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## **REVIEWS**

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### **Defunct Macroeconomists**

*Alfred J. Malabre, Jr, Lost Prophets: An Insider's History of the Modern Economists, Harvard Business School Press, Boston, 1993*

*Reviewed by John Foster*

**A**lfred Malabre, Jr is an eminent journalist who is well known for his insightful commentaries on US economic policy in his capacity as economics editor of *The Wall Street Journal*. In *Lost Prophets*, he examines the reasons why several schools of macroeconomic thought gained and lost influence in the formulation of American economic policy after World War II. However, this is no dry account of the history of modern economic thought. Rather, it is a compendium of personal recollections and opinions, which focuses upon those economists who were most closely involved in policy formulation. Malabre displays an excellent memory for people, places, dates and economic statistics, which are spread liberally throughout the text. Written in lively journalistic style, the book constitutes an entertaining read for economists and non-economists alike.

Malabre interlaces his commentaries with his own evaluations of postwar American policies. Early on he provides a scathing critique of the Bretton Woods agreement in 1946, which gave the Western world a system of fixed exchange rates. So it does not take long to discover that the author has an aversion to government intervention, at least of the Keynesian variety. Yet he correctly points out that Keynes's brand of economics had little influence on economic policy in the immediate post-war years.

Unfortunately, he does not stress the residual power of American institutionalist thinking in this period, following its high point in the era of the New Deal. This is a serious omission that raises questions about the author's depth of understanding of this subject. In this regard, Malabre seems to work backwards and forwards from the monetarist vs Keynesian characterisations of macroeconomics, popular in the late 1960s and 1970s. He appears to have little understanding of the quite different characterisations, whether before, during and immediately after World War II, or in the 1990s. For example, to understand fully Milton Friedman's economics it is essential to appreciate the influence of Wesley Mitchell, the famous American Institutional, both directly and indirectly through the teaching of Arthur Burns. As well, the 'Chicago Tradition' of that period was a branch of American institutionalism, far removed from the monetarism of the 1960s. Malabre focuses, correctly, upon Kenneth Galbraith as an influential Keynesian, but, once again, his presentation is flawed because he overlooks the fact that Galbraith was an institutionalist, applying Veblenian insights.

Malabre provides a fascinating history of the economic advisory process of the 1960s, when Keynesianism came into its own. But the presentation is marred by simplistic statements about budget deficits and by an overwillingness to attribute the economic policy mistakes of that time to economic advice rather than to over-riding political considerations. He commits the common mistake of equating President Johnson's Great Society programs with Roosevelt's New Deal, despite the entirely different circumstances surrounding the introduction of each. Nor does he make clear the fundamental problem with economics at the time, namely, a shift from pragmatic, real-world institutional economics to an abstract theoretical macroeconomics. The rise to prominence of Paul Samuelson, which Malabre traces, was indicative of this unfortunate transition: he proved himself to be an abstract economic theorist *par excellence* and, simultaneously, a warm-hearted but naive 'Keynesian' in matters of economic policy. It was a simple matter, in later years, for politicians, and journalists such as Malabre, to lay the blame for the politically induced economic ills of the 1960s and early 1970s at the door of such economists. In contrast, the earlier generation of American institutionalist economists, such as Allyn Young, Lachlin Currie and John Commons, to name a few of those centrally involved in policy formulation, understood the meaning of 'political economy' and made lasting contributions to the economic well-being of the United States that few politicians, or journalists, are able to denigrate.

Malabre provides an entertaining history of the successive failures of economists to forecast the future. A central figure is, of course, Milton Friedman, who defined economic science in terms of its ability to forecast accurately. He rightly concludes that economists, seduced by the false scientism of applied econometrics, built upon illusory economic theories, proceeded to make fools of themselves in the grand manner. Malabre documents the predictive failures of Friedmanite monetarism in a manner that is both entertaining and amusing. The banalities of supply-side economics, promoted in the era of Reaganomics, are also exposed. Malabre shows how an abstract and simplistic theory, which appealed to political conservatives, was promoted without any attempt to provide evidence in its support. But, once again, there is little appreciation that it was *political* forces that brought this kind of economics to the fore. Malabre does admit that supply-side economics was never very popular among American economists, but he does not explain why a minority viewpoint rose to such prominence.

In Chapter 7, Malabre 'looks ahead' and it is here that the book disappoints. Economic journalists are typically fixated by the economics they were taught, or picked up, in a formative period of their lives: hence Keynes's famous remark concerning 'defunct economists'. They are usually out of their depth in dealing with current developments in economic analysis. Space does not permit me to sort out Malabre's misinterpretations and misjudgments. Perhaps it is enough to point out that in Fig 7-1 (p.223), which provides a guide to a selection of schools of economic thought, he fails to distinguish the powerful New Keynesian school from earlier Keynesianism. He also ignores the important new school of evolutionary economists

who employ nonlinear dynamic methods and revitalise many of the ideas of the old American institutionalist school.

Economics is entering a period of crisis and struggle whereby theoretical habits of thought, implanted by decades of subservience to ideological priorities, have to be exorcised from the discipline before any progress can occur. This is hard to discern from the vantage point of an editorial chair in Wall Street. Indeed, Alfred Marshall or Maynard Keynes could have told us that sitting amidst the chaotic swirl of the financial markets, observing the day-to-day machinations of the policy process, is the worst possible position for understanding the great issues of economic science. Because of this, we should, perhaps, forgive Malabre's misjudgments in his analysis of the development of modern American economic thought, his overstatement of the influence of individual economists and his tendency to ignore the fact that it is politicians, not economists, who have been responsible for policy mistakes.

However, I do not wish to end on a negative note. *Lost Prophets* remains a fascinating account of the involvement of many well-known economists in the process of formulating American economic policy. Malabre's account contains all the elements of good journalism: combining the seductive skills of the gossip columnist with the moral outrage of the investigative journalist, along with the clever presentation of descriptive statistics, which is the hallmark of a good economics correspondent. In sum, the book is a very entertaining read but one that is not to be taken too seriously.

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