SYMPOSIUM

Economics' Fall from Grace

Lloyd I. Rudolph, *University of Chicago*
Susanne Hoeber Rudolph, *University of Chicago*

Not long ago, many political scientists suffered from economics envy. Some still do. They view economics as the queen of the social sciences, claiming that it is "scientific," like physics. Physicists and other natural scientists spend most of their time trying to explain phenomena, but non-behavioral micro-economists spend most of their time on mathematical proofs and econometric tests of *a priori* theories based on intuitive plausibility or principles of "rational action."[1] Being "scientific" it was alleged, meant that economics could access objective knowledge, knowledge that was said to be true independent of time, place, and circumstance. Robert Bates called on political scientists to do the same by arguing that they should be in search of "lawful regularities which . . . must not be context bound" (Bates 1997b).[2]

Economics abruptly fell from grace somewhere between late 2007 and the fall of 2008, when the U.S. stock market crashed and the U.S. and European economies fell into the worst recession since the great depression of 1929 (Sum et al. 2009).

Two of the high priests of market infallibility, Alan Greenspan and Eugene Fama, responded quite differently to the revelation that the emperor had no clothes. Greenspan, who served five terms over 18 years (1987–2006) as Chairman of the Federal Reserve Board and whom Bob Woodward had christened the "Maestro" for presiding over an 18-year boom economy (Woodward 2000), admitted in October 2008 testimony before Congress that he "found a flaw in the model . . . that defines how the world works" (*PBS NewsHour* 2008). He had, he said, put "too much faith in the self-correcting power of free markets" (Andrews 2008).

Eugene Fama, the other high priest of market infallibility, a professor in the University of Chicago's economics department and its business school, spoke for the "Chicago School" of economics founded by Milton Friedman. Fama's signature concept was the efficient market hypothesis, or "EMH." Unlike Greenspan, Fama adamantly stuck to his guns in the face of the financial crisis. He told John Cassidy in an interview in the *New Yorker* that he didn't "know what a credit bubble means. I don't even know what a bubble means" (Cassidy 2010). According to Fama's circular reasoning, bubbles do not exist because they are not predictable, but they cannot be predicted unless there is a consensus among investors that a bubble is in progress, a condition that would burst the bubble (Cassidy 2010). Historically, voices that say there is a bubble have not been heard by investors.[3] For Fama, the credit and housing bubbles that preceded the 2008 recession were illusions. People who could not pay their mortgages and faced foreclosure were victims of the recession, not the credit and housing bubbles.

For many years, Keynes's view that financial markets were "casinos" where bets were made with other people's money had credence among economists, but by the new millennium, Fama's efficient market theory—which held that financial markets always get asset prices right—reigned supreme. When reminded by John Cassidy that his erstwhile University of Chicago colleague and federal judge Richard Posner said that the financial crisis and recession presented a serious challenge to Chicago School economics, Fama replied, "He's not an economist. He's an expert on law and economics. We are talking macroeconomics and finance. That is not his area" (Cassidy 2010).

Comparing the two high priests of market infallibility, Alan Greenspan and Eugene Fama, we are reminded of a thought by Leo Tolstoy: "The most difficult subjects can be explained to the most slow-witted man if he has not formed any idea of them already; but the simplest thing cannot be made clear to the most intelligent man if he is firmly persuaded that he knows already, without a shadow of doubt, what is laid before him" (qtd. in Lewis 2010).

We now turn to the science trope embedded in the economics trope that has beguiled political scientists. Deirdre McCloskey has shown how and the degree to which economists lack reflexivity. They are unaware of how much they rely on rhetorical devices—not the least of which is the ethos of "The Scientist"—to legitimize what they have to say (McCloskey 1990, 57). "The Scientist" ethos justifies conceits such as the idea that scientific knowledge is the only form of knowledge, and that knowledge about human behavior is transparently accessible, unmediated, and unrepresented.

David Laitin, a leader of the effort among political scientists to create a surrogate for microeconomics in the field, rational choice, which was threatening to become hegemonic in political science publications, hiring, and promotion, assumed the mantle of "The Scientist" to discredit Perestroikans, whom he called "Luddites" because they were said to fear modern science.[4] Laitin dismissed a Perestroikan call for pluralism in forms of knowledge and methodologies that was framed as "let a hundred flowers bloom, let a hundred schools of thought contend" (Rudolph 2005) by claiming that the epistemologies of area studies in comparative politics, realism in international relations, and qualitative methods across the subfields were "threats to scientific progress" (Laitin 2005, 131). According to Laitin, "A scientific frame would lead us to expect that [such fallacious theories] will become defunct . . . [and] should no longer be cultivated within the discipline" (2005, 130).[5]

In a letter in the next issue of the *University of Chicago Magazine*, Roger Myerson, a professor of economics at the University of Chicago, sought to save his colleagues in the political

doi:10.1017/S1049096510001150

https://doi.org/10.1017/S1049096510001150 Published online by Cambridge University Press

science department from their Perestroikan folly by informing them that "great departments of political science like Chicago are increasingly requiring that their students must master the fundamentals of statistics and game theory" (Myerson 2003).

We close our account of economics' fall from grace by suggesting that political scientists who want to be "scientific" recognize that the Newtonian or physics model of science is not the only model of science. Indeed, Sven Steinmo recently argued that what political scientists study is not like physics, and that the social world does not work according to the same laws and principles as the physical world. Following a spurious idea of what "good science" is, "many political scientists have created models of politics and behavior as if politics and history were the product of discrete, stable and independent units [or variables] in interaction with other variables in stable and predictable ways" (Steinmo 2009–10, 1).

Steinmo calls for an evolutionary approach to politics that is closer to the life sciences than to physics. Prediction based on linear causation is replaced by a recognition of the uncertainty, contingency, and open-endedness of complex causation. *Pace* Robert Bates, we should teach our students that context matters; they should learn "about people, places and events . . . because in an emergent and contingent world, *these facts are themselves important*" (Steinmo 2009–10, 38, author's emphasis). ■

NOTES

1. Herbert Gintis, in a review of Eric D. Beinhocker's *The Origin of Wealth*, compared graduate texts in physics and economics. The graduate text in quantum physics showed that the field began by scholars addressing anomalies, with Max Planck in 1900 and Albert Einstein in 1905: "The text continued, page after page, with new anomalies. . . . By contrast, the graduate microeconomics text . . . did not contain a single fact in the whole thousand page volume. . . . Rather, the authors buil[t] economic theory in axiomatic fashion, making assumptions on the basis of intuitive plausibility or consonance with the principles of 'rational action'" (2006, 1027).
2. See also Bates 1997a, in which he argues that context-bound area studies scholars who have spent years learning a language and doing field research can be useful as sherpas for political and social "scientists" by supplying "data" to feed into formal models and large-*n* studies.
3. For exceptions of who saw the credit and housing bubbles that broke in 2008, see Michael Lewis, *The Big Short: Inside the Doomsday Machine* (New York: W.W. Norton & Company, 2010).
4. See Laitin (2005, 115) for a riposte to the history and epistemology of the Perestroikan movement.
5. See also Stewart, who quotes Laitin:

   > [Laitin] calls for aggressively weeding the garden of research that lacks scientific validity. "[I]f theoretical logic or scientific evidence finds a theory or procedure to be fallacious," he writes, "that procedure's flower bed should no longer be cultivated within the discipline" . . . Forgetting that context inflects independent variables and is itself explanatory, Laitin attacks qualitative case studies because they select "on the dependent variable" and "will ultimately lead to faulty inferences about causation." (2003)

REFERENCES

Andrews, Edmund L. 2008. "Greenspan Concedes Error on Regulation." *New York Times*, October 23. http://www.nytimes.com/2008/10/24/business/economy/24panel.html.

Bates, Robert. 1997a. "Area Studies and the Discipline: A Useful Controversy." *PS: Political Science and Politics* 30 (2): 166–69.

———. 1997b. "Area Studies and Political Science: Rupture and Possible Synthesis." *Africa Today* 44 (2): 123.

Cassidy, John. 2010. "Rational Irrationality: Interview with Eugene Fama." *New Yorker*, January 10.

Gintis, Herbert. 2006. Review of *The Origin of Wealth: Evolution, Complexity, and the Radical Remaking of Economics*, by Eric D. Beinhocker. *Journal of Economic Literature* 44 (4): 1018–31.

Laitin, David M. 2005. "The Perestroikan Challenge to Social Science." In *Perestroika!: The Raucous Rebellion in Political Science*, ed. Kristen Renwick Monroe, 115–35. New Haven, CT: Yale University Press.

Lewis, Michael. 2010. *The Big Short: Inside the Doomsday Machine*. New York: W.W. Norton & Co.

McCloskey, Donald M. 1990. *If You're So Smart: The Narrative of Economic Expertise*. Chicago: University of Chicago Press.

Myerson, Roger. 2003. Letter to the editor. *University of Chicago Magazine* 95 (6): 6.

PBS NewsHour. 2008. "Greenspan Admits 'Flaw' to Congress, Predicts More Economic Problems" [transcript]. http://www.pbs.org/newshour/bb/business/july-deco8/crisishearing_10-23.html.

Rudolph, Lloyd I. 2005. "Let a Hundred Flowers Bloom, Let a Hundred Schools of Thought Contend: Arguments for Pluralism and against Monopoly in Political Science." In *Perestroika!: The Raucous Rebellion in Political Science*, ed. Kristen Monroe, 230–36. New Haven, CT: Yale University Press.

Steinmo, Sven. 2009–10. "From the President: History and Predictability and Political Science." *Clio* 20 (1): 1–38.

Stewart, Sharla A. 2003. "Revolution from Within." *University of Chicago Magazine* 95 (6): 32–37.

Sum, Andrew, Ishwar Khatiwada, and Joseph McLaughlin, with Sheila Palma. 2009. "The Economic Recession of 2007–2009: A Comparative Perspective on Its Duration and the Severity of Its Labor Market Impacts." Boston, MA: Labor Market Studies, Northeastern University.

Woodward, Bob. 2000. *Maestro: Greenspan's Fed and the American Boom*. New York: Simon & Shuster/Touchstone.

https://doi.org/10.1017/S1049096510001150 Published online by Cambridge University Press