



Economics past and present: An interview with Kurt W. Rothschild

conducted by Andreas Reinstaller and Joachim Becker

Question: Prof. Rothschild¹, thank you very much for giving us this interview. To start I'd like to ask you about John Kenneth Galbraith who has passed away recently. He was a leading critical mind in economics. What do you think was his importance for economics and what do you think will be his legacy?

K.W. Rothschild: I think one of the great qualities of Galbraith was that, he decided at a very early stage that a wider view of economics was needed. He knew economic theory at least as well as any other Harvard economist but he emphasised that economic problems are not devoid of political and social elements and that as a consequence economic analysis should take into account these elements. He also recognized the importance of communicating economic problems and possible solutions in a way to be intelligible at least to every intelligent person. In this way he believed economics and economists could influence political outcomes. He was able to do this because he had accumulated also experiences outside academics by working in politics. He was an U.S. Ambassador in India under Kennedy and he was Kennedy's speech writer and so forth. So he had the rare quality to know economic theory well but to keep in touch with reality all the time, too. So, I believe, he will be missed because there are few who can do that.

Question: If we look at some statements that other very famous theoretical economists made, there seems to be a general bad feeling about the path economics has taken. For instance, Mark Blaug has said that modern economics is sick, that modern economics is becoming an intellectual game played for its own sake. Ronald Coase, on the other hand has stated that economics has become a theoretical system that floats in the air but has very little relation to what happens in the real world. Finally, Joseph Stiglitz has said about how economics is taught at U.S. graduate schools that this is a testimony for the

triumph of ideology over science. What do you make of these statements?

K.W. Rothschild: Generally I would agree. I think that a critical view of economics is missing. This is not necessarily true for neoclassical theory as such, but for the way it is used to keep other approaches out of the economics profession. I also think that the way in which it is applied directly to practical affairs is – given its very strict assumptions – illegitimate. Sometimes it is also presented in its 'vulgar' form just to exploit it for certain ideological and political purposes. The economy and the social system in general that comprise of course also politics and social factors and institutions are such a complex phenomena that you can't expect one single theory to provide a sufficient basis for studying it. So, economics like sociology is necessarily a multi-paradigmatic science. We need several theories to study these complex circumstances. Of course, every theory must be rather abstract as otherwise it can't be used as an analytical tool. But even if we have several such abstract theories none will be able to capture all the relevant features of a social system. So, it is not possible in economics to develop general theories as in the natural sciences. We need to study and to draw on many theories, including past ones. We are all in great debt to Adam Smith, and what he has written is relevant to a certain extent even for us today. This we should not forget. So, the bitter remarks on economics which you mentioned before are really to be understood as a sharp protest against the way in which mainstream economics has been monopolized by general equilibrium theory.

Question: What is different about how economists think and do research nowadays if you compare it to the Keynesian Revolution, which you had occasion to experience in the late 1930s and the 1940s in the UK?

K.W. Rothschild: The situation has changed very much because mainstream economics has become

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such a specific and generally established discipline. As a consequence it has also become very specialized. The main difference is that before the Second World War most economists could have an idea what was going on in most of the different fields of economics. So, the research was not so narrowly focused and dealt with questions of a more general character. The methods were not so much based on mathematics and economics was more a form of logical discourse.

There were of course advantages and disadvantages compared with today. In the old times an editor of a journal could judge whether an article was good or bad. Of course, he couldn't verify all the time whether somebody had plagiarised the piece, but this is also difficult today. There was no referee system and as a consequence articles sometimes contained mistakes and comments and replies followed suit to discuss the problems. But the whole discussion was on a level that most economists could understand and because of these discussions one could see that there were many interesting questions and many interesting answers. I can give you an example on how it worked in the past from my own experience. I sent my first article, a short note, to the *Economic Journal*.² I must add that there weren't many journals at the time, there were no core journals and other journals, there were just journals. Two days later I got a postcard from Keynes stating that he liked it and that he would print it. Unbelievable for today! He didn't know me of course; I was just a little lecturer in far away Glasgow. Nowadays, this is different. A single person can't judge the scientific value of most articles any longer. So, you need a referee system with all its problems. So, to sum up, the difference to how research is done today, is that it has perhaps become too narrow, too specialized, too technical, and that some of the interdisciplinary considerations, which are important, are neglected.

Question: So could one say that economics was more open to the public and that it was more part of the political discourse and other intellectual debates than it is today?

K.W. Rothschild: Yes, this is certainly the case.

Question: So this leads us to the demands of the students of the Post-Autistic movement. In the year 2000 French students have issued a petition raising the problem that there was a lack of pluralism in the teaching of economics in the sense that non-mainstream theories and schools of thought are excluded from most curricula. In principle the issue they raised were very much in line with what you

said before. They claimed that there is a need for plurality in economics. This went so far that important mainstream economists like Blanchard and Solow felt compelled to argue against the students. Now, I would like to connect this with what I've heard from former student of yours. They maintain that while you were very well-known as a critical mind arguing mostly from a Keynesian or Post-Keynesian standpoint in your teaching and in examining students you were very strict that people should know mainstream theory. Is it true, and if so, what was your philosophy behind this?

K.W. Rothschild: There are two issues here. First, I taught mainstream economics because I think that neoclassical theories, like other theories, are an essential part of economic knowledge. One should know these things. Even if one does not like them one should know them because for some problems it is a very useful theory. Second, it was Joan Robinson who said that you should learn neoclassical economics because only then you can show what its mistakes are. But this is only of secondary importance. Of course, I can be attacked somehow that I spent too much time on these theories. During my tenure at the University of Linz we probably committed also the mistake of other universities to neglect the study of the history of economic thought.

Nevertheless, as I said before, the bitter attacks against the economic mainstream you mentioned before were not so much directed against neoclassical theory as such, but against the way it is used to monopolize the discipline. Just look at the publishing policies of large mainstream journals. They prefer to publish papers which are based on mainstream methods. Then you have very good journals that don't follow that policy and they are mostly considered and classified as being of secondary importance at best. Actually, Galbraith is another good example in case. In the profession he has always been regarded more as a freak and not so much as the good economist he was, just because he didn't always use the methods which are taught by the mainstream and refused to talk and write in the established academic fashion.

The French students touched here obviously an important point because, as you said, some very famous economists joined the debate. They wouldn't have done that otherwise. But even within the defenders of the mainstream there are differences as well. Take Solow for instance. He joined the debate with the intent to defend neoclassical theory, but at the same time he has written the famous book with Frank Hahn, where he heavily criticized its use in modern macroeconomics.³ So, he obviously wants to preserve the neoclassical method, but he opposes its sometimes unwarranted use, and I would agree with

²K.W.Rothschild (1942). A note on advertising. *Economic Journal* 52, 112-121.

³Hahn, F., Solow, R. (1995). *A critical essay on modern macroeconomic theory*. Oxford, Blackwell Publ.

him on that. The French students were quite fair I must say. They didn't say neoclassical or more generally mainstream economics should be abolished altogether; they said that they wanted it to be part of a wider, pluralistic view. I think that this is a sensible proposition. I don't necessarily include Marxist theory which probably would be to expect too much, even though it should be part of such a wider view. If you consider that lately even the Financial Times Germany has come to recognize Marx' analysis of economic development and the development of monopoly, then this request of mine is probably not too far fetched.

Question: I didn't know that the Financial Times has started using Marxian theory for its analyses. I fancy the idea that it was probably Groucho Marx they had in mind. Let me refer to your recently published book "Die politischen Visionen grosser Ökonomen" (The political visions of great economists).⁴ I read its introductory chapter as a plea for a revival of political economy in economic research, economic thinking and teaching. You quote Schumpeter's seminal *History of Economic Ideas* where he ranked the study of history before the use of statistics (or econometrics nowadays), before theory as a way to develop economics and study the economy. Is this a possible alternative programme to what we are confronted with today, where the ranking goes exactly the opposite direction? To use Schumpeter's terminology, what do you think would be an appropriate box of tools a modern, young critical economist needs?

K.W. Rothschild: You know that I'm no longer in the teaching business for quite some time now. But I would say that there is no need to give general prescriptions on how economics should be taught. It could be just different from place to place. Ideally students would go to universities where the curriculum stresses certain points they are interested in. To a certain extent you have that already with departments specialising in business economics and others being focused more on theoretical economics. Around the beginning of the last century if you wanted to study the best of theoretical economics there were just a handful of places to go. There was Stockholm, there was Cambridge, there was Vienna and there was Chicago. The problem nowadays is that we have such a uniform teaching. The text books look more or less all the same and other things are neglected. So teaching could be and should give an overview of several theories but then each university could concentrate on its own focus.

Question: Do you think it is possible to pursue a programme of teaching and research that puts its

emphasis on scope and the grand view rather than a narrow specialization and relatively minute technicalities?

K.W. Rothschild: I don't think you can have an overarching theory. The old idea was of course that you study first micro and macro theory and then you are an economist and you can specialize. I would still think that of course such introductory lectures are important but they should be supplemented with the study of the history of economic theory. The problem is not so much whether the basic lectures should be abolished, but the lectures should show at a very early stage that the theories are very much simplified pictures of reality and that you can have several such pictures. Students should be given some idea what the practical problems are and what the value of these theories is to deal with them.

Question: To which extent do you think does the organisation of economics and of the academic disciplines and the predominance of the mainstream affects its political relevance? It seems economics has forgotten the lessons of the 1920s and 1930s, as well as the ideas that were developed to solve them. Is this the reasons why we commit the same policy mistakes today? For example in Germany economic policy has developed and follows prescriptions which are quite similar to the catastrophic policies of the 1930s. To which extent does academic economics affect economic policy? How did this happen and how do you think could that be corrected?

K.W. Rothschild: You see, when the economic crisis of the 1930s happened mainstream economics of the time - I wouldn't call it neoclassical though - was so obviously wrong. During the crisis of the 1930s in Germany for instance prices and wages were reduced by law. The idea was that if everything was cheaper then the economy would recover. The following anecdote captures the state of economics at the time as well: At a seminar at the LSE in the midst of the depression Hayek stated that consumption was harmful to long-term investment. He based this on Böhm-Bawerk's capital theory. So, Kaldor raised and asked Hayek whether he really thought that if he would buy a winter coat today he would harm the economy. Hayek flatly replied that this was what he thought. I hope this anecdote is true, but I can't guarantee it. Nevertheless, it gives a good idea about the obvious failure of economists to come to terms with the reality of depression. The way countries tried to get out of this depression was completely wrong. Economists just had no suitable macroeconomic theory. They didn't see the macroeconomic relationships. Only after some time Keynes, Kalecki and Föhl (in Germany) realized that another

⁴Kurt W. Rothschild (2004). *Die politischen Visionen grosser Ökonomen*. Bern: Stämpfli, 218pp., ISBN: 3-7272-9641-0.

access to the problem was needed. As a consequence Keynesian theory developed and found its way into textbooks in the forties and fifties and the teaching of Keynesian theories became quite dominant. This was the new mainstream of the time. So, why is it then that general equilibrium theory is fashionable again? Partly, this has to do with the fact that the profession relied too much on one theory that did no longer apply fully as things changed. This was not so much true for Keynes as for Keynesian theory. Keynes had really two theories: one for the economy in depression and one under the state of full employment. But he did not bother about the latter and the Keynesians thought that Keynes' General Theory could be applied all time. This led to difficulties, especially when unemployment and inflation rose together in the 1970s. This was the big time for the Chicago people who had never liked Keynes anyway. They started to reintroduce microeconomic explanations for macroeconomic problems jointly with a vision of a perfectly working market. They allowed for frictions, fair enough, but eventually, they established that we live in a Panglossian state, i.e. in the best of all worlds. There are no options available. If you have this picture, then the free market is ideal. Therefore, this new macroeconomic theory was an ideal ideological foundation for all people who are

benefiting from a free, i.e. unregulated, market. It spread from Chicago into the big U.S. think tanks like the Cowles Commission and from there it fed back into university research and became the mainstream. But the moment such a theory is accepted as mainstream and taught to students, you have an enormous investment in human capital which most people of course do not want to loose. An American paper recently reported that now economics students spend too much time to learn mathematics and have no time to learn economics any longer. I think that's not quite true but certainly partly true. And once you have a fairly developed theory, then you always see the reality through these glasses. From this then spring the difficulties to develop new approaches to economic policy.

Question: So it leads us directly to the last question: in your view, what can save economics or what can make it more relevant? Or to put it in a slightly more provocative way: does economics need to be saved by heterodox economists?

K.W. Rothschild: Yes, I think what you are doing and in doing this interview helps to change things little by little.