The Trend of Economics: USA 1924

Heinz W. Arndt*

Tugwell, R.G. (ed.) (1924), *The Trend of Economics*, Alfred A. Knopf, New York.

In December 1922, a young assistant professor of economics at Columbia University took the opportunity of a meeting of the American Economic Association in Chicago to sound out colleagues about the idea of cooperating in a symposium on current and future trends in Economics. Each contributor should give and account of what seemed to him the main lines of development of economic theory and research. The outcome was a book *The Trend of Economics* (Knopf, New York, 1924) edited by R.G. Tugwell.

The twelve economists Tugwell had brought together included some of the best-known twentieth century American economists - Frank Knight (*Risk, Uncertainty and Profit*), J.M. Clark ("workable competition"), Paul Douglas (Cobb-Douglas production function), Morris Copeland (flow of funds), W.C. Mitchell (Business Cycles), George Soule (trade unions) Sumner Slichter (labour economics). All of them were relatively young, six under 35 and only three above 40. Tugwell, in his editorial introduction, described the book as "a sort of manifesto of the younger generation" (ix) and emphasised that most of them were trained in American universities, whereas - and this comes as a surprise - "our teachers were trained in Germany" (ix).

Tugwell himself later had quite a distinguished career: Professor of Economics at Columbia University, member of Roosevelt's brains trust in 1933, prominent New Deal spokesman and administrator, Governor of Puerto Rico, and after World War II for twenty years Professor of Political Science at Chicago and other universities.

By 1924, the US economy had emerged from the sharp post-war depression and was beginning to enjoy Coolidge's "normalcy", several years of rapid economic growth and prosperity. US capital exports helped finance Allied war debt and German reparation payments, reconstruction in Europe and a favourable US balance of trade. Domestic monetary stability had been restored in most European countries, and the international gold standard appeared to be functioning again. But it was a calm before the storm. Britain suffered heavy unemployment throughout the 1920s, in Germany the aftermath of defeat and inflation caused increasing political instability, in Russia the Bolshevik revolution led to Stalin's dictatorship, in India and other colonies nationalist movements began to demand independence, and within a few years sagging prices in world markets for primary products and the 1929 Wall Street stock exchange slump heralded the Great Depression of 1929-33.

A Large Blind Spot

The astonishing fact about this book for anyone reading it in 1996 is that the "trend of economics", current and future, as seen by the contributors hardly alludes to any of these developments. There are a few passing references here and there to business cycles,

unemployment, inflation, the quantity of money, tariff policy and Asia. But there is no discussion of macroeconomic theory or policy, of domestic or international monetary economics, of economic growth or development, and barely a hint at econometrics. In other words, the subjects that fill at least half the pages of a modern textbook of economics are missing. It is worth giving some examples.

Several of the contributors refer to business cycles. Mitchell, already known for his book on the subject, holds out a promise "that the government and private agencies in conjunction will see and attack the problem of controlling the business cycle" (21). Soule refers to "Wesley C. Mitchell's observation that the phenomena of booms and depressions constituted a cycle", but admits that "we do not yet know the secrets of the business cycle", adding hopefully that "the technique of measurement and of graphic statement of cyclical phenomena has undergone a bewildering expansion. In this realm economics is beginning to be an applied science" (364f.). "National income" is mentioned once or twice but neither in a social accounting nor in a macroeconomic context. Frank Knight, in a discussion of the role of the price system in "the apportionment of productive power among different industries" over longer periods, abstracts altogether from changes in national income: "For such periods the total productive power of society may be treated as roughly constant" (265).

Copeland at one point refers to "business-cyclical" unemployment, but only in relation to business behaviour: "If the market is dull or likely to be so owing to an unfavorable turn of the business cycle, it will pay... in most cases to lay off employees" (144). Slichter mentions unemployment in the context of workmen's compensation (317) and of preventable costs: "In the case of unskilled, semi-skilled, and many skilled laborers, it is usually economical for businesses to shift the cost of unemployment to workmen by laying them off" (345).

Raymond Bye, in his chapter on "Recent Developments in Economic Theory", singles out money and credit as a field in which "economic theory has achieved gratifying results". But all the reader is told is that "whether the quantity theory is true or false, we know a great deal to-day about the ways of money, bank deposits, and their accompanying institutions that is of immense value to the banker and statesman. The employment of trained economists by so many banks in recent years is sufficient evidence of this" (295). Slichter comes closest to an issue of monetary policy when he uses the banking system to illustrate the failure of competition to compel businesses to act for the general welfare. On the contrary, when "the public interest required that after a certain point in the period of prosperity the expansion of loans be checked", the interests of banks, depositors and borrowers combine "to consent to an even greater expansion of credit... Competition, far from encouraging banks to do the socially desirable thing, positively encouraged them to do the opposite" (308f.). The only other references to money in the whole book are Mitchell's to the "money economy" as "one of the most potent institutions in our whole culture" (24) and Copeland's brief discussion of the inadequacies of the "pecuniary standard" as a measure of value and, in this connection to Irving Fisher's proposal to "compensate the dollar" (364).

International economics receives even more niggardly treatment. Mitchell does include some foreign economic policy issues among "the problems of reconstruction thrust upon us by the war": "Shall we try to collect the loans to our recent Allies? Shall we continue to export capital on a grand scale? Can we maintain our traditional tariff policy without thwarting our commercial ambitions?" (21) Bye suggests that "the substantiation of the predictions of Keynes

and other economists as to the probable effects of the Versailles treaty" - the only reference to Keynes in the book - "furnish remarkable evidence that the operation of international economic forces is well understood by economic theorists" (297). But international economic theory is never touched upon. There is not a single mention of the gold standard, exchange rates or the balance of payments. The only pronouncement on international economic policy is Copeland's surprising statement that "there is more truth in Mercantilism than most economists have been prepared to admit, and hence it survives all their protests... It is often important to 'keep the dollar circulating at home'" (116).

Given the almost complete absence of short or medium term macroeconomics, one would not expect to find much on the economics of growth and development. Oddly enough, Tugwell refers more than once to "economic development" (e.g. xi), but he means the development of economics. Weld, in his chapter on "Regional Comparison and Economic Progress", points out that "India and China have not participated in the economic progress which has become conspicuous in some of the western countries". He goes on to say that "many explanations have been offered for the economic backwardness of regions in Asia, Africa and South America. Which explanation is nearest the truth? We do not know. It is time we were finding out" (441). The trouble is that "we understand so imperfectly what the quantitative criteria for economic progress are" and therefore "cannot measure the degree to which such countries as India and China lack them" (442). Soule also emphasises the need for "quantitative analysis", citing "problems associated with the accumulation of productive capital" as an example. "Is capital accumulated too rapidly, or too slowly, or at the correct rate for a balanced growth of consumption" (365). These are interesting straws in the wind, but they are few and far between.

Much of the book is devoted to the "new inductive era in economics" (75), economics as an experimental science, studying facts, in "revolt from the traditions of theory, whether classical or marginalistic,... static or taxonomic, *a priori* and deductive, unrealistic, scholarly over-refined" (445f.). But the emphasis is on measurement, on the application of statistical technique, including a whole chapter by Mills on "the statistical method... which deals with relations which are not described by unchanging laws but by generalisations couched in terms of approximation and probability" (38f.). Knight at one point even explains the "scientific treatment of the problem of prediction... that we judge the future by the past" (233). But there is not yet an inkling of econometrics, the construction and testing of models of interaction between parameters and variables as a basis for forecasting

The contributors' strange view of the twentieth century trend of economics is reflected in the ample bibliography. That the majority of authors listed are Americans is only to be expected in an American book. But it is surprising that there are almost as many German and French authors as British; and among the British only six are twentieth century economists or economic statisticians (Pigou, H.D. Henderson, Hawtrey, Bowley, Stamp and Beveridge), most of the others social advocates and historians (G.B. Shaw, the Webbs, G.D.H. Cole, Bertrand Russell, A.J. Hobson, Graham Wallace and Tawney). J.M. Keynes appears only as the author of *A Treatise on Probability*, Schumpeter as the author of *The Nature and Contents of Economic Theory* but not *The Theory of Economic Development*. There are one or two Swedes, but not Wicksell.

Institutional Economics

It will by now be apparent that the book is a manifesto for a particular school of economics - "Institutionalism". Institutional economics has been described as "apart from Marxism,... the principal school of heterodox thought in economics" (Samuels 1987). Derived from the German Historical School, it came to the fore in the USA around the turn of the century with J.R. Commons and Thorsten Veblen in the vanguard. It was a revolt against neo-classical value theory, its preoccupation with static resource allocation and market equilibrium. The institutionalists emphasised the structure of power, social control, technology, non-economic motives and therefore empirical study of facts, institutions, quantitative analysis, statistics, economics as a science.

All these themes pervade the book. Economists are no longer "frenzied over abstract economic theory" (425). Tugwell describes "the gathering force of the renaissance of economic thought we are having in this country" by contrasting "neo-classicists and institutionalists, marginalist logicians and experimentalists, deductivists and inductivists" (x).

In terms of positive economics, this meant going beyond the abstractions of "economic man", recognising "the reality of non-commercial motives in economic life" (the title of Douglas's chapter). Veblen had shown the way with his stress on the "instinct of workmanship" and the pursuit of status through "conspicuous consumption". More generally, it meant "less stress upon wealth and more stress upon welfare" (31). "The economists' avowed reluctance to consider ethical or 'social' values is an error of judgment" (477). It meant studying "the facts of industrial life" (306), "how the business world works" (274). "There are undoubtedly many economic institutions whose detailed study by the economist will produce valuable fruit... A mere description of the organisation and technique of institutions connected with stock and produce exchanges, insurance, corporate organisation, marketing and merchandising, labor management, labor marketing, foreign commerce, banking will furnish much information of value to the business man and statesman" (274).

But there is also a normative, policy, agenda. *Laissez faire* will no longer do. Even nineteenth century economists had come to recognise that problems had emerged "the solution of which might require government intervention" (192). Indeed, "the strain upon the traditional methods of controlling industry becomes more severe and the necessity of improving their effectiveness and inventing new instruments of control becomes more pressing" (354). There is the problem of "trusts". "The anti-trust laws... do not in all cases furnish a sufficient solution of the monopoly problem, and that accordingly governmental price-fixing may be a desirable supplement" (193). The task for economists is "to discover new methods of controlling industry for the public benefit as rapidly as special groups devise ways of controlling it for their particular interests" (354f.). There is the problem of industrial relations and trade unions. "One of the outstanding conditions in modern industry is the intense and bitter struggle between capital and labor" (347). "Special interests within industry are becoming stronger, better organized, and more expert at gaining advantage for themselves. Trade union membership in this country has increased about eight-fold during the last twenty-five years" (354). Other issues calling for economists' study and government action are immigration policy (21) and the "conservation problem", waste of natural resources which occurs "on an enormous scale... when it is profitable" (352).

Echoes

What happened to Institutionalism? Paul Samuelson, in the 1974 edition of *Economics*, explained that "30 years ago Institutionalism withered away as an effective counter-force in economics. Who can explain it when a movement turns sterile? Perhaps it was the case that mainstream American economics had always been more pragmatic and empirical than Austrian or English or French economics; it was therefore able, so to speak, to absorb and take over with superior analytical and econometric tools the descriptive tasks and policy formulations of the Institutionalists" (Samuelson 1974, 847).

That may be part of the explanation, if only because during this century the American economic profession has come, in numbers and quality, to overwhelm all the rest. The Austrian economists emigrated to the USA, French and German economics almost disappeared, and in England theory continued to predominate over empirical work. But the main explanation is surely that, within a few years of the publication of *The Trend of Economics*, the Great Depression, the collapse of the gold standard and the beggar-my-neighbour policies of the 1930s, the exigencies of war economics, and after the war the emphasis on economic growth and development thrust upon economists tasks to which the authors of the 1924 symposium gave little if any thought.

And is Institutionalism really dead? It is arguable that apart from Marxism (which has lost ground with the collapse of communism in the USSR), the principal school of heterodox thought in economics remains Institutionalism. J.K. Galbraith's message, in such books as *The Concept of Countervailing Power*, *The Affluent Society*, *The New Industrial State* and *Economics and Public Purpose*, with their critique of contemporary capitalism and corporate power and their demand for a larger role of government in the economy, is very much in the spirit of the institutionalists of the 1920s; Kenneth Boulding and Fred Hirsch, among others, have echoed and developed the institutionalists' emphasis on non-economic motives; and there is now a whole school of Political Economists who, in often strident contrast to mere economists, much like some of the institutionalists, are interested in power and in the effects of policy decisions on income distribution - *cui bono*? - rather than on average per capita income or poverty. There is also a striking resemblance between the institutionalists' condemnation of neo-classical economics - "abstract theory", "economic man", preoccupation with economic efficiency - and the onslaught on "economic rationalism" which to-day unites protectionists and other advocates of state intervention to temper the winds of market forces to all manner of shorn lambs.

Tugwell and his colleagues would sympathise with some of these strands in to-days debates on public policy.

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* Research School of Pacific and Asian Studies, Australian National University, Canberra ACT 0200.

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