Is Economic Failure an Economics Failure?

By Angus Deaton

PRINCETON – As 2023 begins, it is clear that an ever-growing number of people hold democratic capitalism in disrepute, and economists along with it. But how much responsibility – and what kind – do economists bear for our economies' ills?

In 2010, an influential Oscar-winning documentary portrayed us as scoundrels concerned only with our own financial gain, and as lobbyists and apologists for the rich, who reward us generously for our work. Our pronouncements are often predictable from our politics. Whenever several hundred economists signs a petition in support of some policy, it is only a matter of days before several hundred other economists sign a petition condemning it.

Moreover, we economists often assume a mantle of policy expertise for which we have no qualification, with predictably disastrous outcomes. Even so, thoughtful critics contend that we still retain great influence over economic policy, and thus continue to cause great harm. But does the fault lie with just a few powerful individuals, or is there a deep flaw in economics that continuously leads its practitioners astray?

I tend to favor the latter hypothesis. American democratic capitalism is serving only a minority of the population well. The 2008 financial crisis and its grim aftermath gave the lie to the fable that everyone would benefit from letting financiers get richer. In the intervening years, less-educated Americans have been succumbing to deaths of despair and turning to populism in reaction to a political system that is not helping them.

Not only did most economists fail to predict the crisis; by some accounts, they facilitated it. After all, they are proud apostles for the globalization and technological change that have enriched a narrow financial and managerial elite, redistributed income and wealth from labor to capital, destroyed millions of jobs, and hollowed out communities and their residents' lives. Worse, when confronted with deaths of despair, some economists blame the victims and those who try to help them.

Advise and Consent

According to my friend and colleague Alan S. Blinder, who has held several different roles in government and public policymaking, politicians rarely do what economists suggest. Instead, they use economic analysis in the way that a drunk uses a lamppost: for support, not illumination. The problem is not that all economists are paid hacks who adopt positions to please their masters – though there are plenty of those. It is that that even good work can be selectively misused.

Similarly, Jason Furman, who served as chief of President Barack Obama's Council of Economic Advisers, rejects the idea that economists have too much sway, arguing that he "could only dream of having the power" that is attributed to his profession. And other administration economists have claimed that, at best, they play only a negative role of stopping bad things from happening. Politicians must respect budgets, but they often live in fantasy worlds where their pet schemes pay for themselves. Economists in the CEA or the Congressional Budget Office play a valuable role in bringing some realism to the policymaking process.

I believe that Blinder and Furman are correct, but not always. When Lawrence H. Summers was US Secretary of the Treasury in President Bill Clinton's administration, from 1999 to 2001, he used his enormous intellect, knowledge, and persuasiveness to weaken restrictions on the international flow of speculative funds, as well as on derivatives and other more exotic financial instruments. It is worth remembering that other economists, including Blinder and Joseph E. Stiglitz, fiercely opposed those decisions. Many have since argued that those Clinton-era changes contributed to both the 1997-98 Asian financial crisis and the global financial crisis a decade later.

Earlier, when Robert Rubin was Treasury Secretary, Summers was his deputy, and the libertarian business economist Alan Greenspan was chairman of the Federal Reserve, *Time Magazine* featured the three men on its cover as the "Committee to Save the World," teasing an article about how they had "prevented global economic meltdown – so far." That cover was the product of a time when most economists felt more admiration than antipathy. To a greater or lesser extent, we bought into the notion that modern economics had given us the tools to sweep away the growth-restricting regulations of the past, many of which were based on prejudice and myth, not science. I suppose a mea culpa is now in order.

It is important to recognize that this earlier episode was exceptional. Janet Yellen, another immensely distinguished economist who now serves as Treasury Secretary, does not have same influence or power. As Ezra Klein of the *New York Times* observes, she "holds real weight in internal discussions, and so do some others, but economists are one of many voices at the table, not the dominant voices." President Joe Biden does not listen to economists in the way that Clinton or Obama did. Beyond that, Yellen and Summers are themselves exceptional cases. Academic economists do not usually get to be Treasury Secretary.

The Power of Scribblers

John Maynard Keynes, who spent much of his life advising policymakers, and not without effect, had a different view of the power of economists: "The ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed the world is ruled by little else." Note his inclusion of the word "wrong"; it is not just good ideas that survive and prosper.

For example, Jeb Hensarling, a Texas Republican who chaired the House Financial Services Committee from 2013 to 2019, says he became a politician to "further the cause of the free market," because "free market economics provided the maximum good to the maximum number." Hensarling's view is an example of what James Kwak of the University of Connecticut School of Law calls "economism," the idea that the world operates exactly as described in introductory economics textbooks. Clearly, those textbooks matter. In the US, some 40% of college students – including most future politicians, lawyers, and CEOs – take at least one economics course.

There is folly on the left, too. If the right cannot see the flaws in markets, the left can be equally blind to the flaws in government that prevent it from acting reliably to fix the flaws in markets. Government, it is imagined, is a representative body, elected by fully informed citizens, whose job is to correct the flaws in markets, whether it is the tendency to monopoly, exploitation of workers, or excesses of income inequality. In practice, however, the US government is not at all like this, and like other governments, often makes things worse, and can be beholden, not to all of its citizens, but to the beneficiaries of the system.

In my own view, a central problem of modern mainstream economics is its limited scope. The field has become unmoored from its proper basis, which is the study of human welfare. As Amartya Sen contends, the discipline took a wrong turn with the British economist Lionel Robbins's famous and now-dominant definition of economics as the allocation of scarce resources among competing ends. That was a terrible narrowing of scope compared with what the American philosopher Hilary Putnam called the "reasoned and humane evaluation of the social well-being that Adam Smith saw as essential to the task of the economist."

Sen contrasts Robbins's definition with that of the late nineteenth and early twentieth-century economist Arthur Pigou, who wrote: "It is not wonder, but rather the social enthusiasm which revolts from the sordidness of mean streets and the joylessness of withered lives, that is the beginning of economic science." Economics should be about understanding and doing away with the factors behind the sordidness and joylessness that come with poverty and deprivation. Once again, Keynes's *General Theory* has a good summary. "The political problem of mankind," he avers, is "how to combine three things: economic efficiency, social justice and individual liberty."

We appear to have abandoned the last two of Keynes's trio. We need to overcome our fixation on money alone as a measure of human well-being. We need a better acquaintance with the way that sociologists think. And above all, we need to spend more time with philosophers, recapturing the intellectual territory that used to be central to economics.