

History of economics

Material:

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[Présentation PowerPoint](#)

Course objectives

1) Better understanding of modern economics through studying the historical evolution of economic ideas, concepts and methods. We will read and talk about the works of such influential economists as Adam Smith, Karl Marx, John Maynard Keynes or Milton Friedman. This knowledge will help you to

- better understand contemporary economics
- see how economic knowledge develops through interaction of its internal logic and the impact of external factors (such as big crises or developments in other disciplines)
- realize that there are various economic schools, which offer competing explanations of economic phenomena

2) To develop some practical abilities:

- cooperation (preparing a presentation in a team)
- speaking and discussing the assigned readings in the class
- writing an early academic essay (course paper) – an exercise before writing your diploma thesis

What is economics?

- Lionel Robbins defined economics as: the science which studies human behaviour as a relationship between ends and scarce means which have alternative uses”
- “Economics is what economists do...” — Jacob Viner
- American Economic Association:
 - “It’s the study of scarcity, the study of how people use resources and respond to incentives (ösztönzők), or the study of decision-making. It often involves topics like wealth and finance, but it’s not all about money. Economics is a broad discipline that helps us understand historical trends, interpret today’s headlines, and make predictions about the coming years.”
- <https://www.aeaweb.org/resources/students/what-is-economics>
- This course traces the evolution of economics from the ancient times when economics was a modest **art of household economic management** to the modern period when economics is a **prestigious rigorous social science explaining and predicting human behavior in almost all social settings**

The current state and position of economics

(based on Fourcade, M., Ollion, E., & Algan, Y. (2015). The superiority of economists. *Journal of Economic Perspectives*, 29(1), 89-114.)

- Colander (2005) found that 77% of economics graduate students in elite programs agree with the statement that “economics is the most scientific of the social sciences.”
- Richard Freeman (1999, p. 141) : “[S]ociologists and political scientists have less powerful analytical tools and know less than we do, or so we believe. By scores on the Graduate Record Examination and other criteria, our field attracts students stronger than theirs, and our courses are more mathematically demanding.”
- At first glance, the academic labor market seems to confirm the natives’ judgment about the higher status of economists.
- They are the only social scientists to have a “Nobel” prize, thanks to a grant from the Bank of Sweden to the Nobel foundation.
- Economists command some of the highest levels of compensation in American arts and science faculties according to Bureau of Labor Statistics data

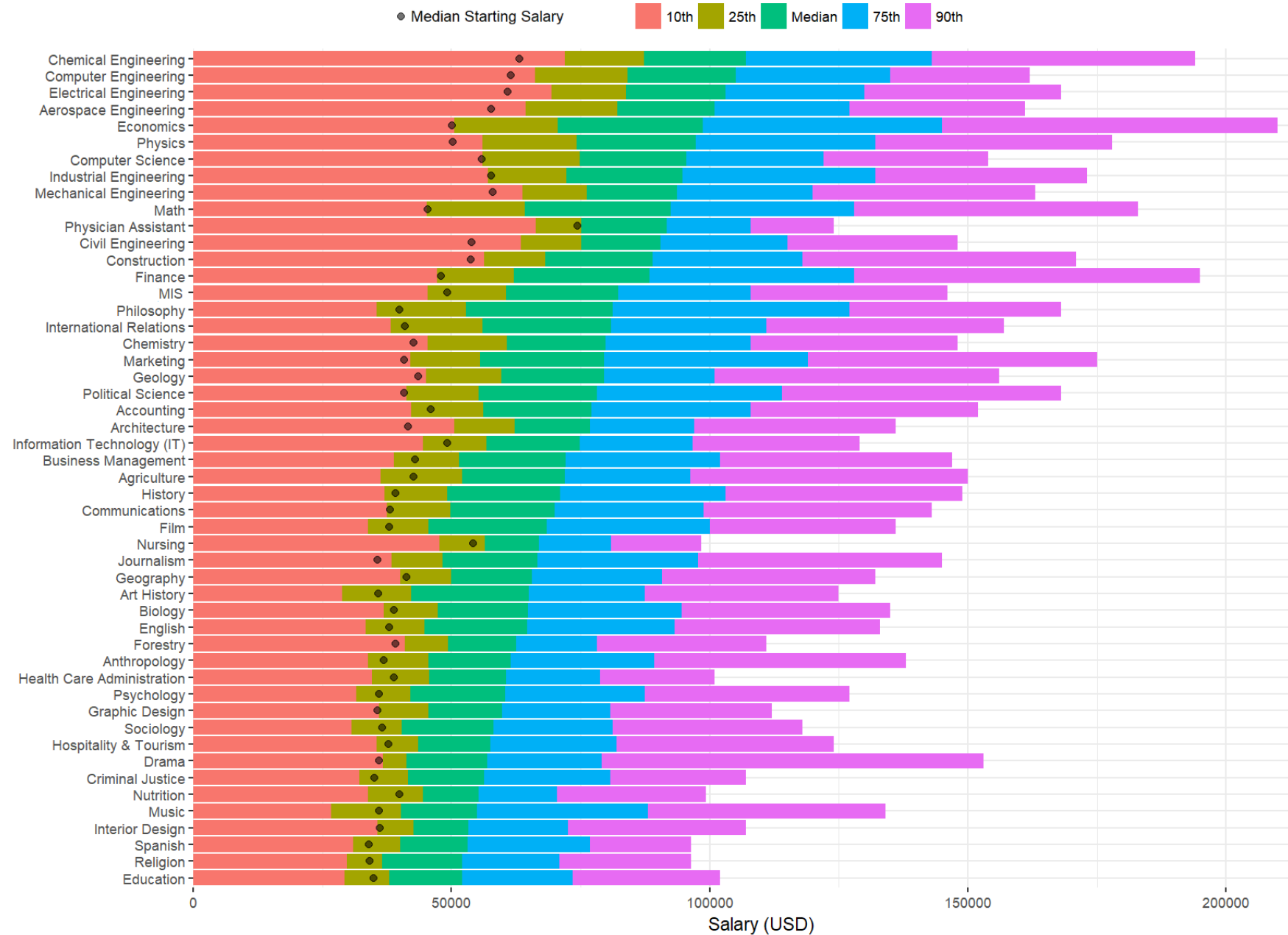
“Nobel Prize” in Economics

- https://en.wikipedia.org/wiki/List_of_Nobel_Memorial_Prize_laureates_in_Economic_Sciences

- Amartya Sen

[Amartya Sen - Wikipedia](#)

Salaries of graduates by different disciplines, US, 2018
<https://www.visualcapitalist.com/visualizing-salaries-college-degrees/>



The current state and position of economics, cont.

(based on Fourcade, M., Ollion, E., & Algan, Y. (2015). The superiority of economists. Journal of Economic Perspectives, 29(1), 89-114.)

- Economics occupies a unique position among academic disciplines. It is characterized by:
 - far-reaching scientific claims linked to the use of formal methods;
 - the tight management of the discipline from the top down;
 - high market demand for services, particularly from powerful and wealthy parties;
 - and high compensation.
- This position of social superiority also breeds self-confidence and dominance over other social sciences
- While the imperialistic expansion of economics into aspects of social science that were traditionally outside the economic canon has spurred some engagement with non-economics scholarship, the pattern of exchange remains deeply asymmetrical, causing resentment and hostility in return **(example)! Having children as a social issue**
- Economists dispense their expertise on practically all matters of **public policy** and have made steady gains in business and government, often in top political positions
- Finance ministries, central banks, government agencies, international organizations, and dominant consultancies harbor large concentrations of professionally trained economists, who claim tutelary power over “the economy”

Topics to be covered

- Pre-classical economics (VIII c. BC -1776 AD)
 - (ancient Greece, physiocracy, mercantilism)
- Classical Economics (1776-1870)
 - Adam Smith, David Ricardo, John Stuart Mill;
 - Reaction to classical economics – K. Marx
- Neoclassical economics (1870 - ca. 1930)
 - Alfred Marshall, Leon Walras
 - Empirical vs theoretical economics
 - Interwar pluralism (institutionalism, historical school, Austrian school)
- Modern economics (ca. 1930s – today)
 - Formalist revolution, mathematization, hardening of the mainstream
 - Marginalization of the non-neoclassical schools
 - Economic imperialism
 - The return to moderate pluralism in recent years (emergence of behavioral economics, complexity economics, computational...)
 - Modern economics in the face of the Great Recession of 2008

Economic ideas and concept we will discuss

- Motivations of economic agents (consumers, producers): self-interest vs other motivations
- Individual well-being: utility, happiness, income
- Supply, demand, exchange and setting of market prices
- Market equilibrium and disequilibrium
- The behavior of firms
- Economic fluctuations, business cycles and unemployment
- Inflation and monetary policy
- Economic growth and its determinants
- Economic inequalities in income and wealth – determinants and consequences
- Capitalism vs socialism and other theoretical economic systems
- Innovations and technological progress – causes and results
- For example, with respect to economic growth ...

The importance of economic growth

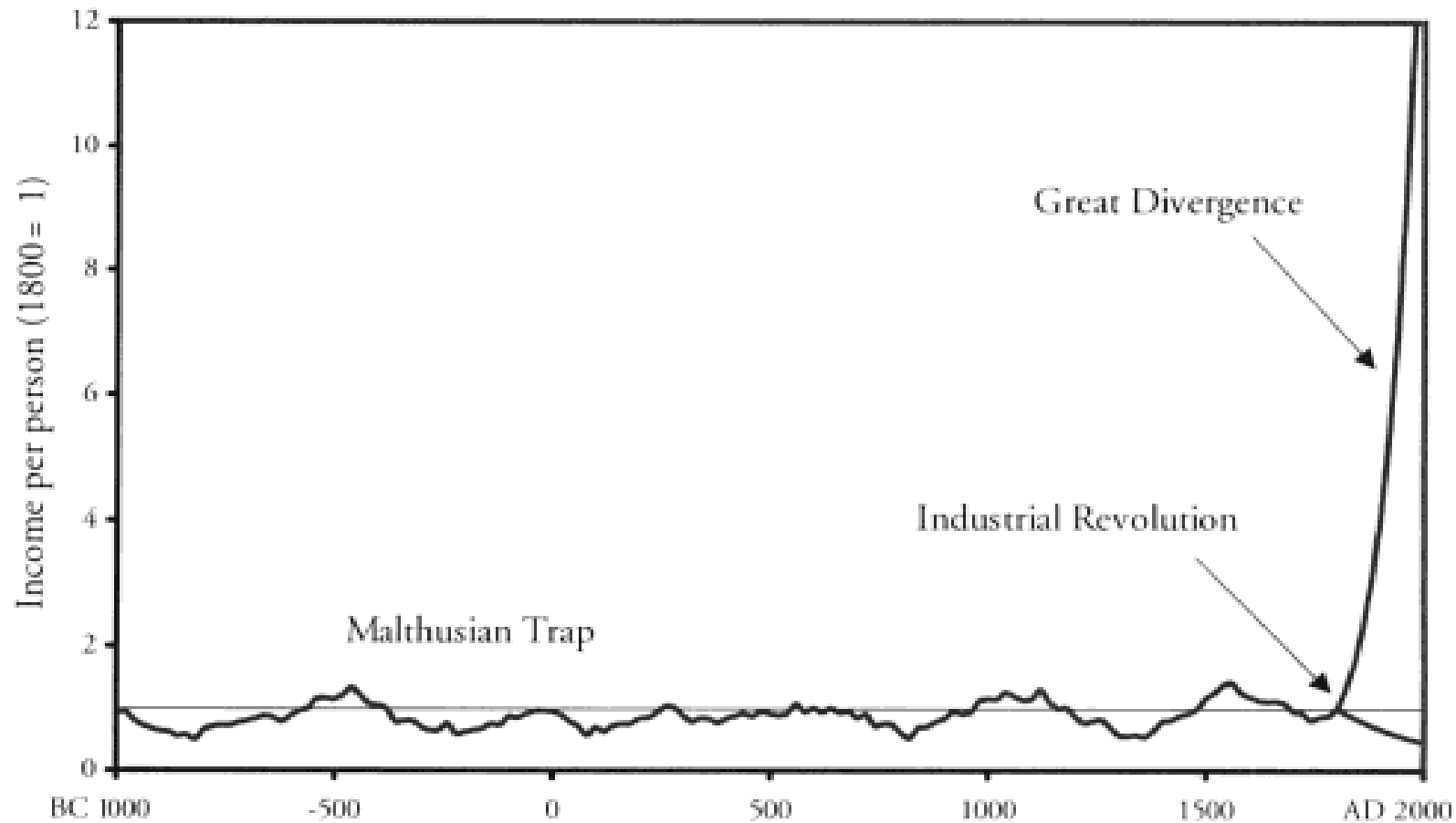


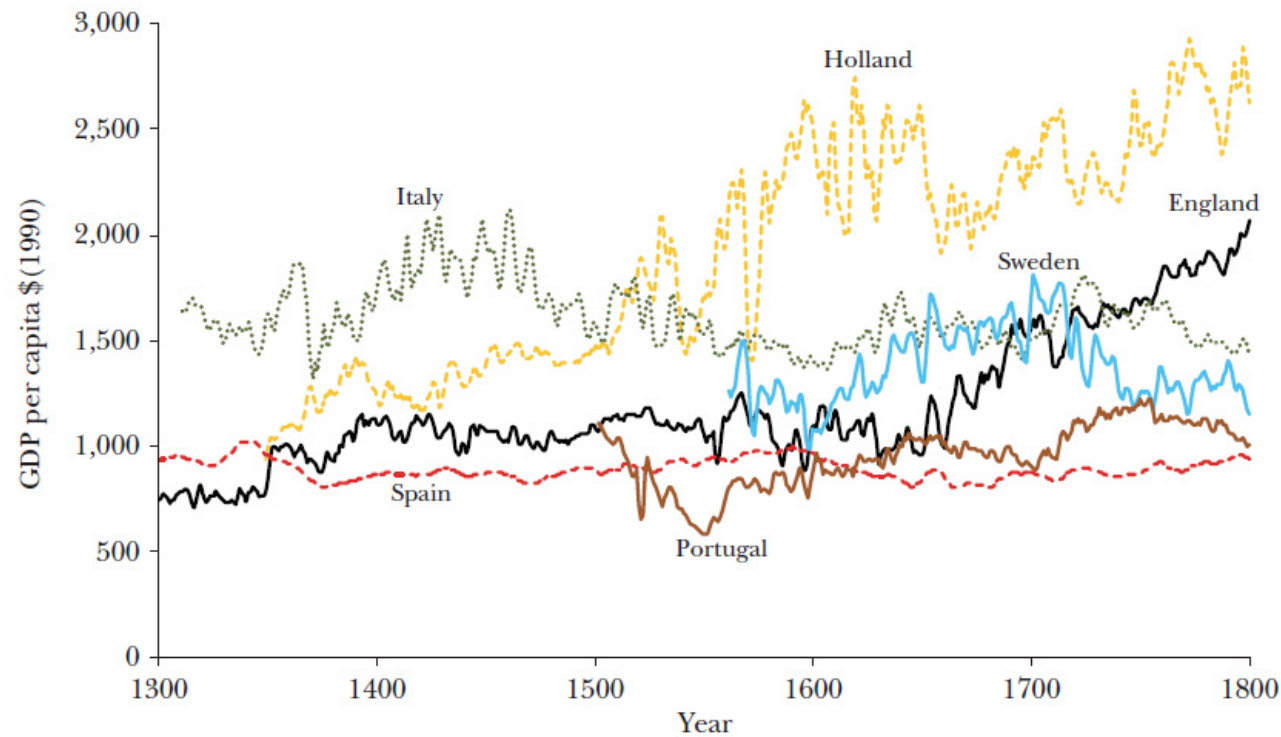
Figure 1.1 World economic history in one picture. Incomes rose sharply in many countries after 1800 but declined in others.

Fouquet, Roger, and Stephen Broadberry. "Seven centuries of European economic growth and decline." *The Journal of Economic Perspectives* 29.4 (2015): 227-244.

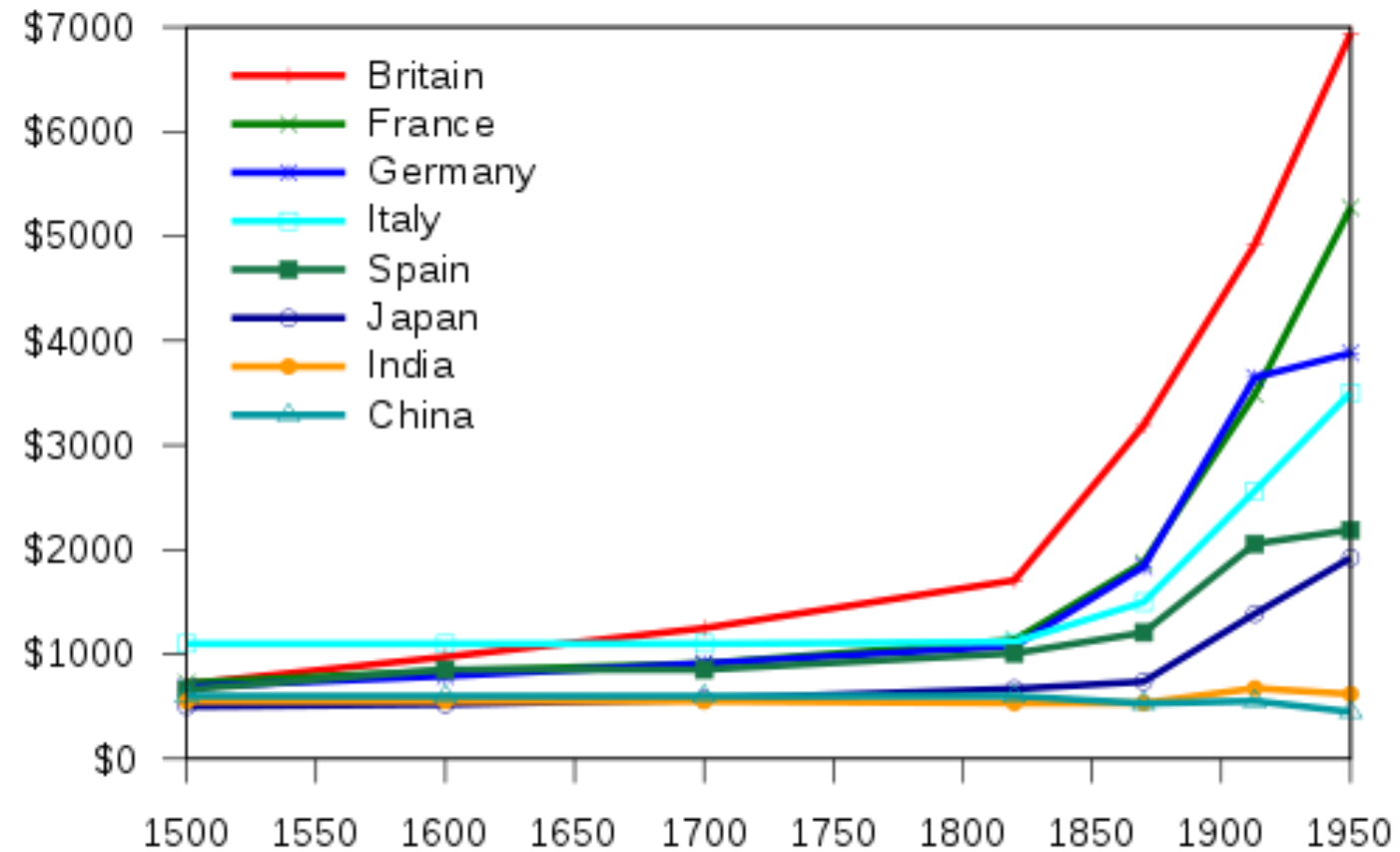
Figure 1

GDP per Capita in Selected European Economies, 1300–1800

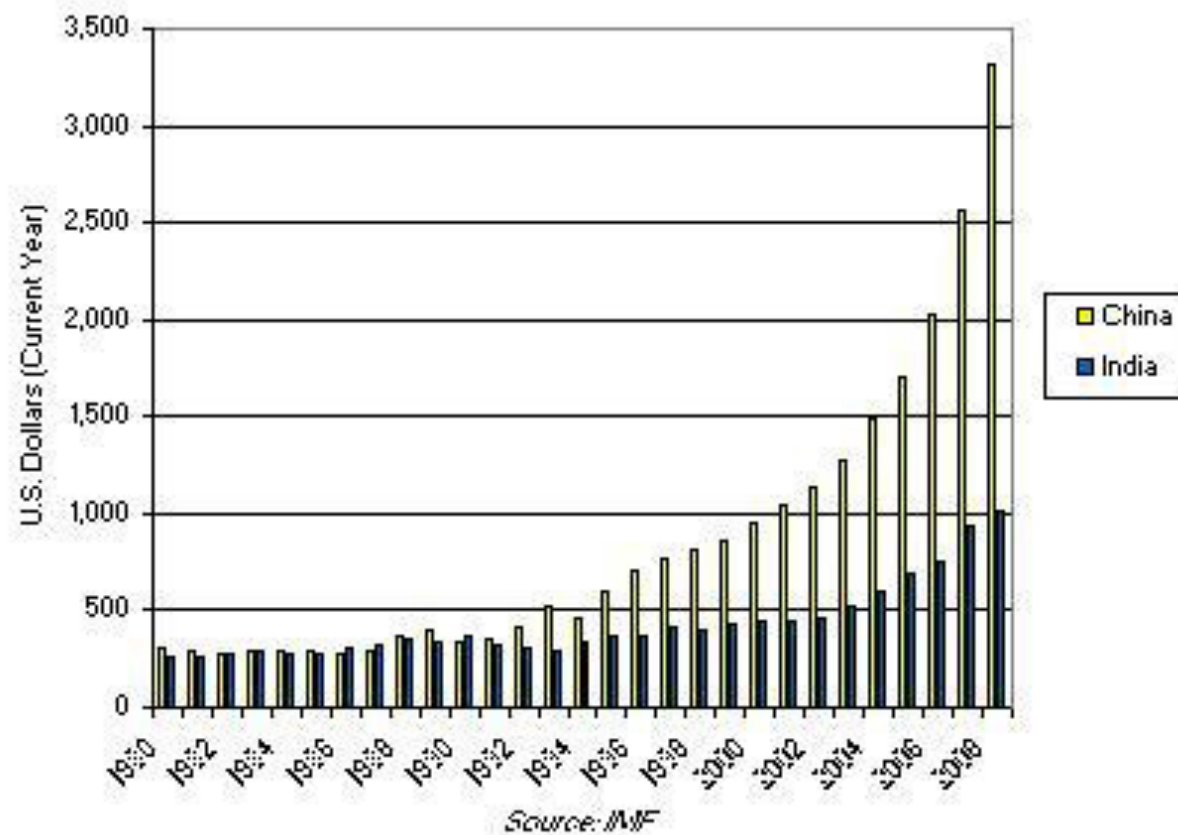
(three-year average; Spain eleven-year average)



Great Divergence

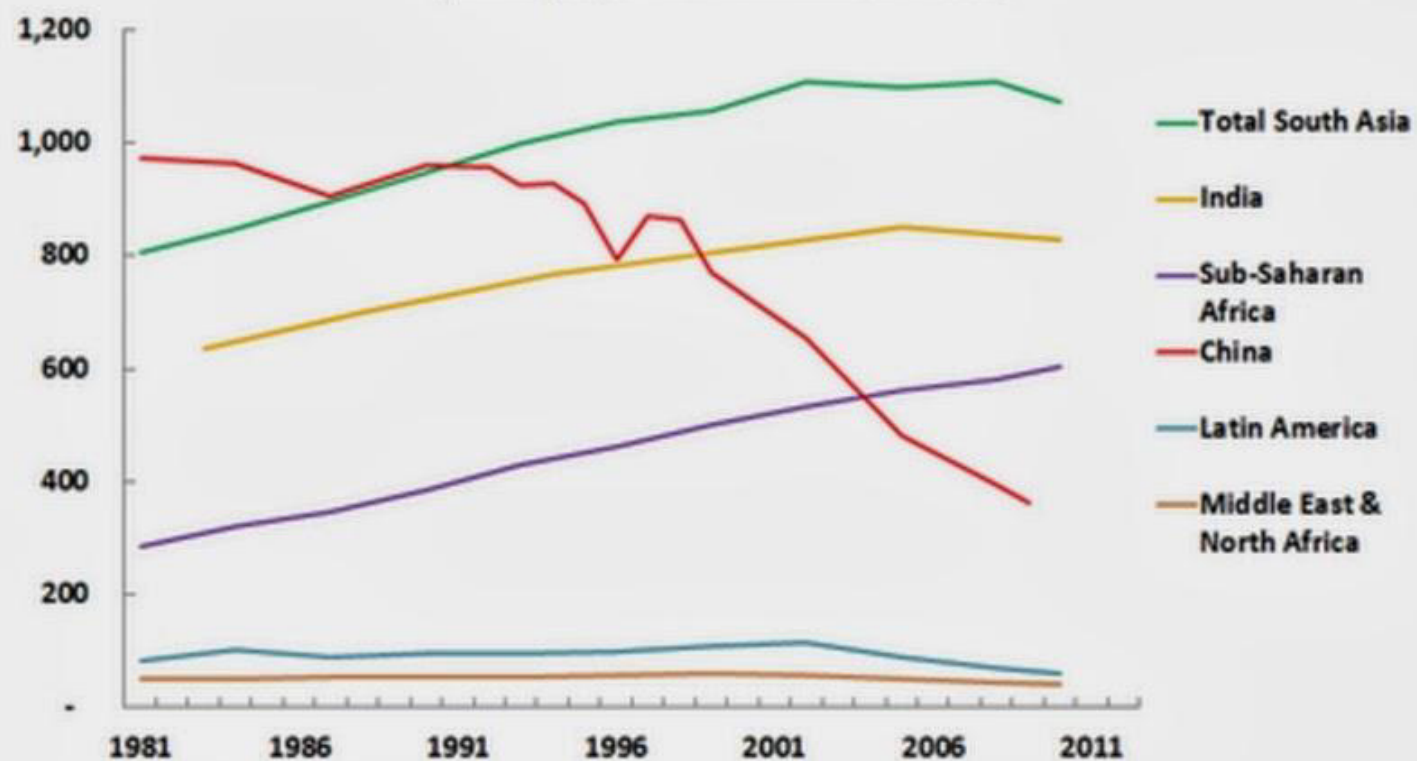


Per Capita Gross Domestic Product for China and India,
1980-2008



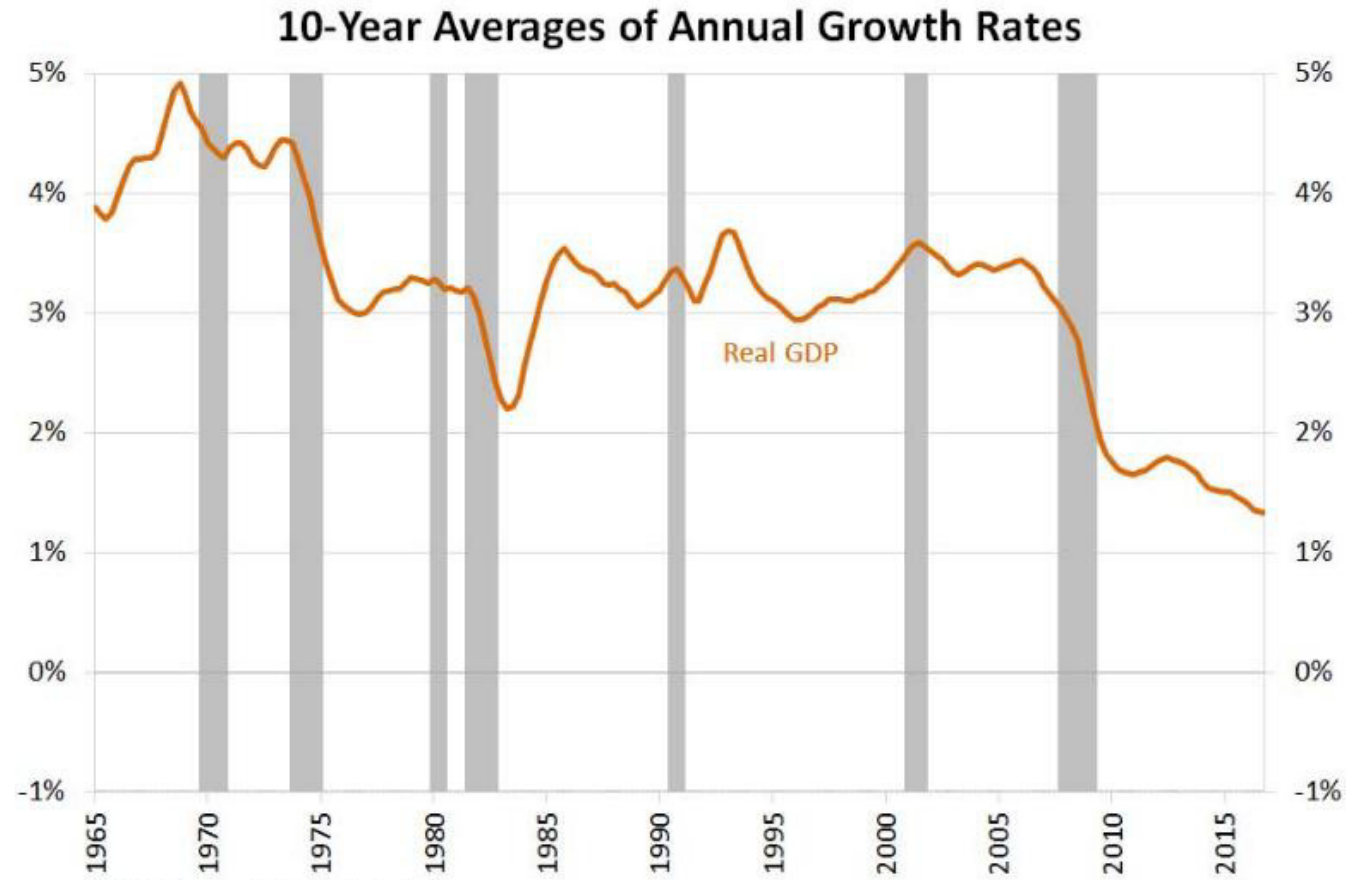
Number of People Living on Expenditure of \$2 a Day or Less

(million people - income measured in PPPs)



Source: Calculated from World Bank World Development Indicators

Economic growth is slowing down in advanced countries



SOURCE: Bureau of Economic Analysis.

FEDERAL RESERVE BANK of ST. LOUIS

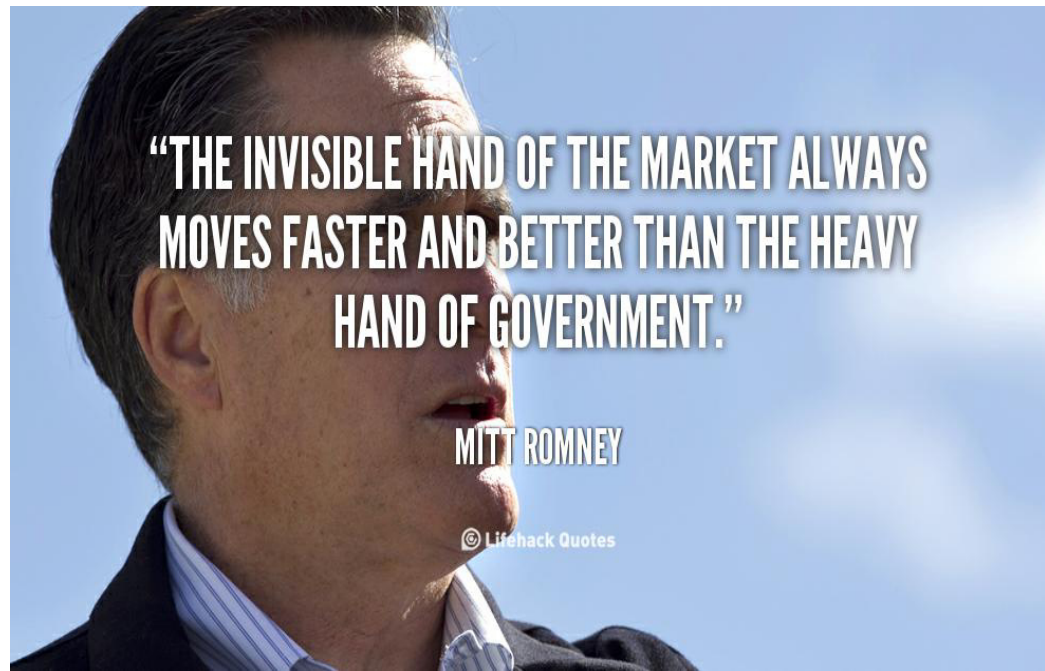
- So, maybe growth is the most important economic idea, but other questions are also important ...

What is the invisible hand of the market?



The invisible hand

... by directing that industry in such a manner as may be of the greatest value, [the merchant] intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention. Nor is it always the worse for society that he was no part of it. ... Adam Smith, *Wealth of Nations*, 1776, p. 456.

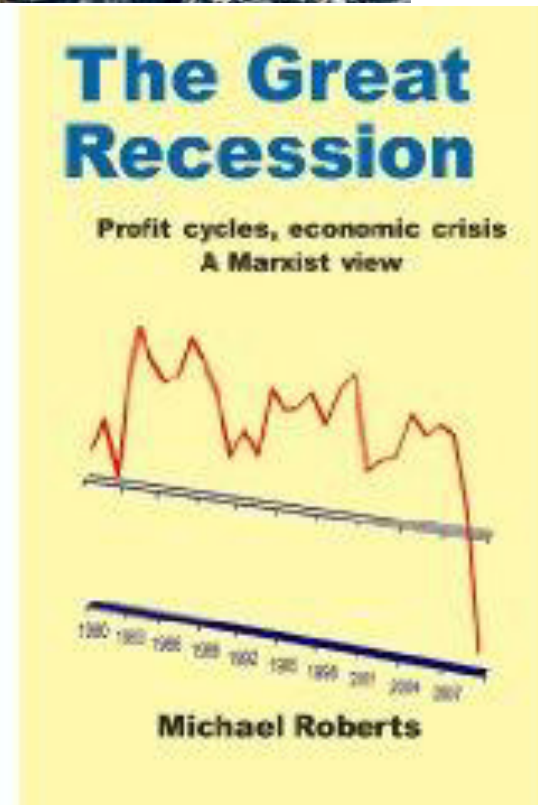
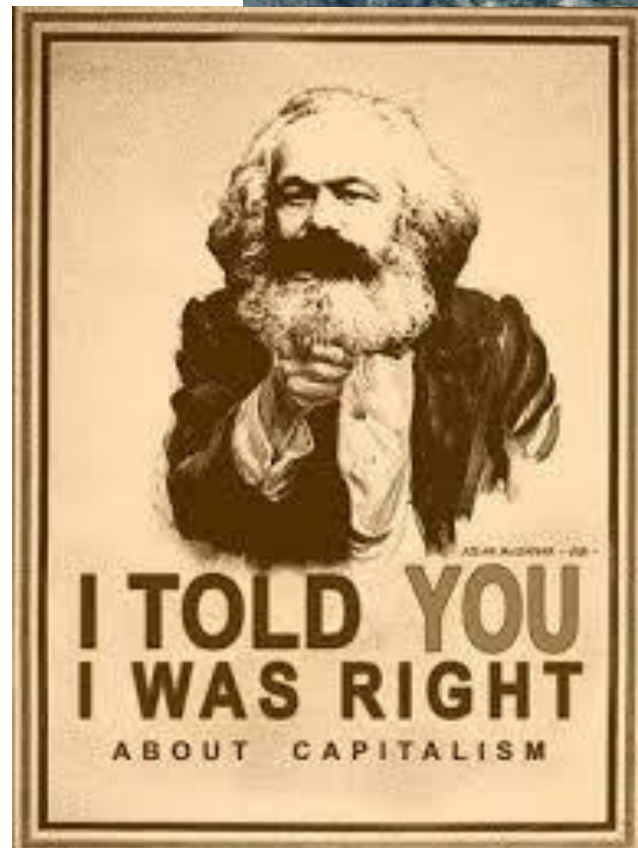


"THE INVISIBLE HAND OF THE MARKET ALWAYS MOVES FASTER AND BETTER THAN THE HEAVY HAND OF GOVERNMENT."

MITT ROMNEY

© Lifehack Quotes

Is capitalism doomed to fail?



Why economics has become a mathematical science?

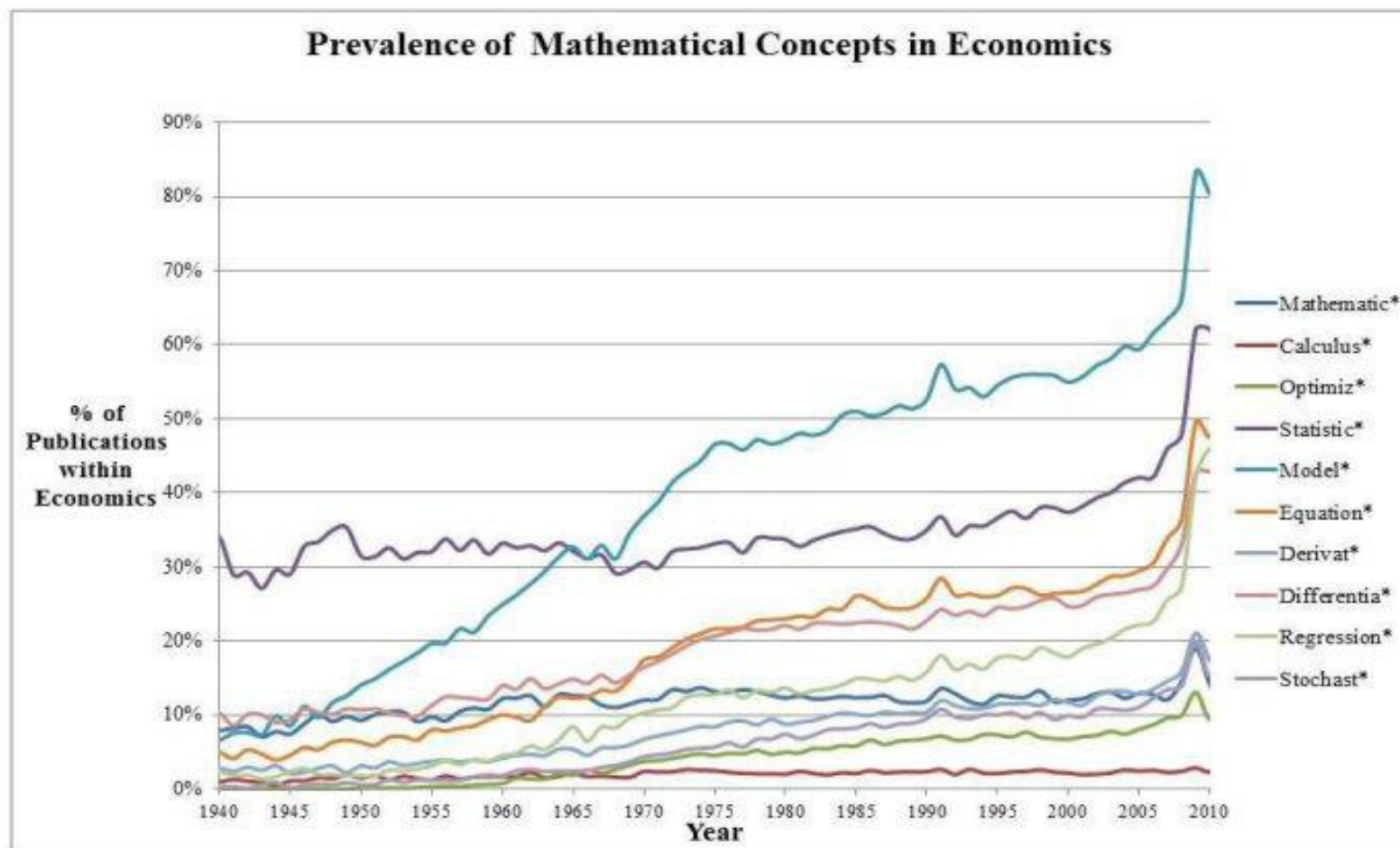
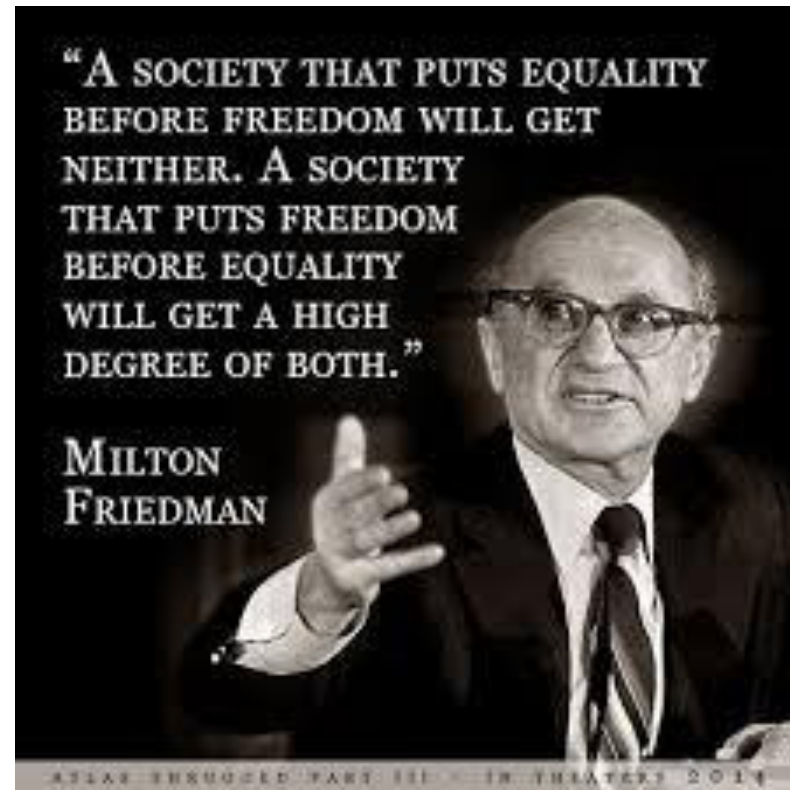
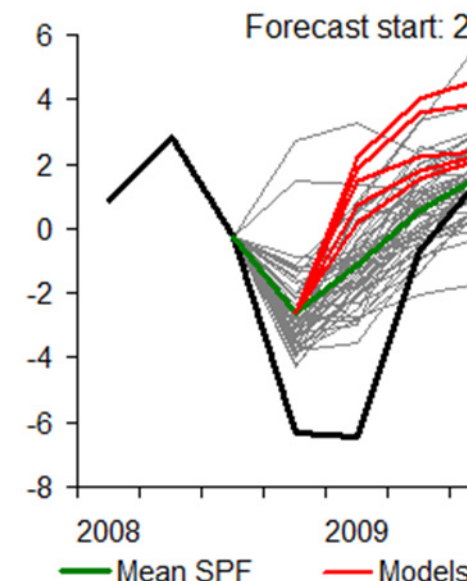
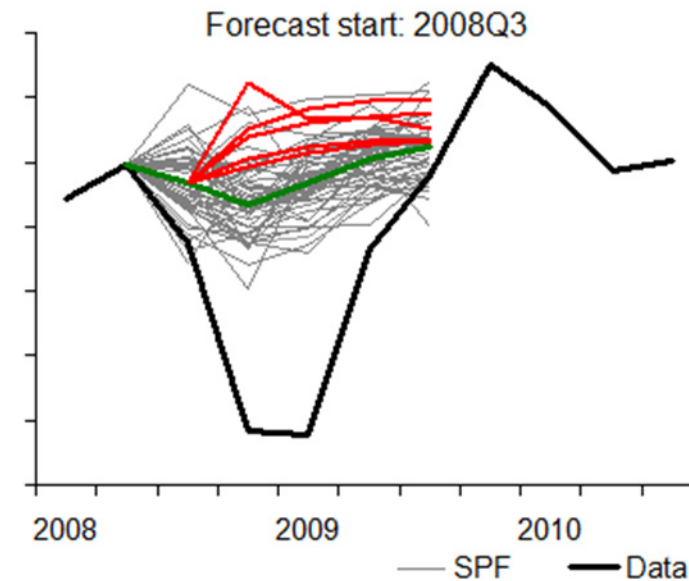
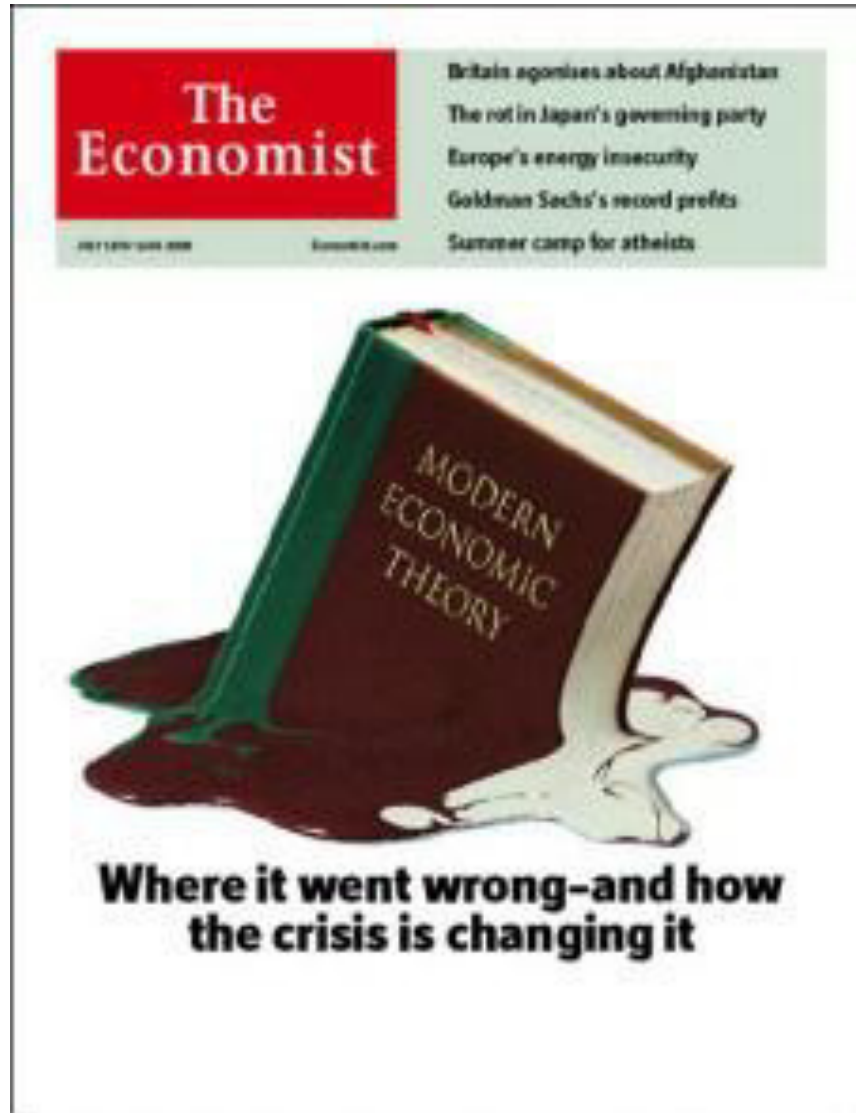


Figure 7. Prevalence of different mathematical concepts within Economics, measured by percentage of all articles meeting the relevant search criteria on an annual basis from 1940 to 2012. Following a reference line at 1990 from top to bottom are Model*, Statistic*, Equation*, Differentia*, Regression*, Mathematic*, Derivat*, Stochast*, Optimiz*, and Calculus*.

Are free markets the optimal solution for all socio-economic problems?



How Did Economists Get It So Wrong?



Can you explain the crisis to the Queen?

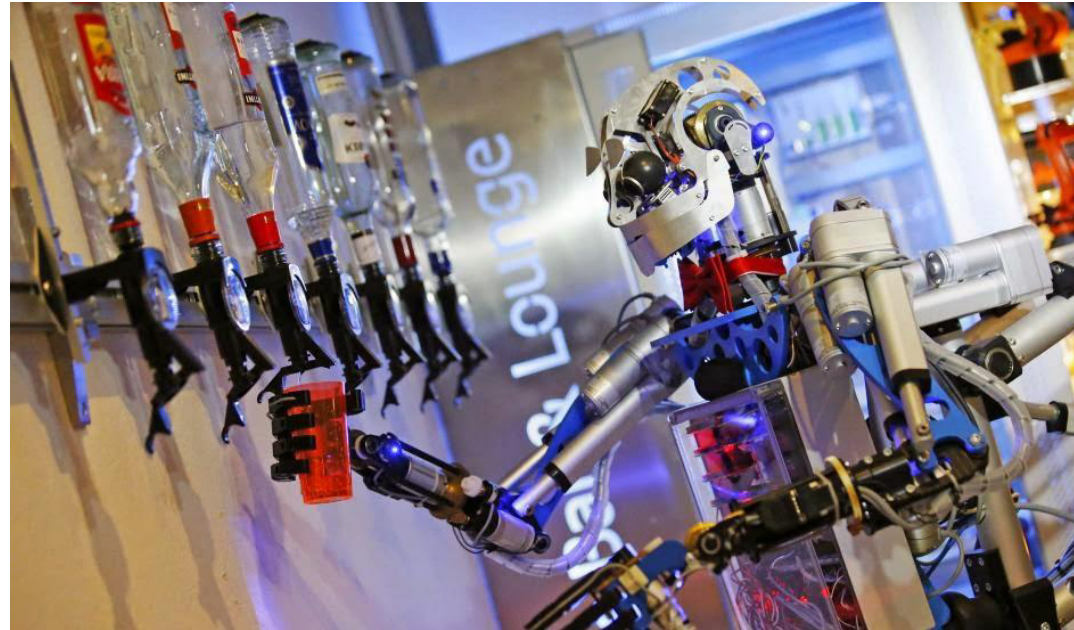
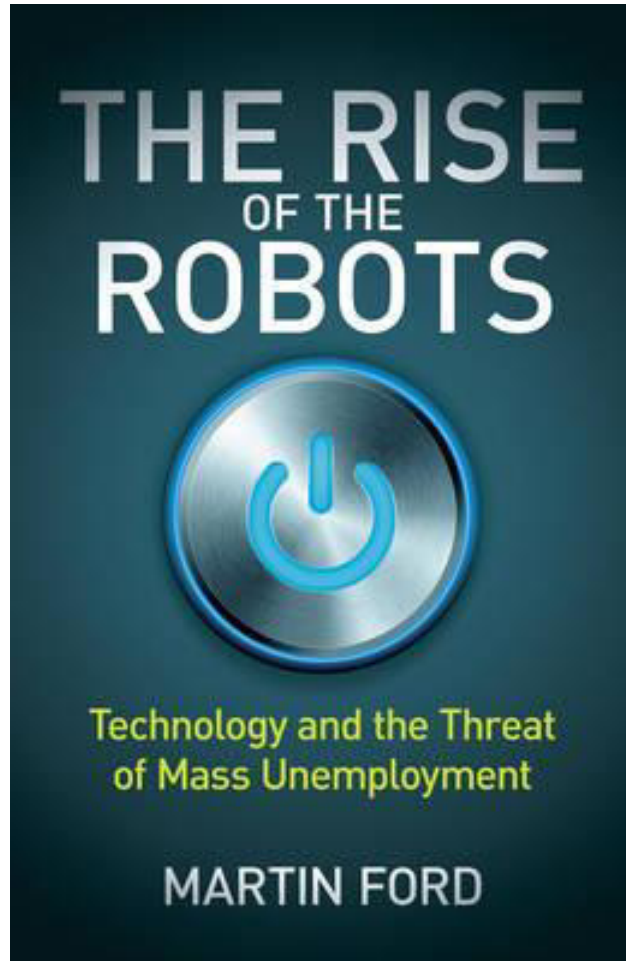
The Queen asked why no one had predicted the credit crunch. Can you answer her question?



Did Keynes get it right? Do we need active government policy to prevent and fight business cycles?



Are the robots coming for our jobs?



Practice 1.

Adam Smith

(427) Adam Smith: The Grandfather Of
Economics - YouTube

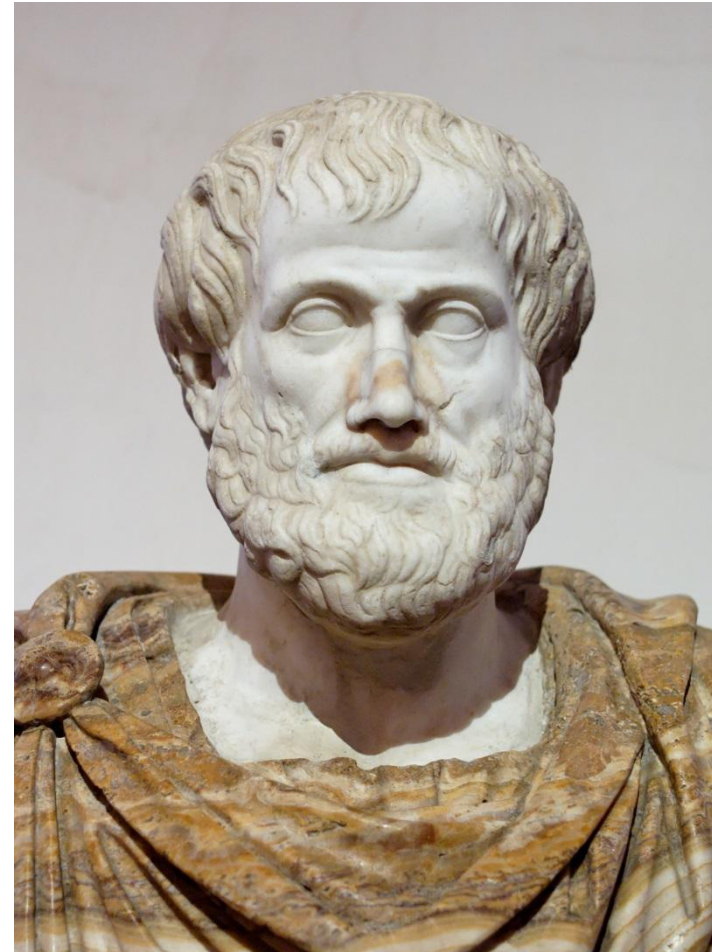
Questions to be answered

1. What was the cause of Smith's book?
2. Zero-sum game? What does it mean?
3. What are the most important views on economy of mercantilism?
4. What is ,value-added'?
5. What was the main idea behind industrial revolution?
6. What is ,capital" according to Adam Smith?
7. What is the problem with land?
8. What is the idea behind building factories?
9. What has to do with service-based economy?
10. Why do we need specialization?
11. What are the problems with Smith's ideas?

2. class

Aristotle (384 BC – 322 BC)

- Was a Greek philosopher, but worked also on logic, mathematics, natural sciences, ethics, politics and economics
- Was a student of Plato in Athens
- Had a profound influence on St. Thomas Aquinas
- Has some influence on modern economics



Pre-classical economics (Ancient Age, Middle Ages)

- Non-formal analysis of the economy (pre-analytical)
- Non-systematic studies
- No grand analytical economic systems; no big, general theories
- Focus on non-market mechanisms of allocation (force, authority , power, tradition)
- Focus on justice (not on economic efficiency)
- Very slow change in economic conditions of social life
- People are rather self-sufficient, not dependent on markets
- Economic thought not interested in markets
- Economics not separable from other activities (like philosophy)
- Economics dominated by ethical considerations

Aristotle's works

- Our course reading includes excerpts from *Politics* and *Nichomachean Ethics*
- Economic problems discussed:
 - Nature of economics, place within other sciences
 - Household management (oeconomicus)
 - Art of wealth acquisition (chrematistics)
 - Private property vs. communal property
- Other problems that we do not discuss
 - Justice; reciprocity in exchange

The place of economics within sciences

- 1) Politics is the science about the origin and functions of a state
- 2) The state is made up of households
- 3) The art of the management of the household is economics (oeconomicus)
 - Therefore, because of 1), economics belongs to the science of politics

What is economics?

- Economics is the science (or art) of household management
- The person managing the household (hh head) has to master the relations between:
 - Master and servants (slaves)
 - Husband and wife
 - Father and children
- Also a question arises if another art – the art of wealth getting – belongs to economics?

Economics vs. chrematistics

- The science of wealth getting (acquisition) is *chrematistics*
- Examples: fishing, hunting, bee-keeping, farming, barter trade, exchange with the use of money, usury etc.
- One kind of chrematistics by nature is a part of the management of a household (economics)
- This kind of chrematistics delivers things (food, clothes, tools, etc.) necessary to (good) life of a hh
- The amount of these things is limited (by the needs of the hh)

- Arisztotelész a **krematisztikát** a természetellenesnek tekintett, korlátlan, kizárólag pénzkeresésre irányuló gazdálkodás formájának nevezte, amely szemben áll a természetes, az emberi szükségleteket kielégítő, korlátozott vagyonnal rendelkező **oikonomiával** (háztartástan). Míg az oikonomia célja a javak előállítása és a háztartás jóléte, addig a krematisztika a pénz öncélú gyarapítását, a pénzgazdagságot, a haszonelvűséget hangsúlyozza, ahol a cél nem a termelés, hanem a pénz forgatása.

Natural vs. unnatural chrematistics

- So, the kind of chrematistics limited by the needs of the hh is *natural chrematistics*
- But, there is also another kind of chrematistics
 - „The origin of this disposition in men is that they are intent upon living only, and not upon living well; and as their **desires** are unlimited they also desire that the means of gratifying them should be without limit”
- While the natural chrematistics is „needed for the satisfaction of men’s natural wants” („needs”)
- Natural chrematistics = fishing, hunting, bee-keeping, farming etc., and also natural trade (barter exchange). Belongs to economics.
- Unnatural chrematistics = exchange with the use of money and usury. Does not belong to economics.

Aristotle on usury

- „The most hated sort [of unnatural chrematistics] is usury, which makes a gain out of money itself, and not from the natural object of it. For money was intended to be used in exchange, but not to increase at interest Of all modes of getting wealth this is the most unnatural”

Private vs. communal property

- Plato held that there should be common property of all things, at least among the members of the highest social class (philosophers-kings)

- Aristotle:

„But indeed there is always a difficulty in men living together and having all human relations in common, but especially in their having common property. The partnerships of fellow-travelers are an example to the point; for they generally disagree over everyday matters and quarrel about any trifle which turns up”

Conclusions

- According to Aristotle:
 - Economics belongs to politics
 - Economics is to be distinguished from chrematistics
 - Only one part of chrematistics belongs to economics
 - Unnatural chrematistics is excluded from economics
 - Usury is condemned
 - Private property has advantage over communal property
 - Self-restraint (fulfilling only needs, not desires)
 - Self-sufficiency as an economic ideal (vs growth in modern times)

What is the Sedlacek's proposal for modern world economy?

- Instead of the modern program of maxGROWTH or maxGDP, you should be...
 - „*targeting reasonable* levels of growth” and focusing on minDEBT
- Gross domestic product (GDP) is a monetary measure of the market value of all the final goods and services produced in a specific time period
- What do you think about this proposal?
- How to target a certain (lower) level of economic growth?
- What is a reasonable level of economic growth?

Does higher income lead to higher happiness? (1): Easterlin paradox

Easterlin, R. A. (1974). Does economic growth improve the human lot? Some empirical evidence. In *Nations and households in economic growth* (pp. 89-125). Academic Press.

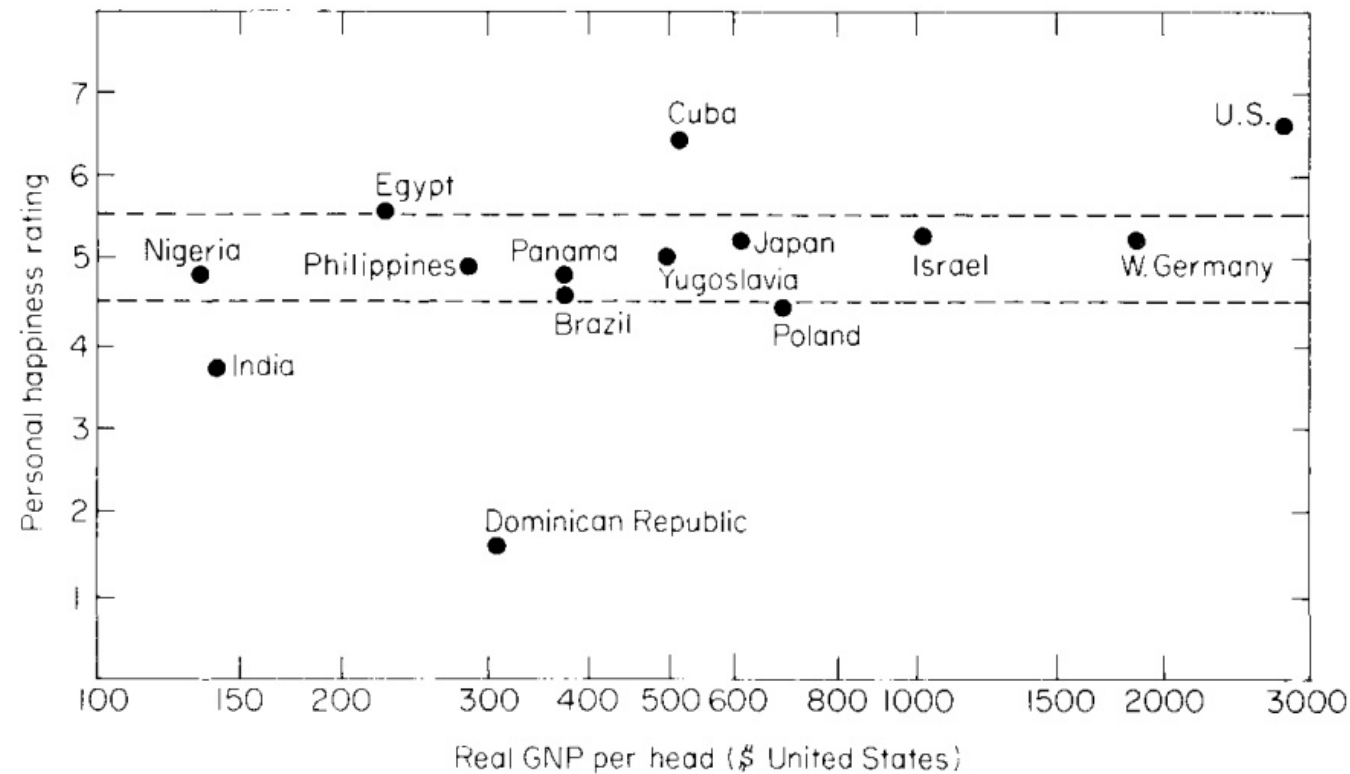


FIG. 1. Personal happiness rating and GNP per head, 14 countries, ca. 1960. (Source: Table 6.)

Do we need to reduce economic growth in order to avoid climate change?

Practice 2.

- [The Most Important Economic Schools of Thought | Economics Explained](#)

Questions to be answered

1. What is the key issue in economy?
2. Why is economics a diverse science?
3. What are the most important economical school?
4. What are the four questions that can be used to examine the differences and similarities between the various schools of economic thought?
5. What are the key ideas of the classical school? (Smith, Kant)
6. What was the reason for the establishment of the Austrian school?
7. What are the key ideas of the this school (Menger, Wieser)?
8. What was the most important critic against Austrian School?
9. What are the key ideas of Keynesian school?

explanation

- **The theory of consumer choice** assumes **consumers wish to maximise their utility through the optimal combination of goods** – given their limited budget.
- Understanding **marginal utility** is key to grasping consumer behavior and economic decision-making. It refers to the **additional satisfaction or benefit a consumer experiences when they consume one more unit of a good or service**.
- **Opportunity costs, also known as alternative costs**, are the potential benefits that are foregone if a decision is made in favor of a particular option and other alternatives are therefore excluded. They represent the value of the next best alternative that is not chosen.
- **Fiscal policy** refers to the **use of government spending and tax policies to influence economic conditions**, especially macroeconomic conditions. These include aggregate demand for goods and services, employment, inflation, and economic growth.

Why would we want to reduce the rate of economic growth?

- Environmental concerns?
 - Too much production leads to the depletion of natural resources, pollution, and emissions of greenhouse gases (climate change!)
- Human-related concerns
 - Focusing on desires (not on needs), working long hours, materialism, too much consumption – too little personal development and happiness, etc.

Idézetek Arisztoteléstől

1. Csupán a bölcsek véleményét kell megvizsgálnunk, mert a többiekkel, akiknek érveik nincsenek, csupán érzelmeik vannak, lehetetlenség érvelő beszélgetést folytatni.
2. Ha valaki azt kívánja elérni, hogy az emberek ne jogtalankodjanak, elegendő, ha barátságot teremt közöttük, igaz barátok ugyanis nem jogtalankodnak egymással. De akkor sem jogtalankodnak egymással az emberek, ha igazságosak. Az igazságosság és a barátság tehát vagy azonosak, vagy igen szoros kapcsolatban állnak egymással.
3. Az ember természeténél fogva társas élőlény.
4. Arra kell gondolnunk, hogy a boldogság nem a nagy vagyonon alapul, hanem a lélek jó állapotán.
5. Aki helyes felismerésekre vágyik, annak előbb helyénvaló kételyeket kell támasztania.
6. Azokat a dolgokat, amelyeket előzetes tanulás révén kell létrehozni, azokat éppen a létrehozó tevékenység révén tanuljuk meg: építőmesterré csak a házépítés - lantművésszé csak a lantjáték gyakorlása által válik az ember. S ugyanígy, ha az igazságos tetteket gyakoroljuk: igazságossá, ha a mértékletes tetteket: mértékletessé, ha a bátor tetteket: bátorrá leszünk.

7. Elragadtatni könnyű magunkat - ez mindnyájunk adottsága - , de az már nem könnyű - és nem is vagyunk mindnyájan képesek rá -, hogy arra haragudjunk, akire kell; annyira, amennyire kell; akkor, amikor kell; azért, amiért kell; és úgy, ahogy kell.

8. Élete során az ember gyakran attól fél, amitől nem kellene, vagy nem úgy fél, ahogy kellene, vagy nem akkor, amikor kellene.

quotes from Aristotle

1. We need only examine the opinions of wise people, because it is impossible to have a rational discussion with others who have no arguments, only emotions.
2. If someone wants to ensure that people do not treat each other unjustly, it is enough to create friendship between them, because true friends do not wrong each other. But even if people are just, they will not wrong each other. Justice and friendship are therefore either identical or very closely related.
3. Human beings are social creatures by nature.
4. We must remember that happiness is not based on great wealth, but on the good state of the soul.
5. Those who desire correct insights must first raise appropriate doubts.
6. The things that must be created through prior learning are learned precisely through the activity of creation: one becomes a master builder only by building houses, and a lutenist only by practicing the lute. In the same way, if we practice righteous deeds, we become righteous; if we practice moderate deeds, we become moderate; if we practice courageous deeds, we become courageous.

7. It is easy to react emotionally—we are all capable of that—but it is not easy—and not all of us are capable of it—to be angry with the right person, to the right degree, at the right time, for the right reason, and in the right way.

8. Throughout their lives, people often fear things they should not fear, or do not fear things they should fear, or do not fear them when they should.