# **ECG Malaga October 2018**

Thank you for being here today and for your interest in *Economics for the Common Good*.

A very personal book, in which I tried to convey my vision of economics as a moral and philosophical science.

**I. THE COMMON GOOD**

1) Ambition of the economics of the common good: ensure that economic institutions contribute to the general interest.

Many situations where the interests of citizens, companies, states, countries diverge from the general interest:

• *Citizen* who emits carbon, hurts the environment, drives too fast, refuses to vaccinate his child: does not take into account the effect of his behavior on others.

• *Business or bank* that takes risks that jeopardize the employment of its workers or the savings of its customers; that abuses its monopoly power.

• *State*: public debt, unfunded pensions, poor education, inequality, the financial crisis...

• *Country*: primacy of the national interest / interest of the world: global warming, trade wars, taxation...

Common feature? Individual interests trump the general interest; incentives are wrong.

2) What to do?

* Persuasion: Encourage good behavior, CSR ... Boost awareness of the consequences of individualism, selfishness. Tobacco in public places: combination persuasion + incentives. Has changed the norm.
* But there are limits to what can be done by changing the norms: Rio 1992- Paris 2015: 23 years of exhortations (but also corruption, tax evasion, incivilities ...).

Incentives are needed to set individual interests to music and put the general interest back in the center.

3) What is the common good? A harmonious society?

• Veil of ignorance. Without naivety (myth of new man)

*Thought experiment*: abstract ourselves from our attributes and our position in society, to place ourselves behind the veil of ignorance

* Suppose you have not yet been born, and therefore do not know what place you will have in society, what your genes or who your family will be, or even what social, ethnic, religious, or national environment you will be born into.
* Now ask yourself, “In what society would I like to live, knowing that I might be either a man or a woman, endowed with good or bad health, from a rich or a poor family, well- or ill-educated, atheistic or religious, a person who could grow up in a big city or the middle of the countryside, or one who could seek fulfillment in work or adopt an alternative lifestyle?” Looking behind the veil of ignorance is not a new idea; it has a long and distinguished intellectual tradition (Hobbes and Locke in 17th century England; Kant and Rousseau in 18th century continental Europe; Harsanyi and Rawls in 20th century US)

*Need to consider personal incentives*: Soviet myth of the “new man” has logically led in the past to totalitarian and impoverishing forms of social organization. Whether they are politicians, CEOs, employees, out of work, independent contractors, people react to the incentives facing them.

*Delivers*: health insurance (market goes against solidarity), equal opportunities / right to education, fight against monopolies, equality between men and women, religious / ethnic tolerance...

• Without prejudging instruments

• Long term vision

**II. Delivering economics for the common good**

Triptych: 1) market, 2) state (the state and the market are complementary, not mutually exclusive; the market needs regulation; the state needs competition and incentives), 3) individual and corporate social responsibility (leave latter to the discussion).

*Public policies*: The design of the state must match the 21st century economy. Three principles:

* *Avoid hubris*: simple policies are often more effective. Do not base policies on information you do not have (“Why make it simple when we can make it complicated?” dismissals, climate change).
* *Resist the siren call of primacy of politics (leave that to the populists):* Cases of successful independence: Central Banking, competition policy, legal system.
* *Use common sense and economic insights. E.g. if uses industrial policy: seven guidelines*

1) Identify the reason for the market failure, in order to be able to respond more effectively

2) use independent, appropriately qualified experts to select projects to receive public funding

3) pay attention to the supply of talent and not only the demand for the project; Field of Dreams mentality

4) adopt a neutral industrial policy that does not distort competition between companies

5) fix goals, do not prejudge the solution

6) evaluate interventions after they have taken place, and publish the results; include a “sunset clause” which ensures support can be withdrawn if the policy is not working or is no longer needed

6) involve the private sector closely in the risk taking

7) strengthen universities. Governance, and not just money.

**III. WHY DOES ECONOMISTS’ DISCOURSE MEET WIDESPREAD RESISTANCE?**

Since the resounding failure of planned economies, the market economy has become the dominant, almost exclusive model for our economies.  *But has achieved only a partial victory, because it has won neither hearts nor minds.*

* *Widespread distrust*; feeling that the world is prey to private interests with neither pity nor compassion; people lament the disintegration of the social contract and the loss of human dignity, the decline of politics and public service, and the environmental unsustainability.
* The popular slogan “*the world is not for sale*” strikes a chord internationally.

Meanwhile, economists, even though they devote most of their research to market failures, are on the whole more pro-market than other social scientists and the public opinion (pardon my French tropism!). View that economists fail to draw a clear line between what has a price and what has dignity (Kant), between the profane and the sacred (Durkheim)

Have we- our societies, we economists- lost sight of the common good?

*Economics for the common good explains why economists’ discourse meets widespread resistance.*

1. *Part of the responsibility lies with economists themselves.*

* Judgment sometimes impaired by financial conflicts of interest, political friendships, or ambitions for public recognition
* Fail to communicate on what they are good at and what they are bad at, so the public’s expectations are often unmet;
* Don’t put enough effort to share their knowledge with a wider audience

[Economics is like any culture, for instance music, literature, or sports. We like it more the better we understand it. Let’s admit it: it’s easier to watch a film or devour a good thriller than to launch into a book on economics]

* They often have insufficient information
* About numbers (financial crisis: OTC, off-BS exposures…)
* About application decrees. Devil is in details:
* Securitization and skin in the game in Europe
* Protectionism that is not tariff- or quota based[[1]](#endnote-1).
* Agricultural subsidies

But part is also associated with *intrinsic difficulties in communicating their knowledge***;** focus on two difficulties: cognitive biases and moral perceptions.

*b) Cognitive biases*

* our understanding of economic phenomena is obfuscated by various cognitive biases; we are all dependent on heuristics and narratives, and we often believe what we want to believe, see what we want to see.
* We all have the ability to understand economics. Errors in reasoning cannot necessarily be explained away by IQ or educational level.

*Motivated beliefs*

First, we *believe what we want to believe*, and we see what we want to see, interpreting facts through the prism of our own beliefs.

We think that *accidents and illnesses* only afflict others, not ourselves or those close to us. [This can lead to harmful behaviour, such as driving carelessly or not looking after our health (although this may not be entirely negative since worrying less can also improve our quality of life).]

In the *economic realm*, we all *dream of a world* in which

* the law would not have to encourage or constrain people to behave virtuously,
* companies would stop polluting and avoiding taxes,
* people would drive carefully even without police officers around.

We also want to believe in

* *green growth* [the idea that being green will cost little or even benefit us; but if this is so, why don’t we already do it? We have to accept to pay for preserving the environment.]
* We do not want to contemplate that *excessive public debt* will endanger the survival of our social safety net, preferring to believe that there will be a miracle growth rate that will absorb the per capita debt or that “someone else will foot the bill”.

Hence a first difficulty for economists to get their message across.

* *Populist parties, both right and left-wing, promote the vision of an economy free of difficult choices*

[Anything that questions this fairytale is perceived at best as scaremongering, at worst as lies spread by global warming fanatics, austerity ideologues, or other enemies of humanity].

* Economists are often the *bearers of bad news*

[While the classical economics representation of a society of purely self-interested individuals is an imperfect description of reality (the book actually details how morality is privately and socially constructed), when economists mention the need for incentives they trigger anxiety and resistance; we would all rather live in a world of honest, hardworking and empathetic citizens. ]

*Direct and indirect effects, visible and invisible victims*

We form our beliefs on *first impressions and intuitions*, seeing the easy-to-understand direct effect of an economic policy, and no further.

* *Rent control*
* We look at the direct and visible beneficiaries, those who have the good fortune to already be renting an apartment and are geographically stable.
* But they are indirect and invisible victims: the stock of quality housing gradually diminishes, creating scarcity and ultimately penalising potential beneficiaries.
* *Labour market reform emphasising flexibility*
* The media tends to portray the tragedy of the direct, visible victims battling to keep their jobs in a country where they have little chance of finding another similarly secure job.
* But the reform’s indirect beneficiaries would be numerous, the unemployed and those on short-term jobs. These “winners” are invisible. The dice are loaded.

Economics is *accessible, but can be counterintuitive if one stops at first impressions.*

Public policies- which is mostly the reflection of the electorate’s beliefs- too often ignore side effects.

*Contrary to general medicine*, these side effects are usually borne by mostly invisible third parties rather than the very visible beneficiaries of the policies. Economists, when pointing to the indirect harm on victims (for example those who don’t find a job or decent housing, or the taxpayers), are often accused of lacking empathy for the intended beneficiaries.

**IV. A MORAL AND PHILOSOPHICAL SCIENCE**

I plead for a *wider vision than classical economics*: economics as a moral and philosophical science, and incorporating knowledge in psychology and other HSS.

*Other HSS, civil society, religions have* *different view of the market* [While they recognize its virtues, they often accuse economists of not sufficiently considering the ethical issues it raises, and of not acknowledging the need to establish a clear boundary between the commercial and the noncommercial.]

*Reflect scientifically on these issues*

* *Things we consider to be morally sound change over time,* even in economic matters (life insurance and interest paid on saving)
* *Morality can have a highly personal dimension*.

[When the flame of indignation burns brightly, people use moral arguments to impose their own value judgments and reduce the freedom of others. Thus, until recently in many societies, sex acts between persons of the same sex or of different races have been considered immoral by the majority of citizens. The best response to such claims of moral superiority is not necessarily another moral claim—pitting my morality against yours leads to confrontation.]

* *Indignation* is often a useful indicator of dysfunction in society or the inappropriate nature of some kinds of behavior. We cannot stop there, though.

*Sandel (What Money Can’t Buy)* : A wide range of goods and services, including babies for adoption, surrogate motherhood, sexuality, drugs, military service, votes, and organs for transplantation, are not to be commoditized through markets, no more than friendship, admissions to elite universities or Nobel Prizes are to be bought, or genes and other life forms to be patented.

Some of these criticisms based on ignorance of what economics has become in last 30 years, some are deeper. Let’s discuss …

*Behavioral economics (3rd Nobel in behavioral in 15 years)*

* *Failure to pursue self-interest: Self-control.* Public interventions in the matter of cigarettes, drugs, savings or excessive interest rates (usury) are in part motivated by self-control concerns.
* *One* of the worries about organ sales is that poor people would enter into contracts that bring them immediate benefits in terms of their consumption in exchange of substantial long-term costs.
* voluntary servitude

*Insufficiently competitive markets*

* *Market power*. Price gouging
* *Asymmetric information*. Admission to elite universities, Nobel Prize. Sandel notes that surrogate mothers may not know what it is like to carry, bear and then give up the child.

*Crowding out*

* May reduce intrinsic motivation (do it for the money?)
* Message sent by laws

*Motivated beliefs*

* *Don’t want to see inequality*
* Kidney markets
* Prostitution

*Don’t want to see society as is*

* Public executions
* Corporal punishment, death penalty
* Layoffs (commoditization of human beings)

*Economists’ role in society*

* Bearers of bad news (economic analysis exposes our deep values).
* Supporting evidence: motivating law and policy by overarching ethical goals such as fairness and equity avoids a confrontation with tell-tale signs that our morality is not necessarily what we strive to believe it is.
* Spillovers in uncontrolled aspects of life.

**V. BEING AN ECONOMIST**

I have been asked whether “Economics for the common good” is an oxymoron. More generally economics has come under sharp attack, especially since the 2008 financial crisis. Many people wonder whether it is a science.

Science: built on to-and-fro between *theory*, which provides a lens to the world and allows us to understand observations and describe their implications, and *empirical work*, lab experiments, fieldwork, econometrics, big data, which measures the importance of effects and helps question the theory

We must also be humble and accept that economics, while a science, is an inexact one.

* good data may be unavailable,
* theories may oversimplify,
* and, more specific to human and social sciences, heterogeneous behavioral patterns and self-fulfilling phenomena (such as bank runs or bubbles) may complicate the analysis.

We must acknowledge that we will generally feel *more comfortable analysing past events and proposing future policies, rather than forecasting*. [A characteristic that is incidentally shared by doctors and seismologists, who detect environments that are conducive to a heart attack or an earthquake and provide useful recommendations, and at the same time may be hard-pressed to predict the exact timing of the event or even whether the latter will occur at all.]

*The role of experts*

Conclude with a few remarks about the role of expertise.

*Economics for the common good* stands as a *reassertion of the value of expert knowledge in the era of Trumpian denial of facts and scientific knowledge*. More generally, populists’ programs have contempt for elementary economic mechanisms.

*But for this we must raise citizens’ sensitivity to expertise. In what way?*

* *Long term: reform education*. Teach more scientific method in school: controlled experiments, difference between causality and correlation, scientific methodology (HSS, medicine, physics…) => shape respect for science.
* *Disseminate majority/consensus view among top scientists* (climate change).

Public opinion’s identification of who is an expert and who is not (BBC syndrome); necessary diversity.

*Should not be seen to bicker over minor technicalities* which draw attention away from key messages and goals (climate change).

* Economists must explain what they are good at—and what they are bad at too. 

Above all, they must be humble, and they must explain how economics can continue to work for the common good.

* Economics has played a major role in guiding public policy over the past several generations. A proper use of economic ideas will in the near future be more important than it has ever been, contrary to current mood.

Populism comes in many guises; and it has specific causes in each country. But everywhere they play on the electorate’s *frustrations* (financial and Eurozone crisis, unemployment, slowdown in economic growth …) and *fears for the future* (rising debt, job-destroying technology progress, climate change, migration…). They exploit these frustrations and fears to foster widespread hostility to immigrants, distrust of free trade, and xenophobia. And they dismiss people with expert knowledge are dismissed.

There is no doubt, and it’s understandable, that *citizens want change.* They feel that policymakers have not done enough, that they do not have a plan. But change for change’s sake is extremely dangerous, particularly when it is based on prejudice and selfishness. Steady, intelligent change is much less exciting than fast, dramatic change, but it is the only change that can give us hope.

*Which brings me to the value of making economic ideas comprehensible to a general audience*

*Repeatedly blaming politicians for flawed policies won’t get us very far*. Like us all, they respond to the incentives they face, in their case the hope of being (re)elected. Very rarely do they go against majoritarian public opinion. So we, citizens, get the policies we deserve.

*In my view, economists can be more valuable now than they have ever been, contrary to the current mood in the US, the UK and Europe. But for that we need to guide our countries through a period of low growth, anticipate the digital revolution and its many socioeconomic challenges, design solutions to unemployment, climate change, financial regulation, inequality … and explain the role of economics in the construction of the common good.*

I thank you for your attention.

1. The case of environmental regulation: promotion of diesel vehicles in Europe (UK: diesel actually faces a slightly higher fuel tax; but road taxes based on CO2 emissions => subsidized.). Miravete-Moral-Thurk (2017): a) Only European producers invested in diesel (local demand for that); b) substantial advantage in terms of fuel taxes (natural comparative fuel efficiency = 20-40%, 63% with tax advantage); c) loose NOx standards (diesel emits large amounts of NOx, and relatively little CO and CO2). Otherwise would have been a shift toward Asian (gasoline-powered) cars. [↑](#endnote-ref-1)