

How to promote alternative macroeconomic ideas: Are there limits to running with the (mainstream) pack?

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Programme

1. Defining “running with the pack”
2. What can “running with the pack” do for you?
3. Problems with incorporating alternative ideas into the mainstream: One example
4. “Running with the pack” and the philosophy of science
5. Alternatives to “running with the pack”
6. Conclusions

WHAT IS „RUNNING WITH THE PACK“?

What does „running with the pack“ mean here?

Definition:

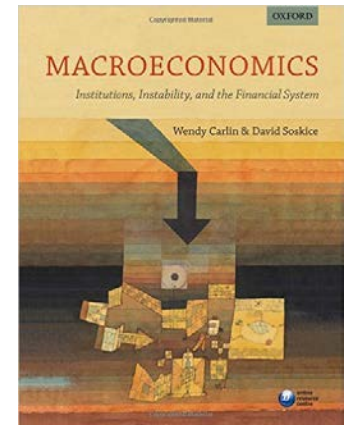
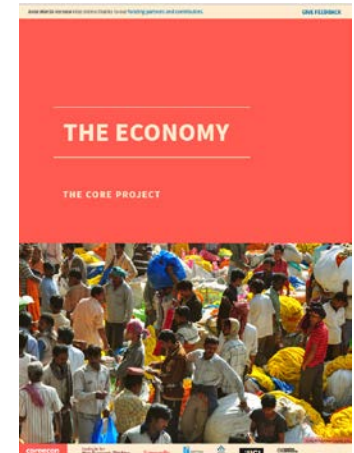
Using of mainstream macroeconomic models (or significant elements thereof) without explicit critical distance to promote economic policy ideas usually found in alternative economic approaches.

Examples for running with the pack: Research

- On Austerity
 - Rannenberg/Schoder/Stráský (2015)
 - Show in a DSGE model that multipliers for fiscal consolidation are much bigger than previously thought when taking into account financial accelerator and liquidity-constrained households
- On inequality
 - Grüning/Theobald/van Treeck (2015)
 - Use a DSGE model to show that growing inequality can lead to growing external imbalances
- On endogenous money vs. loanable funds
 - Jakab/Kumhof (2015)
 - Use a DSGE model to show that if banks create money through lending, financial shocks become much more important

Examples for running with the pack: Teaching

- CORE project (2016)
 - Fails to mention different paradigms
 - Explains Keynesian model starting from household maximising utility by adjusting consumption to changes in interest rates
- Carlin/Soskice (2014)
 - Present 3-equation traditional Keynesian model claiming this to be „mainstream modern monetary framework“, using a quote by Woodford



Question:
Is this a good strategy?

REMINDER: PURPOSE OF ACADEMIC ECONOMICS

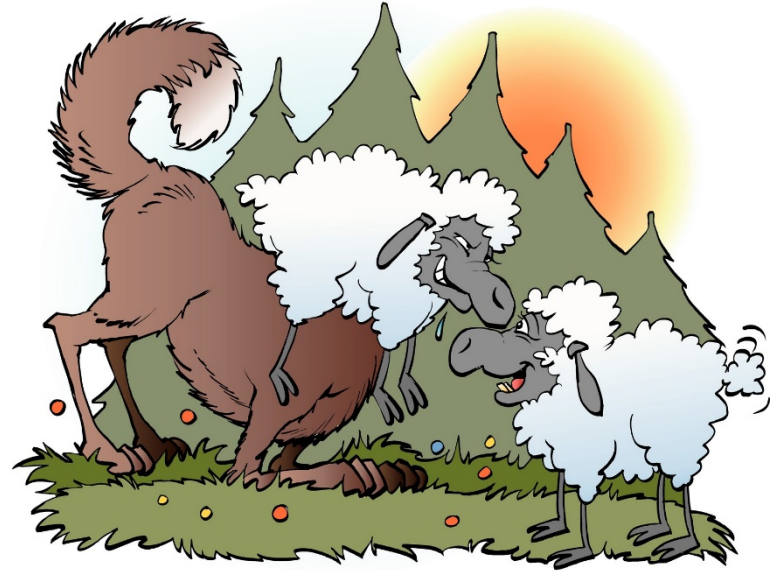
Why does one do academic macroeconomics?

- Spread economic policy ideas
 - Among other academics
 - Among policy makers
- Pedagogy: explain economic mechanisms to students
- Improve policy evaluations and economic forecasts
- Enhance academic career

Why would you be „running with the pack“?

There might be some merits:

- Your ideas might be easier accepted
- You may gain reputation among mainstream economists
- You might get into a position to better spread your ideas



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EXAMPLE FOR POTENTIAL PROBLEMS: AUSTERITY

The effect of cuts in government expenditure and deficits

Original DSGE models

- Reduced government demand leads to lower real wages
- Households see lifetime income increase (Ricardian equivalence)
- Results in detail:
 - Households consume more goods and more leisure time
 - Household offer less labour
 - Households *increase* current consumption
 - Output contracts, but by less than government cuts
- **Overall result: small multipliers, as private consumption makes up for less government demand**





New DSGE models

- Part of households cannot save nor borrow („rule-of-thumb-consumers“)
- When governments cut expenditure, these households offer less labour, but also consume less
- If share of these households is sufficiently large, total private consumption falls with cuts in government expenditure
- **Result: Larger multipliers**

What is now the problem?

1. If you use this model for teaching, you have to explain the students questionable mechanisms
 - Output contracts in the model because real wages have fallen (nominal wages are depressed by less demand) and household adjust labour supply
2. You might get questionable policy conclusions
 - If you combine austerity policy with easy credit to households (reducing „rule-of-thumb-consumers“), austerity becomes less toxic
3. Your models are most likely not able to make decent predictions
 - Remember Lucas (1977) critique: Do not base macroeconomic predictions on questionable microfoundations (Hurtado 2014)

What can „running with the pack“ do?

Reasons to do academic macroeconomics	Can „running with the pack“ help?
Spread economic policy ideas	
Among other academics	
Among policy makers	Possibly indirectly
Enhance academic career	
Pedagogy: explain economic mechanisms to students	
Improve policy evaluations and economic forecasts	

„RUNNING WITH THE PACK“ AND THE PHILOSOPHY OF SCIENCES

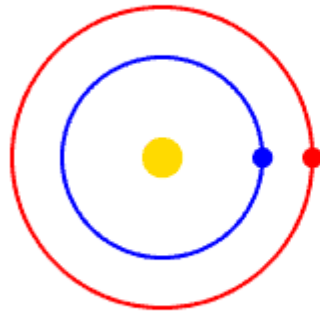
Kuhn's (1962) structure of scientific revolution

- Idea: Science uses **paradigms**
- **Paradigms** are social constructs
- In normal times, scientists try to improve paradigm by small additions and changes („**normal science**“)
- When paradigm runs into large problems explaining empirical observations, „paradigm shift“ might lead to new paradigm („**scientific revolution**“)
- Example: Shift from Ptolemaic world view in Copernican revolution

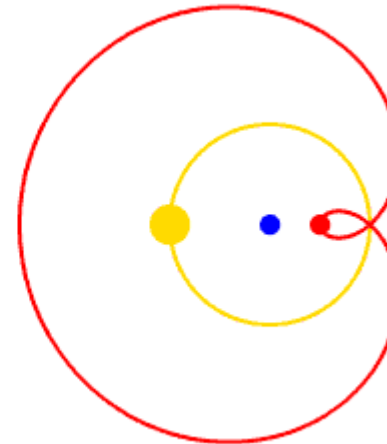
Sun, Earth and Mars in different paradigms

Copernican view

Sun
Earth
Mars



Ptolemaic view



By user:cleonis in the english wikipedia -
http://en.wikipedia.org/wiki/File:Apparent_retrograde_motion.gif, CC BY-SA 2.5, <https://commons.wikimedia.org/w/index.php?curid=17249599>

Question: When is it time for a revolution, when for normal science?

- Time for revolution: Shift from Ptolemaic to Copernican view
- But: Not all empirical failures call for revolution
 - In the 19th century, position of Venus and Uranus was strongly at odds with predictions by Newton's theory of gravity
 - Scientists did not disregard Newton's theory, but looked for other factors which could explain oddity
 - Discovery of Neptune

Is today a time for a revolution or evolution of mainstream macroeconomics?

- In favour of a revolution:
 - Krugman (2016)
 - Paul Romer (2016)
 - Brad DeLong (2016)
 - Solow (2010)

**„Running with the pack“
implicitly supports this
position here!**

- In favour of an evolution:
 - Blanchard (2016)
 - Wren-Lewis (2016)

So who are you when you are running with the pack?



Or



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ALTERNATIVES TO „RUNNING WITH THE PACK“

What are alternative strategies?

- Build alternative models
- Work with up-to-date empirical methods
- Present good empirical studies underlying non-mainstream results – and publish them in mainstream journals
- Confront mainstream with empirical failures
- Highlight paradigmatic differences in teaching
- Communicate your (hopefully superior) empirical results to policy makers

Conclusions

- „Running with the pack“ has some merits
 - Academic success
 - Transmission of economic policy ideas into the mainstream
- Yet, it comes with risks
 - It blurs the differences between paradigms
 - It forces you to work with questionable foundations
 - It makes one vulnerable to criticism of questionable intellectual honesty

**THANK YOU VERY MUCH FOR YOUR
ATTENTION**