

Why Do We Need Pluralism in Economics?

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What is
economics?

What can – and
can't – it explain
about the world?

Why does it
matter?

Ha-Joon Chang teaches economics at Cambridge University, and writes a column for the *Guardian*. The *Observer* called his book *23 Things They Don't Tell You About Capitalism*, which was a no.1 bestseller, 'a witty and timely debunking of some of the biggest myths surrounding the global economy.' He won the Wassily Leontief Prize for advancing the frontiers of economic thought for his book *Kicking Away the Ladder*. He is a vocal critic of the failures of our current economic system.



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HA-JOON CHANG ECONOMICS: THE USER'S GUIDE



A PELICAN
INTRODUCTION

Economics: The User's Guide Ha-Joon Chang

Many Different Schools of Economics

- At least nine major schools of economics
 - **Classical** (Smith, Ricardo, Malthus, Say)
 - **Neoclassical** (Jevons, Walras, Marshall)
 - Marxist (Marx, Engels, Lenin, Bernstein)
 - Keynesian (Keynes, Kalecki, Robinson, Kahn, Kaldor)
 - Schumpeterian (Schumpeter, Freeman, Nelson, Winter)
 - **Austrian** (Menger, von Hayek, von Mises)
 - Institutionalism (Old [Veblen, Commons, Mitchell] and New [Coase, North, Williamson])
 - Behaviouralist (Simon, March & Cyert, Tversky & Kahnemann)
 - Developmentalist (Hamilton, List, Kuznets, Hirschman)
- Several smaller schools
 - Neo-Ricardian, Latin American Structuralist, Evolutionary, Feminist, Ecological

Comparing Different Schools of Economics (Reference: “*Economics: a User’s Guide: a Pelican Introduction*” by Ha-Joon Chang, 2014)

	Classical	Neoclassical	Marxist	Developmentalist	Austrian	Schumpeterian	Keynesian	Institutionalist	Behaviouralist
The economy is made up of...	classes	individuals	classes	no strong view, but more focused on classes	individuals	no particular view	classes	individuals and institutions	individuals, organizations and institutions
Individuals are...	selfish and rational (but rationality defined in class terms)	selfish and rational	selfish and rational, except for workers fighting for socialism	no strong view	selfish but layered (rational only because of an unquestioning acceptance of tradition)	no strong view, but emphasis on non-rational entrepreneurship	not very rational (driven by habits and animal spirits); ambiguous on selfishness	layered (instinct – habit – belief – reason)	only boundedly rational and layered
The world is...	certain (“iron laws”)	certain with calculable risk	certain (“laws of motion”)	uncertain, but no strong view	complex and uncertain	no strong view but complex	uncertain	complex and uncertain	complex and uncertain
The most important domain of economics is...	production	exchange and consumption	production	production	exchange	production	ambiguous, with a minority paying attention to production	no strong view, but puts more emphasis on production than do the Neoclassicals	no strong view, but some bias towards production
Economies change through...	capital accumulation (investment)	individual choices	class struggle, capital accumulation and technological progress	developments in productive capabilities	individual choices, but rooted in tradition	technological innovation	ambiguous, depends on the economist	interaction between individuals and institutions	no strong view
Policy recommendations	free market	free market or interventionism, depending on the economist’s view on market failures and government failures	socialist revolution and central planning	temporary government protection and intervention	free market	ambiguous – capitalism is doomed to atrophy anyway	active fiscal policy, income redistribution towards the poor	ambiguous, depends on the economist	no strong view, but can be quite accepting of government intervention

Debates in economics cannot be settled like the ones in natural sciences I

- A. Human beings have free will, ethical values, and even imagination, which makes it impossible to understand and predict their behaviours in the way in which you can with particles and chemical substances.

Debates in economics cannot be settled like the ones in natural sciences II

- B. We cannot conduct experiments in economics in the way we can in physics or chemistry.
 - The human costs and ethical problems involved in large-scale economic experiments are unacceptably high – the Soviet central planning, the IMF-World Bank Structural Adjustment Programme in the 1980s and the 1990s, the Big Bang reforms in the former Soviet bloc countries in the 1990s financial deregulation and trickle-down economic policies in the rich countries since the 1980s.
 - There are smaller-scale experiments that have lower (but not ‘no’) such costs (like running of ‘games’ in ‘laboratory’ conditions or RCTs [Randomised Controlled Trials]), but they cannot be generalised in the way experiments in natural sciences can be.
 - Also, ethical problems (economists ‘playing God’)

Debates in economics cannot be settled like the ones in natural sciences III

- C. The practice of economics is intricately linked with money and power, so a particular economic theory, or even a whole school, can become dominant for reasons other than its intellectual merits.
 - A theory that favours the powerful and the moneyed may establish dominance due to greater political supports and greater research funding, even if it is *not* superior to other theories (e.g., trickle-down economics, the efficient market hypothesis, public choice theory).
 - In other words, an economic school's dominance does not necessarily imply that its theory is intellectually superior.

Seeing the economy differently I

- **Macroeconomics Theories and Macroeconomic Policy**
- When you study Keynesian economics, you get to take the role of finance in macroeconomics seriously.
- If you also add Behaviouralist theories to your theoretical arsenal and further refine your understanding of the financial sector, you will see macroeconomics very differently from the Neoclassical perspective.

Seeing the economy differently II

- **Theories of Competition and Anti-trust policy**
- The Schumpeterian, the Marxist, and the Austrian schools see competition as a ‘process’, rather than as a ‘state’, as the Neoclassical school does.
- Especially, the Marxists and the Schumpeterians emphasise the productivity-enhancing power of oligopolistic competition through technological innovation.
- If you are informed by these views on competition, you would see the limitations of the Neoclassical theory of competition in designing anti-trust policies .

Seeing the economy differently III

- **Theories of human motivations and the policies intended to change human behaviour**
- The Behaviouralist and the Old (but not New)
Institutionalist schools emphasise how institutions are not just constraints on human behaviour but also shape human motivations ('constitutive role of institutions').
 - This suggests that institutional reforms, which then change people's motivations, may be far more effective than fiddling with incentives under given institutions in changing economic agents' behaviour – at least in the long run.
 - If you learn Marxism, which emphasises how institutions are shaped by material conditions, you can see that sometimes the most effective way of changing people's behaviour is to change their material conditions through economic growth and redistribution, rather than psychological manipulation ('nudge') or even institutional reform.

Seeing the economy differently IV

- **Theories of economic development and development (and foreign aid) policy**
- The Developmentalist and the Schumpeterian schools emphasise the importance of changing productive capabilities, many of which are developed at the level of productive enterprises.
- So, if you knew these schools, you will design your national development policy or your foreign aid programme (if you are a donor country) in such a way that you give priority to the development of productive enterprises over promotion of investments in ‘human capital’ at the individual level.

Seeing different things about the economy I

- **Work and Human Welfare**
- Unlike other schools, the Marxist school has emphasised the oppressive nature of work under capitalism and the importance of work in self-realisation of individuals.
- Once you learn these aspects, you will realise that the nature of work (e.g., how interesting it is, how oppressive the monitoring is) and the control the workers have over their work processes, and not just wages and working hours, as the Neoclassical school would have it, matter in improving human welfare.

Seeing different things about the economy II

- **Production vs. Exchange and Consumption**
- Once you learn the Classical, the Marxist, the Developmentalist, and the Schumpeterian schools, you begin to realise the critical role of production in economic life, and not just consumption and exchange, as in the Neoclassical school.

Seeing different things about the economy III

- **Transparency vs. Bounded Rationality**
- When you learn the Behaviouralist school, you realise the limitations of the Neoclassical view that increasing transparency is a solution to problems in all sorts of areas, ranging from financial regulation to the imposition of ethical standards for consumption goods.
- However, the Behaviouralist school's concept of 'bounded rationality' makes you realise that very often the problem is not the lack of information or asymmetric information, as the Neoclassical school thinks, but the limited human capabilities to process information.

Seeing different things about the economy IV

- **Transparency vs. Bounded Rationality (continued)**
- The solution, then, should be sought in simplifying the system, by restricting or even banning certain activities (e.g., creation of overly complex financial products, use of unethical practices in production), rather than increasing transparency.