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So, If an Economist Falls in the Forest . . .

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By Carlos Lozada
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KEYNES

The Return of the Master

By Robert Skidelsky

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It's the quote that launched a thousand pats on the back.

"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," wrote John Maynard Keynes in 1936. "Practical men, who believe themselves to be quite exempt from intellectual influences, are usually the slaves of some defunct economist."

Economists *love* that line. They can't get enough of it. Sneak into any gathering of dismal scientists, and soon enough some smug professor will parrot the British economist's elegant, self-congratulatory words. Its appeal is bipartisan: Liberal scold and Nobel Prize winner Paul Krugman is [fond](#) of it, and even former Federal Reserve chairman Alan Greenspan trotted it out in a [2005 memorial lecture](#) in Scotland honoring free-market luminary and "Wealth of Nations" author Adam Smith.

It must feel nice to be an economist, so convinced that your ideas run the world. Only problem is, when that world implodes, it's kind of your fault. So, as President Obama [warns](#) that Wall Street hasn't learned its lesson, and as the world's leaders [scrum in Pittsburgh](#) this week to find a way out of the financial crisis, economists everywhere are despairing over how their latest theories on markets and finance led us all astray. And now, more than 60 years after his death -- and three decades since the apparent demise of his notion that government intervention could avert slumps -- Keynes is back to bail them out.

Thanks to the Great Recession, we're no longer talking about "rational expectations" or the "efficient markets hypothesis." Instead, it's all about stimulus packages, federal spending and G-20 summits.

In other words, it's all about Keynes.

[Robert Skidelsky](#), an economic historian at Warwick University and author of a three-volume biography of Keynes, chronicles this intellectual resurrection in his new book "Keynes: Return of the Master." Clearly, Skidelsky admires his subject -- "universal curiosity" . . . "formidably intelligent" . . . "the most intuitive of economists" are a few of his descriptions -- but his new book is less about Keynes the man than about the battle of ideas that Keynes and his followers fought and lost during the 20th century. It is also, implicitly, about an issue at the heart of all this soul-searching: How much influence do economists really exert over the real world? Do they drive the policies and preferences of our leaders, or are economists just a bunch of math nerds telling politicians what they want to hear?

In short, do economists matter?

Before Keynes, Skidelsky writes, the dominant vision of the economy was like "a world of independent atomic particles (human beings) whose actions and reactions keep it in a state of balance or equilibrium." Rational self-interest and free competition would bring economies into balance, promoting growth and employment, as long as those pesky governments left well enough alone. It sounded great -- right up until the Great Depression.

An investor, civil servant, lecturer, prolific writer, member of the Bloomsbury Group, husband to a Russian ballerina and leader of the British delegation to the Bretton Woods conference, Keynes was scarcely an economist at all, Skidelsky muses. Rather, he was "a heretic who learned how to play the game" and "set himself the task of rewriting a large chunk of the Western intellectual tradition." The crash of '29 and the Depression that followed were the crucial events that "changed his economic philosophy and sharpened his moral critique of capitalism," Skidelsky writes.

In hindsight, Keynes's revolutionary insights seem pretty straightforward: First, free-market economies do not inevitably lead to growth and full employment. If demand for goods and services drops off, balance is restored not by changing prices but by declining production, i.e., by recessions. Governments should step in, he said, using tax and spending policies to stimulate demand and avoid the downturns.

Second, markets are not self-correcting, Keynes argued, but face constant uncertainty. The distinction between absolute "uncertainty" and manageable "risk" is critical to understanding today's mess, Skidelsky writes, with Wall Street's seemingly sophisticated risk management systems failing miserably to assess the real dangers.

Keynes died in 1946, but for about three decades after World War II, his theories reigned supreme, with governments embracing their role as economic managers. But this embrace, Skidelsky cautions, occurred less out of conviction than expediency. Business leaders accepted Keynesianism as a barrier to socialist agitation; conservatives as an argument for tax cuts; and liberals as a rationale for more public spending. It worked for them, whether or not they really believed it.

The model seemed to peter out in the 1970s, however, when inflation and unemployment came together and Keynesian tools couldn't save us. As the Thatcher and Reagan revolutions took over the political world, free-market models once again took over economics. [Milton Friedman](#) (Skidelsky calls him the "gnome of Chicago") became the prophet of the new era, and Keynes was cast aside by many in his profession and in the public -- until today.

Greedy bankers and bungling regulators have become the scapegoats of today's turmoil, but Skidelsky disagrees. "Intellectual failure seems more important than venality or incompetence," he writes. "The 'light-touch regulation' philosophy of the Reagan-Thatcher years stemmed from the notion that markets could regulate themselves." Essentially, ideas matter -- and adherence to them matters even more.

But how much? Intellectual influence is trickier to measure than, say, gross domestic product. Friedman and his University of Chicago colleague, the late George Stigler, debated the issue in the 1970s and 1980s. In an essay titled "Do Economists Matter?" Stigler argued that economists would give in to market incentives and produce the theories and messages that politicians and interest groups prefer. Friedman countered that economists do wield power through their ideas. "My own self interest leads me to believe that on the whole economists have exercised a good influence," he wrote in *Economic Inquiry*, even speculating that if economists' push for free trade had helped the world by reducing global tariffs by 10 percent, that benefit alone would pay the salaries for the entire profession many times over.

In a recent [essay](#) in the New York Times Magazine -- titled "How Did Economists Get It So Wrong?" --

Krugman argues that economists were seduced by their mathematical models depicting capitalism as a perfect system. But he also offered a Stigler-like perspective, suggesting that his profession's "renewed romance" with free markets was "partly a response to shifting political winds, partly a response to financial incentives." Skidelsky also asks whether economic ideas are "society's building blocks or weapons in the struggle for power." He sides with the former view, more on faith than on evidence.

Keynes offers a compromise, a few lines after that most-favored quote. Economic ideas trump political interests, Keynes continued, but only after "a certain interval; for in the field of economic and political philosophy there are not many who are influenced by new theories after they are twenty-five or thirty years of age, so that the ideas which civil servants and politicians and even agitators apply to current events are not likely to be the newest." Basically, if you're an economist with a big idea, you probably won't win over the politicians of your day. Just wait until you're defunct.

In the meantime, the world will just have to make do. Fortunately, it usually does. Greenspan acknowledged as much during his Scotland speech on Adam Smith. "Perhaps if the 'Wealth of Nations' had never been written," he observed, "the Industrial Revolution would still have proceeded into the nineteenth century at an impressive pace."

What a relief.

lozadac@washpost.com

Carlos Lozada is deputy editor of Outlook.

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