

Economic Theory and Public Policy: Do Economists Actually Matter?

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I should like to begin with a very famous quotation from Lord Keynes:

“...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. Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually the slaves of some defunct economist. Madmen in authority, who hear voices in the air, are distilling their frenzy from some academic scribbler of a few years back. I am sure that the power of vested interests is vastly exaggerated compared with the gradual encroachment of ideas.”

My purpose here today is to examine whether Keynes' faith in the power of economists to shape policy has any significant empirical support. But before I get to the specifics of history on that point, it might be profitable for us to divide economists into categories, an endeavor that has often been carried out, usually by economists themselves because—as a variation of a well-known joke would put it—there are two groups of economists: those who divide economists into two groups and those who don't. For my purposes in this speech, I am—quite obviously—in the former group.

To begin, I want to look at an essential tension in the field, a sort of paradox, and I will label my categorical antagonists on the opposite sides of this paradox “Friedmans” and “Stiglers,” after two Nobel-winning Chicago school colleagues who nonetheless represent significant philosophic, positional differences on this issue, especially during Stigler's late years.

“Friedmans” wholeheartedly agree with Keynes' position, at least as enunciated in the quote I just read. They believe that power lies with elite intellectuals who persuade people to take particular actions—even when those actions need to be explained and even “sold”—to those very people by those same elites, and even when those actions make people worse off generally.

“Stiglers” deny that people are duped into supporting public policies that economists find “inefficient” and counter-productive. Stiglers want to apply the assumed rationality of individual people to the *political sphere* just as they apply it in economic theory. Policy, for “Stiglers,” *is rational* no matter the apparent facts. Voters *do understand* just what they are voting for, and are getting what they

desire regardless of the criticisms offered by the “Friedmans” of the world who are ceaselessly working to convince people to change their minds. Stiglers would agree with Oliver Wendell Holmes’ observation on the true purpose of the Supreme Court: “If my fellow Americans wish to go to hell, my job is to see to it that they get there as quickly as possible.”

This is, of course, an old and ongoing discussion in our field, and others, and it is unlikely that I—or anyone else—can settle once and for all this lengthy debate. I am myself conflicted because, while I intellectually find myself in great sympathy with the Stiglers, I nonetheless believe that the “Friedmans” are mostly right.

Only a person who agrees with the Friedmans’ position could love the old H.L. Mencken aphorism that “if (x) is the average level of stupidity of a population, and (y) the number of voters, then democracy is the theory that (x) times (y) is less than (x).”

This quite obviously leads to a belief that proper education will somehow change things. As the social rationalist Ludwig Von Mises believed, once people were shown by economists that their policies did not produce the results they hoped for, they would change their minds and repeal useless and counterproductive economic regulation. This worldview allows one to observe the real world, and yet remain optimistic. Of course, the definition of an optimist is “one who believes that this is the best of all possible worlds.” We should always remember, however, that *pessimists* are in whole-hearted agreement!

If the contention of the Friedmans is true, then the task becomes explaining *how* they can be right *given their own assumptions* about human nature and the rationality of acting individuals. And this is where economic and policy *history*—rather than the history of economic *theory*—is of great importance, and can be a useful tool for our inquiry.

What I need to show, if I am to be very convincing about the correctness of the “Friedmans” position, is that economists *do* in fact control—however indirectly, and with whatever time lags, as Keynes noted—ultimate public policy debate, and *ipso facto*, the laws and regulations that flow from those debates.

I need to show that economists—and other policy elites—are the small tail that wags the polity dog. I have to refute the oft-heard lament by economists that “no one listens to our brilliant theories and analyses;” on the contrary, my own view is that we economists have influence out-of-proportion with the actual value of our theories and policy recommendations....that our influence, in fact, *exceeds* our collective wisdom.

That’s probably not a good way to begin with an audience of teachers of economics, but nonetheless, that’s what I intend to try and demonstrate during this presentation: that we *have had*, and still *do have* tremendous influence, and

that—just maybe—we ought *not* to have quite so much. Having said that, I beg for your forgiveness, knowing full well that I shall receive precious little from my colleagues!

It is impossible to state when the first economic theory was thought, or spoken; we *can* trace concerns about efficient resource use back to the ancient Greeks, specifically to the writings of Xenophon in his major work—the *Oeconomicus*—for which our discipline is named.

And certainly Aristotle’s ideas concerning the proper configuration of households, as well as their relationship to wealth and wealth-getting, qualifies as early—and influential—economic theorizing even though the greatest influence was to come centuries later when the Greeks were rediscovered by medieval scholastic writers such as Albertus Magnus, Gerald Odonis, Jean Buridan, and Thomas Aquinas. The intellectual disputes over exactly what these writers were recommending for society have been argued for some time, and are far from settled today. Some historians of thought—such as Mark Blaug and Robert Ekelund and Robert Hebert—have little respect for their efforts. The old saying that the scholastics spent their days arguing about "how many angels could sit on the point of a pin" is a simple, dismissive way of dealing with their ideas, most of which were Greek in origin. It didn’t help any that they named their conception of long-run costs of production the “just price,” thus hopelessly infusing ethical considerations—at least, according to their *critics*—into their economic analyses.

Other historians of thought, e.g., Joseph Schumpeter and Murray Rothbard, allow that the scholastics made sensible arguments, at least no less sensible than Adam Smith’s when it came to Ircop, though Smith was smart enough not to call this concept a “just” price. Schumpeter is especially generous in his treatment of the scholastics, and it is a continuing theme throughout his masterpiece “history of economic analysis.”

Any person who has ever claimed to have been “ripped off,” has accepted—even *if only implicitly*—the idea of a just price, and economists have not been immune from suggesting that actual market prices are somehow often illegitimate. In fact, without such a notion, antitrust laws make absolutely no sense, let alone MC and AC pricing rules for public utilities. (I am assuming, of course, that they *do make sense* if we accept the notion, itself still a highly debatable proposition.)

For example, the most recent edition of the micro text I am using treats the price outcomes in monopolistically competitive markets as somehow “wrong” and “wasteful,” a contention that generations of students have been taught. It is clear that modern economists are more than capable of the same sort of “just price” reasoning that the scholastics practiced, though of course they claim a scientific basis—rather than an ethical one—for their own beliefs.

What is *not arguable* is that the scholastics had a large impact on policy. The first organized school of economic thought—physiocracy—was in fact nothing but a rehash of their doctrines, and yet the writings of Francois Quesnay and others in that French school certainly influenced British political economy through writers such as Adam Smith who fails, in his *Wealth of Nations*, to cite anyone as being his theoretic predecessor *other than* the physiocrats. This is good in that Richard Cantillon was, like Smith and well before him, a thoroughgoing newtonian on the economy, and the physiocrats—like the scholastics who influenced them—were huge admirers and advocates for the idea of *natural law*, a position that Smith adopted as well. Natural law is, of course, nothing more than the idea that the universe is rationally constructed and behaves according to relationships that are *invariant*, both in the natural—and *social*—realms. In other words, things do not occur by accident, but have a “design” that includes both human—and physical—nature. As Francis Bacon observed, “Nature, to be commanded, must first be obeyed.” This idea is powerful and even so-called post-moderns embrace it, whether knowingly or not. Modern environmentalism, for example, is based on this intellectual foundation, even though its adherents do not seem to understand this simple fact.

Smith, who supported natural law doctrine, was hugely influential in his own time, as he remains in ours. The golden age of British political economy was about real-world policies to an extent that the profession has probably not approached since. This real-world policy appraisal attitude of economic practitioners was summed up well by the very influential teacher and writer Edwin Cannan when he wrote: “...When people ask us whether such and such a change will be good or bad, they will find us tiresome if we pretend that we know nothing of good and bad ends in economic matters and can only talk about the cheapness or dearness of different ways of attaining a given end. They will say: "you know perfectly well that what we want from you is to be told whether this proposed change will make us and our children better off..." benefactors endow chairs of economics, audiences listen to economic lectures, purchasers buy economic books, because they think that understanding economics will make people better off. Is it really necessary for us to destroy this demand for economic teaching by alleging that we do not know what the phrase "better-off" means?"

Given this attitude in British economics, it is not surprising that economists have had a long, profound influence on English public policy, sometimes for good and sometimes, unfortunately, for ill. It was, after all, the view of the classical school that the world was an orderly place, set in motion by God's hand, and that human reason could be applied to social problems in the same way that it could be profitably employed in the natural sciences—as a problem-solving device. And so it has been used—as in natural science—both for good and ill.

The debate over whether ideas move policy or policy leads to rationalizations of it—so prevalent in the work of our friends Friedman and Stigler—has no finer example than British policy in the nineteenth century—the so-called Victorian era,

ending with the death not of Queen Victoria in 1901, but with the end of King Edward's reign in 1910, and the coming storm of WWI.

Did Adam Smith's ideas, refined by successors such as Ricardo and Mill, create British *laissez-faire* doctrine, or did Smith simply record the world as he saw it and, in Stigler's view—simply tell people what he thought they wanted to hear? Did Smith defeat mercantile doctrine, or was it already well on its way out before he wrote about it? Friedmans would argue that it was the former, while Stiglers would, of course, credit—in a peculiarly Marxist way—events, technologies etc, driven by forces mostly *outside* of human control—with creating a *laissez-faire* cocoon of accommodating public policies. I cannot definitively answer this question this morning, but I will try and offer some examples that would seem to buttress Friedman's case.

Even though Smith's arguments for free trade had been made decades before—and Locke and Hume's well before Smith—it was not until 1846 that the Corn Laws were repealed in England. And that repeal had more to do with the political efforts of Cobden and Bright's anti-Corn Law League than with Smith, especially in light of Smith's exemption he afforded to the food supply when it came to whatever preaching he did about implementing *laissez-faire*.

Today, people still look back at the anti-Corn Law League as an organizational-tactical model upon which to base current antiprotectionist initiatives. But in fact only one prominent classical political economist of that earlier era—Ricardo—made their repeal a central aspect of his writings. The general appeal of abolition had as much to do with resentment against the land-owning class than it did with theory, although it would be wrong to underemphasize Ricardo's efforts in getting these laws repealed, and Britain on her way to almost perfect free trade policy. He made a difference—he *was* influential—and his efforts undoubtedly led to a policy change that may well *not* have occurred anyway.

The repeal of the Corn Laws was but one manifestation of the power of political economy to shape policy in Victorian England. Jeremy Bentham's "utilitarianism" was all the rage, and public servants found numerous ways to try and implement policies consistent with its principles.

The most influential economists in England during the second half of the 19th century were Nassau Senior, John Stuart Mill, and Bentham's last secretary—Sir Edwin Chadwick. Mill and Chadwick especially applied Benthamite views to British policy, and Mill was also a member of parliament. Senior was a longtime consultant to the government, occupying a prestigious chair in political economy at Oxford for many years. Against the historical backdrop that represents Britain's closest adherence to *laissez-faire*, political economists appeared to drive policy decisions.

What made their success possible were fiscal restrictions placed on the English government by the gold standard, and by chancellor of the exchequer William Gladstone, both of which had the effect—if not the specific intention—of denying to the government sufficient resources with which it might meddle—in any systematic way—in the English economy.

Of course, resources or not, all governments are going to regulate and, during this era, England passed a series of far-reaching laws that abrogated *laissez-faire*, among them the factory acts, the previously mentioned Corn Laws, the poor laws and various welfare policies, including even a small amount of income redistribution.

Nassau Senior's analysis of the factory acts was a major precursor to what we today call "public choice" theory. He showed clearly, and with a "lack of compassion" and a "cold-heartedness" that we economists today can only envy from afar—that the factory acts were primarily about protection for older, male, higher-paid labor at the expense of children and female workers. So successful were the initial regulations that such relatively cheaper labor was reduced over 50% in just the three years between 1835 and 1838. So successful were the older males in restricting the supply of such labor that they successfully lobbied for—and achieved—an amended, strengthened act in 1844 that placed even more restrictions on potential female competitors.

At the time, these regulations were seen mostly as obvious "reforms." In retrospect, we can see clearly—thanks mainly to Nassau Senior's report on these acts—that behind every so-called reform lie powerful economic interests, and that every piece of public policy—regardless of the avowed *intentions* of its supporters—benefits some at the expense of others.

This was true of the Poor Laws as well. Mill especially decried the tendency of welfare to discourage work among the poor, citing the need to design assistance so as not to penalize low-wage workers, nor make it attractive for them to forego work in order to receive welfare. This concern manifested it-self—in reality—in the form of workhouses, all of which were run under the act, and all of which were decried, of course, by reform-minded intellectuals and like-minded members of the general public. But Mill remained unmoved, an advocate in his own day of what today we call "welfare reform."

Such was Mill's general reputation that, later in his life when he modified his view as to whether the *wages fund doctrine* was accurate, his change of opinion shook politics in England for some time, and his later views undoubtedly hastened England's transformation from a quasi-*laissez-faire* economy into an explicitly socialist one.

Another very influential political economist, and follower of both Bentham and Mill, was Sir Edwin Chadwick. Chadwick was a thoroughgoing utilitarian and his

policy ideas reflected that orientation. Chadwick rejected Adam Smith's idea about a *natural harmony* between private and public interests and decided that what the government needed to do was create an *artificial harmony* between those two interests. Avoiding the trap of having to measure interpersonal utility in order to effect a utilitarian solution, he fell into a different sort of trap, and decided that anything that enhanced economic "efficiency" was, *ipso facto*, in the public's interest. This should sound familiar to anyone who has read a good deal of output by University of Chicago economists and for good reason; as a welfare criterion, it is not different from what Chicago—especially its law and economics wing—has generally advocated.

For example, faced with a high mortality rate during the transportation of prisoners from Britain to Australia, Chadwick's solution was pure common sense and a dramatic example of the power of incentives: pay per head *on delivery* rather than on embarkation, a simple change that cut prisoner mortality by 98%.

Always the dedicated empirical researcher and compiler of statistical reports, Chadwick learned from many prisoner interviews that high probability of capture outweighed severe retribution in the minds of most criminals; in other words, they acted rationally on expected benefits and costs. Policing was changed to reflect this reality. The police were better paid to reduce their incentive to become corrupt, and Chadwick also implemented judicial reforms to increase the probability of being found guilty once indicted, a calculation almost every professional criminal knows with remarkable accuracy.

Chadwick applied opportunity cost considerations to water consumption, and was the first to advocate home delivery as a way of minimizing the total cost of acquisition. This had the happy side benefit of improving sanitation and, hence, the public's health as well.

Anticipating public goods arguments, he explicitly laid out a conception that we have come to call the idea of "natural monopoly." as a thoroughgoing centralist, he wanted to create as many public monopolies as possible. He anticipated—and even explicitly outlined—the idea of *franchising public services*, a practice followed today in many American cities, which is based on a sophisticated understanding of search and information costs that Chadwick learned from gathering market data about—of all things—funeral homes!

It is clear that the movement toward alleged "natural monopoly" public utilities in late 19th century America was one that had digested Chadwick's many arguments, including even the proposed nationalization of rail lines, which in fact came to pass during WWI. The original ICC Act explicitly accepts Chadwick's contention that railroads are, in fact, natural monopolies. The federal government later abandoned this idea.

One man, armed with a version of classical economic doctrine, filled with so many ideas—ideas that led to policies that had such a large impact on his nation—and, indirectly, on *our own*—and yet how many Americans have ever heard of him?

Of course, Chadwick was not the first nor the last English economist to dramatically affect policy. No discussion relating to this topic can fail to address the so-called Keynesian revolution. But again, the nagging question returns: did Keynes change policy, or did Keynes merely *rationalize* policy that was already in place and quite likely to continue?

In 1936, seven years into the great depression, *the general theory of employment, interest and money* appeared. It is a difficult read, and that's why most people—including most economists—don't bother. Yet it became an instant classic, well before its theory and policy implications could possibly have been verified—or *falsified*—by experience. Did Keynes revolutionize economic theory? Or was his work, in the words of Leland Yeager, a "*digression*?" Did governments read the book and decide to meddle in their economies, or were they already meddling and Keynes provided them with intellectual justifications and, hence, with political cover? Again, this is not an argument that is likely ever to be settled definitively. But what cannot be denied is that post-WWII policy-makers used what they thought were Keynesian models and concepts when they carried out macro economic policy.

The general domination of Keynesian theory—or what passed for it—on macro policy from the end of WWII through the 1960s is also pretty clearly a fact. So it's not surprising that the *anti-Keynesian* revolution was lurking just off the Keynesians' radar screens until it found the most appropriate moment to bloom—the 1970s when the H.M.S. Keynes hit an iceberg called "stagflation," never to be the same again, even after limping back to port. The heyday of alternative macro ideas had arrived.

Foremost among them was, of course, "monetarism," propelled into the public's sleepy consciousness by the irrepressible Milton Friedman—and his students and supporters. Derided as cranks by the Keynesians during the '50s and '60s, suddenly there was an explanation for what ailed the economy in the late '70s that clearly traced its intellectual lineage back to Locke and Hume, rather than to Cambridge U.K.

When Paul Volcker and the Fed decided to implement money supply targeting in late 1979, they were following the monetarist playbook, and the results were as economic theory predicts in such situations: depression—sorry, that word is just *too* depressing; I meant to say *recession*—and price disinflation. Few clearer instances of the link between theory and policy can be found than during the period 1979–83.

But as is so often true in life, at the moment of its seeming greatest triumph, monetarism was already waning as the macro theory *du jour*. And to add insult to injury, the fed quickly returned to its Phillips-curve-based policy making just as soon as the inflationary dragon had been returned to its cage. Other central banks followed suit, which must please antimonetarists such as Nicholas Kaldor who wrote at the height of Thatcherite power in Britain—and no doubt with great Keynesian frustration—a book gently titled, *The Scourge of Monetarism*.

Looking back at the macro texts of the 1980s, the two competing paradigms were Keynes' and Friedman's. But today's texts have a much wider variety of potential non-Keynesian possibilities, including real business cycle theory, raterex, several varieties of "post-Keynesianism," monetarism, supply-side, and even neoaustrianism. To say that macro is "in flux" is, of course, to express the obvious. But as all policy requires justification, and some policies are just plain terrible, there will doubtless be no shortage of "new" macro ideas in the future.

I think the Keynesian and monetarist episodes clearly demonstrate that the Friedman's are onto something when they argue that individual economists can change not just policy—but the world itself—through the power of their ideas. The twentieth century powerfully supports this contention as it can be viewed as a monumental struggle between the ideas and insights of—with apologies to the multiculturalists who dominate academe these days—two old, dead, white, male political economists: Adam Smith and Karl Marx.

Of course, it might not have seemed that way, but even recasting the protagonists as, say Keynes and Hayek—as was done in the book *The commanding heights*,—obscures, but does *not change*, the fundamental nature of the idea conflict that is personified by Smith and Marx: are you for the market's "invisible hand," or Marx's—and Keynes'—and yes, even Chadwicks'—*central authority*, a.k.a. "the state"?

Because really, there is but one central, all-important policy issue: *individual freedom or state control?*

So many momentous theoretical debates turn on this issue; so many economists devote themselves to furthering one or the other approach even as they tell others—and sometimes even themselves—that they are completely disinterested "scientists." but of course, we know that is not the case most of the time. There are liberal economists, and conservative economists, and libertarian economists, and socialist economists. And it is far from a *coincidence* that their research findings almost always confirm their *a priori* political beliefs. Of course, it's not a coincidence at all, but inevitable, self-chosen design.

When economists' politics remain the same across their entire professional lives, and they claim that reality is best modeled in conformity with their politics, then it is surely the *politics* that is the driving centerpiece of their beliefs, and not any

research evidence or random empirical finding. Remember that Keynesianism swept the profession long before the empirical results were in. So on what grounds other than politics did one become a Keynesian in, say, 1938?

There are so many names that I have not the time to discuss in detail this morning, but whose writings profoundly influenced their own times, and even ours....theorists such as Hume, Ricardo, Malthus, Walras, Wickseil, Clark, Veblen, Kuznets, Knight, Sraffa, Fischer, Coase....the list truly is long and varied, and seems to me to confirm the Friedmans' position that some theory changes reality at least as much as reality drives theory. Indeed, Milton Friedman's own life is testimony to the truth of the relationship between ideas and policy.

So after all of this exposition, I suppose I ought—unambiguously—to provide an answer to the question my title raises: do economists matter?

I hope that I will not be guilty of self-promotion of my chosen profession if I answer in a strong affirmative voice. Economists not only matter, but I would argue that they sometimes matter *too much*...they are listened to as carefully when they are wrong as when they are right, and that can be a bad thing.

For every success story, there is also a bad policy that was enacted with the enthusiastic backing of at least some influential economists. In my personal view, the most destructive economist—at least to date—is Marx. The price paid for his writings has been so vast and so terrible that it defies simple categorization. And from whom did Marx learn his economics? Primarily, from Smith and Ricardo, whose systems had built into them—unfortunately—a crude version of the labor theory of value. The rest, as they say, is history.

Or consider Malthus' *Essay on Population*, which was wrong when he wrote it and is still wrong today—*The Club of Rome* notwithstanding—but which has driven—and *continues to drive*—irrational population and environmental policy decisions.

Or the naive faith in Keynesian macro "fine tuning," which drove policy down a one-way street into chronic inflation followed, inevitably, by stagflation. Certainly, it is legitimate to argue about what Keynes really meant—and that has been a cottage industry ever since *the general theory's* 1936 publication. But what cannot be denied is Keynes' own belief that he had discovered the way to maintain *permanent prosperity with full employment*. It was his *followers* who invented such things as counter-cyclical policy; for Keynes, the "Big Rock Candy Mountain" had arrived and cycles were to be a thing of the past!

(Here, I cannot resist giving you the following advice. Whenever famous economists start saying—and they will again at some point—that "the business cycle is now dead,"—then sell, my friends—and sell *quickly!*)

The credulous and, in retrospect absolutely silly, pronouncements of economists are easily documented. John Law's creative financing of the French government that led to the South Sea bubble; the disastrous attempt by Britain to return to the gold standard at the wrong parity after WWI; Irving Fischer's prediction of a long boom two weeks before the 1929 crash; John Kenneth Galbraith's early-1950 pronouncement that removing price controls in West Germany would destroy their economy—just as the "German miracle" began to unfold precisely *because the controls had been abandoned*; Paul Samuelson's remarkable opinion that the Soviet economy was booming, written just a few months before the Berlin wall fell and with it, the entire *Potemkin village* that was the Soviet system.... I suppose, to be entirely fair, that I ought to add a *mea culpa* for the Fed, since it pursued a particularly perverse policy during the late 1920s and early 1930s, a sort of real bills doctrine, thereby deepening the severity of the Great Depression.

I could go on, and I am not mentioning these examples as if they are the sole examples of silly predictions, or the advocacy of incorrect policies. That's something that—to paraphrase Will Rogers—every economist does, only on different subjects. Economists, no less than others, often fall into holes while admiring the stars.

So—yes, economists matter—a great deal, both when they are right and when they are wrong—and just as Keynes suggested—because they are taken seriously, and the level of understanding of their theories is no bar to their being taken seriously. It really doesn't matter how complex the advice is as long as it can be sold to voters and politicians in some simple way. An example is Arthur Laffer's reworking of the fiscal implications of tax revenue collections as a function of incentives rather than tax rates. Nothing new in it, really, and Laffer's contention is hard to grasp at first sight, but nonetheless it became the foundation of a successful presidential campaign and the generator of one of the largest tax cuts in American history.

The reason probably is that, during hard economic times when the numbers are bad—or conversely, in great times when *very* good—voters are more likely to embrace alternatives than when things are more normal. All the talk of social security privatization seems to have abated dramatically these days even though a well-designed privatization plan is probably a very good, long-term idea. Politically, however, this is not the time that such a change can be accomplished. Social security itself, recall, is a plan from the depths of depression. It could never have been implemented in 1928. But by 1935, it was politically unstoppable.

And that leads me to my final point: during times of economic difficulty, economists and voters are more likely to support what we have come to call a "paradigm change." Some economic historians—notably Mark Blaug—deny that the history of economics can be accurately modeled by paradigm changes, but the history of macro seems—at least *to me*—to conform fairly well with Thomas

Kuhn's ideas about paradigm change as he expressed them in *the structure of scientific revolutions*. Periods of "anomaly"—when the prevailing theories seem no longer to explain or predict well—are the times when we get new ideas, or the resurrection and "improvement" of old ideas. Or, as one writer's cute title put it: "New Ideas from Dead Economists."

For examples of anomaly and change, look at the industrial revolution and the way in which it changed markets. Free trade was suddenly the "in" thing, and mercantilism was intellectually destroyed. (don't tell that to the always-ubiquitous, anti-trade protesters, of course. They still think it's 1650 and the workers' guilds require strengthening!)

Obvious problems with the labor theory of value led, in the late 1870s, to the modifications in classical economics that we now call neoclassicism, which were based on subjective value theory and the so-called marginal revolution. The great depression caused the casting aside of classical ideas—such as say's law—and paved the way for Keynes. Stagflation had the same effect on the Keynesian revolution, and led to monetarism, supply-side, real business cycle theory, and rateg. The next anomaly might be happening right now—and that's the point—it's hard to see paradigm change coming. But something *will* come along—it always does.

Each era requires, because of empirical changes, different theoretical explanations—and justifications. Ours is no different in this regard. (the question of whether things *really* change or not I will pass over, but a reading of Fredrick Lewis Allen's wonderful study of the 1920s—*only yesterday*—suggests that, as the Greek philosopher Parmenides argued so very long ago—they don't).

Which is why, during the 1990s, we heard a lot of talk about the "new economy," with its slogans such as "distance doesn't matter," "profits are irrelevant," "p/e ratios are useless," "debt is just a four letter word," and so many other mantras that seem, as they always do in retrospect, to have been either wrong, or pushed a bit too hard. Time will, as usual, give us a final answer. By then, of course, different economists will be advocating a host of new ideas—or dusted off, souped-up old ideas—and the entire cycle will repeat once again.

So where does that leave you if you want to evaluate the advice that economists are never bashful about tendering? Here are my personal views on that:

- 1) Tanstaaf!
- 2) If it sounds too good to be true, it isn't true, which leads to the inevitable, sad corollary—"a fool and his money are soon parted";
- 3) Prediction is always best when looking backwards; always ask those making predictions if they have money riding on the truth of their forecasts. Generally, they don't—and for very good reason!

- 4) If an idea is called "revolutionary," it was probably first suggested by someone like Plato;
- 5) Free markets are not and have never been a utopian solution for all human problems—but then—what major problem has government ever solved, with or without the input of economists?

Thank you for your kind attention.