, the respondents should assume they are taking the position with respect to all areas simultaneously. For example, when asked about the maximum rent that property owners can legally charge for an apartment, the respondents should know the options refer to all areas and assume the legal maxima cannot be changed in different areas in different directions.

Finally, it is important to point out that the data from the survey outlined above would be directly useful for studying the existence and the shape of the theory-policy gap. Apart from using the past consensus surveys to find out what economists deem to be a desirable policy and then comparing it to what the policy actually looks like, with this alternative type of survey it is enough to test the null hypothesis that the mean response is 'no change'. If such a hypothesis is rejected, the gap between theory and policy is established.³⁶ Comparing the mean response with the 'no change' option will also indicate the *direction* in which the policy deviates from the theory and *how much*.

1.1.2.1 SAMPLE SURVEY AMONG CZECH ECONOMISTS

The survey³⁷ was undertaken in December 2008 and January 2009 in cooperation with the Czech Economic Association. It was administered through a web-based system that allowed participation to invited respondents only, while at the same time keeping the identity of individual respondents anonymous throughout the process.³⁸ A total of 708 economists were addressed (were sent the email) out of which 182 economists signed in and participated in the survey. Of these, roughly 75 percent were men; 2 percent were economists below 25 years of age, 48 percent between 26 and 35, 18 percent between

³⁶ Of course, abstracting from the problem of the sample selection.

³⁷ For full details, see Šťastný, 2009.

³⁸ There is no person that has had access to both email list and the login data list. The administrator of the survey (different from the present author, who remained anonymous up to releasing this article) generated the login data, while representatives of the Czech Economic Association compiled the list of addressed economists. Each person on the list (represented by her email) was thus randomly matched with one item from the login data list.

The invited respondents (economists on the email list) came from two sources: 1) members of the Czech Economic Association (both past and present whose email addresses were available), and 2) economists participating in teaching economic subjects at higher education institutions (universities and colleges) in the Czech Republic. While the former group are economists by self-identification, the latter group are economists by profession. Duplicated emails (members of both groups) were eliminated.

36 and 45, 10 percent between 46 and 55, 16 percent between 56 and 65, and 4 percent economists over 66 years of age; 56 percent identified themselves as primarily academic, 20 percent as employed by private business, 9 percent as government employed and 4 percent mainly as enthusiasts.

Table 1.5: Structure of respondents

Age		Gender		What sort of economist do you conceive yourself of?		Gross income per year (in thousands, CZK)		Which political party's program is closest to your vision of economic policy?	
1: below 25	2.2%	1: male	75.8%	1: academic	56.0%	1: 250 or less	9.9%	1: ČSSD (social democratic)	12.6%
2: 26 to 35	48.4%	2: female	22.5%	2: private	20.3%	2: 250 to 500	24.2%	2: KDU-ČSL (Christian conservative)	3.9%
3: 36 to 45	18.1%	3: declined to answer	1.7%	3: government	8.8%	3: 500 to 750	20.9%	3: KSČM (communist)	2.2%
4: 46 to 55	9.9%	-	-	4: enthusiast	3.9%	4: over 750	26.4%	4: ODS (civic conservative)	44.0%
5: 56 to 65	15.9%	-	-	5: other	3.9%	5: declined to answer	18.1%	5: SZ (environmental)	2.7%
6: 66 or more	4.4%	-	-	6: declined to answer	6.6%	-	-	6: other	4.4%
7: declined to answer	1.1%	-	-	-	-	-	-	7: declined to answer	27.5%
Blank response	0%	Blank response	0%	Blank response	0.5%	Blank response	0.5%	Blank response	2.7%

The survey questionnaire consisted of a total of 27 questions, out of which 22 were substantive and 5 were control questions relating to personal traits of respondents.³⁹

Of the 22 substantive propositions, one was a general opinion on the theory-policy gap, and the remaining 21 focused on changes in policy. These could be broadly classed as 3 related to international trade, 4 to fiscal policy,

³⁹ A sample of such a survey designed for Czech Republic can be found in the Appendix.

2 to monetary policy, 9 to regulatory issues, and 3 to subsidies of various kinds.

Most of the issues have their counterparts in previous studies, the exception being perhaps the proposition 21 on university education cost sharing by students, which is peculiar to Czech Republic.⁴⁰

The responses to substantive propositions were coded with numerical values of 1, 2 or 3.⁴¹ The value of 1 means 'higher', 2 means 'unchanged' and 3 means 'lower' with the exception of propositions #19 and #21 where the order is reversed (1 means 'lower' and 3 means 'higher').⁴²

Table 1.6: Survey propositions and responses overall characteristics

#	Proposition	Mean	Std. Dev.	Response distribution			
				1	2	3	Blank
1	Do you think the economic policy reflects in a sufficient way the insights of economic theory and the policy recommendation made by economists (i.e. that they are not systematically distorted by policy)?	1.812	0.391	18.7%	80.8%	-	0.5%
2	The extent to which trade barriers (tariffs, quotas etc.) are used should be:	2.370	0.698	12.6%	37.4%	49.5%	0.5%
3	The extent to which antidumping and similar trade-political proceedings against foreign producers are used should be:	2.162	0.806	25.3%	31.9%	41.2%	1.6%
4	The amount of attention paid by policy-makers to the balance-of-trade deficit should be:	1.867	0.702	31.9%	48.4%	18.7%	1.1%
5	The size of the budget deficit should be:	2.749	0.558	6.0%	12.6%	79.7%	1.6%
6	The size of the government expenditures should be:	2.584	0.692	11.5%	17.6%	68.7%	2.2%

⁴⁰ University education is supplied free of charge to all students of public universities. Introducing some sort of students' participation in covering the cost has been a subject of public debate ever since the beginning of the transformation.

⁴¹ Proposition #1 was an exception: 1 means 'yes' and 2 means 'no'.

⁴² The reason for such reversal is to have a common interpretation of value 1 as a plea for more (and value 3 as a plea for less) interventionist policy compared to the status quo (see below, p. 39 and on).

#	Proposition	Mean	Std. Dev.	Response distribution			
				1	2	3	Blank
7	The marginal rate of the income tax should be:	2.421	0.693	11.5%	33.5%	52.7%	2.2%
8	The size of the total tax burden should be:	2.683	0.582	6.0%	19.2%	73.6%	1.1%
9	The rate of the money supply growth should be:	2.045	0.485	9.3%	74.2%	13.7%	2.7%
10	The level of the inflation target set by the central bank should be:	2.039	0.490	9.9%	74.2%	13.7%	2.2%
11	The extent to which environmental regulation is used should be:	1.852	0.805	39.6%	31.9%	25.3%	3.3%
12	The extent to which regulation is used to protect consumers should be:	1.709	0.728	44.5%	37.9%	15.9%	1.6%
13	The extent to which the anti-trust authority interferes with the economy should be:	1.944	0.721	28.6%	47.3%	23.1%	1.1%
14	The difficulty with which employees can be laid off should be:	2.581	0.596	5.5%	30.2%	62.6%	1.6%
15	The legislated power of the labor unions should be:	2.580	0.576	4.4%	33.0%	62.1%	0.5%
16	The extent to which trade in illicit drugs is regulated should be:	1.737	0.800	47.8%	28.6%	22.0%	1.6%
17	The extent to which trade in human organs is regulated should be:	1.680	0.714	45.6%	37.9%	14.3%	2.2%
18	The level of legislated minimum wage should be:	2.361	0.721	14.3%	34.6%	50.0%	1.1%
19	The legislated maximum rent that can be charged for apartments should be:	2.506	0.705	12.1%	24.2%	61.5%	2.2%
20	The extent to which farming is subsidized by government should be:	2.440	0.722	13.7%	28.6%	57.7%	0.0%
21	The extent to which university students share the cost of university education should be:	2.725	0.536	4.4%	18.7%	76.9%	0.0%
22	The extent to which investment perks are used should be:	2.326	0.757	17.6%	31.9%	50.0%	0.5%

CONSENSUS

The strength of consensus on individual issues is something one may infer in various ways.⁴³

⁴³ These could easily include the standard deviation of response values (for standard deviations, see table 2 above). It is not, however, considered here due to a lack of a sensible dividing line between consensus and non-consensus. One could then use such criterion for consensus *ranking* only.

The elementary indication of *some* degree of consensus can be gained by testing the null hypothesis that there is no consensus whatsoever, i.e. that there is a uniform distribution of answers.⁴⁴ By using the χ^2 goodness-of-fit statistics, one can find out that the idea of no consensus can be – at 1% significance level – easily rejected in 19 out of 21 policy issues. The two exceptions were a) the extent of use of antidumping proceedings (#3, p-level=0.0169) and especially b) the extent of use of environmental regulation (#11, p-level=0.0739). On this account then, it seems that the proverbial idea that there is no consensus among economists is unwarranted: even on a significance level of 0.01%, such a hypothesis would be rejected in 16 out of 21 cases.

Another measure of consensus, used in all traditional consensus surveys, is the relative entropy index (ϵ). Although such a measure is non-linear, and indicates only a rank of consensus, some authors take $\epsilon=0.80$ as the threshold for positive indication of consensus (Fuller and Geide-Stevenson, 2003, p. 370).⁴⁵ By such a standard, only 8 of the 21 propositions can be regarded as consensual. This is remarkable for two reasons that immediately come to one's mind. First, the hopes of drawing a dramatically more consensual image of economists' opinion seem to have been too optimistic. The values of the relative entropy, compared to the values in the past surveys, not only do not seem lower, but are in fact higher. The lowest relative entropy in the present survey was 0.556 (the proposition about the size of the budget deficit) while in other surveys the values of below 0.5 are not exceptional. Second, the issues that were in previous studies

⁴⁴ Arguably, rejecting the uniform distribution is a long way from proving the existence of consensus, but it at least rules out the situations where economists as a group would not even lean to any particular opinion.

⁴⁵ The relative entropy indices may not be readily comparable across different surveys. Their exact values will depend on the number of response options and the choice of whether to consider unanswered propositions as one of the options. The present study disregarded the blank answers, which is why the resulting indices are actually higher (indicating *lower* consensus) than in some of the previous surveys where reported indices were taking blank answers as a separate option (e.g. Kearn et al., 1979).

traditionally very consensual do not stand out in the present survey among Czech economists as the subject of much consensus. The traditional proposition on tariffs and quotas as reducing the welfare of society, for example, places always among the most consensual issues with ϵ ranging from 0.47 to 0.81. In the present survey (in a modified form that aspired to draw *greater* consensus), the tariff proposition (#2) came out as only moderately consensual: it ranked 12 out of 21, with $\epsilon=0.89$.⁴⁶ Similarly mediocre consensus was indicated in the proposition regarding rent control (#19): while in previous studies the ϵ ranged from 0.45 to 0.80, here it ranked 9 out of 21 with $\epsilon=0.817$.

There are two alternative indicators of consensus. One is focused on the frequency of the modal response. If one chooses to flag propositions with the frequency of the mode at 67% or more as consensual, only 6 propositions would appear as consensual.⁴⁷ The other alternative would be to focus on the least frequent of the three responses (the 'anti-modal' response) to indicate consensus that policy should decidedly not change in a particular direction, i.e. a broad agreement it should stay the same or move in the other direction.⁴⁸ At a frequency limit of 16.6%, 15 propositions pass as consensual; at a stronger limit of 10%, only 6 will pass.⁴⁹

*

Taking all four consensus benchmarks together, the following 6 propositions pass as strongly consensual: a) the

⁴⁶ A closely related issue on the use of antidumping proceedings (#3) fared even worse: it ranked 20 out of 21, with $\epsilon=0.981$.

⁴⁷ As much as the precise choice of the limit requisite for consensus will always remain arbitrary, the choice of 67% is rationalized as double the frequency expected under uniform distribution.

⁴⁸ All distributions were unimodal, the middle option of 'unchanged' was never the least frequent response. This provides another rationalization of such measure of consensus: some respondents might have presumably oscillated between the two neighboring options, which is why the sum of their frequencies may be interpreted loosely as a 'broad agreement'.

⁴⁹ The choices of threshold are again arbitrary, yet the 16.6% limit is substantiated as a half of the expected frequency under uniform distribution.

size of the budget deficit (#5), b) the government expenditures (#6), c) the total tax burden (#8), d) the money supply growth (#9), e) the level of inflation target (#10), and f) the university education cost-sharing by students (#21). Three out four indicators of consensus were met by the propositions relating to the employee lay-off difficulty (#14) and the labor union power (#15), and at least two out of four indicators were met by another 7 propositions, relating to a) trade barriers (#5), b) the marginal income tax rate (#7), c) consumer protection (#12), d) organ trade regulation (#17), e) minimum wage (#18), f) rent control (#19) and g) the farm subsidies (#20). On the other hand, two propositions failed to meet any of the benchmarks: a) the use of antidumping proceedings (#3), and b) the environmental regulation (#11). As far as *areas* of policy are concerned, Czech economists showed the greatest consensus in the macroeconomic area of fiscal and monetary policy.⁵⁰

Table 1.7: Testing the consensus existence

#	Propositions	Uniform distribution hypothesis (χ^2 GOF)		Relative entropy (RE)		Mode Frequency Test (MFT)		Anti-mode Frequency Test (AMFT)		Composite consensus	
		p-value	GOF rank	s	RE rank	Mode frequency	MFT rank	Anti-mode frequency	AMFT rank	Sum of ranks	Composite rank
2	The extent to which trade barriers (tariffs, quotas etc.) are used should be:	0.000	12	0.890	12	0.497	14	0.127	11	49	12
3	The extent to which antidumping and similar trade-political proceedings against foreign producers are used should be:	0.017	20	0.981	20	0.419	20	0.257	20	80	20
4	The amount of attention paid by policy-makers to the balance-of-trade deficit should be:	0.000	16	0.937	17	0.489	15	0.189	17	65	16
5	The size of the budget deficit should be:	0.000	1	0.557	1	0.810	1	0.061	5	8	2

⁵⁰ On the strikingly opposing nature of such consensus, see the end of the next section and footnote 54.

#	Propositions	Uniform distribution hypothesis (χ^2 GOF)		Relative entropy (RE)		Mode Frequency Test (MFT)		Anti-mode Frequency Test (AMFT)		Composite consensus	
		p-value	GOF rank	ϵ	RE rank	Mode frequency	MFT rank	Anti-mode frequency	AMFT rank	Sum of ranks	Composite rank
6	The size of the government expenditures should be:	0.000	4	0.740	7	0.702	6	0.118	8	25	7
7	The marginal rate of the income tax should be:	0.000	11	0.867	11	0.539	11	0.118	8	41	10
8	The size of the total tax burden should be:	0.000	3	0.648	3	0.744	5	0.061	4	15	3
9	The rate of the money supply growth should be:	0.000	8	0.651	4	0.763	3	0.096	6	21	4
10	The level of the inflation target set by the central bank should be:	0.000	9	0.658	5	0.758	4	0.101	7	25	7
11	The extent to which environmental regulation is used should be:	0.074	21	0.982	21	0.409	21	0.261	21	84	21
12	The extent to which regulation is used to protect consumers should be:	0.000	17	0.929	16	0.453	19	0.162	15	67	17
13	The extent to which the anti-trust authority interferes with the economy should be:	0.000	19	0.956	19	0.478	17	0.233	19	74	19
14	The difficulty with which employees can be laid off should be:	0.000	5	0.741	8	0.637	7	0.056	3	23	5
15	The legislated power of the labor unions should be:	0.000	6	0.727	6	0.624	9	0.044	2	23	5
16	The extent to which trade in illicit drugs is regulated should be:	0.000	18	0.950	18	0.486	16	0.223	18	70	18
17	The extent to which trade in human organs is regulated should be:	0.000	15	0.914	14	0.466	18	0.146	14	61	15
18	The level of legislated minimum wage should be:	0.000	13	0.903	13	0.506	12	0.144	13	51	13
19	The legislated maximum rent that can be charged for apartments should be:	0.000	7	0.817	9	0.629	8	0.124	10	34	9
20	The extent to which farming is subsidized by government should be:	0.000	10	0.863	10	0.577	10	0.137	12	42	11
21	The extent to which university students share the cost of university education should be:	0.000	2	0.594	2	0.769	2	0.044	1	7	1
22	The extent to which investment perks are used should be:	0.000	14	0.925	15	0.503	13	0.177	16	58	14

THEORY-POLICY GAP: EXISTENCE

Overall, there is the general statement on the theory-policy relationship the respondents were asked to agree or disagree with (proposition #1). Over 80% of respondents answered in the negative, which can be interpreted as substantial disagreement with the way economic insights are incorporated into policy. This is a fairly robust substantiation of the notion of economists' overall frustration with the transfer of knowledge.

With respect to particular areas of policy, one can detect economists' disagreement with it in several ways.

Most simply, one gets a good idea of the size of the gap (although not of its existence) by taking the deviation of the measured mean of economists' responses from what it would be were economists in perfect agreement with the current policy (i.e. from the mean value of 2.0). The greater the deviation, the greater the gap.

Second, one can test the existence of the gap by testing the null hypothesis that the mean response value equals 2.0, meaning preference for the status quo ('unchanged'). If the hypothesis is rejected, there is a reason to believe the policy does not reflect the economists' recommendation. By this standard, on 1% significance level, 16 out of the 21 policy propositions (as judged by economists' mean opinion) seem at variance with the current policy, while 15 would have passed such a gap test even on the 0.01% significance level. The propositions that would not pass such a test even on the 10% significance level relate to a) the money supply growth (#9), b) the level of inflation target (#10), and c) the anti-trust legislation (#13).

An alternative test of the existence and size of the theory-policy gap is the ratio of the greater of the two pro-change response frequencies to the sum of the frequencies of the alternative responses, which I call a *Strength-of-Change Index* (SoCI). Its value will be 0 where there is a unanimous consensus on the appropriateness of the current policy ('unchanged'), and will rise with the size of the support for

either change. The values of SoCI over 1 indicate a greater support for any change than for the status quo, i.e. they provide some evidence of the theory-policy gap. While on such an account, 11 out of the 21 policies in consideration show a gap, 4 of these policies show a substantial degree of the gap by virtue of the SoCI exceeding the value of 2: a) the size of the budget deficit (#5), b) the government expenditures (#6), c) the total tax burden (#8), and d) the university education cost-sharing by students (#21).⁵¹ On the other hand, the idea about a theory-policy gap is least substantiated (SoCI below 0.5) in these areas: a) the money supply growth (#9), b) the level of inflation target (#10), and c) the anti-trust legislation (#13).

*

In sum, the existence of the theory-policy gap is fairly well established both on the general level and on the level of some of the policy issues. Taking the ranks of all 3 measures of the gap together, one may design a composite gap index to rank propositions or areas of policy according to the size of the gap.

There is a remarkable fact to be noted about the size of the gap – i.e. frustration – when it comes to macroeconomic issues. While there is a widespread agreement that fiscal policy *should change*,⁵² there is by contrast an overwhelming consensus on the appropriateness of the current monetary policy.^{53, 54}

⁵¹ The SoCI value of 2.0 indicates that $\frac{2}{3}$ (67%) of the respondents are in favor of the particular change. As in previous cases (see note 47), 67% threshold is double the frequency expected under uniform distribution of responses.

⁵² All 4 propositions relating to it (#5 through #8) ranked in terms of SoCI of their response distributions among the most pro-change (1st, 3rd, 4th and 9th of 21 in the composite gap index).

⁵³ The response distributions of both propositions related to it (#9 and #10) were overall the least pro-change of all, which implies a great deal of approval of the policy.

⁵⁴ This may seem to be a result of a self-serving bias of Czech economists: there is a high share of central bank employees and fellows (past or present) among Czech economists (especially members of Czech Economic Association). On the other hand, the survey responses are far from confirming this hypothesis: all three big groups of types of economists (academic, private business and government) have similar mean responses to these statements.

Table 1.8: Testing the existence of the theory-policy gap

#	Propositions	Deviation of Mean from Status Quo (2)		Status Quo Mean hypothesis		Strength of Change Index (SoCI)		Composite Gap	
		Value	Deviation rank	p-value	p-value rank	Value	SoCI rank	Sum of ranks	Composite rank
2	The extent to which trade barriers (tariffs, quotas etc.) are used should be:	0.370	10	0.000	10	0.989	12	32	10
3	The extent to which antidumping and similar trade-political proceedings against foreign producers are used should be:	0.162	16	0.008	16	0.721	16	48	16
4	The amount of attention paid by policy-makers to the balance-of-trade deficit should be:	0.133	18	0.012	17	0.475	18	53	18
5	The size of the budget deficit should be:	0.749	1	0.000	2	4.265	1	4	1
6	The size of the government expenditures should be:	0.584	4	0.000	6	2.358	4	14	4
7	The marginal rate of the income tax should be:	0.421	9	0.000	9	1.171	9	27	9
8	The size of the total tax burden should be:	0.683	3	0.000	3	2.913	3	9	3
9	The rate of the money supply growth should be:	0.045	20	0.217	19	0.164	20	59	19
10	The level of the inflation target set by the central bank should be:	0.039	21	0.286	20	0.163	21	62	21
11	The extent to which environmental regulation is used should be:	0.148	17	0.016	18	0.692	17	52	17
12	The extent to which regulation is used to protect consumers should be:	0.291	14	0.000	14	0.827	15	43	14
13	The extent to which the anti-trust authority interferes with the economy should be:	0.056	19	0.302	21	0.406	19	59	19
14	The difficulty with which employees can be laid off should be:	0.581	5	0.000	5	1.754	5	15	5
15	The legislated power of the labor unions should be:	0.580	6	0.000	4	1.662	7	17	6
16	The extent to which trade in illicit drugs is regulated should be:	0.263	15	0.000	15	0.946	13	43	14
17	The extent to which trade in human organs is regulated should be:	0.320	13	0.000	12	0.874	14	39	13
18	The level of legislated minimum wage should be:	0.361	11	0.000	11	1.022	10	32	10
19	The legislated maximum rent that can be charged for apartments should be:	0.506	7	0.000	7	1.697	6	20	7
20	The extent to which farming is subsidized by government should be:	0.440	8	0.000	8	1.364	8	24	8
21	The extent to which university students share the cost of university education should be:	0.725	2	0.000	1	3.333	2	5	2
22	The extent to which investment perks are used should be:	0.326	12	0.000	13	1.011	11	36	12

THEORY-POLICY GAP: PATTERN

Another interesting fact retrievable from the survey is the pattern of the gap, i.e. the direction of the change economists deem desirable. Namely, the survey responses may be used to analyze economists' opinion on the appropriateness of government involvement (interventionism) in the economy.

All policy-specific propositions invite responses that can be interpreted as more interventionist, neutral, or less interventionist. The pro-interventionist responses were coded with value 1, while the responses calling for lower interventionism were coded with value 3.⁵⁵ The intermediate 'unchanged' option was always coded with value 2.

The pattern of the gap may be analyzed in two dimensions. One can consider the gap with respect to an individual proposition to find out, for instance, whether economists find the current policy too interventionist, too laissez-faire, or just about right. Alternatively, one may diagnose the pattern of responses of an individual economist to all propositions to find out, for example, how interventionist or laissez-faire the particular economist is.

Individual Propositions

To facilitate the first type of analysis, a simple benchmark – the *Laissez-faire index* (LFI) – was developed to measure how much the mean response deviates from the 'unchanged' response in the less interventionist direction. The positive values of LFI indicate less interventionist responses, while negative values are indicative of more interventionist opinions. Areas in which the LFI passes the test for being significantly positive (the null hypothesis being $LFI \leq 0$) are then considered areas in which economists share a less interventionist position.

⁵⁵ The response 'higher' is generally the more interventionist one, while 'lower' is generally the less interventionist one. There are only two exceptions: the propositions on a) rent control (#19) and b) the university education cost sharing by students (#21). The coding, however, remained unaffected: 'higher' was taken as less interventionist and coded 3, while 'lower' as more interventionist and coded 1.

On 1% significance level, 13 out of 21 policies seem currently too interventionist for economists' tastes. Of the 8 remaining, only 5 areas of policy are too laissez-faire,⁵⁶ while the 3 are not significantly different from being just about right.

The results are surprising in many respects. On the one hand, there is an unusually strong support for lower interventionism in fiscal policy (#5 through #8) and labor markets (#14, #15 and #18). On the other hand, there is strikingly high support for *more* interventionism when it comes to a) trade in human organs, b) trade in illicit drugs, c) consumer protection, and perhaps even d) the role of trade deficit as a policy benchmark. Opposition to all these issues of course enjoys high *popular* support, while economists are typically the rare (if not the only) detractors. Apparently, this is not the case of economists in the Czech Republic.⁵⁷

⁵⁶ This is established by testing the alternative hypothesis that LFI is negative (i.e. the null hypothesis being $LFI \leq 0$).

⁵⁷ Of particular interest are opinions on the human organs and illicit drugs trades. In fact, both of these markets are completely black. There is an absolute ban on any trade in these goods (in Czech Republic, as much as in most other places). There is then not much scope for policies to be conceivably more interventionist – which is what economists on average are calling for – save perhaps for better enforcement of these bans (more resources to prevent trades and/or higher penalties from breaking the bans).

Table 1.9: Testing the gap pattern

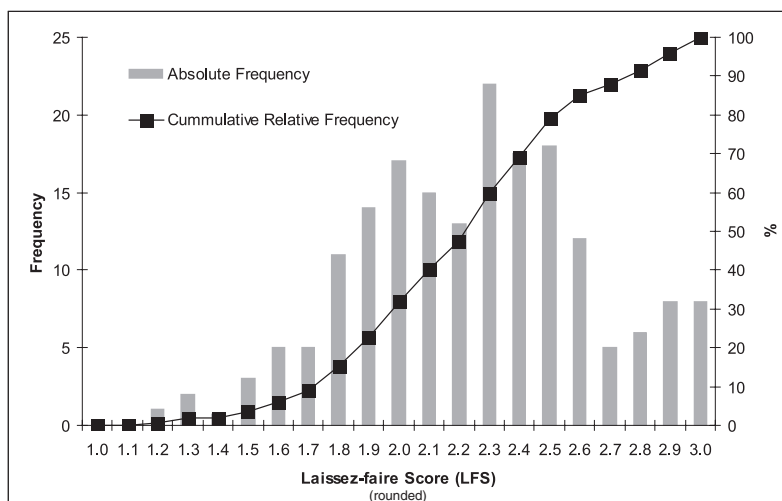
#	Propositions	Laissez faire Mean hypothesis (>2)		faire Index (LFI)	
		p-value	p-value rank	Value	LFI rank
2	The extent to which trade barriers (tariffs, quotas etc.) are used should be:	0.000	10	0.370	10
3	The extent to which antidumping and similar trade-political proceedings against foreign producers are used should be:	0.004	13	0.162	13
4	The amount of attention paid by policy-makers to the balance-of-trade deficit should be:	0.994	18	-0.133	17
5	The size of the budget deficit should be:	0.000	2	0.749	1
6	The size of the government expenditures should be:	0.000	6	0.584	4
7	The marginal rate of the income tax should be:	0.000	9	0.421	9
8	The size of the total tax burden should be:	0.000	3	0.683	3
9	The rate of the money supply growth should be:	0.108	14	0.045	14
10	The level of the inflation target set by the central bank should be:	0.143	15	0.039	15
11	The extent to which environmental regulation is used should be:	0.992	17	-0.148	18
12	The extent to which regulation is used to protect consumers should be:	1.000	20	-0.291	20
13	The extent to which the anti-trust authority interferes with the economy should be:	0.849	16	-0.056	16
14	The difficulty with which employees can be laid off should be:	0.000	5	0.581	5
15	The legislated power of the labor unions should be:	0.000	4	0.580	6
16	The extent to which trade in illicit drugs is regulated should be:	1.000	19	-0.263	19
17	The extent to which trade in human organs is regulated should be:	1.000	21	-0.320	21
18	The level of legislated minimum wage should be:	0.000	11	0.361	11
19	The legislated maximum rent that can be charged for apartments should be:	0.000	7	0.506	7
20	The extent to which farming is subsidized by government should be:	0.000	8	0.440	8
21	The extent to which university students share the cost of university education should be:	0.000	1	0.725	2
22	The extent to which investment perks are used should be:	0.000	12	0.326	12

Individual Economists

One can infer the laissez-faire predilections of individual economists by his or her mean response to all survey propositions, which I call a *Laissez-faire Score* (LFS). With values naturally ranging from 1 to 3, the higher the score, the more laissez-faire responses the given economist provided. The LFS – as a proxy for ideology – can be used along with

other variables describing personal traits of respondents to analyze possible determinants of responses. Distribution of LFS across the survey respondents is shown on the following histogram.

Figure 1.1: The Laissez-faire Score histogram for all survey respondents



The LFS histogram sketches the ideological structure of respondents. The rightward skew of the distribution seems to confirm the bent of the economic profession to prefer less intervention than is the case with the current policy.⁵⁸

SAMPLE SURVEY CONCLUSION

By way of concluding, there are several general remarks regarding the goal and the finding of the survey that merit mentioning.

⁵⁸ This is far from establishing the general existence of such preference. For findings to the contrary, see e.g. Klein and Stern, 2007.

1) The idea that there is a greater degree of consensus regarding changes in policy (rather than regarding the absolute state of policy) was not established.

Although almost all issues show certain opinions to which responses of economists gravitate, the degree of consensus (measured e.g. by the relative entropy index) is not higher than the consensus regarding the absolute state of policy. Failing to establish the superiority of the present type of survey in generating a consensual impression is not, of course, tantamount to denying it. It is possible that had the traditional type of survey been submitted to Czech economists, one would see lower degrees of consensus compared to the ones generated by the present type of survey. Thus, given the differences among degrees of consensus in different countries (Frey et al., 1984), it seems essential to compare the two types of surveys on the same sample of respondents.⁵⁹

2) The very existence of the gap seems established.

In most of the issues the survey was looking into, the theory-policy gap is established by rejecting the null hypothesis on the 'no change' option being the mean response. Moreover, in many cases the gap was very substantial, as measured by the prevalence of the 'pro-change' option relative to the 'no change' option.

3) The economists seem to find policy too interventionist.

Although perhaps less frequently than one would expect, the policy typically deviates from prescription in a pro-interventionist direction.

1.2 THE FRUSTRATED ECONOMIST

In the previous chapter, I hope to have provided some evidence of the gap between the economists' advice or opinion

⁵⁹ Ideally, the Czech economists should have been submitted both types of surveys. This was not done out of concerns of diminishing number of respondents.

and the actual policy, even though I showed the evidence could be made more persuasive than it is now.

An average economist, being aware of this gap, particularly in combination with his social-reform proclivities (discussed at the beginning of chapter 1) and given the size of the gap and its endurance in time, must necessarily feel frustrated. No matter how persuasive one finds the gap evidence presented above, economists *are* on record expressing precisely such sentiments.

Moreover, it is not just a matter of the last couple of decades. As early as 1926, Glenn Hoover sighed in an excellent concise essay about the lack of progress in the application of economics, making use, of course, of the protectionism example:

There is probably no science which has made so little progress in its application as the science of economics. The most elementary principles are as hotly disputed today as ever, except where despair and boredom has supplanted prejudice and passion. The British electorate fights over "protection" [...] with the same weapons their grand-fathers used in the days of Cobden and Bright. (Hoover, 1926, p. 57)⁶⁰

F. A. Hayek, only a few years later, commented on economists influence upon policy as follows:

[T]he economist appears to be hopelessly out of tune with his time, giving unpractical advise to which the public is not disposed to listen and having no influence upon contemporary events. (Hayek, 1933, p. 121)

Interestingly, this was written amidst the Great Depression, during which some economists – the progressive institutionalists and would-be Keynesians – enjoyed quite some attention, or

⁶⁰ Hoover's complaints are ironic in the light of the outbreak of protectionism during great depression that his namesake helped to spark (or, at any rate, refused to prevent): on May 4, 1930, 1028 American economists asked President Hoover in an open letter to veto the Smoot-Hawley tariff. Published on May 5, 1930, in the New York Times, it came to no effect.

more attention, at any rate, than before. It was no lesser a person than Keynes who famously declared three years after Hayek's complaints that

Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually the slaves of some defunct economist. (Keynes, 1953, p. 383)

In this passage, as evident from the use the pejoratively loaded adjective, Keynes was by no means conceding his own influence. Unbelievable as it is, as late as in 1936 he was complaining about too much of an influence of his intellectual rivals (whom he termed classic, or orthodox), and a lack of influence of his own – by implication non-defunct – ideas.

Whoever was defunct at that time, both groups did feel frustrated. In the very same year, Will Hutt expressed that on behalf of the economists of the 'classical tradition':

Every independent and serious economist who has some concern for the well-being of the community must, if his beliefs lie in the path of 'orthodox' or Classical tradition, be aware of a periodic recurrence of a sense of utter helplessness. On all sides he thinks he sees the survival of ignorance and confusion of thought on matters which affect human welfare; and he feels that nothing that it is within his power to do or say can have the slightest effect in checking the accumulation of wrong ideas and false policies which they bring forth. He recognizes that in spheres in which policy and action can be influenced, he is doomed to virtual dumbness to-day. (Hutt, 1936, p. 34)⁶¹

The complaints in this regard went well beyond the immediate 1936 controversy between Keynes and his converts and the rest of the profession. Frank Knight, by that time a doyen of American economists, voiced his disappointment in his 1950 AEA presidential address in a particularly moving fashion:

⁶¹ See also *ibid.*, pp. 34-37.

I have been increasingly moved to wonder whether [...] economists [...] may not be in a position that Cicero, concerning Cato, ascribed to the augurs of Rome – that they should cover their faces or burst into laughter when they meet on the street. Thus, [...] my interest has of late tended to shift [...] to the question of why people so generally, and the learned élite in particular [...], choose nonsense instead of sense and shake the dust from their feet at us. And also, why the theorist is so commonly ‘in the dog house’ among economists [...].

The free-traders, as has been said, win the debates but the protectionists win the elections [...]. Inflation is of course to be brought on as a more pleasant alternative to taxation and then suppressed by law and police action [...].

The serious fact is that the bulk of the really important things that economics has to teach are things that people would see for themselves if they were willing to see. And it is hard to believe in the utility of trying to teach what men refuse to learn or even seriously listen to. (Knight, 1951, pp. 2-4)

By the middle of the 20th century, some economists felt not only lacking influence, but loosing it too. The simple truths economists thought they were able to instill in policy were no longer taken for granted and were ridiculed as old dogmas:

[T]here can be no doubt that in recent years the authority of economic theory has declined. The scholars in many important branches of the social sciences related to economics do not even deem it worth while to acquaint themselves with the economist’s techniques. Those who make the important economic decisions of the world often brush off the simpler truths of economics as irrelevant or even misleading. The very mention of economic laws arouses generally a restive feeling that some very old, utterly uninteresting, and entirely obsolete incantation is being mumbled. (Jewkes, 1955, p. 90)

Feelings of frustration may seem a bit hysterical to people who point out the necessity of a difference between theory and policy everywhere.⁶² If this were the case, economists would

have as much to complain about as any other scientists. But there are reasons to believe that economists are special in the extent they are being ignored. This was aptly brought home by many authors. Frank Fetter complained:

In building a costly house, architects are employed; in making roads and bridges, engineers; in all the material arts and sciences the value of special training is recognized. But the work of fitting our economic legislation and policy to rapidly changing conditions is still entrusted to men with little or no economic training. (Fetter, 1925, p. 16)

In Europe, Erwin von Beckerath drew almost an identical parallel:

It is hardly possible to imagine the Government giving a contract for the construction of a large bridge without calling upon the services of engineers and technologists who received their training at universities and colleges [...]. However, it is quite possible, although no longer the rule, for a statesman, when making an important decision of policy in economic or financial matters, to dispense with the cooperation of economists. (von Beckerath, 1956, pp. 16-17)

While Fetter and von Beckerath were writing this in the 20's and 50's, there hasn't been much change since. Arnold Harberger describes the life of policy economists in the 1990's and its impact on their numbers:

[Having] to endure with frustration, waking up every morning to go out and fight battles they rarely expect to win. [...] This is the life of the typical policy economist; small wonder that after some years many end up disillusioned and

⁶² Robert Merton, the eminent sociologist of science, tentatively lists several factors making for the gap between research and policy (Merton, 1949, pp. 175-178):

- focus of research on problems of no practical importance,
- contingency of theoretical advice upon conditions uncontrolled in practice,
- impossibility of extrapolation of findings from one group of problems to another,
- prejudice of either researcher or policy maker,
- limited finding of research,
- risk attitudes of the policy-maker,
- lack of communication between researcher and policy-maker,
- status of the researcher.

drift off to less frustrating occupations and pursuits. (Harberger, 1993, p. 2)⁶³

Similarly, Paul Krugman adds:

The role of the economist who cares about policy can be dispiriting: one may spend years designing sophisticated theories and carefully testing ideas against evidence, then find politicians turn again and again to ideas you thought had been discredited decades or even centuries ago, or make statements that are flatly contradicted by the facts. (quoted in Wyploz, 1999, p. 66)⁶⁴

As long as economists believe their knowledge can contribute to the wellbeing of mankind, ignoring this knowledge by policy-makers and the public at large cannot fail to cause bitterness among economists. Looking at the role of science in policy-formation in such a perspective was given a fitting name by one scholar: an 'orphan theory' of the scientists' political status.⁶⁵

Given the fact that economists as separate scientists have been around for some two or three centuries, trying to influence policy all along, largely failing in it all along, and ending up bitter and frustrated, one can conjecture there is something interesting going on in the field. Let me then delve into the economics of economic science in order to see the relationship between theory and policy in a better light.

⁶³ It is significant to note that Harberger – apart from previous authors – talks specifically of 'policy economists', which implies some sort of process within the economic profession which turned part of the economists into scientists not concerned with policy, a process that will be discussed in chapter 2.1.2.1.

⁶⁴ All these complaints have a cheerful – though no less comforting – version due to Alan Blinder who calls it a "Murphy's Law of Economic Policy":

Economists have the least influence on policy where they know the most and are most agreed; they have the most influence on policy where they know the least and disagree most vehemently. (Blinder, 1987, p. 1)

⁶⁵ Robert Wood writes:

One prevalent interpretation, often advanced by the scientists themselves, amounts to an "orphan theory" of the scientists' political status [which] would have us believe that although the potential of their profession for constructive contributions to public-policy making is enormous, their counsel is misunderstood, misused, feared, and neglected. In this view, scientists bear the burden of men possessed with the capacity to solve the burning issues of the day, who are nevertheless excluded from counseling the great by reason of popular ignorance and cynical political manipulation. (Wood, 1964, pp. 42-43)

2

THEORY-POLICY RELATIONSHIP: THE MARKET FOR ECONOMIC IDEAS

In chapter 1, I laid down the foundations for my claim that the economic science is largely inconsequential and that economists are frustrated.

The naïve – progressive – conception of the theory-policy relationship, with economists as value-free technicians churning out knowledge about the most efficient means to society's ends which are in turn chosen and pursued by democratic politicians, is vastly off the mark.⁶⁶ This simple – and simplistic – idea needs to be adjusted in order to allow for explanations of the above frustration.

It is typical of economists to conceive of social phenomena in terms of 'markets', however awkward it may sometimes appear to be. I have no intention, for a change, to be original in this respect: I will investigate the relation between economic theory and economic policy precisely as workings of a *market for economic ideas*.

Apart from the traditional supply-and-demand approach, I am here less interested in the price and quantity parameters of this market and their equilibrium. In fact, I will carefully *avoid* all the convoluted reasoning regarding these parameters which exists due to great heterogeneity of both ideas and the rewards for their production. Yet, as it is undeniably a set of voluntary

⁶⁶ Although the 'progressive era' of the turn of the 19th and 20th centuries was ended by the tragedies of the world wars, its spirit tends to survive in some areas to this day. The role of economists in government in this period and the subsequent changes is discussed in Nelson, 1987, pp. 51-60.

activities of two cooperating parties,⁶⁷ I hold this approach to be a legitimate one, if only for sorting out the different actors in this arena and their incentives. This should be enough to help us understand the determinants of the evolution of the product on this market – the development of economic ideas.

I will next look successively at the supply and demand side of this market and examine the ramifications of their interaction.

2.1 SUPPLY OF ECONOMIC IDEAS

It will probably not be very much contested if I stipulate that economic ideas are supplied by economists. In fact, this is true by definition.⁶⁸ It is economists who devote their scarce resources to the production and marketing of economic ideas and theories which they deem potentially valuable to others, even if only collectively.⁶⁹

The only interesting point left to answer here is what exactly makes one an *economist*, and his ideas *economic*, in the scientific sense.

While everyone who considers himself an economist has a rule of thumb to distinguish between an economist and a non-economist, the consensus on such rules is not likely to be very great. Thus, there is a set of conditions either of which is usually enough to qualify one as an economist. For Roger Middleton, for instance, an economist is someone who fulfils *any* (or more) of the following conditions:

⁶⁷ These activities are *voluntary* in the sense of the cooperation between economists and policy-makers. This is of course not to imply either that it is inconceivable that some force may be used, or that the actors rely on voluntary cooperation also outside of this market.

⁶⁸ In a similar fashion, Jacob Viner, though perhaps with his tongue in his cheek, is said to put forth a peculiar definition of economics: "economics is what economists do".

- Self-identification as an economist; and/or
- Possession of expertise, whether validated within the peer group (academic qualification and/or publication) and/or revealed by demand for their knowledge, which is recognised both as economic and expert. (Middleton, 1998, p. 70)

While one can hardly come up with better criteria, it goes without saying that it is very troublesome when it comes to the group's consensual opinion. Particularly the self-identification as economist is likely to be a source of unlimited dissent and heterogeneity within the group. While it is not easy for outright lunatic ideas to find their way into scholarly journals, there are virtually no limits to what a member of a professional association can claim.⁷⁰

This is not to imply there is necessarily a need for limiting the possibility to call oneself an economist by educational requirements. After all, many renowned economists had no special education in economics.⁷¹ It does, however, explain away some of discord among economists that is not only

⁶⁹ Some authors conceive of the supply of economic ideas quite differently. George Peden, for instance, uses a broader perspective and talks about various "forms of economic knowledge available to policy-makers" that includes – besides economic theory – also practical experience, information deriving from government agencies, informed opinion and the like (quoted in Middleton, 1999, pp. 50-51). While it is factually true that policy-makers do draw economic ideas also from businessmen, bureaucrats or even the public, it is indispensable – within my agenda of economics of economics – to limit the meaning of supply of economic knowledge just to economists. After all, as Frank Fetter remarked, alluding to Gresham's Law:

What does the word 'economist' mean? A glorified publicity agent broadcasting opinions that have passed the censorship of the counting office? If such be the understanding of the public, if a clear distinction be not made between business advisers and scientific students in economics, then has the business world accomplished by indirection what no attacks on academic freedom succeeded in doing: it has destroyed the scientific significance, the claim to public confidence that the term 'economist' has begun to carry. The counterfeit, the debased coin, if accepted and allowed to circulate, will drive out the coin of genuine metal. (Fetter, 1925, p. 22)

⁷⁰ None of the professional organizations (AEA, RES, or the CES – the Czech Economic Society, for that matter) impose any educational or professional requirements for its members. The historical debate about barriers to entry into the RES, which followed soon after its establishment in 1890, is covered in Coats, 1964, pp. 96-98.

⁷¹ Besides many early economists, the most prominent of the moderns is J. M. Keynes. Otherwise, one could mention e.g. Ralph Hawtrey or Gordon Tullock.

attributed to economists, but was also well evident from the surveys discussed in chapter 1.1.1. The economists' opinion would likely turn out much more consensual if the responding group was limited just to authors who published in professional journals, to university teachers of economics or even their students.⁷²

The surveys, on the other hand, typically focused on professional organizations. The responses in the survey showed unusual heterogeneity even in the most consensual statements. It was George Stigler who claimed that "it is *not* possible to enlist good economists to defend protectionist programs or minimum wage laws" and calls those who do "*ersatz* economists" (Stigler, 1982, p. 60, emphasis original). By this standard, a good part of the economists responding in the surveys is simply no good.⁷³

⁷² Students of economics are taught a fairly homogeneous range of principles. It is significant to note that economic textbooks, when surveyed, draw a substantially more consensual picture than opinion surveys.

⁷³ The answers are particularly striking for French economists. For instance:

- almost 3 in 4 economists in France do not 'generally agree' with the statement that "tariffs and import quotas reduce general economic welfare";
- only 1 in 4 of them would 'generally disagree' with the statement that "the government should be an employer of last resort and initiate a guaranteed job program";
- only 1 in 6 of them would 'generally agree' with the statement that "a minimum wage increases unemployment among young and unskilled workers";
- only 1 in 5 of them would 'generally agree' with the statement that "a ceiling on rents reduces the quantity and quality of housing available"; and
- only 1 in 10 of them would 'generally agree' with the statement that "inflation is primarily a monetary phenomenon" and less than 30 per cent of them would 'generally disagree' with using the wage-price controls to be used to fight it. (see Frey et al., 1984, pp. 991-992)

Similarly striking are opinions of students of certain graduate schools as surveyed by David Colander and Arjo Klamer. For instance:

- only 1 in 5 graduate students of economics at Harvard would 'agree' with the statement that "tariffs and import quotas reduce general economic welfare";
- only 15 per cent of graduate students of economics at Harvard would 'agree' with the statement that "a minimum wage increases unemployment among young and unskilled workers";
- only 7 per cent of graduate students of economics at MIT 'agree' with the statement that "inflation is primarily a monetary phenomenon" (Colander, Klamer, 1987, p. 104).

From this perspective, some US graduate schools resemble small islands of France within the United States.

In a similar vein, Peter Bauer talks about a teacher's dilemma:

How can one fairly assess a student's performance if what he says or writes is plainly untenable, even bizarre, and if at the same time he can cite in support a leading economist or two? (Bauer, 1984, pp. 160-161)⁷⁴

It is interesting that the dissention among economists is always considered a reason for ridiculing economic science and doubting its scientific status. There is, however, an alternative – equally meaningful – explanation for it. It may be that it is precisely the broad definition of an economist that causes the group to include too many heterogeneous elements. Thus, instead of asking what is wrong with economics one may ask what is wrong with some economists.⁷⁵

Natural sciences are less susceptible to this kind of schism within their fields for three reasons.

First, because of the experimental method, knowledge about relations in natural sciences tends to be more exposed to

⁷⁴ Stanislaw Andreski, talking about social scientists in general, goes vitriolic:

[As in social sciences] the criteria for excellence are so dubious, it is impossible for a layman seeking advice to find who the real experts are. Neither a degree, nor a university chair, nor a membership of a famous society or institution constitutes a warranty that a given social scientist deserves being taken seriously, because in the competition for these honours knowledge and integrity often matter less than skill at intrigue and self-advertisement. It is not surprising, therefore, that – far from being particularly good in sociology or political science – the wealthiest American universities contain an unusually large proportion of phonies who bask in the collective glory deservedly won by their colleagues in the exact disciplines. (Andreski, 1972, p. 203)

⁷⁵ One wonders why the discord gleaming for instance from Frey's European survey (Frey et al., 1984) generally moves scholars to ask what is wrong with the *economic science*, rather than what is wrong with *French economists*. One exception to this rule is Charles Wyploz (see Wyploz, 1999, pp. 64-65), and another, somewhat amusing exception in this respect is Harry Johnson:

France [one of the countries where research is misidentified with literary facility and a capacity for grandiloquent rhetoric] lives on dreams of grandeur and on rhetoric instead of scientific analysis from its economists. Big prizes go to those so-called economists who can snatch ideas from the English literature and translate them into French concepts and the French language; and due to the unreality of French culture in relation to the rest of the world, prizes are often won by snatching unscientific pseudo-philosophical ideas from the Anglo-Saxon world and translating them into even more pseudo-scientific French. In this respect, the most esteemed French economists are often the most fraudulent economic scientists. (Johnson, 1973, p. 73)

the test of its meaningfulness. As a result, crankiness and lunatic ideas are eliminated from the body of knowledge much quicker than in social sciences, and natural sciences then appear – in fact, are – more unanimous.⁷⁶ A scientist denying the existence of gravity will not pass for a physicist, and soon be revealed as a fraud, or at least a practitioner of something else than physics. On the other hand, a scholar claiming that minimum wage has nothing to do with unemployment can pass for an economist as long as he has a story to tell in which minimum wage did not coincide with unemployment.⁷⁷

Such a difference between natural and social science is recognized by non-economists as well. Says Stanislav Andreski:

[In natural science there] is little room for bluffing. No amount of plausible talking and posturing will make a bridge stand if it has been incompetently designed; while ignorant dabbling with chemicals will soon lead to a fatal explosion. In contrast, nothing will immediately blow up or fall down in consequence of a politologist's or economist's inanity; while the harm caused by his ignorance or dishonesty may not materialize until years later, and will in any case be debatable and difficult to blame on a particular man. (Andreski, 1972, p. 203)⁷⁸

Second, because of the subject of the sciences, natural sciences are not as seductive for nonprofessionals to nurture strong convictions and opinions. Economics, on the other

⁷⁶ Gordon Tullock provides a typical example:

[A]rguments in the natural sciences normally are settled by some further advance in knowledge which makes one point of view or the other (sometimes both) obsolete. This is less common in the social science. The fallacious defenses of tariffs which were invented in the fifteenth and sixteenth centuries still appear with monotonous regularity in the literature. [...]

Thus, a dispute which intellectually was settled over a century ago still continues. (Tullock, 1966, p. 193)

⁷⁷ It will, of course, be always possible to detect such instances due to uncontrolled, non-experimental nature of historical stories.

⁷⁸ Interestingly, Andreski considers economics the only social science where this is only partially applicable.

hand, being concerned with virtually every day issues everybody deals with (prices, income, taxes, regulations etc.), successfully invites many people to hold firm beliefs without much thinking about them. In the great masses of people, only few chat about chemical reactions over beer, but surely many of them discuss the (rising) price of beer or politics. David Friedman commented on this fact from his personal – family – experience:

Sometimes it seems that everyone is an economist. My father in law, for example, would not seriously consider challenging my views on physics, a subject in which I acquired a doctorate before switching to economics – although, as a geologist, he actually knows something about physics. But he has no reservations about preferring his views on foreign trade to mine, despite the fact I have taught and published in economics for more than twenty years. (Friedman, 1996, p. 78)

Much earlier, Glenn Hoover made a remark directly linking such ‘thisworldliness’ of economics to its failure to matter:

One explanation of the relative backward state of economics is that it is applied, in all matters of general concern, not by experts, but by the erratic man in the street, the uninitiated, leaders of trade unions, employers’ associations, and, God save the mark, members of Congress. The failure is colossal; it inspires; but it probably is no greater than would be the failure of chemistry if it were applied by the same individuals who apply the science of economics. (Hoover, 1926, p. 58)

On a more general level – in the context of comparing the natural and social sciences – Andreski makes again a similar point:

There is an asymmetry between the expertise in the natural and in the social sciences. Someone unacquainted with an exact science is completely dumbfounded in any discussion about it; but, being reduced to silence, he is saved from any

possible temptation to spout nonsense. On matters pertaining to the social sciences, on the other hand, the opposite is the case: everybody feels entitled to express strong views, and there are no solid signposts to warn against the pitfalls of ignorance, sophistry or even folly; while the lack of knowledge regularly breeds a conviction that things are simple and require no deep study – which explains why so many exact scientists have been ready to make silly statements about politics. (Andreski, 1972, p. 201)

Thirdly, natural sciences focus on questions that are less likely to attract attention and pressure from a special interest group. Social sciences, with policy-relevant economics at the forefront, deal almost exclusively with precisely this question. As Thomas Hobbes supposedly said:

If there were anyone with the interest to argue that 2 and 2 are 5, arithmetic would not be the wonder that it now is. (quoted in Tullock, 1966, p. 192)

For these reasons, *more* people tend to enter, and stay within, the ranks of economists to debate issues, which makes for the greater dissention among them than can be observed among professionals in different fields of natural sciences.

For economics, unfortunately, there does not seem to be a way out of this predicament. Fortunately, while worth knowing and keeping in mind, it does not much affect the following analysis. In other words, the existence and relevance of phenomena, tendencies and principles I will point to below does not hinge on where the borders of the profession are drawn or recognized. It may be important for *levels* of opinion, but not for *changes* in it.

Thus, being aware of the difficulties of even a rough definition, let me proceed to the discussion of economists' objectives.

2.1.1 ECONOMISTS' OBJECTIVES

Economists, just like any other producers, are in their business for various reasons. The attempt to explicitly enumerate all of them would necessarily be incomplete and pretentious at the same time. Yet, I propose to split all of them into two categories by singling out one particular – and familiar – objective: the *desire for social change*.

It is of course no coincidence that it is precisely achieving this objective that, as pointed out in chapter 1, is common to many economists and is in many cases explicitly the ultimate motive for being an economists. By *desire for social change* I mean the hope that by discovering and explaining the interdependencies of various social phenomena, the mankind will learn and organize its institutions in such a way that will make the world 'a better place'. Admittedly, there are bound to be differences in the understanding of what 'a better place' actually is. For my purposes here, however, such differences do not matter. As long as an economist produces a theory in order to improve the state of affairs in society – whatever the author's specific visions of the improvement – I will class his objectives in the first group and call his objective *benevolent*. It is important to point out that such a benevolent objective is entirely fulfilled once the change takes place. It is the economist's pure personal *awareness* that society has changed in the desired direction. It does *not* involve any recognition or other benefits for pioneering, or for advocating the theory that brought about the given social change. Though such an objective is still self-interested, it is probably the most distant from the usual market motives as the self-interest lies in this case, as suggested by the term *benevolent*, in satisfaction of others.

Having specified the first class of objectives, I proceed to define the second class as complementary to the first. Thus, all possible objectives of economists for producing or disseminating economic theory other than the social change will be classed

in the second group and be called *selfish*. To name the most likely ones, the selfish objectives will include discovery of scientific truth *per se*, the recognition by peer economists, other scientists or the public in general, status in society, decision-making power and all forms of material benefits (income, comfortable job environment, free travel and eat-outs, etc.).

Thus, I have broken down all objectives economists pursue into two different classes:

- 1) Benevolent – social change
- 2) Selfish – all other benefits

Reality, of course, allows for a blend of the two. In fact, any living economist is most likely motivated by a *combination* of both objectives: to some extent, he may be interested in bringing about social reform, and, at the same time, he would also like to be recognized and get paid for what he has created.

Despite empirical concurrence of both motives, there is a rationale for their differentiation into benevolent and selfish. It lies in my contention that to a large extent, these two objectives are mutually *incompatible* – they tend to exclude each other. Although at any given time, an economist can pursue a certain combination of them, I hold that, on the margin, the more one focuses on the benevolent objective, the less successful one will be in achieving the selfish objectives, and *vice versa*. In other words, the more production or advancement of certain economic theories contributes to the attainment of the benevolent objective, the less it is fit to satisfy the selfish objective.⁷⁹

There are two reasons for such incompatibility. First and foremost, it can be argued that most people are unaware of the

⁷⁹ Such incompatibility is sometimes referred to as a question of whether economists can do *well* and *good* at the same time. Dan Klein, in the introduction to the collection of essays on the economic profession, mentions this as the primary impetus:

The impetus for the present volume stems from the belief that [...] economists might find that pressures to pursue academic work divert them from contributing to the art and science of political economy. They are torn between *doing well and doing good*. (Klein, 1999, pp. 1-2, emphasis added)

link between the theory and their potential, or actual, wellbeing. This is caused by the social nature of such theory. Ignorance of this theory on the part of an individual is quite comprehensible in the light of the little practical use it poses for him. Besides limited personal usefulness, such insights are ordinarily quite counterintuitive as they are at odds with what individuals dealing with the same problem on their level expect. This is further complicated by the fact that such theories, their subtlety notwithstanding, are typically quite simple,⁸⁰ and their implied policy prescription is very often non-activist. It typically suggests that the policy-makers should refrain from doing something they are doing (rather than that they should do something they are not doing yet). Indeed, these hands-off – *laissez-faire* – policies are extremely difficult to associate with any good performance. They do not impress people as very sophisticated and active enough to bring about anything good. To the proverbial everyman, it seems almost unbelievable and beyond comprehension that ‘doing nothing’ could be actually socially beneficial. Thus, these theories face the common presumption that in order to achieve something good, one has to ‘do something’. And to the extent these theories have non-activist implications, their association with social wellbeing is discounted on that account. Either way, without understanding (or at least admitting the existence of) the link between such economic theorizing and its wellbeing, the community cannot appreciate the role of economists in this field and economists will not be given any credit, and thus cannot hope for recognition and status.

Second, even if all people were aware of the benefits accruing to society because of economists’ theories,⁸¹ the

⁸⁰ Many economists subscribe to this view. Frey and Eichenberger, for instance, say:

Advice and policy proposals essentially require core economics taught in the first semester, but rarely ever the work produced in [specialized, theory-driven subfields].
(Frey and Eichenberger, 1997, p. 27)

⁸¹ It has to be admitted that it is highly *unlikely* that *everybody* would know. Many, and perhaps most, individuals are not – quite understandably – even aware of any potential benefits of any economic theorizing.

possibilities of economists to satisfy their selfish objectives will still be quite limited. This is because their output that focuses on the achievement of the benevolent objective has necessarily a *public-good* character.⁸² A theory concerned with social organization and wellbeing is almost *ipso facto* something whose benefits will not be limited to individuals willing to pay for it.⁸³ Along the lines of a standard public good story, while just about everybody could benefit from the existence and acceptance of a given theory, every individual knows he cannot be excluded from the theory's benefits once it exists and is heeded. Every individual is thus motivated to free-ride – to stay back and let the others take care of it – with the familiar result of zero (or, at least, less-than-optimal) demand due to everyone staying back. With zero or negligible demand for such theories, producing them will not be rewarded by benefits flowing to economists from other members of society. With no 'sales', economists will be paid as philosophers or literary critics, and must be content with the benefits they derive from the prospects of achieving the first

With regard to knowledge about these issues on the part of an everyman, a case could be made that ignorance of these issues is quite rational. To wit, knowledge about organization of society is almost of no use to particular individuals (save perhaps the conceivable psychic pleasure from pure knowledge). This is certainly more true in the era of democratic government than under, say, monarchies when the ruler could be thought of as an 'owner' of the country and could at least *possibly* benefit personally and materially from purchasing the product of economists.

⁸² Although without explicitly invoking the public good theory, Gordon Tullock considers lack of financial incentive (a lack of "patent system for social inventions") a reason for backwardness and slower progress of social science in general. See Tullock, 1966, p. 182.

⁸³ In fact, such theories have so much of a public good character that they benefit not only people who do not pay for them but use them, but also individuals who *do not* use them (i.e. live by, obey them), provided that others do.

This implies that not only the production, but also the application and acceptance of these ideas is subject to constraints imposed by coordination problems. A good example is the property rights system advocated as an institutional framework of society. Among the beneficiaries of this system, there will be individuals who violate it. This is because the more respected the property system will be, the more profitable it will be for the few individuals to violate it: there will be more to 'steal' (such a society will be more productive) and it will be easier (people will take less precaution to prevent violation of property rights).

objective. Thus, when it comes to marketability, economic theories aimed at the benevolent objective resemble rather basic research than a search for knowledge and understanding that individual people would be willing to pay for.^{84, 85}

Simultaneous achievement of both classes of economists' objectives is therefore doubly cursed: 1) socially beneficial theories are not recognized as such by the public because of the subtlety in their reasoning, and, even if they were so recognized, 2) economists would still be largely prevented from satisfying their selfish objectives by the public-good nature of the socially beneficial theories.

*

To sum up, production of a theory aimed at bringing about social improvements and achieving the benevolent objective of economists warrants very few buyers and very weak chance for fame, recognition and status. Having shown *what* the economists supply and *why*, I may now attempt to use this to reconstruct the evolution of the economic science and theories it has been producing.

⁸⁴ In fact, it could be claimed that the public good character is greater in economics than in natural sciences.

Admittedly, there is an enormous basic research agenda in natural science. However, along with this, there is an equally enormous amount of applied research conducted for specific clients who indeed *pay* for it. Economics has of course some privately applicable output too, but overall, I submit, it is relatively much less important a part of the science. As Pigou once reminded:

[I]t is not the business of economists to teach woollen manufacturers how to make or sell wool, or brewers how to make or sell beer, or any other business [people] how to do their job. (quoted in Bernstein, 2001, p. 40)

A further important consideration that still limits the private use and funding of economic science might be the fact that economists' discoveries cannot be patented!

⁸⁵ In this context, it is perhaps of interest to note that economics would lose much of its importance and real world relevance if it was not for governments and their ways of intervening with markets.

2.1.2 EVOLUTION OF SUPPLY

Let me start by alleging that the whole history of economic science⁸⁶ can be thought of as a history of average economist's focus *switching from the benevolent to the selfish objective*. This is not to say that the selfish objective was absolutely unknown to the early economists, or that the benevolent one is unknown to current economists, just as it does not say anything about individual economists. In fact, I think that the benevolent objective is to this day extremely important, perhaps even dominant among economists. Yet, at the same time, I am convinced that over the two-and-a-half centuries the selfish objective has gained so much in its importance as to substantially affect the output that economists produce.

One can safely claim that the early economists were motivated almost exclusively by the benevolent objective: by the desire for social reform. All of the issues the early economists up to the whole 19th century were concerned with were policy issues that these economists wanted to communicate to politicians and policy-makers.⁸⁷ They were certainly not troubled by the lack of pecuniary sales. For them, the political economy was not a profession but rather a mission: a full-time calling, vocation for some and an

⁸⁶ By the 'whole history' I mean – in line with the standard view – the period from mid-eighteenth century onward, but I take the liberty and choose not to delve into the question of who personally was the first economist.

However, I believe the same story could be told about economic thinking before mid-eighteenth century, i.e. the period from Greek philosophers up until mercantilism, which suggests a fascinating history-repeats-itself argument! If this is the case, we have an age of new mercantilism in front of us!

⁸⁷ Adam Smith considered political economy as "a branch of the science of the statesman or legislator". It is readily admitted that for his *Wealth of Nations* the politicians constituted a main audience. Jerry Muller, for example, writes:

The legislator for whom the [Wealth of Nations] was written was the politician who could be motivated to promote public interest. The "science of the legislator" that Smith set out to provide was intended to improve the politician's ability to foresee the consequences, both positive and negative, of laws and policies. (Muller, 2002, p. 65)

Notorious reformers included Say, Malthus, Bentham, Ricardo and both Mills. Some of them actively participated in dissemination of their ideas (worked in parliamentary committees, witnessed before parliamentary commissions).

avocation for many.⁸⁸ At the dawn of economics, contributing to this science was decidedly *not* a means to make a living.

Even if it was, economists would be largely disappointed at achieving this particular goal. The product of these economists had some peculiarities that rendered their position as suppliers somewhat difficult.

First, the economists were marketing a good that was most unattractive to precisely those who were the most prospective buyers – the governments. It is they who could benefit from acquiring the economic ideas most directly, and thus would – of all possible buyers – most likely be interested in buying them. However, as I insinuated above, the early reform-motivated economists were led by their scientific inquiry to policy prescriptions that ran quite contrary to what the rulers were, and were interested in, doing. The passive character of the prescriptions implicit in their ideas was then a primary curse to their success on the ‘market’. The products of a ‘dismal science’, and their producers with them, were simply unwanted. The public was unsympathetic or even hostile to economists. If there was anything *popular* about economics, it was its being subject to jokes and jibes.⁸⁹ The public recognition they enjoyed for their scientific and reform achievements was ambiguous, and very limited at most. Although some of the early economists may have become relatively well known, it is uncertain whether that fame was always a pleasurable one: some positive recognition, mostly by their peers, may well have been undone by the ill fame of

⁸⁸ The ‘vocational’ character of economics and its influence on the product of economists is emphasized by Joseph Salerno in Salerno, 2005. Salerno’s “vocational” economist corresponds broadly to my concept of an economist motivated primarily by benevolent objectives, and his “professional” economist to my selfish-objective-driven economist.

⁸⁹ Edmund Burke wrapped up economists together with “sophisters” and “calculators”. Walter Bagehot (himself an economist and a great popularizer) is attributed the famous “no real Englishman in his secret soul was ever sad by the death of an economist” (quoted e.g. in Hayek, 1991, p. 39).

economists in the eyes of some non-economic scientists, intellectuals, and the public in general.⁹⁰

Second, on top of targeting predominantly the most unwilling-to-buy buyers, there was still the public good character of their scientific insights. This was particularly troublesome precisely in case of theories aimed at social reform, i.e. theories economists were preoccupied with in the first place. With the public good character of most of the reform recommendations,⁹¹ the chances of finding an audience willing to pay for their ideas were very slim. Moreover, the limited number of teaching, research and advisory positions made the opportunities and demand for economists, and the corresponding material benefits derived by them, very scarce.

Economists had therefore faced this double hurdle in marketing their output: their product, due to its collective usefulness, had a limited market in the first place, and those who could yet be interested in it were quite alienated by its design.

The selfish objective was thus either absent, or (even if present) correspondingly weak or inoperative. It did not seem to matter dramatically. After all, Cantillon, Smith, Say, Ricardo and others were relatively – indeed, some of them *very* – rich persons. Even reverend Thomas Malthus, the first professor of political economy in history, was born into a wealthy and well-secured family, and had no reason to professionalize for money.

⁹⁰ Hayek recounts that

the dislike for most of the teaching of the economists in the past has built up a picture of the economist as a sort of monster devouring children. (Hayek, 1991, p. 39).

Similarly, George Stigler describes the general sentiments as follows:

[T]he convention of denouncing economists has been established [at the end of 18th century] and was pursued with enthusiasm by men great and small. [...] Why has it been fashionable to abuse economists (even granting the possibility that they may deserve it)? The main reason is easily named – economists have been the premier “pourers of cold water” on proposals for social improvement, to the despair of the reformers and philanthropists who support these proposals. (Stigler, 1988, p. 4)

⁹¹ The whole anti-mercantilist agenda of classical economists (free trade, free industry entry, etc.) consisted of reforms promising great but very dispersed benefits.

In the early period then, the rewards flowing to economists for production of their ideas were by and large only the high *hope* of contributing to future social change. In contrast, material and personal benefits from practicing economics (satisfying the selfish motive as stipulated above) were small and irrelevant with respect to their output.

This state of affairs, however, was not to last indefinitely. Even though economists focused, almost proverbially, on the long run and exhibited a tremendous amount of patience, their hopes of having an impact upon the world were repeatedly frustrated. In fact, even if we admit that there *are* instances in history when some major changes in government policies were a consequence of the works of economists, no economist *lived to see* having much impact on the society. Even the most notoriously cited example of economists' consequentiality – the move towards freer international trade in the middle of 19th century – took place well after the authors of the theoretical underpinnings of such reforms passed away.

It is, I believe, precisely this *disappointment at the lack of impact upon policy* that is responsible for the change in the course taken by the economic profession. It must have meant that doing economics – i.e. doing it the way economists had been doing it – was seen as impotent for the satisfaction of the benevolent objective, i.e. for bringing about social reform. In light of this disappointment, the 'marginal' economist either changed his way of doing economics to cater more to satisfaction of the other – selfish – objectives (i.e. recognition, and material benefits), or left the profession altogether. Directly or indirectly then, this must have meant a gradual relative weakening of the first – and, until then, the major – incentive among economists to engage in economic theorizing and a corresponding rise in relative importance of the other incentives.

The shift in focus to the other objectives, however, implied a profound change in the product economists were supplying. Let me look at the changes I submit were triggered or boosted by the economists' frustration.

2.1.2.1 GROWING POLICY IRRELEVANCE

The first systematic tendency on the supply side triggered by economists' being unable to succeed in fulfilling their benevolent objectives was *a shift away from policy relevant issues towards pure theory*. This process is almost invariably associated with mathematical formalization of economic theory, and is sufficiently acknowledged and recognized as to receive a name coined by D. McCloskey: a "*Samuelsonian Vice* is claiming that proofs on the blackboard are the main job of the economic scientist" (McCloskey, 1996, p. 63, emphasis added).⁹²

Most importantly, this shift towards technical and mathematical analysis was for economists an escaping strategy from frustration at the lack of their impact upon opinion and policy. That such a step may be a *consequence of such frustration*, was explicitly recognized by many authors. Frank Graham, citing another author (A. S. J. Baster), talks in the mid-1930's about "logical gymnastics" having offered "an intellectual retreat from disillusioning contemplation of the march of events" (Graham, 1942, p. 31). William Hutt is worth quoting at length:

[The economist's] response [to his impotence to influence opinion] may be to retire from that field of intellectual activity in which he could be of direct service to the community and [...] concentrate on the development of an intricate technique of analysis. He may then find himself the possessor of a logical system applicable to conditions which *might* conceivably exist, but a system which no legislator or administrator could be expected to understand, let alone find of service in the case of any concrete problem. Such an economist will correspond to the 'pure scientist' in other fields. The results of his efforts may occasionally have repercussions of the greatest moment upon knowledge relevant to the sphere of practical affairs (as the techniques

⁹² McCloskey also offers an excellent analysis of, including some data on, the transformation of academic journal article and their authors in McCloskey, 1991.

of the pure mathematician and the pure physicist have had an immense influence in the field of technology). But his studies can hardly be said to be consciously directed towards that end. He escapes, in consequence, from the sense of baffled striving, of frustrated effort, that confronts his colleague who announces his concern with contemporary happenings. The 'pure theorist' is apt to become a hermit, and whilst he may hope that the practical men may sometimes visit his cave and humbly ask advice on matters in which his mysteries are believed to give him an insight denied to others, in his heart he knows that they have no faith in his mysteries [...]. (Hutt, 1936, p. 35)

Tackling less policy relevant questions meant some sort of retirement to a refuge, a place economists found themselves less exposed to heated policy debate and denunciations for their alleged coldbloodedness, social Darwinism, nay-saying and dismal thinking.

The gradual retraction from earlier agendas and research programs and refocusing on technical questions farther removed from policy brought economists – besides relief from frustration – other benefits as well.

The relative self-containment of economics and its isolation from the outside world that this shift brought about catered to economists' own scientific curiosity, originally perhaps only dormant, if not altogether non-existent. Discouraged from 'working for the society', they turned to each other. The intellectual and the man-on-the-street in the audience of a typical economist was here and there supplanted by a fellow economist.⁹³ This led to a gradual 'professionalization' of the field: economics started attracting

⁹³ Thomas Mayer states this fact and links it with formalization:

[As contrasted with academic researchers in such fields as law and medicine] who work for a large market of practitioners, academic economists write for each other. Hence their tastes and not the consumers' determine what is produced.

[Such producer sovereignty may lead to] an over-emphasis on sophisticated high-tech methods. (quoted in Hutchison, 1994, p. 287)

⁹⁴ Fields that first come to one's mind in this context are e.g. game theory, econometrics, or linear programming.

pure scientists with lesser policy bent, and their share among economists thus increased correspondingly and changed the general perception of the scientific status of the whole field.⁹⁴ Deirdre McCloskey comments on “the rise of scientific ethos”:

The theoretical articles of the 1920s took the philosopher as their model; the empirical articles took the historian; in English, the “scholar”. The implied author of the recent theoretical article is the mathematician, with his theorems and proofs. The implied author of the recent empirical article is a bench scientist, with his controlled experiments (in the guise of regressions) and his applications to policy. In English: The Scientist. (McCloskey, 1991, p. 141)⁹⁵

Replacing verbal arguments with symbols and equations was seen as achieving better clarity and precision and matching in this way finally the sophistication of natural sciences. Searching for – and finding – solutions for highly abstract and formal problems was recognized by economists as a route to securing recognition not only among themselves, but among other scientists as well. Importance of such recognition is assumed by Terence Hutchison:

[I]t may be assumed that enhancing their own feeling of scientific status has been an important element in the utility function of mathematical economists, which is satisfied by the lavish use of mathematics and by the promotion of abstract, vacuous ‘rigour’ as the – profoundly unsuitable – overriding criterion and aim of the subject. (Hutchison, 1999, p. 287)

The drive for scientific and academic recognition leading to policy-irrelevant theory was a matter of complaint in 1940’s to Frank Graham:

⁹⁵ Although in a different context, McCloskey makes a point about the changed comprehensibility of articles as well: “A non-economist could pick up the *American Economic Review* or the *Economic Journal* in the 1920s and read it” (p. 143), whereas today “most economists do not feel competent to read or judge the contents of the *American Economic Review*” (McCloskey, 1991, p. 155).

Economics has always been under 'suspicion' as a science, and the consequent defensive attempts on the part of its exponents to force their theory into rigid scientific forms have frustrated its application to the facts of life. [...] Theory has, at length, become so 'scientific' and abstract as to intrigue mathematicians who have taken delight in developing the concept of a kaleidoscopic and frictionless play of atomistic units in a complex and eternally unfolding equilibrium. [...] [T]he game has gone on until the pages of the more esoteric economic journals have become a mass of hieroglyphics intelligible only to those who know the code. [...] [T]he 'science' has come to move in a realm of pure abstraction useful for purposes of cerebration but of steadily declining practical importance.

[...]

Much first-rate analytical skill and much scholarly industry has miscarried because the road to academic recognition lay in the refinement of traditional technique, or in assiduous dust-gathering, with little consideration of ultimate purpose. The means have been exalted over the ends, and the neophyte, compelled to show his mastery of the technique, has quickly learned to love and practice it for its own sake. (Graham, 1942, pp. 28 and 29)

Assuming the status of hard scientists, using language increasingly incomprehensible to outside intellectuals, has added much to the scientific respect of economists in the eyes of the general public. Sophistication and separate lingo may have provided economists with a shield not only against denigration for not being scientific enough. It has also immunized economists' theorizing against criticism, coming both from within economics and from outside the field, including the public. For instance, Thomas Mayer notes that

mathematics can readily be used to silence most non-economists who pontificate on the subject. Economics is not the only field that uses mathematics as a barrier against criticism by the unwashed. (quoted in Hutchison, 1999, p. 286)

Thus, to a large extent, as a result of its frustration, the economic profession eventually gave up trying to achieve its original goal, and its output became largely policy-irrelevant. As Hutchison sums up, it was substituted with scientific sophistication and rigor:

[T]he traditional prime aim, or end, of the subject [i.e. advice on policy] has apparently been increasingly replaced, in recent decades, by games-playing (as Sir John Hicks described 'much of economic theory'); by displays of brilliantly wise 'new conversation', or by technical virtuosity in the form of empirically vacuous mathematical 'rigour' or aesthetics. Such activities are then dignified as promoting some unspecified, non-predictive 'understanding', 'wisdom' or even 'beauty', or as examples of on-and-on-going, ever-changing, intriguing 'discourse'. (Hutchison, 1994, p. 292)

The increased sophistication and, what went hand in hand with it, the decreased comprehensibility of economics served to improve economists' scientific status. Robert Nelson, quite unsurprisingly, given his predilection at the economics-as-religion analogy, likened this to the use of Latin by the medieval Roman Catholic priests:

The medieval Roman Catholic priesthood conducted its religious preaching and other discussions in Latin, a language no more understandable to ordinary people than the mathematical and statistical formulations of economists today. [...] The use of Latin also separated the priesthood from the ordinary people, one of a number of devices through which the Roman Catholic Church maintained such a separation in the medieval era. It all served to convey an aura of majesty and religious authority [...]. In employing the arcane language of mathematics, Samuelson and [his] fellow economists today seek a similar authority in society. (Nelson, 2001, p. 100)

Such useless sophistication is, according to some authors, a distinguishing feature of economics:

Another way economists strive for status and self-respect is by using complicated theory even when discussing straightforward problems that could be resolved without it. It is something that only those with training in economics can do and, besides, it seems to justify the effort made in acquiring the theoretical tools of economics. Beyond this, it distinguishes economics from the other social sciences. (Thomas Mayer, quoted in Hutchison, 1999, p. 286)

Such formalism in economics was not only an escape from the practical, policy affairs but, in fact, proved to be incompatible with it. New ranks of students of economics were directed toward rigorous mathematical method, which hindered their mastering of the economic logic and intuition. Rigorous – and often unrealistic – assumptions, so necessary to obtain any degree of formality, moved the economic agenda away from policy-oriented work. Due to the mechanism of academic selection, these habits and directions of work were self-perpetual. By economics becoming less policy and more technique oriented, it also attracts future economists who are less interested in (and capable of) undertaking policy-related work and more interested in (and capable of) excelling in formal advancement of the theory. With time, this will feed into the original tendencies and reinforce the change in the profession. Moreover, it is not mere attraction to become part of the profession, but the sheer capability to survive in it, that drives the change.⁹⁶ As Peter Bauer concludes:

Once mathematical methods have become fashionable, the desire to be in the swim and the operation of the established interests set up forces of self-perpetuation. (Bauer, 1981, p. 264)⁹⁷

One of the ways the thesis about growing irrelevance can be substantiated is through article surveys. Klein and Romero,

⁹⁶ I thank Mario Rizzo for making me explicitly aware of this instance of self-selection bias.

⁹⁷ Bauer was critical of the use of mathematics for its suppression of economic logic and justification of false policy. See his quote on page 76.

for instance, analyzed all 66 articles in the Journal of Economic Theory published in 2004 (Klein and Romero, 2007). They found that only 12 per cent of them were able to pass what they consider necessary conditions for a model (or description) to be called a theory: a) relation to a real-world phenomenon and explanation of its existence, b) importance of the real-world phenomenon for the community's attention, and c) novelty or superiority of provided explanation. (Klein and Romero, 2007, pp. 246-247) While the purport of their article is not a comparison of relevance in time, they do focus on relevance and do conclude indirectly that such relevance is declining.⁹⁸ In any case, their analysis, when replicated and properly applied to multiple points in time, could be elegantly used to illustrate the change in the degree of relevance of economics.

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To sum up, one of the tendencies promoted by economists' frustration was a turn towards self-containment, accompanied by a focus upon impressive sophistication and technique, rather than policy-relevant advice.

2.1.2.2 GROWING INTERVENTIONISM

Another – and simultaneous – manifestation of economists' frustration at being inconsequential and re-focusing rather on their selfish objectives as I defined them was the *adjustment of their product to the demands of policy-makers*. In a broad sense, this is what D. McCloskey – while hardly making the same point – pinned down as a *Tinbergean Vice*, “a notion that you can engineer society the way you can engineer a bridge” (McCloskey, 1996, p. 99).

As hinted at before, the product economists originally supplied to policy-makers was an extremely unattractive one due to its passive, hands-off and *laissez-faire* implications. Economists had to start paying attention to what the

⁹⁸ They talk about “flight from relevance” and “escapism” and even offer a summary of hypotheses about its causes (Klein and Romero, 2007, pp. 266-267), which are subject of this chapter.

surrounding world thought about them, and what the 'market' for economic ideas demanded. In this respect, economists only then started to resemble typical producers on the market, paying closer attention to consumer demands than to their own preference.⁹⁹

If economists were to benefit materially and gain recognition, they needed to modify their teachings and insights to something more agreeable to, and would thus be better received by, their audience. 'Doing nothing' sold poorly for three reasons.

First and foremost, the politicians and bureaucrats want to *engage in active policy*. They are in their positions to 'do something'. On the other hand, 'doing nothing' would defy the need for their very existence. Even if one assumes the members of government hierarchy and bureaucracy to be strictly benevolent, it is clear that they must be convinced of the indispensability of their activities – otherwise they would not occupy such positions in the first place. Now if we take into consideration the fact that their benevolence may not be altogether complete (which few would doubt), the bias of this group towards interventionism cannot be denied.

Second, politicians' interventionism bias aside, from the standpoint of the whole political market (relationship between government and the electorate), 'doing nothing' warrants very few votes. This is because voters, for an outcome they are satisfied with (jobs, health, food quality or anything else), would hardly credit a politician who would refrain from active intervention in, and paid no attention to, the given area

⁹⁹ The tendency to avoid unpopular conclusions in social science in general is thoughtfully described by Stanislaw Andreski:

[E]ven without pressures from the politicians, capitalists or the bureaucrats, the desire for popularity can undermine independence of thought and induce anxious conformity. [...] [A] student of society who does not go in for beating about the bush and mealy-mouthed pussy-footing has little chance of being left alone like his colleagues in the natural sciences. And, as not everybody has a stomach for a never-ending fight for intellectual integrity, most social scientists gravitate towards problems, methods and conclusions which, no matter how sterile, are least likely to incur the displeasure of the potentates or of the populace. Prompted by the desire to play safe they often go even further than necessary in trimming their sails to the prevailing winds. (Andreski, 1972, p. 39, emphasis added)

or issue. In contrast, the recognition with the electorate will be earned by the politician who actively solves problems by proposing, pressing and implementing certain policy. Thus, the lack of recognition on the part of electorate that the best policy might be no policy at all, and the resulting lack of credit for those politicians who indeed propose the 'doing nothing' policy create another bias in favor of political interventionism.

Third, both previous sources of bias aside, the economists offering 'doing nothing' prescriptions do not seem to be supplying anything worth buying. Even if politicians and bureaucrats were honestly interested in what is the 'socially-best' policy, they would prefer to listen to, and buy, interventionist prescriptions. In politicians mind, just as in the minds of voters, 'doing nothing' prescription does not create an impression of a well-thought-of, sophisticated, scientific and effective plan.

Thus, for politicians and members of government bureaucracy, the last thing they would be willing to accept was – and still is – that they should do less than they do now, or, in particular cases, that they should not even exist.

And yet, it was pretty much what they were recommended by the early economists. In fact, the political economy as it was born and much of the classical political economy can be seen as a protest, if not an outright intellectual rebellion, against government activities in many areas.¹⁰⁰

The idea I put forth here is that economists were aware of this fact, and given their frustration at, but will to exercise, an impact upon policy, the overall outlook of the product of the economic profession altered to something closer to what was demanded and thus had a better chance of implementation. And indeed, since perhaps the second half of 19th century, one may trace a gradual metamorphosis of the community of

¹⁰⁰ No matter who is taken as the founder of economic science – whether it be Cantillon, Turgot or Smith – the works of these economists were rife with criticism of instances when the government (i.e. the state or the politician) does something that it (he), according to these authors, *should not do*.

economists from 'dismal' scientists preaching about what *should not* be done into 'public' servants offering advice on what *should* be done, and that in a wide variety of areas.

The eventuality that economists might be adjusting the product they supply to what is demanded is part of the more general story hinted at by George Stigler:

Each sector of the public [demands] services from intellectuals favorable to the interests of that sector. Those whose skill and viewpoint are congenial to the interests of large groups will prosper and become "leaders of opinion" and those lacking either skill or acceptable viewpoint will write letter to provincial newspapers.

Thus the intellectuals find themselves addressing audiences with the message the audiences want to hear. (Stigler, 1982, pp. 60-61)

In the context of economics, the most instructive case of such adjustment of theories to the demand is probably the Great Depression and its New Deal policies. As Gordon Tullock explains:

[S]tudents in [the social] field have a strong tendency to devote large amounts of effort to 'confirming' popular opinions. [...] New currents of opinion will develop in the 'real world' and then investigators [in social science] will undertake research which 'proves' them to be true. The 1930's, for example, witnessed a tremendous change in the economic policies of most Western countries. This was not at all the result of economic research; in fact, the economists largely used theories which condemned the new policies. After it was clear which way the wind was blowing the bulk of the economic profession jumped on the bandwagon, and the economic journals were full of articles which fitted in well with contemporary opinion. (Tullock, 1966, pp. 188-189)

To the story of increasing interventionism one can nicely fit the mathematical formalization of economics, alluded to above as a means to greater respectability. To wit, greater

mathematical rigor substantially contributed to economists' belief they can do much more in terms of active policy advocacy. Namely, it bolstered economists' faith in their capability to replace the market coordination by designed plans of social equilibria arrived at through complex modeling, simulation and computation. The economists' theories (and advocacy) of planning would have been impossible without mathematization.¹⁰¹ The formalization also served to obscure simple principles, and worked as a cloak for seriously faulted policies. This is a perennial complaint of Peter Bauer in his development economics:

In economics [the benefits of mathematics] have, however, been bought at a heavy cost. An uncritical attitude to mathematical methods has inhibited understanding, and obscured or confused basic issues. It has thereby contributed to the survival or spread of simple transgressions. (Bauer, 1981, p. 262)

In the United States, the establishment of the *American Economic Association* (AEA) in 1885 offers a story indicative of such transformation. It was an attempt by the American institutionalists at wresting the name of economic science away from its current practitioners and filling it with quite different, if not opposite, content. Unable to condone *laissez-faire* of the early economists, they preached government economic activism and interventionism. Richard Ely, a leading mind in this respect and a designer of AEA, made sure no one is mistaken about the thrust of AEA by instilling into its principles pronouncements such as that "we regard the state as an agency whose positive assistance is one of the indispensable conditions of human progress" (quoted in Nelson, 1991, p. 181).

Though fierce critics of economics originally, the German-*social-politik*-inspired, explicitly anti-theoretical institutionalists became a respectable part of the profession. By that time,

¹⁰¹ In fact, a mathematical pioneer, Léon Walras, put forth his general equilibrium theory as a contribution to some future possibility of government's direction of economy.

much of the early American economists – uncompromising towards government policy – were scathingly referred to as ‘old Manchesterites’ or ‘American apologists’¹⁰² – ‘apologists’ for *laissez-faire*, that is. Such an account is attested by no lesser person than Irving Fisher:

It is noteworthy that [early economists’] attitude of academic aloofness not only failed to give to economic study, in the eyes of the world, that status of a “true science” which they claimed for it but, on the contrary, brought it into disrepute and provoked a vigorous reaction. The world demanded that economics should become something more than “the dismal science.”

Accordingly, a new economics sprang up, intent on “doing something.” This new school was centered in Germany as the older “Manchester School” was centered in England. (Fisher, 1919, p. 5)

The progressive spirit of the turn of the century contributed to this change. The faith in new science and its capabilities to make everything work better left its mark on the new generation of economists. In the same speech, Irving Fisher, though himself hardly a major progressivist, captures the spirit of the time right after the WWI:

It is given to us as to no previous generation of economists to share in fixing the foundations for a new economic organization and one which shall harmonize with the principles of democracy.

If we are to succeed it will be because we perform our task with wisdom, unselfishness, and impartiality. As economists in public service in a democratic world we are pledged not to serve simply our local community, our own country, or our own time, but to serve rather all humanity throughout the world and throughout future generations. (Fisher, 1919, p. 21)

For doing this, economists’ involvement in wartime management of the economy prepared a solid ground. As one

¹⁰² These include e.g. Simon Newcomb, John Bates Clark, or William Graham Sumner.

respectful historian put it, the economists' engagement in WWI "helped to change attitudes about the value and practical utility of the economist's product", and "greatly increased the appreciation of economists in public service"; one of the AEA founding members insisted that "no other academic discipline gained more in popular esteem" (quoted in Bernstein, 2001, p. 40). Names worth of explicit mentioning in this respect are surely Edwin Gay, a head of the Central Bureau of Planning and Statistics (a short-lived but, as far as employment of economists during WWI goes, enormously important institution), and Wesley Mitchel, who – together with Gay – started the vastly influential National Bureau of Economic Research (NBER), a private institution, but one closely linked with central government.¹⁰³

Such sentiments changing economists' role in society were all but curtailed by events that followed. Indulging in advocating increased policy activism was given a great boost with the advent of the great depression of the 1930's. Keynes's revolutionary theory put forth in his 1936 book owed much of its quick acceptance to being the first work to seemingly lay down theoretical grounds for policies that policy-makers had long been practicing and some economists had for some time been backing up. In contrast to popular belief, however, Keynes was by far not alone in advocating policy activism. What he did was to firmly establish such a progressive milieu in policy-making – a new secular religion (Nelson, 2001, p. 33). This was only reinforced and consolidated

¹⁰³ Bernstein describes this link as follows:

Gay and Mitchell [secured] the support of arguably the most influential presidential cabinet secretary in modern American history in winning foundations grants and awards for the Bureau's work. [They] provided an example of how a private research organization could combine forces with government [...] in the execution of economic policy analysis and implementation. (Bernstein, 2001, p. 43)

It has to be admitted that among the founding precepts of NBER, one would also find an explicit avoidance of policy recommendations. This can be, however, easily squared with the economists' effort as I describe it: while refraining from drawing policy *conclusions*, its *research agenda* was immensely policy-relevant. As long as it could influence policy-making and the economists recognized for it, it did not preclude them from deriving benefits through achieving their selfish objectives.

definitively with the coming of one of the most influential figures in postwar economics, a person I showed above (chapter 2.1.2.1) to have shared some responsibility for economics having turned more abstract and technical: Paul Samuelson.¹⁰⁴

To some extent, economics became an arena where theories originated and were diffused and passed around *for political purposes*. Blatantly wrong theories were kept alive, sometimes by top-notch economists, in order to provide intellectual backing for policy governments wanted to start or sustain practicing. Peter Bauer holds that these theoretical lapses (“transgressions” as he calls it¹⁰⁵) are systematically anti-market and pro-interventionist:

The transgressions in development economics are not random: their thrust reflects systematic hostility to the operation and outcome of market forces, and accords with the views of influential groups within the modern political nation. The influence of these groups, including prominent academics, has been indispensable for the continued widespread acceptance of the simplest errors of fact and logic. These groups tolerate and shield crude lapses if that will help to discredit or to criticize the operation of the market forces. [...]

¹⁰⁴ The progressive nature of Samuelson’s 1948 textbook *Economics* and his role in the development of economics science is thoroughly studied by Robert Nelson (Nelson, 2001, pp. 49-118). Nelson draws many parallels between economic science and religion.

¹⁰⁵ Peter Bauer stresses the common element of all those transgressions: the absence of the role of prices. Hence, he calls this a price-less economics, and points out that it always implies government intervention:

The proposition that price affects the quantity supplied and the quantity demanded is central to economics. Recognition of these functional relationships has been the hallmark of economists since the earliest days of the subject. [...]

It is therefore all the more remarkable that so much of the post-war economic literature has ignored the fact that supply and demand depend on price, and that a shortage or a surplus can never be discussed sensibly except in relation to price. [This] disfiguring practice [...] may conveniently be termed price-less economics. [...]

The practice implies that government direction or control is indispensable for the effective deployment of resources. (Bauer, 1984, p. 158)

The influential groups protect not only the invalid notions but also those responsible for them. Even when their statements have been conclusively refuted by evidence or exposed by criticism, the authors will continue to be acclaimed as experts so long as their stance accords with the prevailing ideology or vested interests. Thus, influential exponents of the vicious circle of poverty are still regarded as world experts on development or even as outstanding figures in the subject. (Bauer, 1984, p. 156)

The growth of interventionism was also given some boost by the spread of mathematical formalism discussed in the previous chapter. The fascination with rigor and alleged accuracy helped to obfuscate the basic intuition and practical verity of many policy conclusions of the orthodox, 'verbal', economics. Peter Bauer makes this point and adds a list of development issues where economists were led seriously astray:

The use of [mathematical] methods has even come to serve as a barrier to criticism of a wide range of transgressions. Many of the lapses in analytical and applied economics [...] have at various times been surrounded protectively by a façade of technique and jargon which is apt to obfuscate the discussion and so to deter and blunt the criticism. A list of these transgressions which at times have been buried in a welter of mathematical formulae and manipulations would include the following: that export earnings are independent of exchange rates and of supply conditions. (Bauer, 1981, p. 265)¹⁰⁶

¹⁰⁶ It is important to note that growth of unintelligible jargon, mentioned by Bauer, is by no means limited to economics, but is rather symptomatic for social sciences. Stanislav Andreski, while typically scathing, drives the point home:

The attraction of jargon and obfuscating convolutions can be fully explained by the normal striving of humans for emoluments and prestige at the least cost to themselves [...]. [N]ebulous verbosity opens a road to the most prestigious academic posts to people of small intelligence whose limitations would stand naked if they had to state what they have to say clearly and succinctly. (Andreski, 1972, p. 82)

[T]he easiest kind of work [in social sciences] is an endless exegesis of widely known texts; and in this case vagueness and obscurity help to provide such work while clarity and conciseness curtail it. Any author who (like Hegel or Husserl) writes in a tenebrous and ponderous fashion, gives work to a large number of smaller fry who can busy themselves commenting on what he *really* meant; whereas a writer like David Hume or Bertrand Russell, who makes perfectly clear what he means, creates no such opportunities for

To the list of policy issues enhanced by formalism, one may surely add the great socialist calculation debate, which tended to produce the most interventionist economic theories imaginable – theories showing socialism as a more doable program.

The thesis about growing interventionism in economic theory can be supported by looking at changes in economists' opinion. The opinion surveys I made use of above provide good opportunities to do so.

First, one may take a look at the response differences in two surveys that were undertaken among the same group of economists with a time gap of 14 years: in 1976 (Kearl et al., 1979) and 1990 (Alston et al., 1992). Three of the four issues I chose were covered in both surveys and in all of them, one can spot a change towards more interventionism.¹⁰⁷

Table 2.1: Comparing responses in time (1976-1990)

Statements	Response (3 – yes; 2 – yes, but; 1 – no)	1976 (Kearl et al., 1979)			1990 (Alston et al., 1992)		
		%	Mean	Relative Entropy [%]	%	Mean	Relative Entropy [%]
Tariffs and import quotas reduce general economic welfare.	3	81	2.8	47	71.3	2.63	57
	2	16			21.3		
	1	3			6.5		
A ceiling on rents reduces the quantity and quality of housing available.	3	78	2.8	46	76.3	2.7	52
	2	20			16.6		
	1	2			6.5		
A minimum wage increases unemployment among young and unskilled workers.	3	68	2.6	75	56.5	2.36	74
	2	22			22.4		
	1	10			20.5		

mediocre intellectuals to make a living by endlessly going round in circles, and so is less likely to become a totem. The creators of mental fog are boosted into fame by intellectuals to whose parasitic propensities they have ably ministered. (Andreski, 1972, p. 93, emphasis original)

¹⁰⁷ In fact, Alston et al., 1992, look into the differences in time and test their significance. After eliminating the differences in the respondents group, the

Second, one may do the same between 1990 (Alston et al., 1992) and 2000 (Fuller and Geide-Stevenson, 2003). In fact, Fuller and Geide-Stevenson do just that, after adjusting to differences in respondents groups between the two surveys.¹⁰⁸ With the question on rent control dropping out of the 2000 survey, but with the one on resources in agriculture appearing in the 1990 survey, there were again three out of the four issues that were covered in both surveys. Moreover, I added two additional statements that relate to interventionism. Response differences in all five statements are again suggestive of the continuation of the tendency towards more interventionism (or less counter-interventionism).

hypothesis about similar distribution of answers is rejected for protectionism and minimum wage (Alston et al., 1992, p. 206).

If overall results are compared (which is what I do), the differences are more pronounced than what Alston et al., comparing just the respondent tiers common to both surveys, find. However, there is a rationale for not eliminating the differences in the respondents group. One would assume that the choice of the group in each case reflected the understanding of the extent of the profession. As I am interested in changes in what economists as a group think, I have to take into account the change in the composition of the group, not only the changes in opinion of its particular members.

¹⁰⁸ The Alston et al. data were reweighed by Fuller and Geide-Stevenson in order to bring the structures of the two samples closer in order to increase comparability (see Fuller and Geide Stevenson, 2003, p. 371).

Table 2.2: Comparing responses in time (1990-2000)

Statements	Response (3 – yes; 2 – yes, but; 1 – no)	Adjusted 1990 (Alston et al., 1992) ¹⁰⁹			2000 (Fuller and Geide- -Stevenson, 2003)		
		%	Mean	Relative Entropy [%]	%	Mean	Relative Entropy [%]
Tariffs and import quotas reduce general economic welfare.	3	76.7(71.3)	2.73 (2.63)	59 (57)	72.5	2.67	66
	2	17.3 (21.3)			20.1		
	1	4.8 (6.5)			6.0		
A minimum wage increases unemployment among young and unskilled workers.	3	62.4 (56.5)	2.45 (2.36)	83 (74)	45.6	2.19	97
	2	19.5 (22.4)			27.9		
	1	17.5 (20.5)			26.5		
Economic evidence suggests there are too many resources in American agriculture.	3	50.6 (48.7)	2.48 (2.29)	92 (85)	33.9	2.09	99
	2	22.9 (23.9)			32.2		
	1	20.6 (21.3)			25.5		
The level of government spending relative to GDP should be reduced (disregarding the expenditures for stabilization).	3	41.7 (35.6)	2.04 (1.91)	95 (79)	29.2	1.78	92
	2	19.0 (19.0)			18.5		
	1	38.2 (46.6)			50.3		
The redistribution of income within the U. S. is a legitimate role for government.	3	42.3 (56.5)	2.17 (2.4)	98 (73)	49.0	2.33	93
	2	31.1 (25.4)			32.2		
	1	25.2 (16.8)			16.8		

Issues that used to be somewhat of a hallmark of economists' unanimity in opposition – namely the rent control and minimum wage – have gone through a process of revisionism. As described by one author:

In recent years [...] there has been a wave (or at least a swell) of revisionism among housing economists on the subject of rent control. While few actually advocate controls, most are considerably more muted and qualified in their opposition. Perhaps a majority, at least in the younger generation, would agree with the statement that a well designed rent control program can be beneficial. (Arnott, 1995, p. 99)

The revisionism on rent control [...] is strikingly similar to the revisionism that has occurred concerning the effects of the

¹⁰⁹ Data in brackets are unadjusted data, i.e. based on the original Alston et al. sample.

minimum wage [(Card and Krueger, 1994)] that, contrary to predictions based on competitive models or the labor market, recent increases in state minimum wages have not had a discernible effect on employment. (Arnott, 1995, p. 117)

As another indicator of the above revisionism, rather than comparing the change of opinion in time, one can compare opinions of economists to graduate students of economics (who are *future* economists) at the same time. This can be done using e.g. the Alston et al. survey of American economists ran in 1990 (Alston et al., 1992) and a survey among graduate student of economics at leading American universities, carried out by David Colander and Arjo Klamer in 1985 (Colander, Klamer, 1987).

Table 2.3: Comparing responses across generations

Statement in exact wording	Response (3 – yes; 2 – yes, but; 1 – no)	Future Generation: Graduate students in 1985 (Colander, Klamer, 1987)			Current Generation: Professional economists in 1990 (Alston et al., 1992)		
		%	Mean	Relative Entropy [%]	%	Mean	Relative Entropy [%]
Tariffs and import quotas reduce general economic welfare.	3	36	2.29	86	71.3	2.63	57
	2	49			21.3		
	1	9			6.5		
A minimum wage increases unemployment among young and unskilled workers.	3	34	2.18	96	56.5	2.36	74
	2	39			22.4		
	1	18			20.5		

For both policy issues in which the surveys overlap, there is a tendency for graduate students of economics, i.e. the next generation of professional economists, to be more interventionists compared to current professional economists. Also, on both issues, the degree of consensus as indicated by the relative entropy is lower among future economists than among current economists.

*

To sum up, willing to become just as useful to society as other scientists, and, moreover, *recognized* as such, economists started proposing a positive agenda for the government to follow. No more were the economists' prescriptions for government policy to be couched in terms of what government *should not* do, but rather of what the government *should* do. For the idea that government policy can improve the state of affairs by active policy (rather than by refraining from its intervention) to gain ground, there are two types of economists' activities I think it worthwhile to distinguish. First, it is the search for market failures, and second, more subtly, it is a redefinition of some key economic concepts. Let us look more closely at each of them.

SEARCH FOR FAILURES

For economists to advocate active government policy, they first had to show there is some sort of ideal situation, a 'social optimum', to which the real world could be compared. Attempts at definitions of such optima were of course implicit in the works of many economists for some time, but they explicitly found their way into the analysis only at the end of 19th century. Walras's idea of general equilibrium and Pareto's definition of efficiency stand out most clearly. With this benchmark at hand, economists could apply it to the real world and discover instances where such a world deviated from it. These instances were named a market failure and became an important research program, exploited to this day. With a market failure at hand, it is a short step for economists to indicate and supply a policy that would move the state of affairs closer to the optimum.

And thus, economics, originally devoted to explaining the importance of markets for peaceful and wealthy society (and contrasting it to the government intervention as a source of conflict and poverty), gradually absorbed various qualifications to its previous position. In the light of discovered market failures, the unfettered markets were seen as suitable *only* if those failures did not obtain. On the other hand, should they

obtain, it was considered imperative to impose certain regulations on such markets, which created almost unlimited space for possible improvements by policy.

Specifically, these failures may take the form of:

- the *externalities*; benefits or cost that are not included in decisions of the trading parties resulting in the market producing too little (in case of external benefits) or too much (in case of external costs), making it possible to subsidize or tax just about any activity;
- the *public good*; a positive externality (a good rendering external benefits) writ so large that the good in question is not just ‘under-produced’ but virtually non-existent, making it possible to use the non-existence of anything as a reason for intervention;
- the *market power*; an ability to influence the market price resulting in the price being either too high (higher than marginal cost), or too low (lower than marginal benefit), making it possible to use a non-zero market share of any company as a reason for its regulation
- the *information and coordination imperfections*; a fact, that market participant have incomplete and different information about (and control over) the actions of each other, resulting in them doing something they would not do and not doing something they would do if they had that information, and thus making it possible to use any missing or asymmetric information as a reason for limiting the freedom of contract and other interventions.

The area of trade policy offers good examples of such searching. Even though it is probably to this day the most unanimously opposed government intervention, economists devoted increasing energy to discovering instances in which some intervention might be justifiable. Any of the above failures do of course have implications for trade policy, with free trade ceasing to be the best policy option. Anne Krueger, perhaps emphasizing the scientific aspirations of economists, notes:

Much of the [trade] theorizing that took place was concerned with what I call the 'negative results'. That is, analyst sought to find reasons why, for example, an exception to free trade should be made. Once the principle of comparative advantage was laid down as a basis for policy, there was little left for theorist to prove supporting an open trading system, so the *challenge to theorist* was to find conditions under which the free trade precept did not hold. As for theory, these findings were significant. But for policy, there were unhelpful, and probably served to perpetuate inappropriate policies. (Krueger, 1999, p. 39, emphasis added)

SHIFTING DEFINITIONS

The above process of discovering market failures was complemented, and in some cases facilitated, by careful semantic change in some important economic terms and concepts.

Some concepts economists originally used were so inextricably associated with government activity and intervention that they in fact amounted to names of specific government intervention. Under such circumstances, it would be hard to retain their original meaning *while at the same time* creating room for, and justifying, government activities in the given area.

What happened then in economic theory is that such concepts took on an entirely new meaning, stripped of any association with government policy. With this seemingly formal and innocuous step, economists not only freed the government of the charge of being the villain, but also prepared ground for the government to get back into the picture in an entirely new – therapeutic – role.

Consider the following cases.

Inflation

Originally, inflation meant creation of money substitutes not backed by monetary commodity. Such inflation always

resulted in higher prices than there would otherwise be and was thus considered as a *cause* of rising prices. However, this definition of inflation was gradually transformed (and finished perhaps with Keynes's assault upon the quantity theory of money) so that today it signifies the price increases themselves, regardless of their cause. So while originally the term described the cause, now it describes the effect. This shift in meaning was very important since prior to it, inflation was something that politicians (governments) and governmentally sanctioned fraudulent bankers were responsible for. Now, after the shift, politicians are no longer directly associated with inflation and can therefore claim to be fighting it. And so, this shift not only makes politicians look innocent, but also creates room for just another 'policy' – this time the *anti-inflation* one. By performing this shift, economists helped to distract the attention of the public from the fact that it is still the government that is responsible for inflation, and, which is rather incredible, helped the politicians to be viewed as inflation fighters protecting the public from the dire effects of inflation.¹¹⁰

Monopoly

The same story could be told for the term *monopoly*, which makes for a remarkably close analogy. Originally, monopoly meant a government privilege, protecting governmentally favored companies from competition.¹¹¹ Such grants of monopoly resulted in fewer companies operating on the

¹¹⁰ The evolution of the term *inflation* is described in Bryan, 1997. This report is the all the more remarkable as it is coming from a Federal Reserve Bank of Cleveland's Vice President. In his words:

For many years, the word *inflation* was not a statement about prices but a condition of paper money – a specific description of monetary policy. Today, *inflation* is synonymous with a rise in prices, and its connection to money is often overlooked. [...]

What was once a word that described a monetary cause now describes a monetary outcome. This shift in meaning has complicated the position of anti-inflation advocates. As an inflation of the money stock, an inflating currency has but one origin – the central bank – and one solution – a less expansive money growth rate. But as a condition of price level, which may have originated from a variety of things (including a depreciating dollar, rising labor cost, bad weather, or a number of factors other than "too much money"), the solution to – and prudence of – eliminating inflation is much less clear. (Bryan, 1997, p. 1, emphasis original)

¹¹¹ For example, Machovec claims:

market specified by law than there would otherwise be and were thus considered a *cause* of the existence of (ultimately) only one seller on that market. However, this definition of monopoly was gradually transformed so that today it signifies the existence of one seller on a given market itself, regardless of its cause. Again, while the term originally described the cause, now it is descriptive of the effect. This shift in meaning was very important since prior to it, monopoly – as understood and used by the early economists – was something that politicians (governments) were responsible for. Now, after the shift, politicians are no longer directly associated with monopoly and can therefore claim to be fighting it. And so, this shift not only makes politicians look innocent, but also creates room for just another ‘policy’ – this time *anti-monopoly* (or *anti-trust*) one. By performing this shift, economists helped to distract the attention of the public from the fact that it is still the government that is responsible for monopolies, and, which is rather incredible, helped the politicians to be viewed as monopoly fighters protecting the public from the dire effects of monopolies.

‘Policies’

Political rulers had traditionally two and only two ways of obtaining means for living. They could either take it directly away from the subjected people through taxation, or create such means through inflation. However, the early economists – along with the public – had great reservation about both of these activities because of their re-distributive and discoordinating character. They were then considered as tools used by rulers to enrich themselves on behalf of the subjects. Today, in contrast, economists view taxation largely as a legitimate payment for services (partly the service of rectifying market failures) and, on a ‘macro’ scale, a part of *fiscal policy*. The same holds for money creation – without any

[T]he classical concept of monopoly was tightly linked to the permanent profits garnered from mercantilist franchising rights which insulated favoured firms from fear of entry by rivals. (Machovec, 1995, p. 16)

Machovec, 1995, is a meticulous study in the development of the concept of monopoly and competition.

negative connotations, it goes under the name of *monetary policy*. With the help of economists, plundering was turned into scientifically and euphemistically sounding 'policies'.

2.2 DEMAND FOR ECONOMIC IDEAS

Economic knowledge as produced by economists is found valuable by only a limited range of consumers. It may be valued directly as consumption by anybody curious about economics and the answers it offers *per se*. This group includes for the most and increasing part the economists themselves,¹¹² but at least conceivably it may satisfy curiosity on the part of some laymen as well.

Besides this, it may be valued as a higher order good by those who can use this knowledge as a means for achieving further goals. To some extent these include the businessmen, although to a lesser degree than is commonly assumed. But who stand out in this category are of course the policy-makers. It is they who are viewed as charged with pursuing certain goals and tasks in society and thus it is they who make decisions about how to achieve them. And to these questions and problems economics may – and, in fact, aspires to – provide some answers and solutions.

In discussing the demand for economic knowledge, of all agents who may value economic knowledge, I am here concerned exclusively with the policy-makers. This is for two reasons. First, as discussed above (see chapter 2.1.1), policy-makers are the prospective and the most likely *buyers* of this knowledge as it is easier for them as a group to overcome the public-good character of economic ideas. Second, I am after all interested in the theory-policy relationship which makes the policy-makers necessary partners to the economists.

¹¹² The idea that economists produce economics in a growing degree for themselves was discussed above, see chapter 2.1.2.1.

The last thing that remains to be explored under this heading is who falls within the group of policy-makers. This is much easier than defining the economists because there are no questions of scientific competence or recognition. What suffices for a person to qualify as a policy-maker is simply the power to make, or influence the making of, the public policy. The numbers of policy-makers fitting my definition surely depend upon the political system: in a monarchy it will be relatively smaller than in a democracy. In a standard republic today, we see the professional politicians in government and parliamentary positions to be the primary policy-makers.¹¹³ It is through them, that other groups can and do participate in shaping the policy. On the one hand, the influence upon policy is exercised by party members. On the other hand, it is government officials and clerks – partisan or non – appointed by the professional politicians to the government sub-hierarchies (departments, ministries, committees, bureaus or agencies). All of the above are further subject to influence of their advisors, aides, and, last but not least, lobbyists.

Let me now turn to the objectives the policy-makers may pursue.

2.2.1 POLICY-MAKERS' OBJECTIVES

Just like in the economists' case, the host of all possible objectives of policy-makers can be divided into two classes bearing, for reasons of symmetry, identical names and very similar content. The first objective is the desire for good social organization, while the second class is anything that remains outside of the first.

The first objective is clearly a *benevolent* one. It is an objective policy-makers have always liked to believe – and advertise. In fact, it is rarely the case that a policy-maker

¹¹³ This is not to say these professional politicians have an ultimate and thorough control over all aspects of policy. While many aspects of day-to-day policy can go on without these politicians even being aware of them, these politicians still are the ultimate policy-makers in the sense that *changes* in any must be initiated or approved by them or their subordinates.

would admit he is motivated primarily by anything else but public interest.¹¹⁴ All policy-makers in history – despotic rulers or democratic officials – professed their dedication to the welfare of the people, even though the term welfare state suggests it is a comparatively recent phenomenon. Historian and sociologist Jack Douglas comments:

A welfare state is a state asserted by its rulers and other supporters to be dedicated to the welfare of the citizens. But this obvious meaning is absurd to anyone who examines it the least bit critically. *What state has ever been presented by its rulers and other supporters as a “dyswelfare state”?* Is it conceivable to anyone with common sense that a ruler who wants to remain a ruler would announce to his subjects, “I rule not to increase your welfare, but to bring you dyswelfare – poverty, misery, suffering, and a great knashing of teeth”? [...] Though it is not obvious, it also seems likely that almost all rulers have also believed their powers were necessary for the welfare of the whole state. (Douglas, 1989, p. 7, emphasis original)

A policy-maker is assumed to know what modes of social organization are in the interest of the society (the ends), to be aware – perhaps with the assistance of sciences like economics – of the ways these goals could be achieved (the means), and, of course, he is assumed to desire to bring this all about.

Here too, some differences regarding these goals and means may exist, but they are of minor importance as it is only the *ultimate* motives that I want to focus upon when making this classification. Finally, such a benevolent objective is fully achieved when the policy-maker knows the society is better off – it is not contingent upon other people being aware of his role in it.

¹¹⁴ This is perhaps the greatest difference from the economists. Even though both economists and policy-makers will profess objectives more benevolent than they are, economists are more likely to admit being motivated by selfish objectives than policy-makers are.

The other class of objectives contains all the other motivations, for which I reserve the name *selfish*. Besides all forms of material gain and power, it may, for example, include the fame and celebrity status due to the association of the policy-maker's name with a particular government or reform.

As in the case of economists, there are then two different classes of policy-makers' objectives:

- 1) Benevolent – social good (change)
- 2) Selfish – all other benefits

While analytically different, the benevolent and selfish motives may and will mix in reality, even if not in policy-makers' rhetoric. The point, however, is again that even if these motives are both operative at the same time, there tends to be a trade-off between the fulfillment of one as opposed to the other. The more successful a policy-maker is in effectuating the public interest policy, the less he is likely to succeed in gaining fame or material benefits from his position.

The reasons for the incompatibility of the two classes closely parallel reasons for divergence of economists' benevolent and selfish objectives. They hinge on the fact that, generally, policy conducive to public interest tends to be rather passive, non-interventionist. Such policy based on refraining from active engagement in private affairs always appears less sophisticated and its practitioners then less credit-worthy. Thus, such policy invites weaker appreciation of the policy-maker among people and lesser recognition and fame. At the same time, refraining from active policy means relinquishing the possibility to serve special interest groups, and consequently, warrants no votes and other benefits from them. Without large bureaucracies, the policy-maker is left with less support for the necessity of his own position. In short, practicing good policy warrants weak chances of recognition and almost guarantees no reelection and no extra income or pork-barrel.¹¹⁵

¹¹⁵ The above holds for *perpetuating* a good policy. *Improving* the policy is even more less instrumental towards the selfish objective. Retracting activist policies implies resistance from all agents who feel hurt (bureaucracies, special interest groups).

Given policy-makers' objectives, it is perhaps in order to explicate in more detail why economics may be found helpful in achieving both the benevolent and the selfish motives.

For a benevolent policy-maker, it is only natural to turn to social scientists – economists among them – for advice on matters of social organization. But so is it for a selfish policy-maker, if for a very different reason. While the benevolent policy-maker hopes to learn what to do in order to contribute to the public cause, the selfish policy-maker, in order to exploit his position, must make sure his position is well secured. It is decidedly in the policy-makers' interest to have policy appear to voters as science rather than as partisan politicking and favoritism. Having the 'science' back up their policy can not only make their policy more palatable to the public, but can also relieve them of some responsibility for practicing it.¹¹⁶ This is why they have a stake at the economic science: it is a source of justification for what they are doing.

The idea of social scientists – and economists – churning out theoretical reasons for policy-makers to justify what they have been doing anyway, or are just interested in starting to do, may surely seem a bit far-fetched to some people. But it is part of the picture of social sciences as drawn by many scholars. Consider the following statement of Will Hutt:

The 'pure theorist' is apt to become a hermit, and whilst he may hope that the practical men may sometimes visit his cave and humbly ask advice on matters in which his mysteries are believed to give him an insight denied to other, in his heart he knows that they have no faith in his mysteries; that they do not genuinely seek his advice; and that *if they do come to his lonely dwelling, it is to get from him some mystic formula that happens to suit their purpose, and which can be used*

¹¹⁶ All that, and the latter in particular, can be extended to science in general. In fact, Harvey Brooks – a physicist – made that the very same point:

Too often the politician or administrator is tempted to throw the onus of difficult or controversial political decisions onto his scientific advisers. An important decision may be much more palatable to the public and to Congress if it is made to appear to have been taken on technical grounds. (Brooks, 1968, p. 95)

with his authority to refute their opponents on some special topic.
(Hutt, 1936, p. 35, emphasis added)

Peter Bauer makes a similar observation:

The practice of governments of appointing economists as advisers may have helped to propagate the notion of the influence of economists, notably as government appear often to follow their advice. In fact, particular advisers are often chosen because governments rightly believe that their advice would accord with what they wish to do in any case. (Bauer, 1984, p. 153)

Lastly, Harry Johnson, in his analysis of the national styles of economic research (Johnson, 1973), points to remarkably similar tendencies, particularly in Britain and in Canada:

The function even of the better academics [in Britain] is either to provide sophisticated rationalizations for government policy decisions or to provide new and challenging ideas on policy that government (or its opposition) might be able to use sometime. This function involves no research at all, only cleverness in making forensic use of other people's research for political purposes. [...]

[The Canadian academic] has two alternatives. The majority choose to acquire still more learning without using it to raise any new questions about Canadian society, though they may legitimately use it to refute the wilder public answers to old questions, provided they do so decorously and without having any real impact on public opinion. A minority choose to abandon all academic standards and to use academic status as a platform from which to encourage the wildest of public emotions, especially in support of a form of nationalism which would guarantee its academic exponents academic promotion without academic delivery. (Johnson, 1973, pp. 71-72)¹¹⁷

¹¹⁷ Johnson remarks that such tendencies are (i.e. in 1973) still least visible in the United States,

the only country where government policies are still not regarded as sacrosanct and where a man is not only free but encouraged to think of government policies as arbitrary interferences rather than unquestioned national necessities. (Johnson, 1973, p. 74)

Having shown what the policy-makers' objectives are and the role economics might play in fulfilling them, I may now proceed to the evolution of policy-makers' involvement in economic science.

2.2.2 EVOLUTION OF DEMAND

Ever since the policy-makers (rulers of all kinds and levels) started using reason – besides brute force – to justify their status and the policy they engaged in, they turned to scholars for both inspiration and justification. These were mostly religious priests at first, but the renaissance turned the balance of advisors to secular thinkers – with economists among them.

In contrast to economists, the objectives of policy-makers do not appear to shift in time from benevolent to selfish. Rather, it is ultimately the selfish objectives dominating throughout the history with the benevolent motives at the same time used ostentatiously as a veil for display.¹¹⁸

The policy-makers' primordial objectives were decidedly selfish. The origins of state units were always associated with conquest of property and power. The purpose of demand for scholarly ideas about society was to generate justification for government privileged existence and its operation. Some scholars supplied well suited theories: for instance, the divine origin of kings was in most parts of the world replaced with more persuasive social contract theory and an ideal of democracy.¹¹⁹ The product of economists, however, seemed to be particularly ill-suited for these purposes. This is because when one looks at the historical record, one can view the birth of economic science almost as a *protest against* much of what policy-makers used to do.¹²⁰

¹¹⁸ The real-world case of a benevolent policy-maker cannot be denied, but these instances are occasional and short-lived only.

¹¹⁹ Another area that was well received by policy makers was social statistics. Gathering of data about society furnished policy-makers with ideas about areas that could be addressed with intervention policies.

¹²⁰ See note 100 above.

From the policy-makers' perspective, the economists' product was a bad.¹²¹ The reaction to the existence of this bad may be viewed as comprising two phenomena: the *policy sieve* and an effort to directly influence science.

2.2.2.1 POLICY SIEVE

The first type of reaction towards the unfavorable economic theories was to carefully filter the attention policy-makers paid to them.¹²² This is what I propose to call a *policy sieve*. Through this imaginary sieve, policy-makers screen economic theory and manage to separate those parts that are wholly hostile to their activities from those that could potentially become useful. The former theories get ignored, while the latter get twisted and paid due attention to.¹²³

¹²¹ The consensus surveys suggest that to this day economists' policy opinions remain largely a bad for policy-makers' tastes. All the tendencies described above and below notwithstanding, economists' opinion remains on average more conservative than the actual policy (see e.g. chapter 1.1.2.1, particularly p. 39 and on) or the average citizen (see e.g. Caplan, 2007, especially chapter 8).

¹²² The idea of a filter between theory and policy appears in Jones and Cullis, 1993. While they focus on the perceived certainty of the results of theoretical research that their notional filter is supposed to increase (Jones and Cullis, 1993, p. 63), they do recognize similar effects on the demand side, regarding both ignoring and twisting the theory:

Actors in the political process only have interest in promoting the results of economic research which supports their view. In academic circles results can be obtained to support various positions but much of this is overlooked when the political contest lies between only two or three political parties. In this way the political process filters out those results which support the ideology of the main parties. (Jones and Cullis, 1993, p. 70)

To this they add, putting the famous Keynes' dictum on its head: "It is in this respect that economists are owned by extant politicians, rather than politicians being the slaves of defunct economists" (Jones and Cullis, 1993, p. 70).

¹²³ It would be inconsistent to claim that this tendency is unique to policy-makers. As Frank Fetter wrote along very similar lines about businessmen:

Whenever the precepts of economics favored, or could be made to appear to favor, the commercial interests, its virtues were unduly extolled; but when the precepts of economics have been opposed to dominant commercial interests, it has been either ignored or condemned. (Fetter, 1925, p. 17)

Manufacturers saw no inconsistency in continuing to laud the high statesmanship of 'protective' tariffs, in the same breath in which they proclaimed the sanctity of the great economic principle of free competition. (Fetter, 1925, p. 19)

However, focusing my attention on policy-makers is not being unfair to them. From a policy-formation point of view, one has to recognize such tendency on the

Anne Krueger, in the context of development economics, points this out and calls it “an apparent paradox”:

[W]e desperately need excellent theory to underpin policy analysis and yet good theory is liable to rejection or misapplication on the part of people benefiting from policies supported by other dogmas or wanting to carry out a particular set of policies at any event. (Krueger, 1999, p. 34)

IGNORING THEORY

When the particular part of economic theory allows for no market failure and or no possibility of improvement, it has non-interventionist policy implications. In such cases the policy-makers, intent upon carrying out certain activities, have to *evade* the application of these theoretical conclusions. In order to practice policies *in spite of* explicit recommendations of economic science, the policy-makers act as if such conclusions did not exist or, at least, were irrelevant for the policy they are practicing. The theory, when discussed at all, is labeled and dismissed as ‘only theoretical’ and ‘detached from the real-world’.

The first typical attitude of policy-makers toward economic theory is then simply one of *ignoring* it. This explains the fate of many economic theories that are unfavorable to government intervention: e.g. the international trade theory and its free trade conclusions or the price theory and its general anti-price-regulation conclusions.

TWISTING THEORY

There are areas and concepts in the economic theory that identify a state of affairs where improvement is conceivable. Implicit in all such concepts of market failure is that it is the political action that might play the remedial role (see also

part of policy-makers as of primary importance. Businessmen and all other groups – while no doubt exhibiting the same tendency – can influence the policy only through the policy-makers, and are then only secondary.

chapter 2.1.2.2): the policy implication of these theories is clearly pro-interventionist.¹²⁴

In such cases economics does deliver what is demanded by policy-makers and they do not hesitate to use it with a vengeance. Expressions such as ‘public good’, ‘asymmetric information’, ‘monopoly’, ‘effective demand’, to name just a few, became a commonplace in public policy discussions.

Yet, unsurprisingly, that is not the end of the story. In line with the policy-makers’ motives for demanding economic theory, they do not necessarily spend much time learning what *exactly* economists have to say when they theorize about such market failures. They are satisfied with the fact that there *are* market failures to be remedied by them. They do not inspect too closely under what circumstances the market is said to fail, and *how* can that failure be really rectified. Thus, when applying economic theory to economic policy, they take the basic idea of a market-failure theory, very often just the terminology, and distort the rest so that, in the end, the scope for their interventions is even larger than what the economists’ theories would suggest. That explains the fact that the policy rarely follows the conclusions of the theory but, rather, goes far beyond it.

A typical way in which a theory gets twisted is the ignorance of its context. In many cases, the solution to a particular market failure (the second-best solution) is known to exist theoretically, but economists recognize it as hard-to-implement. In fact, even if the second best solution could somehow be turned into an actual policy economists still discourage it for political reasons: for fear that the political process will not be able to handle the matter properly with the result being inferior to market failure left un-remedied. This was nicely articulated by Harry Johnson:

¹²⁴ As Jones and Cullis remark:

The political policy makers’ case for government involvement appeared to spring almost automatically (especially as far as those inclined to the left of the political spectrum are concerned) from the mere argument that such failure might exist. (Jones and Cullis, 1993, p. 68)

The fundamental problem is that, as with all second-best arguments, determination of the conditions under which a second-best policy actually leads to an improvement in social welfare requires detailed theoretical and empirical investigation by a first-best economist. (quoted in Krueger, 1999, p. 40)

A good source of instances where theory gets misused and is given a pro-interventionist bias is again the trade theory. Anne Krueger, an undisputed authority in this field, provides some examples:

[T]he identification of comparative advantage with the two-sector, two-good model, and the implication that the developing countries would for ever have to specialize in primary commodity production if they maintained free trade was the most abused idea. [...]

A second serious misapplication of good theory [is] the interpretation of the 'infant industry' argument. It was widely used as a rationale for import substitution and generally recognized as a 'legitimate' case for a departure from free trade. (Krueger, 1999, p. 37)¹²⁵

Jones and Cullis offer another historical example of theory twisting:

Pigou [Pigou, 1947], for example was well aware of the need to consider the distortion costs of government and the marginal costs of taxation. 'Certainty' was being ascribed by those at a 'distance' from the debate, where the temptation to stereotype positions is often irresistible. For example, although by 1960 Coase's well-known article argued that small number externalities would be self-correcting, Mishan [Mishan, 1976] claims this insight was well known at the academic level much before this. *Developments at the 'core' then appear to have been overlooked in an attempt to manufacture 'answers'*. (Jones and Cullis, 1993, p. 68, emphasis added)

¹²⁵ For reasons why the interventionist interpretation of these theories was misusing them, see Jones, 1971, and Krueger, 1977 (for two 2-sector, 2-good comparative advantage model), and Baldwin, 1969 (for the infant industry argument).

To summarize, in cases of pro-interventionist theory the typical attitude of policy-makers is *twisting* the theory (in order to magnify the intervention potential) and then ostentatiously applying it as a value-free scientific measure. Such is the fate of those parts of economic theory that do identify market failures: e.g. the perfect competition theory with its anti-trust implication or the public good theory with the implication for the need of public provision of certain goods.

2.2.2.2 SCIENCE INTERVENTIONISM

When policy ideas are produced by economists, they face the policy sieve before they are applied in policy. But there is another route the policy-makers may take when not satisfied with the product they are being offered by economists: they may try to influence the production of economic ideas. Namely, they may attempt to reduce the output of theories with non-interventionist implications. This requires channeling the research activities either into policy-irrelevant areas (pure theory), or – better yet – into pro-interventionist theories. In this way the economists' resistance to the policy they are interested in practicing is tempered or even turned into active support.

Economists, just like all other members of society, are influenced in their agenda by ideas present in society. To suppose otherwise – that economist only influence their environment – would not seem warranted as it would require me to exempt the economists from the rest of society and deny their human traits. Such susceptibility of economics to influence from outside, particularly to *political* influence, is a theme entertained by Peter Bauer:

Over the last half century or so, outside influences have much affected the activities, themes, methods and findings of economists. Even an incomplete list of these must include the extensive politicization of social and economic life; the spread of egalitarian ideology and of the belief in environmental determinism; the much-increased importance

of media, and therefore of the influence of those working in it [...]. (Bauer, 1984, p. 153)

A partial list of these transgressions [invalid theories propounded and popular for political reasons] includes the notions such as that poverty perpetuates itself (the vicious circle of poverty); that external contacts are economically damaging; that economic development must produce balance-of-payments problems; and that better-off societies, groups and individuals owe their prosperity to the exploitation of others. These opinions have often been advanced by prominent economists. (Bauer, 1984, p. 155)

Upon elementary reflection it is clear that if economists are to supply more and better suited theories for policy, it is necessary to make that particular activity more rewarding for them. One should then expect the economists to be courted by money and prestige – something that conspicuously resembles what has actually been happening.

EMPLOYMENT

One direction in which this process turned was that government started to hire economic advisors and researchers. This happened sooner in continental Europe than in either the United Kingdom or the United States.^{126, 127}

¹²⁶ In fact, in continental Europe, especially in areas with strong German influence, something in the way of economic advisors in the government service were an early phenomenon dating back to at least the 18th century. Cameralism as a science about government management and administration was established and supported by governments and was supposed to generate cadres of government clerks and servants. It later evolved into *Nationalökonomie*, a distinct German brand of political economy, or, later, economics. It also precipitated a peculiar German school, German historical school, known to rebel against English classical tradition and inspiring the American institutionalists. Almost all major German economists of the 19th century were heavily engaged in government service, socialists, and devout interventionists.

¹²⁷ An early, and prophetic, plea for employment of economists within government by Torrens is documented by Alfred Coats:

Though the time may not have actually arrived, yet it is rapidly approaching, when it will be deemed as necessary to select the members of the Board of Trade from the Economists, as it is to take the Bishops from the Church, or the Law Officers from the Bar. (quoted in Coats, 1964, p. 91)

The area in which economic expertise first started being employed on a grand scale was agriculture. US Department of Agriculture (or similarly the Ministry of Agriculture in the UK) was not only the biggest employer of economists but also the first organization through which government subsidized economic research. As explained straightforwardly by Alfred Coats, it “occurred first in agriculture because the government adopted a more active and detailed interventionist policy in that sector than elsewhere” (quoted in Middleton, 1988, p. 81).¹²⁸

Particularly fertile times for enlarging the role of economists in general within government bureaucracies proved to be emergency situations. Both world wars of the 20th century, and the Great depression in between them, meant a spike in economists’ involvement in government administration. About the WW I impact in US conditions,¹²⁹ Michael Bernstein writes:

A bit over a month after the Armistice, the American Economic Association and the American Statistical Association held a joint meeting on the benefits the social scientific knowledge and practice could offer to the public sector. The conference was, in particular, focused upon “credentialed economic inquiry that a number of prominent government and business figures believed could greatly enhance a society’s capacity for planning and purposeful management.” In arousing this conviction among the social scientists, the wartime experience had played an important part. In fact, the pressures and challenges of national mobilization had created an unprecedented demand for the

¹²⁸ These agriculture interventions date back to mid-19th century, and it is a reason of a remarkable early detachment of agriculture economics from the discipline. As Bernstein says:

[A]gricultural economists were [...] able to capitalize on long-standing ties between farmers and federal agencies in their own pursuit of professional standing and influence. [...] It is hardly surprising [...] that agricultural economics has maintained (and further deepened) its separation from the discipline of economics through the creation and maturation of separate faculties, degree programs, and professional societies. (Bernstein, 2001, pp. 212-213)

¹²⁹ Unless indicated, the data and events in this chapter refer to the situation in the United States. A practical reason for this is that such history is well described and accessible.

skills of economists. (Bernstein, 2001, p. 40, inside citations of Ellis Hawley)¹³⁰

It was particularly in the early 1930's when various government departments were opening new positions specifically for economists.¹³¹ The timing was no coincidence: in the advent of the Great Depression with the general sentiment of the laissez-faire economy having failed, it was almost overnight taken for granted that the economy must be managed. And just like the natural scientist and engineers have been manipulating nature to the apparently great benefit of people, economists and social scientists were hoped to do the same with organization of society.

In the United States, economists achieved the most prestigious position among all scientists when congress, notably in the Full Employment Act of 1946, legislated the *Council of Economic Advisers* – the first and only scientific body advising directly to the US president. The first chairman of CEA, Edwin Nourse, is famous for having tried to remain as value-free as possible by even refusing to testify before Congressional committees and for being – for the President's taste – relatively conservative. This was in conflict with the

¹³⁰ To indicate the order of the change, Bernstein reports on a work of Leonard White, who counted 25 “economic and political science” specialists in federal government employment in 1896 – a number that rises, in his calculation, to 848 during Herbert Hoover's presidency. (Bernstein, 2001, p. 211)

¹³¹ John K. Galbraith, in his memoirs, was quite explicit in describing it:

By the spring of 1934, after a year of F.D.R., the views of the young professors and especially of the graduate students at Berkeley had changed. Against all learned prediction, much was being attempted in Washington; Roosevelt now seemed a wonderfully compelling leader. Word has also reached university that a nearly unlimited number of jobs were open for economists at unbelievably high pay in the federal government. All the new agencies needed this talent. Students who had been resisting for years the completion of theses and the resulting unemployment now finished them up in weeks. So a new gold rush began, back across the American River [...] the Rockies and the Plains to the Potomac. When I got to Washington in the early summer of 1934, many of my friends were already at work. [...]

I went to Howard Tolley's office in the Agricultural Adjustment Administration [he was my former teacher from Berkeley], and he immediately suggested that I go on the payroll for the summer. I as promptly agreed. [...] After filling in forms, I was, however, required to go to a small room on the upper floor and meet the resident representative of James A. Farley, the Postmaster General and custodian of Democratic patronage. There I affirmed that I was a Democrat; one could be a Democrat without being a citizen or a voter. My salary was at a rate of \$3200 a year. In the next month I paid off all my college debts, and not since have I been short of money. (Galbraith, 1981, pp. 35-36)

tasks the President wanted his CEA to perform: it amounted to refusal to take over (or, at least, share) the responsibility for the President's economic decisions. This led to dissatisfaction on the part of the President Truman, and replacement of Nourse by more explicit and expansionist Leon Keyserling in 1950 (see e.g. Price, 1964, pp. 181-182). Keyserling was, for instance, insisting that increased spending on the Korean War will not affect the standards of living (Brune, 1989, p. 363), promising, in fact, the proverbial free lunch. He was also extremely cooperative towards the labor unions, AFL-CIO (Wehrle, 2004).¹³²

By the 1970's, economists were perceived as highly influential, as is evidenced by cheerful remarks of a contemporary analyst:

Economists have had institutionalized access to the President, Federal Reserve Board, and high levels of the bureaucracy. They have become policy makers without administrative responsibilities. They are closely interwoven within the policy-making process because decision-makers need their expertise and because it is so important that governmental actions in managing the economy be successful. (Schooler, 1971, p. 171)¹³³

Employment of economists by government has predictable links with their opinions. Economists employed in the public sector are more pro-interventionist. As Werner Pommerehne et al. report from their survey:

The theoretical expectations that economists employed in the public sector have a special inclination to support increases and reject decreases of the public sector, and that they are convinced of the effectiveness and desirability of public interventions, is borne out well by the results of probit analysis. In 12 of the 15 propositions the empirically

¹³² Some authors associate Keyserling's CEA stint with a distinct attitude of economists' way of thinking about policy: the *growthmanship*, "the emergence of the economic growth as an overriding goal of postwar policy" (Collins, 2002, p. 138).

observed responses correspond to the hypothesized answer in a statistically significant way. [...] The outcome of our analysis thus corresponds well to the assumptions commonly made in the economic theory of bureaucracy. (Pommerehne et al., 1984, pp. 260-261)

RESEARCH SUPPORT

Besides creating employment opportunities, policy-makers (i.e. the governments) set off to support economic research.¹³⁴ In continental Europe, the mechanisms for government funding of science were operating long before anything similar took off in the United States. This is due to a longer tradition of government involvement in the economy, particularly in countries under German influence. In the US, research started to be supported first again in agriculture, but after WW I it took a grander scale of operation.

After ad-hoc support given to private research institutions the US government started funding research on a regular basis either through its field-specific departments or agencies, or through its specialized grant-making agencies. The latter include most importantly the *National Science Foundation*, established in 1950, administering some 20 per cent of all government grants for basic research. Altogether, the US

¹³³ In 1970, government economists in the US established their own society – the SGE. It is not affiliated with the US government, but its establishment indicates how important an employer the government had become by then.

¹³⁴ Government tinkering with science in general is, of course, a much older enterprise. Scientists – besides being persecuted – were also at times being maintained by the ruling classes even for quite open-ended and general projects. One of the notoriously known examples is of course the court of Rudolph II in 17th century.

However, the modern era of full government involvement in science started with the 20th-century wars.

In the United States, the United Kingdom, and elsewhere, World War II led to an enormous demand-induced expansion in the scale of scientific activity, financed largely by national governments. Governments acquired a new financial responsibility for science and, for the first time, scientists found themselves well supported by (but dependent on) politicians and bureaucrats. In the United States, for the first time, both sides had become conscious of their need for the other; in Britain a similar view, emerging under the pressures of an earlier war (that of 1914-1918), received new stimulus. (Blume, 1974, p. 19)

government spends over \$130 billion on Research and Development (Meeks, 2006b, p. 7). Economists receive of course only a small fraction of this: in 2005, the US federal obligations for all social sciences (excluding psychology) well exceeded \$1 billion, with approximately a quarter of it going to economics proper (Meeks, 2006a, p. 59).¹³⁵ To imagine the relative size of this government-driven market, the total amount of resources for economic research at US universities is about \$300 million (Britt, 2004, p. 14). Institutionally, these funds are coming from diverse sources – among which one agency stands out in magnitude: the US Department of Agriculture, with more than 50-per-cent share in the total (Meeks, 2006a, pp. 73-75). Agencies administering grants of over \$1 million in 2003 included – in order of magnitude – the US Department of Health and Human Services, National Science Foundation, US Agency for International Development, US Department of Housing and Urban Development, US Department of Labor, US Federal Communications Commission, Environmental Protection Agency, US Department of Transportation, US Federal Trade Commission, and US Department of Commerce.¹³⁶ Besides these institutions, one has to take into account the fact that many project economists take part in are not classified as primarily economic, and the research funds going to economists are hidden in other categories.

Either way, the research projects economists apply for at these institutions are subject to review and decision procedures administered by these institutions. As these institutions are interested in justifications and enlargement of their activities, it would be fantastic to assume they would not be biased in favor of projects with precisely such conclusions rather than their opposite. This is not necessarily due to

¹³⁵ Approximately \$200 million is designed for basic research in social sciences (Meeks, 2006b, p. 25).

¹³⁶ Other institutions granting resources (but less than \$1 million each) to economic research in 2003 were US Department of Interior, US Department of State, and US Department of Justice.

outright inferior or ulterior motives of the committee members. It is because pro-interventionist theories appeal to many people – especially non-economists and progressives – as more path-breaking, sophisticated and consequently more support-worthy. Moreover, people in those committees, as predominantly members of the grant-awarding institution, or sympathetic with its agenda, are likely to be sincerely – and disproportionately – enthusiastic about its activities in the first place. Overall, every institution is likely to support research (through both grants and employment) in proportion to its friendliness towards the institution's agenda and mission, and this is no less true in case of *government* institutions.¹³⁷

Such biased nature of governmentally sponsored research (and employment, as well) did not go unnoticed in Harry Johnson's analysis of national styles of research. In the British context, he observes:

In accordance with [the British] socio-political structure, research money is available in austere amounts for applied research projects deemed socially useful; in much more generous amounts for applied research projects demonstrably useful to governments such as large-scale forecasting models of the British economy [...]; and in still more generous amounts for academic economists prepared to take leave from their universities and accept much higher-paid temporary employment in government in order to

¹³⁷ Larry White, in his analysis of influence of the Federal Reserve System on the nature of monetary research, soberly concludes about this institutional bias:

These incentives and filtering mechanisms may produce a result *as if* the Federal Reserve were deliberately subsidizing research that takes the institutional *status quo* for granted. This should not be surprising, nor is it scandalous. We naturally expect the research that any organization sponsors to tend to promote rather than to undermine that organization's interests. When (say) the insurance industry sponsors a report on the advisability of federal subsidies for terrorism insurance, the sponsorship alerts cautious readers to scrutinize the research methods and findings for pro-industry bias. Raising the question of the Fed's *status quo* bias alerts us that the same sort of scrutiny is appropriate to monetary policy research, to avoid employing a double standard. The Fed has an institutional interest in preserving the legal restrictions that generate its seigniorage revenues and the privileges that give it discretionary monetary policy and regulatory powers. Fed-sponsored research generally adheres to a high level of scholarship, but it does not follow that institutional bias is absent or that the appropriate level of scrutiny is zero. (White, 2005, p. 344)

write policy-oriented papers that rarely if ever get published, except when necessary to refute academic criticism of government policy decisions. (Johnson, 1973, pp. 71-72)

Thus, the net effect of government-sponsored economic research – even if not intentionally so designed – is a promotion and perpetuation of government activities. Economists' product is in this way made more interventionist than it would have otherwise been.¹³⁸

ECONOMIC EDUCATION

Complementary to the above was government influence upon economic science through the educational system. Most immediately is it felt at the university level where economics proper is studied and disseminated.

First, even universities are to a large extent dependent on research funds provided from government, and these research grants, as hinted at above, are more likely to support pro-interventionist ideas and projects.¹³⁹ In the US, for example, typically over a third of research funds come from the federal government (Britt, 2004, pp. 14-15). Second, government exerts enormous influence on economic curricula through its processes of accreditation. Especially in continental Europe,¹⁴⁰ governments more or less directly control curriculum of every study program through the ministry of education or other agencies.

¹³⁸ It is conceivable to provide evidence for the fact that government (or public) institutions have 'ties' with the researchers. This is what e.g. Klein (2004) or White (2005) do. It is, however, much more difficult to evidence the existence and the size of the bias these ties produce.

¹³⁹ This is particularly the state of affairs when universities are nationalized. This is a typical feature of the German model where a state funded university becomes a propaganda machine for government (see Kealey, 1996, pp. 183-184).

¹⁴⁰ Universities in the United States, for example, have a much larger degree of autonomy compared to those in continental Europe. There, say Frey and Eichenberger,

universities are parts of the state administration in practically all continental European countries, where the allocation of the academics to various positions is governed by a bureaucratic process. (Frey and Eichenberger, 1993, p. 186)

On lower levels of education, the influence of government is even greater. Particularly the curriculum regulation imposes strict limits and rules upon what is allowed or ought to be taught. It is true that on these levels there are rarely explicitly economic subjects.¹⁴¹ However, many classes touch upon economic points and provide students and pupils with often very twisted accounts of it. Illustrative examples are the history classes with their account of the Great Depression or Industrial Revolution, or civic education classes with their roles of government.

2.3 SUMMARY: THE MARKET FOR ECONOMIC IDEAS

After describing both sides of the market for economic ideas, it is time to wrap up and review all phenomena determining the type of product and its success with the customers.

Both economists and policy-makers have objectives that can be sorted as *benevolent* on one hand, and *selfish* on the other. Because of their incompatibility, the economists

- a) produce less policy-relevant, and
- b) produce more interventionist theories,
while policy-makers
- c) ignore or twist the economic theory, and
- d) engage in shaping economists' research agenda in order to achieve a) and b).

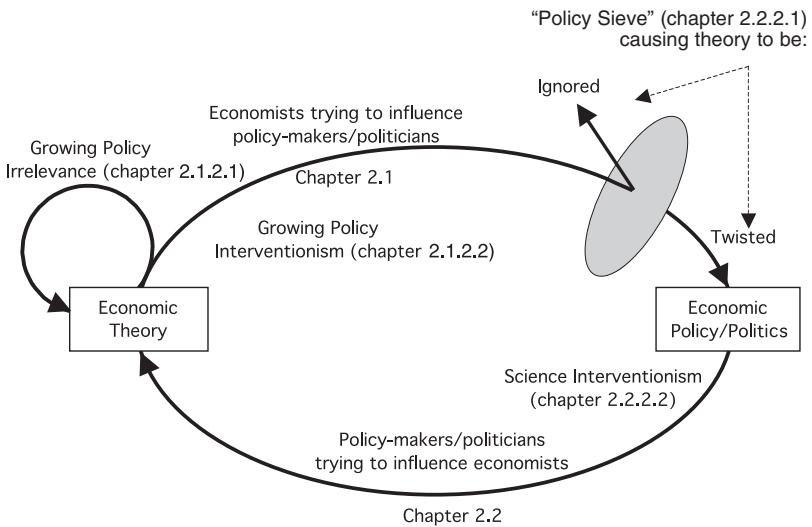
These phenomena explain the evolution of the economic science and the way it has travelled from the times of the early economist-reformer. The gap between theory and policy exists because of c), and the resulting frustration of economists

¹⁴¹ Indeed, the very absence of explicitly economic education in the curricula may be indicative of government influence upon economic science. On benefits of such education see chapter 1.

causes the economists themselves to do a) and b), which tends to eliminate the gap and the frustration. At the same time, the gap is being closed by the policy makers engaging in d), which reinforces both a) and b).

Graphically, the relationships and phenomena on the market for economic ideas are depicted on the following figure.

Figure 2.1: The market for economic ideas



Before I turn to the conclusions that can be drawn from the above analysis, there is an additional point I would like to preempt. In order to alleviate the outrage it might invite, it has to be emphasized that this mechanism does not necessarily hinge on a presumption of any inferior motives on the part of either economists or policy-makers involved. Both can engage in this behavior with perfectly honest feelings. For the economist, it is only natural that his theoretical interest in a particular issue is bolstered or even aroused by the policy that he sees is being practiced, particularly if he desires to

maintain value neutrality.¹⁴² Similarly, the benevolent politician, in his drive to do good, is interested in finding out what else, besides what he is already doing, he could possibly do for the public. The last thing he may be willing to accept as his program is the 'laissez-faireish' hands-off, do-nothing type of policy.

On the other hand, it should be clear how much more important this aspect becomes when one – quite realistically – allows both economists and politicians to act also as self-interested individuals. In such a case, it is even clearer how both parties can cooperate. The politician has power and funds and needs reasons to tell the public why it is not only good he has the power and funds, but that it would also be better if he had more. The economist can provide reasons that appear scientific – objective and detached, especially if such research work will turn out to be more rewarding in financial terms or in terms of power, prestige or status.

¹⁴² As Marc Roberts commented:

[The] effort to maintain neutrality makes it difficult for [economists] to develop new lines of inquiry. [...] [I]t is disconcertingly difficult to make [decisions about the new lines of inquiry], and careerism, chance, inertia, and imitation often fill the gap.

[P]rofessional interest is more likely to follow social policy than to lead to it. Work on Keynesian models of the economy grew greatly only after Congress, in the Full Employment Act of 1948, assumed responsibility for the level of employment. Studies of urban housing markets, poverty and early childhood education all became much more extensive in scope after major federal programs were instituted in these areas. In part this pattern reflects the availability of outside funding, but not entirely. A failure of intellectual imagination is also at work. Because social science is a campfollower to public controversy, social and economic policy is often made at a time when only the slimmest scientific results area available. (Roberts, 1976, pp. 59-60)

3

LESSONS FOR ECONOMISTS

In the above text, I attempted to describe the workings of the market for economic ideas, and used it to provide some ground for understanding the economists' frustration.

It is now time to derive some conclusions for those economists who still strive to be consequential. The picture drawn on the above pages looks no doubt quite dismal, even if in a different sense from Carlyle's. It might look that such economists' enterprise is forever doomed.

However, this might be the case only because the economists spent the last two centuries talking to the policy-makers, not necessarily without knowing, but without appreciating the fact that they are simply not a very receptive audience. After so much time economists should realize the policy-makers *do not want to listen*. They generally know what they want to do, and are mostly only interested in justification for it. They have no incentives to listen to economists.

Can they ever have? Is there any way the economists can make it in the interest of policy-makers to listen to sound economic advice? I feel there is. Economists have to answer themselves the question of whether there are no people to whom the policy-makers listen more closely? And the answer is that there are: it is the people whom they have to please – the voters. So why not try talking *directly* to people?

3.1 ECONOMIC LITERACY

For a long time there has been an awareness of large systematic discrepancies between the economists' policy opinion and that of laymen. Bryan Caplan in his attempt at empirical description and explanation of this gap shows that

[a]s a rule, the public is more pessimistic than economists, ranking problems' severity higher, the net benefit of change lower, and outlook for progress worse. (Caplan, 2002, p. 439)

Caplan further indicates that the disagreement between the two groups cannot be explained by biases on the part of economists (the self-serving, or ideological bias) as some authors sketchily suggested. What seems to matter most is the economic training – i.e. the knowledge of economics. Caplan's conclusion is of extreme relevance for my current purpose:

Economists have often explained deviations from efficient policy as the product of special interest politics. [My research] empirics suggest an alternate explanation: political failure could simply be a byproduct of the electorate's systematically biased beliefs about economics [...]. (Caplan, 2002, p. 456)

If this is even partly true, then it is something economists may affect.

If voters understood the true effects of many current policies, they are very unlikely to be supportive of them, or even condoning them. Even though there would still be a long way towards actively demanding a better policy, it would surely make it at least much more likely than it is now. At any rate, a policy-maker in democracy interested in gaining or retaining her office would be more motivated to supply it.

The current relative illiteracy among the public as far as economics goes is not to be considered as too surprising. While in many other branches of science it is common to educate the general public through media or schooling

system, economics is conspicuously missing. Educational TV programs on biology, physics, astronomy, geology, zoology, history, philosophy, and others are quite commonplace and often target children as well as adults. As for economics, there is a total silence in most media outlets.¹⁴³ The same holds for schools as well. It is only at the university level when economics is seriously communicated to students while other subjects – many of which much less ‘every-day’ sciences – are introduced to pupils well before high school.

Turning to people is seen as a logical response to the existence of the opinion gap between what people (and politicians) on one hand, and economists, on the other, think. As authors of one of the consensus survey study conclude:

If, as economists, we find our models and/or discipline seriously out-of-step with the political decision-making process, it calls for serious educational efforts or reconsideration of the basic premises of our models. (Fuller et al., 1995, p. 233)

Alice Rivlin, in her AEA presidential address, mentions economic (il)literacy as a serious issue:

Economists should devote more serious attention to increasing the basic economic literacy of the public, the media, and the political community. (Rivlin, 1987. p. 8)

Moreover, this should not be understood as simply a byproduct of economists’ feeling underappreciated. The importance of economic education in schools is acknowledged by non-economists, too, including a prominent Harvard psychologist, Steven Pinker:

[Schools] should provide students with the cognitive skills that are most unlike the cognitive tools they are born with [by emphasizing] economics, evolutionary biology, and probability and statistics [in order to root out biased beliefs, especially those regarding government policy.] [...]

¹⁴³ Milton Friedman’s *Free to Choose* series was a classic exemption to this rule, though its impact outside of the US of the 1980’s was symptomatically negligible.

There are only twenty-four hours in a day and a decision to teach one subject is also a decision not to teach another one. The question is not whether trigonometry is important, but whether it is more important than statistics; not whether an educated person should know the classics, but whether it is more important for an educated person to know the classics than elementary economics. (quoted in Caplan, 2007, p. 198)

It was, incredibly, more than 100 years before then when Simon Newcomb made a remarkable comment on the need for special economic education:

The popular political economy seems to have taken a greater hold on the public mind, in opposition to the views of professional economists, during our time, than it ever did before. [...] Paradoxical though it may seem, it can, we conceive, be shown that the reaction in question is due to the diffusion of popular education. [It] had done nothing to promote the careful analysis, continuous thought, or the study of facts. By these alone, not by mere intelligence, can fallacies be made evident. Thus increased intelligence and knowledge of the world have only served to lay a wider base for crude thinking and fallacious conclusions. In the fact that the masses have been educated to a certain point where a system looks plausible, but not to a point where they can see the fallacy, we have the key to the whole situation, and an indication of the only remedy. (Newcomb, 1893, p. 393)

What we want is better training in the art of thinking. This training cannot be given by the mere teaching of facts. A person can no more be trained into a thinker by lecturing to him than he can into a gymnast. (Newcomb, 1893, p. 396)

It is also desirable that the student be taught not only to think rightly and reach correct conclusions, but to analyze and expose popular fallacies. (Newcomb, 1893, p. 397)

It does not seem much has changed since the time of Simon Newcomb. The job of eradicating “popular political economy” and improving upon the economic literacy still creates plenty of unfilled room for an old but neglected role of an economist: the economist-educator.

3.2 ECONOMIST-EDUCATOR

There is a large role to be taken up by economists who want to change the outlook of the world. Of course, the theories that help us understand the world and formulate appropriate policy are indispensable. However, as long as economists do aspire to leave some mark, they cannot afford to rely just on pure scholars. If talking to people should be tried as a solution for their frustration, some of the economists – and not necessarily the first-class theorists among them – must become first-class educators. Of what use is a grand theory if its implications are not understood and its implied policy demanded from policy-makers?

History witnessed great teachers, popularizers and disseminators of economic knowledge. The early economists to some extent combined their roles of theorists and educators. They successfully reached broad classes of intellectuals of their time. While this must have contributed to economic literacy in population, the masses needed to change the policy were addressed by specialists not aspiring to create grand theories.

Arguably the most successful ones, policy-wise, were Richard Cobden and John Bright, the men who orchestrated a movement that helped to turn free trade theory into policy in Britain in the mid-19th century. We should not forget about Frédéric Bastiat of 19th century France, an author of pamphlets readable to this day. The early economists had other disseminators,¹⁴⁴ although less known (perhaps because all of them were women): Sarah Trimmer, Jane Marcet, and Harriet Martineau. While all of them were writers and

¹⁴⁴ It is interesting to note that not all economists were exactly friendly towards these authors. At the end of the 19th century Marshall made a famous disparaging remark about them, considering their work simplistic and dogmatic:

[General economic principles] became less dictatorial, and more willing to admit of their own limitations. Never again will a Mrs. Trimmer, a Mrs. Marcet, or a Miss Martineau earn a goodly reputation by throwing them into the form of a catechism, or of simple tales, by aid of which any intelligent governess might make clear to the children nestling around her where lies economic truth. (Marshall, 1897, p. 117).

educationalists, Marcet stands out by having written stories for children. The 20th century was relatively, and, perhaps, absolutely too, poorer in terms of such authors. A notable exception is perhaps Henry Hazlitt, Leonard Read and the activities of the Foundation for Economic Education these gentlemen helped to establish. Besides this foundation, operating to this day, the contemporary efforts along these lines include the Foundation for Teaching Economics. The present day authors working in this direction would surely include e.g. Russell D. Roberts with his economic novels (Roberts, 2001a, b), or Ken Schooland with his children's fiction translated into more than 30 languages (Schooland, 2005). Without aspiring to provide a comprehensive list of such authors, we should not forget also about the much more scholarly but very popular work of David Friedman (Friedman, 1996), Steven Landsburg (Landsburg, 1995), or Steven Levitt (Levitt and Dubner, 2005).

It is difficult to gauge exactly the influence of these minds, but it is safe to say that – maybe with the exception of Cobden and Bright¹⁴⁵ – it wasn't very great. But even if it could be shown they had absolutely no share in manipulating the course of policy, it would still not imply that this strategy is useless. Their numbers have been so modest that it would be rather fantastic to assume anything better than modest results.

Besides such popular writers, it is indispensable not to forget about teaching economics on a professional level. Good teachers in economics will impress more students of economics some of whom may become great educators and disseminators at a more popular level. Teaching should

¹⁴⁵ Not all authors share this account of economic history. Probably the best known dissenter is George Stigler:

I believe [contrary to the traditional history] that if Cobden spoke only Yiddish, and with a stammer, and Peel had been a narrow, stupid man, England would have moved toward free trade in grain as its agricultural classes declined and its manufacturing and commercial classes grew. (Stigler, 1982, p. 64)

¹⁴⁶ The need for real-worldliness was recognized as important even for teaching at the graduate level by the Commission on Graduate Economic Education (COGEE) established by AEA (see Krueger et al., 1991).

emphasize the real-world applications and stop creating the impression of abstract theorizing.¹⁴⁶ To that end, teaching economics should not be considered an extra duty of a researcher, for it is a different professional academic activity that calls for specialization. Who else – if not economists – should be appreciative of a division of labor. Research and teaching (to a certain level) have, in fact, not much in common, and the practice of judging and rewarding academic economists by their research activities only causes some of the university faculty to *pretend* research work with the consequence of having less time for, and expertise in, teaching proper.

A long time before the birth of the publish-or-perish culture, Glenn Hoover blamed economists for the backwardness of application of their science:

The fundamental difficulty is that most of the university economists are little interested in the advancement of their science in the sense of working for a more general acceptance of its truths. They have a professional interest in advancing themselves in the science, they prefer research to teaching, they purify, qualify and rarefy definitions and doctrine until they are accused with some justice, of indulging in the sterilities of medieval scholasticism. (Hoover, 1926, p. 60)¹⁴⁷

Thus, the educative mission of economists is as important even at the level of undergraduate economic instruction. As Paul Krugman exhorts:

[O]ur primary mission should be to vaccinate the minds of our undergraduates against the misconceptions that are so

¹⁴⁷ Another consequence of the publish-or-perish ethos is an explosion of output that makes economics – just like other sciences – less intelligible to both outsider and insiders than before. While emphasizing this effect, Stanislaw Andreski comes to the same conclusion about the disproportions of research and teaching activities:

Perhaps [the world-wide mushrooming of production, and a dilution of the quality of the printed matter] is an inevitable result of foisting upon too many people a duty to be 'original'. Perhaps it would be better if they were allowed to *confine themselves to transmitting to the young the ideas of a few great thinkers* of the past, instead of being cast in the role of pioneers for which very few of them have either aptitude or inclination. [...]

It seems that (like love or happiness) originality never comes to those who consciously pursue it. (Andreski, 1972, pp. 222-223, emphasis added)

predominant in what passes for educated discussion about international trade. (Krugman, 1993, p. 23)

In the last decade of the 20th century, the essential things to teach the students are still the insights of Hume and Ricardo. That is, we need to teach them that trade deficits are self-correcting and that the benefits of trade do not depend on a country having an absolute advantage over its rivals. (Krugman, 1993, p. 26)

It is good teachers and disseminators, and in great numbers, that economics needs in order to escape that vicious circle and to become more consequential than it is – a goal many economists share to this day. They must refocus their attention from policy-makers to the general public despite the fact that the former link is a more direct one than the latter. After all, some roundabout methods of production are known to yield better results.

Hoover, in as early as 1926, made a strikingly similar plea:

[W]e do not now see either the men nor the movements which might popularize economic truths in our time, we shall content ourselves with pointing out the direction whence they may come. We must wait for some man of ability of sound judgment, capable of crusading for economic truth with the same fervor that Marx, Brya, Samuel Gompers, Lenin and the American Protective League have displayed in their advancement of economic darkness. It is doubtful if he will come from professional class; they lack the apostolic fervor. We need a Turgot, a Cobden or a Henry George. Why is it that the Truth may not secure the same zealous devotion that Error so frequently inspires? (Hoover, 1926, p. 60, emphasis original)

Admittedly, this is not then an all too novel call on my part. But obviously, it still can bear – and needs – some repetition.

3.3 THE ECONOMICS FACTORY

I have attempted above to conceive of economic science as a market with its supply and demand. Let me now push this analogy on the supply side even further: let me look at it as an *economics factory*, a factory that *produces* and *sells* goods. The reason for this analogy is to emphasize the balance of activities on the supply side.

Every profit-seeking company (outside the perfect competition box) has to engage in both production and selling of its products. One without the other will prove ineffective with respect to the goal of the company. The production and selling departments have to be in certain balance. If the inventories run low and there is nothing to sell, it makes sense to withdraw some resources of the company from the selling department and place them with the production department. If, on the other hand, the inventories are increasing but the sales are lacking, the resources must be shifted in the reverse direction.

Now, our economics factory is not primarily profit-seeking, but rather recognition-seeking: the avowed goal of its employees is to make their products known and used by other people outside the factory. This, nonetheless, changes very little in the previous story about a profit-seeking company. Even here, both departments, and their balance, are crucially important. The production department has to produce ideas so that there is something to sell (distribute, disseminate etc.), while the selling department is indispensable in putting the produced ideas to use, which only is the goal of the factory.

The actual state of affairs in our economics factory, however, resembles the following situation. The amount of ideas that have been produced for the whole history of its operation is impressive, and while our production department is still capable of improvements, the hard fact remains that most of it is still sitting in our factory warehouse. In fact, most of these products – key products, given the factory's goals –

have been sitting there for decades and some even for centuries.¹⁴⁸ Why? Because our selling department was always working sporadically, understaffed and underinvested, as if its members were on a permanent leave. If this has recently changed at all, it has changed to the worse. Few employees are interested in working for the selling department. Everybody desires to be part of production, or more realistically, to be at least viewed as such. From the point of view of the goals of the factory, this is an incredibly wasteful behavior. The expected benefit – in terms of making-the-world-a-better-place – of another idea made in the production department might well be approaching zero. On the other hand, the benefits of selling just a few items from the warehouse might turn out gargantuan. As Gordon Tullock summarized so nicely:

[T]here are two problems: inventing new ideas and getting the government of private citizens to adopt them. I suspect that the latter is the more difficult of these problems because there are so many good ideas for government policy that have been invented a long time in the past and are not now being applied. Indeed, an entrepreneur who would simply succeed in getting the government to carry out a policy recommendation randomly selected from the pages of *The Wealth of Nations* would in all probability deserve extremely high rewards. (quoted in Colander and Coats, 1989, p. 237, emphasis original)

If, as economists themselves would know and say, the marginal product of a unit of resource is greater in the selling department than in the production department, it is worthwhile from the factory's perspective to shift resources from production to selling.

In short, the problem of the factory is not bad or insufficient products, but rather their marketing. This is, after all, echoed by Alan Blinder:

¹⁴⁸ As Herbert Stein supposedly opined, "most of the economics that is usable for advising on public policy is at about the level of the introductory undergraduate course" (quoted in Hamilton, 1992, p. 62).

The lack of knowledge that fosters bad economic policy today is of a different character. The critical problem is not that the limits of economic science are too confining, true as that is. Rather, it is that society makes such poor use of what economists know. (Blinder, 1987, p. 199)

4

EPILOGUE

I started off at the beginning of this text with a reference to George Stigler, and it is perhaps only fitting to return to this author at the end. Besides claiming that the market for economic ideas is efficient and economists matter as much as they should (i.e. that the public is not systematically mistaken), he also believed the time for economists to matter more would only come.

I am convinced that economics is finally at the threshold of its golden age [...]. The revolution in our thinking [due to quantification capabilities] has begun to reach public policy, and soon it will make irresistible demands upon us. [...] It will become impossible for an import-quota system to evade the calculus of gains and cost. It will become an occasion for humorous nostalgia when arguments for private and public performance of a given economic activity are conducted by reference to the phrase, external economies, or by recourse to a theorem on perfect competition [...]. Our expanding theoretical and empirical studies will inevitably and irresistibly enter into the subject of public policy [...]. And then, quite frankly, I hope that we become the ornaments of democratic society whose opinions on economic policy should prevail. (Stigler, 1975, pp. 56-57)

He finished his 1964 AEA Presidential address with these words, and he drew tremendous applause from the audience. One wonders how he would judge his prediction today, were he alive. It seems that, whatever happened to economists' quantification capabilities, economists are still stuck at the threshold. Import quotas continue to evade the calculus of gains and cost, and policy is still justified by claiming the existence of external economies, with the same ease as ever.

Stigler assumed all actors – both the policy-makers and the public – are efficiently informed about the means for their ends, and thought therefore that increased influence of economists requires their greater professional powers. In this respect, and with all due respect, I do not share Stigler’s vision and make no such assumption. It was my thesis in this text that economists’ frustration at the lack of real-world influence is of different origin: I believe they have for centuries been mistargeting their audience. The suggestion I make is that economists should address in a far greater degree the interested laymen and broader public. To this end, economists may indeed stand in need of greater capabilities as Stigler claims, but it will not be the capabilities of theorist, but those of a teacher and disseminator.

For economics to enjoy due respect and heed, it may not only need its Samuelsons, Friedmans or Hayeks, but also its Cobdens, Brights and Bastiats. When economists figure this out, there will be a better chance that they may at last become as important as garbagemen, at least in the eyes of those who consider handling of ideas as momentous as handling of garbage.

APPENDIX

ECONOMIC POLICY SURVEY QUESTIONNAIRE

Instructions

Please, always select just one answer – the one that is closest to your position. In part B you are asked in which direction you would change the current policy in the Czech Republic. All questions are couched as recommendations, and sound therefore necessarily normative. In case of any uncertainty about the values by the policy in question, please assume that the ultimate goal of economic policy is the welfare of the people in the Czech Republic as you understand it.

In some cases, the policy in question is in fact a bundle of several policy instruments or tools and/or an instrument that may differ locally within the Czech Republic. In such cases, please assume you cannot change the *structure* of these instruments, but only their *average level*.

Part A – General View

- 1) Do you think that the economic policy sufficiently reflects insights provided by economic theory and policy recommendations made by economists, i.e. that economic policy does not systematically deviate from them?
 - yes
 - no

Part B – Particular Policy Opinions

- 2) The extent to which trade barriers (tariffs, quotas etc.) are used should be:
 - higher
 - unchanged
 - lower
- 3) The extent of anti-dumping and anti-foreign-subsidies cases that the trade-policy authority brings against foreign producers should be:
 - higher
 - unchanged
 - lower
- 4) The attention paid by policy-makers to the balance of trade deficit should be:
 - higher
 - unchanged
 - lower
- 5) The size of government budget deficit should be:
 - higher
 - unchanged
 - lower
- 6) The size of public expenditures should be:
 - higher
 - unchanged
 - lower
- 7) The marginal income tax rate should be:
 - higher
 - unchanged
 - lower
- 8) The size of the overall tax burden should be:
 - higher
 - unchanged
 - lower

- 9) The rate of money supply growth should be:
- higher
 - unchanged
 - lower
- 10) The inflation target set by the central bank should be:
- higher
 - unchanged
 - lower
- 11) The level of environmental regulation should be:
- higher
 - unchanged
 - lower
- 12) The level of consumer protection should be:
- higher
 - unchanged
 - lower
- 13) The extent to which the Anti-trust authority interferes with the market should be:
- higher
 - unchanged
 - lower
- 14) The level of difficulty with which employees may be laid off should be:
- higher
 - unchanged
 - lower
- 15) The extent of the labor union power granted by the legislation should be:
- higher
 - unchanged
 - lower
- 16) The extent of limits on trade in illicit drugs should be:
- higher
 - unchanged
 - lower

- 17) The extent of limits on trade in human organs should be:
- higher
 - unchanged
 - lower
- 18) The level of the legislated minimum wage should be:
- higher
 - unchanged
 - lower
- 19) The level of the legislated maximum rent landlords can charge to tenants should be:
- higher
 - unchanged
 - lower
- 20) The level of government support of agriculture should be:
- higher
 - unchanged
 - lower
- 21) The share of university education cost covered by university students (as opposed to government) should be:
- higher
 - unchanged
 - lower
- 22) The extent of foreign investment perks offered by government should be:
- higher
 - unchanged
 - lower

Part C – Respondent information

- 23) Age:
- 25 or less
 - between 26 and 35
 - between 36 and 45
 - between 46 and 55
 - between 56 and 65
 - over 65
 - I decline to answer

- 24) Gender:
- male
 - female
 - I decline to answer
- 25) What sort of economist do you conceive yourself of?:
- academic economist
 - business economist (private sector)
 - government economist
 - enthusiast
 - other (please state):
 - I decline to answer
- 26) What is your gross income per year (in CZK):
- under 250000
 - between 250000 and 500000
 - 500000 and 750000
 - over 750000
 - I decline to answer
- 27) Which political party's program is closest to your vision of economic policy?:
- The Czech Social Democratic Party
 - The Christian and Democratic Union – Czechoslovak People's Party
 - The Communist Party of Bohemia and Moravia
 - The Civic Democratic Party
 - The Green Party
 - other (please state):
 - I decline to answer

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INDEX

A

AFL-CIO, 105, 141
Alston, Richard M., 7, 10, 11, 13–17,
19, 20, 81–84, 131, 134
American Economic Association
(AEA), 10, 11, 45, 51, 76, 78, 115,
124
Andreski, Stanislav, 1, 53, 54–56,
73, 80, 81, 119, 131
Arnott, Richard, 83, 84

B

Bagehot, Walter, 63
Baldwin, Robert E., 100
Baster, A. S. J., 66
Bastiat, Frédéric, 117
Bauer, Peter T., 53, 71, 76, 79, 80,
95, 101, 102
Beckerath, Erwin von, 47
Bell, James Washington, 6
Bentham, Jeremy, 62
Bernstein, Michael A., 61, 78, 103,
104
Blinder, Alan, 48, 122, 123
Block, Walter, 7, 9, 14, 16, 17
Blume, Stuart S., 106
Bobe, Bernard, 8
Bright, John, 44, 117, 118
Britt, Ronda, 107, 109
Brittan, Samuel, 6
Brooks, Harvey, 94
Brune, Lester H., 105
Bryan, Michael F., 88, 114
Burke, Edmund, 63

C

Cairncross, Alec, XVI, 26
Cantillon, Richard, 22, 64, 74

Caplan, Bryan, 5, 97, 114, 116
Card, David, 84
Carlyle, Thomas, 113
Cato, Marcus Portius (the Censor),
46
Cicero, Marcus Tullius, 46
Clark, John Bates, 77
Coase, Ronald H., 100
Coats, Alfred, XVI, 51, 102, 103,
122
Cobden, Richard, 44, 117, 118, 120,
125
Collins, Robert M., 105
Council of Economic Advisers
(CEA), 104
Covey, Ted, 24
Cullis, John G., 97, 99, 100

D

DiLorenzo, Thomas, 7
Douglas, Jack D., 92
Dubner, Stephen J., 118

E

Ebeling, Richard, XI
Eichenberger, Reiner, XVI, 59, 109
Ely, Richard T., 76
Etchegoyen, Alain, 8

F

Farley, James A., 104
Federal Reserve System (FED), 108
Fetter, Frank Whinston, 47, 51, 97
Fisher, Irving, 77
Foundation for Economic
Education (FEE), 118
Foundation for Teaching
Economics (FTE), 118

Frey, Bruno, XVI, 7–9, 14, 16, 17, 43,
52, 53, 59, 109
Friedman, David, 55, 118
Friedman, Milton, 10, 23, 115
Fuchs, Victor R., 7
Fuller, Dan A., 7, 11, 14, 15, 17, 19,
20, 24, 32, 82, 83, 115

G

Galbraith, John Kenneth, 104
Gay, Edwin, 78
Geach, Stephanie, 10, 14, 16, 17, 19
Geide-Stevenson, Doris, 7, 11, 14,
15, 17, 19, 20, 32, 82, 83
George, Henry, 120
Gompers, Samuel, 120
Graham, Frank D., 66, 68, 69
Gresham, Thomas, 51

H

Hallam, Arne, 7
Hamilton, Lee H., 122
Harberger, Arnold C., 47, 48
Hawley, Ellis, 104
Hawley, Willis C., 44
Hawtrey, Ralph, 51
Hayek, Friedrich A., 44, 45, 63, 64
Hazlitt, Henry, 118
Hegel, Georg Wilhelm Friedrich, 80
Hicks, John R., 70
Higgs, Robert, XI
High, Jack, 7
Hobbes, Thomas, 56
Hoover, Glenn E., 44, 55, 119, 120
Hoover, Herbert, 44, 104
Hülsmann, Jörg Guido, XI
Hume, David, 22, 80, 120
Husserl, Edmund, 80
Hutchison, Terence W., 67–71
Hutt, William H., XVI, 45, 66, 67,
94, 95

J

Jewkes, John, 50
Johnson, Harry G., 57, 99, 100, 104,
113, 114
Jones, Philip R., 101, 102, 103, 105
Jones, R. W., 105

K

Kealey, Terence, 109
Kearl, James R., 6–10, 13–17, 32, 81
Kelman, Steven, 5
Keynes, John Maynard, 45, 51, 78,
88, 97
Keyserling, Leon, 105
Kirchgässner, Gebhard, XVI
Klamer, Arjo, XVI, 2, 52, 84
Klein, Daniel B., XI, 42, 58, 71, 72,
109
Knight, Frank H., 45, 46
Krueger, Alan B., 84
Krueger, Anne O., 86, 87, 98, 100,
118
Krugman, Paul, 48, 119, 120

L

Landsburg, Steven, 124
Lang, Nancy A., 11
Lansing John B., 10
Leet, Don R., 11
Lenin, Vladimir Ilyich 127
Levitt, Steven D., 124
Lipka, David, XI

M

Machovec, Frank, 88, 89
Malthus, Thomas R., 62, 64
Marcet, Jane, 117, 118
Marshall, Alfred, 117
Martineau, Harriet, 117
Marx, Karl 120
Mayer, Thomas, 67, 69, 71
McCloskey, Deirdre, 66, 68, 72
Meeks, Ronald L., 107
Merton, Robert C., XVI
Merton, Robert K., XVI, 47
Middleton, Roger, 50, 51, 103
Mill, James, 62
Mill, John Stuart, 62
Mishan, Ezra, 100, 138
Mitchell, Wesley C., 78
Muller, Jerry, 62

N

National Bureau of Economic
Research, 78

- National Science Foundation (NSF), 106, 107
Nelson, Robert, XVI, 49, 70, 76, 78, 79
Newcomb, Simon, 77, 116
Nordhaus, William D., 10
Nourse, Edwin, 104, 105
- P**
Pareto, Vilfredo, 85
Peden, George, 51
Pigou, Arthur C., 61, 100
Pinker, Steven, 115
Polanyi, Michael, XVI
Pommerehne, Werner 8, 105, 106
Pope, Rulon, 7
- R**
Read, Leonard, 118
Reekie, Duncan, 10, 14, 16, 17, 19
Ricardo, David, 62, 64, 120
Ricketts, Martin, 7, 9, 10, 13, 14, 16, 17, 19
Rivlin, Alice, 115
Rizzo, Mario, XI, 71
Robbins, Lionel C., XIII, 2, 3
Roberts, Marc, 112
Roberts, Russell D., 118
Romero, Pedro, 71, 72
Roosevelt, Franklin Delano, 104
Rudolph II (Roman Emperor), 106
Russell, Bertrand, 80
Rustici, Thomas, 7
- S**
Salerno, Joseph, 63
Samuelson, Paul A., 10, 70, 79
Say, Jean Baptiste, 62, 64
Schneider, Friedrich, 8
Schooland, Ken, 118
Schooler, Dean Jr., 105
- Shoemith, Edward, 7, 9, 10, 13, 14, 16, 17, 19
Šíma, Josef, XI
Smith, Adam, 1, 22, 62, 64, 74, 96
Smithies, Arthur, 2
Smoot, Reed O., 44
South African Economics Society, 10
Šťastný, Dan, VIII, IX, 28
Stein, Herbert, 122
Stern, Charlotta, 42
Stigler, George J., XIII, 2, 23, 52, 64, 75, 118, 124, 125
Sumner, William Graham, 77
- T**
Tolley, Howard, 104
Torrens, Robert, 102
Trimmer, Sarah, 117
Truman, Harry S., 105
Tullock, Gordon, XIV, XVI, 3, 51, 54, 56, 60, 75, 122
Turgot, Anne Jacques Robert, 74, 96, 120
- V**
Vaughan, Michael, 7
Viner, Jacob, 50
Volný, Michael, XI
- W**
Walker, Michael, 7, 9, 14, 16, 17
Walras, Léon, 76, 85
Wehrle, Edmund F., 105
Whaples, Robert, 7, 25
White, Lawrence H., 104, 108, 109
Wood, Robert, 78
Wyploz, Charles, XVI, 48, 53
- X**
Xenophon of Athens, 1