Econ 210a: U.C. Berkeley: January 20, 2010

First Class: In the Words of the Talking Heads: "How Did I Get Here?"

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January 11, 2010

How did we get here—me teaching and you taking a class in economic history during your first year in graduate school, a year otherwise filled with economic and statistical theory?

For the first class:

(1) Reading:

Read the following before the first class, and come to Evans 608-7 at 1 PM on Wednesday January 20, 2010 prepared to discuss them:

I. Growth and Development

- Paul Krugman (1999), "The Fall and Rise of Development Economics" http://tinyurl.com/20100105a.
- Tyler Cowen (2010), "Daron Acemoglu on the U.S.-Mexican Border" http://tinyurl.com/dl20100105h.

- Daron Acemoglu (2009), "What Makes a Nation Rich? One Economist's Big Answer" http://tinyurl.com/dl20100105i.

II. Macroeconomics:

- Narayana Kocherlakota (2009), "Some Thoughts on the State of Macro" http://tinyurl.com/20100105b.
- John Cassidy (2009), "Letter from Chicago," New Yorker (January 11), pp. 44-49 http://tinyurl.com/20100105c.
- Richard Posner (2009), "Honesty About the Stimulus," Atlantic http://tinyurl.com/dl20100105d.
- Robert Lucas (2009), "Why a Second Look Matters," Council on Foreign Relations http://tinyurl.com/dl20100105e.

III. Comparative Systems:

- Alex Tabarrok (2010), "Soviet Growth and American Textbooks" http://tinyurl.com/dl20100105f.
- David Levy and Sandra Peart (2009), "Soviet Growth and American Textbooks" http://tinyurl.com/dl20100105g. (Note: in some ways Levy and Peart inhabit a strenge alternate universe: Rose Wilder Lane, V. Orval Watts, and William F. Buckley were not and should never be called "libertarians"—well, maybe Wilder Lane, but only if you overlook her McCarthyite campaign against Lorie Tarshis...)

(2) Writing:

Write a 200-500 word essay on any of the three sets of readings, discussing whether in your view a knowledge or lack of knowledge of economic history is helping or hindering the economists who write and whose ideas are discussed in the readings. At least 18 hours before the first class—by 6 PM PST on January 19, 2010—email your paper (either in the message text or as an attachment) to delong@econ.berkeley.edu and post it as a comment on the webpage at http://tinyurl.com/dl20100105j.

You might, as you write your essay, think about one or more of the following questions:

1. Paul Krugman is certain that his "thin" model-based set of techniques would have been better than Albert Hirschman's techniques for trying to deal with the now-two generation ago "crisis in development economics." Is Paul correct?

2. Why is Daron Acemoglu so certain that Mexican growth would skyrocket if only somebody could, in Woodrow Wilson's words, "teach the Mexicans to elect good men"?

3. Why is Tyler Cowen so suspicious of Daron Acemoglu's certainty that Mexican growth would skyrocket if only somebody could, in Woodrow Wilson's words, "teach the Mexicans to elect good men"?

4. It is clear what Narayana Kocherlakota does not think modern macroeconomic theory is good for. As he writes: "Why do we have business cycles? Why do asset prices move around so much? At this stage, macroeconomics has little to offer by way of answer to these questions..." What does he think modern macroeconomic theory is good for?

5. In June 2007 the S&P Composite U.S. stock index closed at an index value of 1503 and a ten-year 5% coupon $1000 U.S. Treasury bond sold for $990. In March 2009 the S&P Composite U.S. stock index closed at an index value of 798 and a ten-year 5% coupon $1000 U.S. Treasury bond would have sold for $1170. Over that 21 month period investors in long Treasuries gained 23% (in real terms) while investors in diversified equities lost 45% (in real terms). Richard Thaler (and I) would say that this extraordinary divergence in the values of these asset collapses is the result of market irrationality: the unwinding of an "irrational exuberance" in which the risk tolerance of the market was

artificially elevated into an irrational pessimism in which the risk tolerance of the market was artificially depressed. John Cassidy quotes Eugene Fama as seeing no evidence for any form of market "irrationality" whatsoever: "Stock prices typically declne prior to a recession.... This was a particularly severe recession.... This was exactly what you would expect if markets are efficient.... I don't know what a credit bubble means. I don't even know what a bubble means. These words have become popular. I don't think they have any meaning." What are Fama's arguments that the enormous wheeling of asset prices between June 2007 and March 2009 is "exactly what you would expect if markets are efficient"? Why don't Thaler and I find Fama's arguments convincing? Why doesn't he find our arguments convincing?

6. In August 2009 Richard Posner attacked our own Christina Romer for saying that she believed for reasons that fiscal stimulus had already been effective in reducing the size of the recession: "her claim is that the stimulus had a dramatic effect on output and employment during that quarter. I do not think her analysis is responsible, and I am concerned with the fact that academic economists, when they become either public officials or public intellectuals (like Paul Krugman), leave behind their academic scruples..." In January 2010 John Cassidy quotes Richard Posner as saying that while he had never before "bothered to investigate [John Maynard Keynes's] The General Theory..." he now believes that it has "more of a grasp of what is going on in the economy" and believes that modern theoretical economics is a menace: "very mathematical... credulous about the self-regulating power of markets. That combination is dangerous." Reflect on Posner in the context of Saul of Tarsus on the road to Damascus, or perhaps of Martin Luther in the lightning storm--"St. Anne save me! I shall become a monk!"

7. For the brave who want to undertake extra reading. In 1983 Ben Bernanke published his still most-cited paper: Ben Bernanke (1983), "Nonmonetary Effects of Financial Crisis in the

Propagation of the Great Depression," American Economic Review 73:3 (June), pp. 257-76 http://tinyurl.com/dl20100105k. In this paper, Bernanke argued that the money stock is not a sufficient statistic for the determinants of nominal spending but instead that the capitalization and soundness of the banking system affects its ability to perform financial intermediation and has at times a powerful independent effect on nominal spending. In March 2009 Robert Lucas said that he did not understand this worry about an independent influence of the "credit channel" on nominal spending: "I avoided this bank bailout issue.... I don't really get it. Some of the problems you're talking about about deciding who gets paid and who doesn't, that's the whole function of bankruptcy law is to deal with that in an effective way. Now, it may be that the kind of neighborhood effects of the bankrupt banks are sufficiently different from the neighborhood effects of a bankrupt auto company -- that they need some kind of special treatment. But then it seems like the right public policy is something that -- maybe some kind of accelerated bankruptcy proceedings. Just to say make them well on all the money they've lost over this thing, I just -- I do not get it and I know of -- I don't know whether we're headed that way or not. I hope not.... Friedman and Schwartz have got a lot to tell us about the current situation..." Why do you think that Friedman and Schwartz's 1963 ascription in their Monetary History of the United States of the depth of the Great Depression exclusively to the collapse of the nominal money stock has had intellectual traction in a way that Bernanke (1983) apparently has not?

8. Why did so many economists retain their confidence that the USSR would in less than a generation catch up to the US in total GDP for so long?

January 11, 2010: 1294 words