The Problem of Experts

• “People in this country have had enough of experts” says Michael Gove
• Is it better to consult charlatans, then?
• More to the point: how to tell the difference?
• Easy to figure out that Sean Penn doesn’t know much about the economy of Venezuela.
• How can you tell they are charlatans when they have Nobel Prizes?
It Isn’t Easy

Over my career I have been presented with the economic equivalent of perpetual motion machines more times than I can tell you

- Nobel prize winning physicists
- award winning mathematic professors
- my own grandfather

Specialists learn from past mistakes – non-specialists are often unaware of these mistakes

still: some common sense and numeracy go a long way
The cost of bad advice...
The Denver baggage claim in 1995: a business school case study in failure – the completion of the airport was delayed by 16 months and the baggage handling system was scrapped in 2005

The UCLA card catalog?
When experts are charlatans...
The Advisors: Mishkin

Mishkin (Columbia)

- his book: *The economics of money, banking, and financial markets* has nearly 5000 citations
- in 2006 paid $124,000 by the Icelandic Chamber of Commerce to co-author a report on the Icelandic financial system
- the report said that the Icelandic banks were sound
- in 2008 dramatically proven wrong when the banking system in Iceland collapsed.
The Advisors: Walt Rostow

Walt Rostow (MIT)

- his book *The stages of economic growth: A non-communist manifesto* has nearly 15,000 citations
- interviewed in India in 1983: India is now in the post take-off stage
A Cautionary Note

- the right idea, just the wrong country
Limited Experience with Stable Democratic Institutions

minimal criterion: majority must have the right to vote, institutions at least 50 years old

- Australia, New Zealand: 120 years
- US, Canada, Ireland, Denmark, Sweden: 100 years
- Western Europe (excluding Switzerland), Japan, India: 70 years
- Switzerland: 50 years

Growth in India versus China, versus catastrophes in India and China

Role of ideology?

Post WWII was particularly bad: ideas such as socialism, central planning, government control of industry, trade protectionism, stimulus spending were fashionable everywhere

notice that India avoided both extremes of China...
Incentives Matter

- economists are motivated by the same things as everyone else:
  - greed, money, social approval, sex, altruism, ideology
- who is paying?
- political views?
- looking to be exciting and controversial?
- looking for entrée into particular social circles?
Does a Nobel Prize make you an expert?
Nobel Prize Winners: Krugman

Krugman (CUNY)

• “It has been obvious for some time that the creation of the euro was a terrible mistake...Greece should vote ‘no,’ and the Greek government should be ready, if necessary, to leave the euro.” [2015]

• “The transition costs of euro exit and restoration of a national currency would be huge: massive capital flight would cause a banking crisis, capital controls and bank holidays would have to be imposed, problems of how to value contracts would create a legal morass, business would be disrupted during a long interim period of confusion and uncertainty.” [2017]
Krugman the Academic

the profession “turned a blind eye to the limitations of human rationality that often lead to bubbles and busts”

• a fellow named Stephen Morris has written extensively about bubbles
• not a fringe member of the economics profession
• at the time of the quote was the editor of *Econometrica* (one of the leading journals in economics)
• also Krugman’s colleague at Princeton at the time
“During the golden years, financial economists came to believe that markets were inherently stable — indeed, that stocks and other assets were always priced just right...

most economists to ignore... especially financial markets — that can cause the economy’s operating system to undergo sudden, unpredictable crashes”

papers that were never written:

Salant, Stephen W. “The vulnerability of price stabilization schemes to speculative attack.” *Journal of Political Economy*

based on an earlier paper:

“A model of balance of payments crises”
Stiglitz (Columbia)

on Greece:
“...A yes vote would mean depression almost without end. Perhaps a depleted country – one that has sold off all of its assets, and whose bright young people have emigrated – might finally get debt forgiveness; perhaps, having shrivelled into a middle-income economy, Greece might finally be able to get assistance from the World Bank. All of this might happen in the next decade, or perhaps in the decade after that.

By contrast, a no vote would at least open the possibility that Greece, with its strong democratic tradition, might grasp its destiny in its own hands. Greeks might gain the opportunity to shape a future that, though perhaps not as prosperous as the past, is far more hopeful than the unconscionable torture of the present.

I know how I would vote.”
Depression Almost Without End
Advice not to Follow

• No working economist with expertise in the area agreed with this advice
• You don’t sell many books by telling people that life is tough
• Although if your political leaders have managed to run up huge debts on your behalf it is tough...
• You would have to be barking mad to take the advice of these fellows
• Look for sense not rhetoric
A Few Things to Look at

- What did they get the Nobel Prize for?
- Where do they teach now?
- Do they work for some partisan think tank?
- What do they do research on?

Krugman: trade and economic geography
Stiglitz: microeconomic theory of asymmetric information

neither received it for work in monetary theory or macroeconomics, nor did either do any important work in either area

- Linus Pauling: chemical bonds...vitamin C?
- Sante Fe Institute
Disagreement Among Economists? Not so much so...

Things all economists agree on

- tax incidence: doesn’t matter who write the checks [Spain]
- lowering non-tariff trade barriers benefits the country that lowers the barriers
- “jobs” are not exported
- Venezuela
- Large increase in the minimum wage
- Lower tax rates (versus lower tax payments)

...example of Prescott and Italy
The Good

• Tom Cooley in Forbes [wrote with macroeconomic Nobel Prize winner Ed Prescott]
• John Cochrane [macroeconomic and finance]
• Marginal Revolution blog – not experts but read the experts
• Michele Boldrin
• Anat Admati [finance] and Martin Hellwig [general equilibrium theory] *The Banker’s New Clothes*

populists diagnosis isn’t wrong, just the the cure is worse than the disease
The Bad

The Nobel winners are pretty smart...the lesser figures not so much so.

The Left:
Brad DeLong (Berkeley, economic historian),
Yanis Varoufakis (University of Athens, “game theorist”) 
Mark Weisbrot [Venezuela...]

The Right:
Laffer (USC...why was he there not the University of Chicago?)
Navarro (UC Irvine)

and the ugly:
Dani Rodrik (Kennedy School),
Common Sense: Overnight Markets

- enables firms to hold a smaller cash reserve, so get a higher interest on the extra
- in a firm with billions in annual revenue perhaps worth a few millions
- So worth paying someone a few hundred thousand to do it

But when the New Yorker...or the head of the Federal Reserve Bank... says how when this market gets frozen it is a danger to the entire economy, I say: don’t worry about overnight paper - worry about toilet paper because it is a lot more important

it isn’t that common sense is always right

just if someone says something that goes against common sense they have a lot of explaining to do...and it better not involve big words and talk about studies that haven’t yet been published in obscure journals
Do economists suppress non-orthodox ideas?

- As you know, economists suppress ideas that go against the “orthodox”
- this is done by refusing to publish papers written by non-economists or non-orthodox economists in top economics journals

by consensus as well as bibliometrics the top journals in economics are

- The Quarterly Journal of Economics
- The American Economic Review
- Econometrica
- The Journal of Political Economy
An Example

• a PhD psychologist argued strongly against the orthodox mainstay of economic theory, expected utility theory

• began submitting papers to economics journals in the late 1970s and persisted for several decades


awarded Nobel Prize in Economics in 2002
What Ideas are Suppressed

• when people complain about ideas being suppressed
• they usually mean: nobody wants to listen to my bad ideas
• or: “I am a charlatan”
• be wary of those who know all the answers

What I do know

• how you can destroy your economy

What I don't know

• how to fix it after you break it
The Perpetual Motion Machine

“I am a Keynesian” = “I am a religious zealot”

“Animal spirits” = “I am clueless”

one does not believe in science, it is not a religion

Keynesianism and stimulus

• debt: the way up and the way down

• austerity = paying back what you owe
Amateurs

- a long history of discoveries in astronomy by amateurs
- Nick Brown who exposed extensive fraud in the psychological literature
- applied common sense and statistics
- didn’t try to solve all the world’s problems
- do demand answers – don’t let people hide behind gobbledygook or academic credentials
Know what cannot be true...
The Uncertainty Principle for the Social Sciences

- you can’t forecast the stock market
- you can’t predict the outcome of elections

non-rational expectations = you can fool all of the people all of the time

- Lucas critique
- Neumann principle

- physicists cannot predict the movement of a particle
- failure of physicists has a name “Heisenberg's uncertainty principle”
- nobody criticizes physicists for this failure
- spooky particles seem to anticipate what other particles will do
- failure of economists and political scientists is for the much less spooky reason that people can and do anticipate what other people will do
Polling

- Jan and Dean are going to play rock-paper-scissors
- Nate interviews them
- Jan tells Nate she is going to play rock and Dean tells Nate he is going to play scissors
- Nate publishes his prediction on his website: Jan is going to beat Dean by playing rock to his scissors
- what happens?
The Neumann Principle

- John Von Neumann showed in 1928 only one solution to this paradox
- Jan and Dean cannot know how the other is going to play - they must be uncertain
- uncertainty can be quantified: each must believe the other has one chance in three of playing rock, paper or scissors - or one of them is either stupid or wrong
- only if Nate announces that there is a 1/3rd chance of Jan and Dean each playing rock, paper or scissors will Jan and Dean be content to play as he forecasts
- empirical research shows that in real contests - soccer matches, tennis matches - the good players play randomly and with the right probabilities
Predicting Crashes

- clever Nate discovers from his big data analysis that the stock market will crash next week
- he posts his prediction on his website
- are you going to wait until next week to sell your stocks?
- poor Nate: always wrong, he should be like Sam and eat a bug
The End

• be numerate
• use common sense
• ask questions
• expect answers