

Neoclassicism watch

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9 September 2004

I've spent a lot of time complaining about neoclassicists, as have many others—Mirowski comes to mind, but a huge amount of non-economist social scientists talk about this; a very active anti-Chicago-school club of political scientists called Perestroika also stand out. But despite the alarmists, I think the purist neoclassical worldview is on the wane, and the hardcore neoclassicist is becoming a rare breed.

Academia [Some readers may want to skip to the policy section, below.] My impression of the last decade or so of economic theory is that it has been concerned with going beyond the standard 'everybody perfectly maximizes a self-interested utility function' framework. There are a few reasons for this, the first being that the framework is obviously too narrow. The pro from overnarrowness is that you can explain a lot of behavior using a few simple rules, which is generally a scientifically good thing and worth pursuing as far as it'll go. The cons are that from a few axioms you only get a few results before you have to start trying too hard. After so many decades of pushing a handful of axioms, even the most driven and devout are basically running out of things to explain, and the explanations are becoming increasingly tenuous.

Where to from here? The prevailing method is not to throw out the whole framework, but to expand things. People are still maximizing a utility function, but the utility function may be allowed to have other elements. E.g., I am a fan of including an axiomatic desire to emulate others. That plus the standard framework leads to more (and more plausible) results. Others, notably the Kahneman and Tversky school, are revising the 'perfectly maximizing' part to take into account that people commit systematic errors in perception and reasoning. From my perspective, these wide-path approaches are the prevailing standard in economics, and will be for a long time. There are other approaches as well, where people have rules of behavior that don't use the word 'maximize' at all, but I think they remain on the fringes (which is not to imply that they are less valid or should remain on the fringes).

There are still defenders. In my own limited experience, I think that people starting off life as an economist are very likely to be attracted to narrow-path neoclassicism, and in an ontogeny-recapitulates-phylogeny sort of way, they go through the process of finding out that the narrow path has basically found all it has to find, and that it has valid critiques. And, as below, politics influence methods.

So to summarize this section: the narrow-path Chicago school has become a straw man that few if any academics fully believe in. I acknowledge that I myself am very guilty of beating this straw man at times, and narrow-path fans do certainly still exist,

but the energy of the non-economist social scientist could probably be better spent just ignoring the narrow-path people and working on making the wide path work for everybody.

Policy I met an IMF economist last night. To overgeneralize the overgeneralizations made in the past, IMF economists are famous for being obnoxiously narrow-path; this is in contrast to World Bank economists who are a bunch of hippies, most of whom have little faith in the narrow path, while others are off the path entirely. Ms PM of Washington, Columbia, has been an economist at the IMF for about a year now, but being young and hip and two degrees of social separation from me, she was not inclined to be a cold-hearted conservative. So I asked her about these critiques of the IMF.

Her first response was that it's the politicians. The Treasury and even the U.S. Congress have a say on what the IMF publishes, and can veto research. She bitterly cited examples of political censorship. The narrow-path Chicago school is as pro-business as a methodology can get, meaning that political influence (invariably by conservatives) filters out anything that isn't narrow-path. I have hung out with many more WB people, and have never heard them mention political censorship of WB research.

Her next argument was that the neoclassical methodology is the only one that's relevant to the currency-type issues that the IMF studies, so all the wide-path stuff is just off track. I think this isn't wholly true, but it is true that the macro literature is behind the curve on widening the path, meaning that the bulk of established literature is indeed hardcore neoclassical. On top of this, the IMF senior staff is another decade or two behind the curve, because that's when they stopped learning new tricks (that'll be us someday). This is also consistent with another of Ms PM's explanations: that those who are interested in other methods (which are evidently still cutting-edge) tend to leave the IMF for academia. Maybe fifteen years from now, their wide-path research will become IMF orthodoxy.

The other prevalent complaint about the IMF is that they are maximizing currency stability where they could be maximizing education, class or gender equality, or any of a number of touchy-feely things that we humans care about. P was more-or-less unapologetic about this: although economists come to the IMF because they care about the developing world and truly want to help, it's the IMF's mandate that they focus on money issues and leave development issues to the World Bank.

But this is a truly problematic stance because IMF policy clearly, obviously affects development. Most directly (and P has the literature to prove this), if the IMF cuts off a country, then nobody will lend to them ever, regardless of the reasons for the IMF's decision. When the WB tries to fund a project to build a sewer system in a few villages in that country, it won't be able to get backing. As a result, the IMF pretty much never truly excommunicates a country.

More indirectly, every IMF loan comes with conditions. All loans of any sort do, of course: it would take me all day to list the conditions on my mortgage. P gives the example that a loan to Ethiopia a few years back with the condition that the money be used to pay the wages of workers who were on the verge of revolt. The IMF started the funding, saw that it was all being stolen by kleptocratic governors, and cut off the

loans. What are ya gonna do.

Other conditionalities are a bigger deal, notably about size of government. This harks to the competing macroeconomic schools: the Keynesian school says that government spending can expand growth, while the narrow-path Chicago school says that big government is always bad. The Chicago school won at the IMF on this point, and cuts in government are often demanded, without regard to the development and distributional impact of these cuts.

It is my opinion that the conditionalities can and should be development oriented. Why not demand that a country take steps to put more girls in schools before loaning them cash? Is this really more interventionist than a demand that a country cut government bureaucracy before lending cash? I'd like to write a whole lot more on this, but you get the picture: the IMF is an interventionist institution which places conditionalities on its loans, and those conditionalities need to be written in concert with the people who care about development, even if the narrow path dictates that accommodating these other issues may hinder the IMF's core goals. But you knew that.

All of these are probably factors in the overall story of why the WB is filled with wide-path hippies and yet there are no recycling bins in the IMF public spaces. There are probably other ineffable issues: Bob Lucas is said to have said: "Once you start thinking about growth it is difficult to think about anything else"; the WB's economists think about growth all day long nonstop, and that's just not the job of the IMF's economists. That plus political pressure can create a different mindset where the narrow-path isn't unattractive.

Generalizing beyond the IMF, the narrow path is convenient for a certain set of conservative beliefs (as I've discussed endlessly in this essay), and so the narrow path will always have a place in propping up the conservative side. I'd like to say that there's a trickle-out effect where as academic research becomes more wide-path, the discourse in the rest of the world will gradually take on the same direction, but this is probably too optimistic. So long as conservatives still walk the Earth, the narrow path will never die in public discourse and the policymaking community.