

Political Economy 2023-2024

Course 1: Political economy in times
of crisis

Education and training

1980-83 BSc economics and politics, Bristol (UK)

Rise of neoliberalism and “capitalism with Chinese characteristics”

1986-87 M1 economics – Paris 1 (comparative economic systems)
perestroika – attempted reform of the Soviet economy

1994-95 M2 economics and social policy (2 years)

1997 started teaching at Paris 1 as an adjunct

Jackson Hole Consensus and “economic and monetary union” in EU

1998-2002 PhD in British Studies (*civilisation britannique*) – reform of public sector by Thatcher & Major (1979-97)

September 2003 – tenure as associate professor in “English for economics”
The heyday of “Anglo-Saxon” capitalism

Course Outline

1/ Introduction – from crisis to crisis:

The end of the liberal order?

2/ What is political economy, what is capitalism?

3/ A return to first principles – some new perspectives in economics

Introduction - the context

A succession of major shocks:

Global financial crisis: 2007-2008

Covid-19: 2020-2022/3

War in Ukraine: 24 February 2022

War in Israel and Gaza: 7 October 2023

2024 – stronger “national populism”

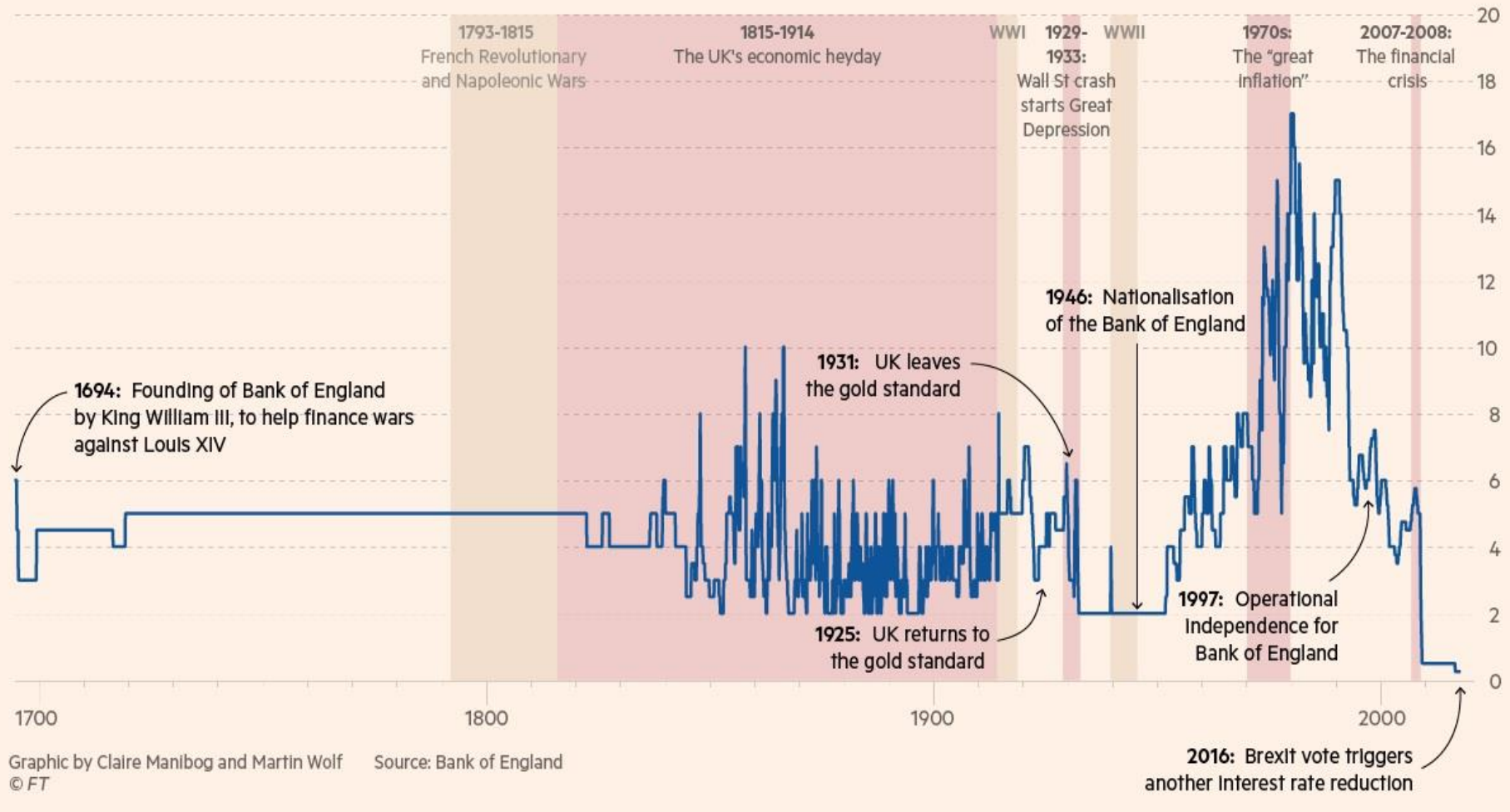
On-going global warming

Fundamental challenges to globalisation, the “liberal order” and economics

The long shadow of the GFC

This time really is different

Bank of England official lending rate (%), 1694-2017



Martin Wolf: "Nothing like this has happened in 323 years", *The Financial Times*, August 16, 2017

Mervyn King: IMF, November 2019

“Following the Great Depression, there was a period of intellectual and political upheaval. First, Keynesian and then rational expectations revolutions altered our views on economic policy. **No-one can doubt that we are once more living through a period of political turmoil. But there has been no comparable questioning of the basic ideas underpinning economic policy.** That needs to change.”

Covid-19 2020: unparalleled peace-time crisis

- Not a war – but entirely global
- Jan 2024 - future unknown – but controllable
- Vaccines – have worked – **amazing!**
- Diverse consequences: sectors, countries, international relations – the return of inflation

Never-ending QE: Federal Reserve and ECB assets

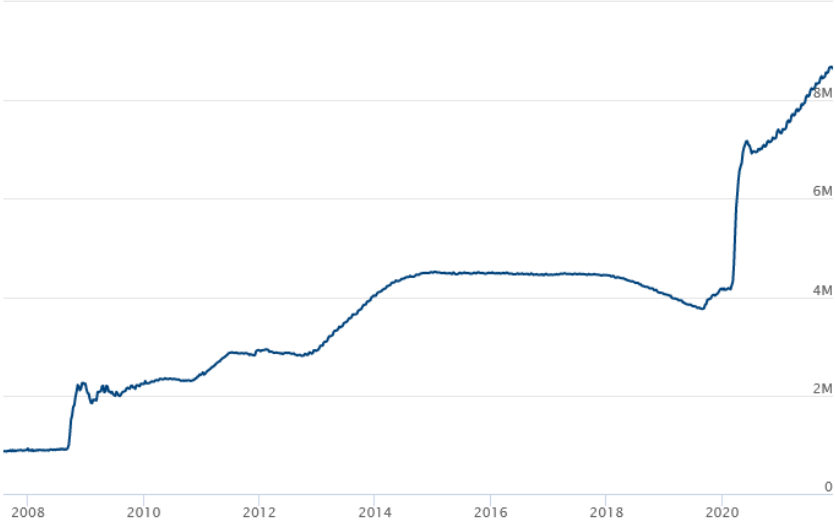
Recent balance sheet trends

Choose one of the 5 charts.

Total Assets of the Federal Reserve

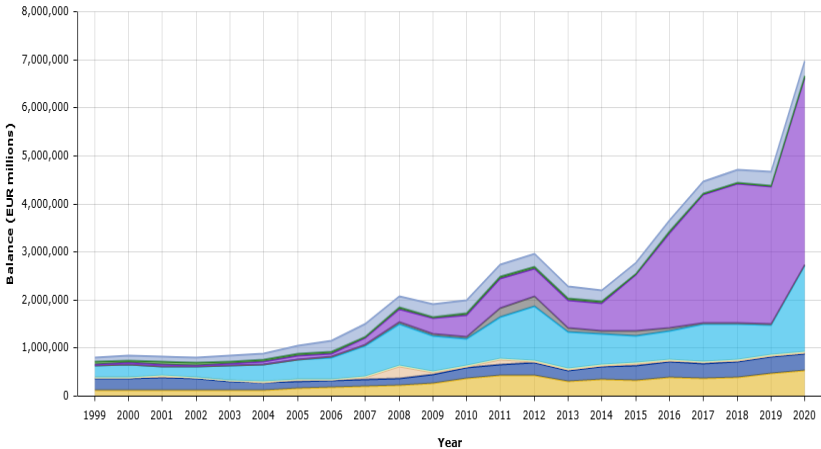
Zoom 1m 3m 6m YTD 1y All

Jul 30, 2007 -- Nov 30, 2021



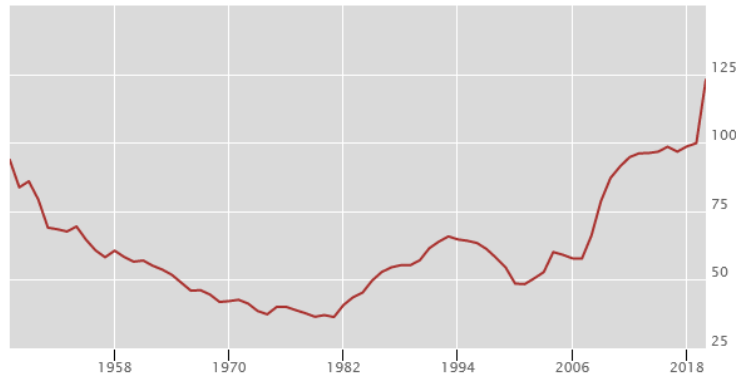
Assets | Liabilities

Chart | Table

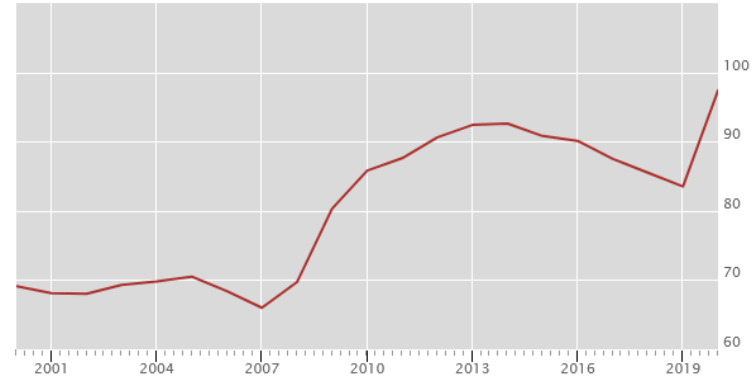


Total credit to government sector at nominal value (core debt), as a percentage of GDP: Source BIS

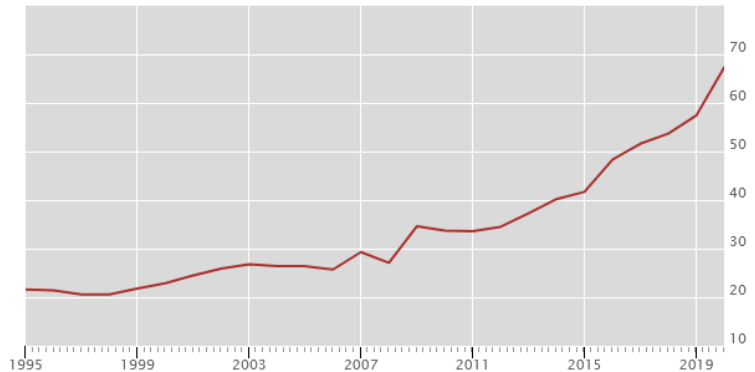
USA



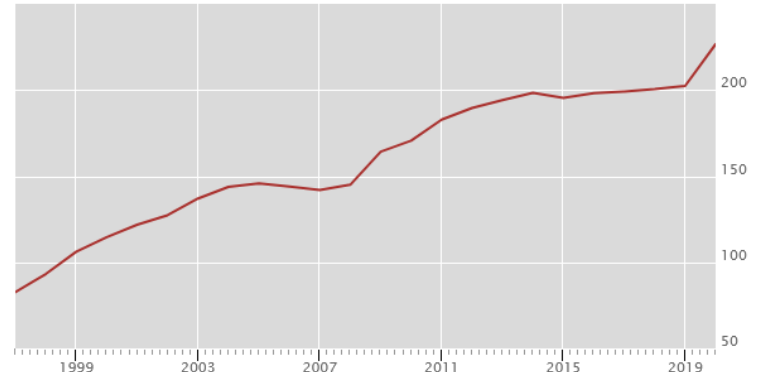
Eurozone



China



Japan

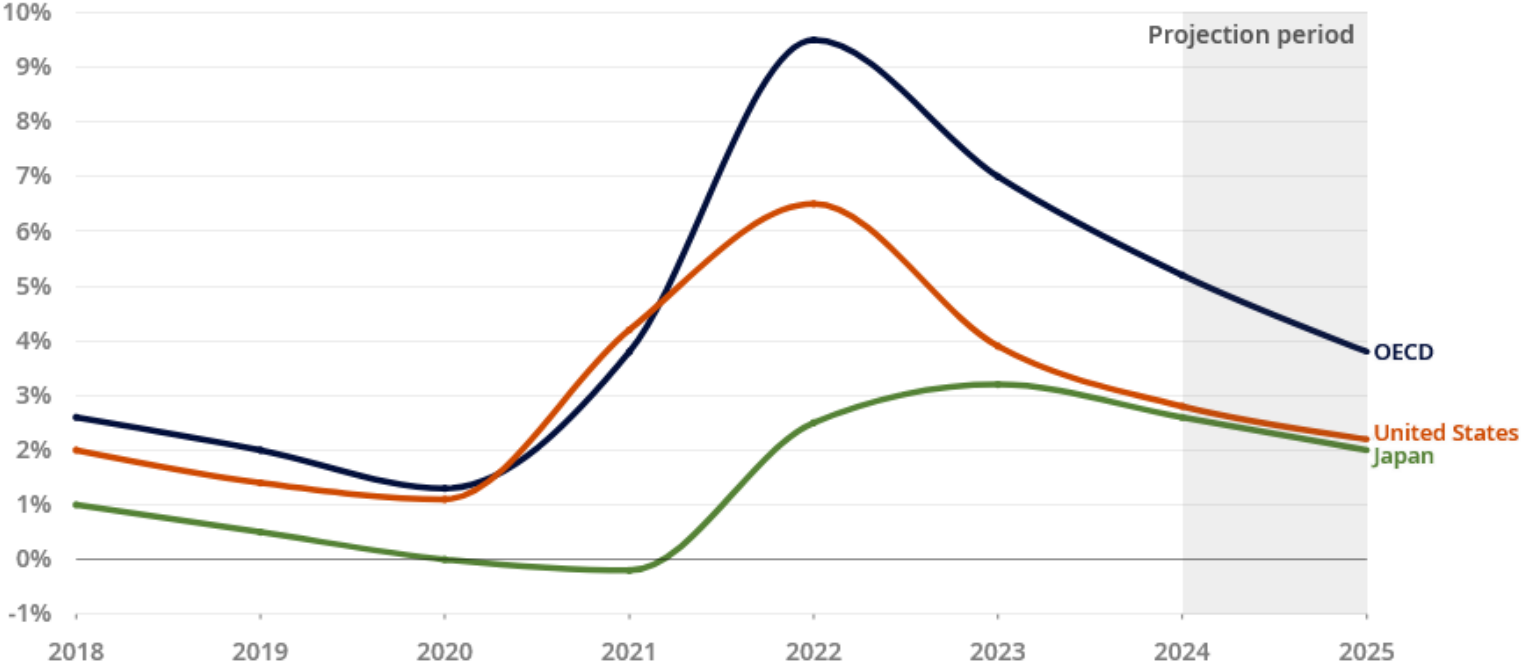


Source: Bank of International Settlements (updated on 13 June 2022).
Available from: <https://www.bis.org/statistics/totcredit.htm> [Accessed 1/2/24].

Headline inflation

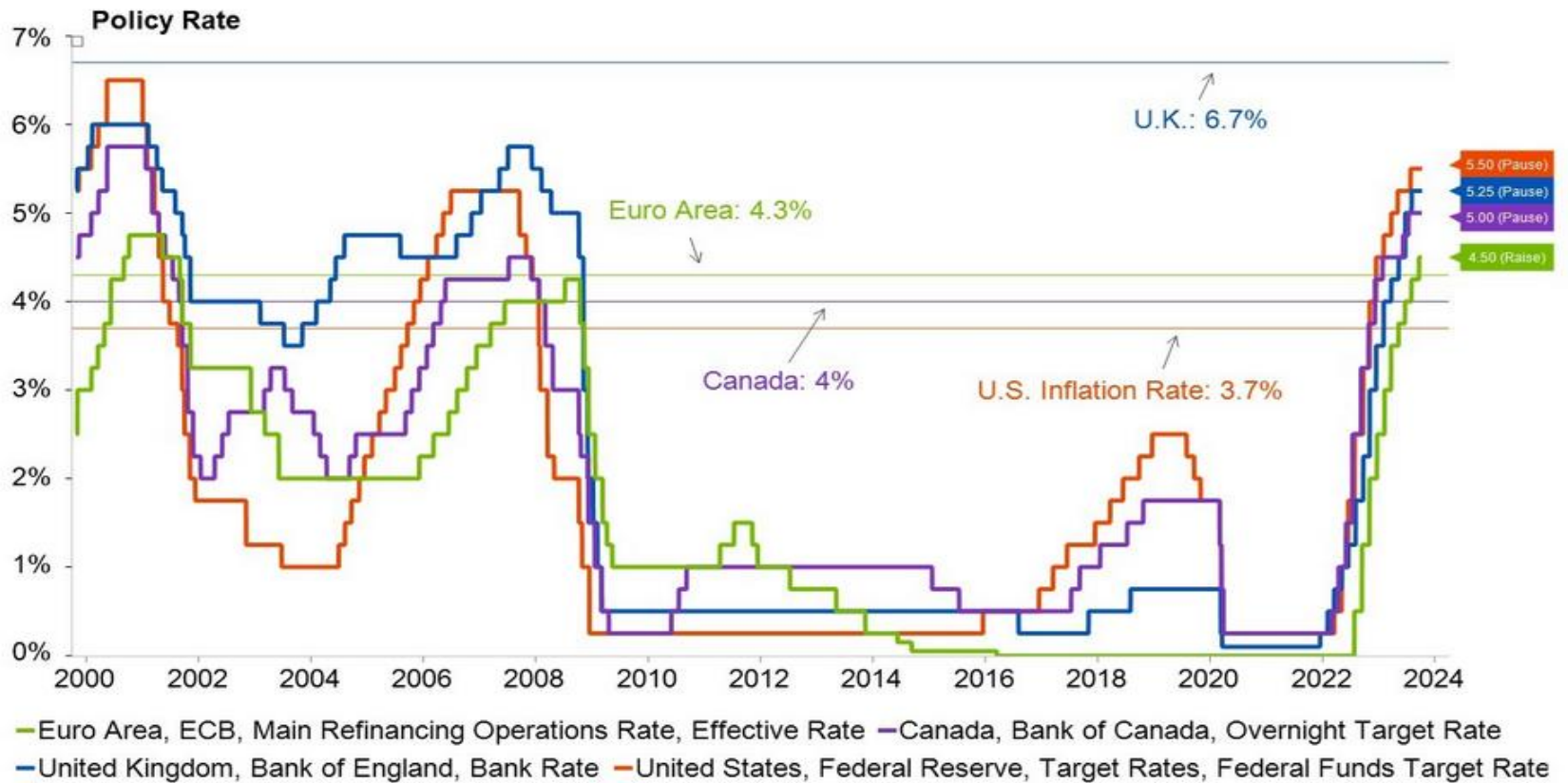
%, year-over-year

Japan × United States × OECD × Select countries



Source: [OECD Economic Outlook, November 2023](#).

Central Banks Rates Rival Highs of Great Recession



Source: ECB, Bank of Canada, Bank of England, U.S. Federal Reserve; October 2023



1/2/2024: Fed funds rate 5.25% - 4.5%; Bank of England 5.25%;
ECB: main refinancing rate 4.50%.

Covid-19 - fragmentations

- Conflict within countries (masks/vaccines) – populism undermining democracy
- Weakening cooperation between countries: no coordinated global health campaign
- Increasing inequalities *within* countries and maybe *between* countries
- Rise in absolute global poverty

War in Ukraine: 24 February 2022

- **The end of “The End of History”**
- **Renewed blocs:** Nato and “the West” / Russia-Iran and tacit support from China / the Global South seems largely unaligned
- Hard power politics > military spending > nuclear proliferation?
- Energy imbalances
- Food shortages

Israel-Gaza war: 7 October 2023

Brutal Hamas attack killing 1,200 people (about 250 hostages): memories of pogroms and Holocaust

Horrendous military riposte by the Netanyahu government: (1/2/2024: [27,000 dead; 66,000 wounded](#)). Hundreds of thousands displaced and at risk of famine.

War is spreading: Houthis attacking ships in Red Sea. [30 January attack on US base](#) (3 dead, 34 wounded)

Possible political & economic implications

Further political fragmentation:

East-West, North-South

Further weakening of democracy in “the West” and elsewhere.

Further decline of the “liberal order”:

- challenges to economics
- challenge to cooperation on global warming

2a/ What is economics? What is political economy?

What is Economics?

- **Merriam-Webster** (30 Jan 2020)

<https://www.merriam-webster.com/dictionary/economics>

Economics : a social science concerned chiefly with description and analysis of the production, distribution, and consumption of goods and services

- **Lionel Robbins (1932):**

“Economics is the science which studies human behavior as a relationship between ends and scarce means which have alternative resources” (the key “mainstream” definition)

Jean Tirole (sole Nobel winner 2014): *Economie du bien commun* (2016) – *Economics for the common good* (2017)

- **We all react to incentives**
- The “common good” – institutions to reconcile individual and general interest as far as possible
- If the availability of a good is limited ... then its use must necessarily be privatised one way or another
- Public authorities must make agents responsible for use of resources
- But institutions (including the market), a “right” or a public economic policy take on lives of their own
- Economics can offset this
- The role of economists is not to decide, but to identify the “regularities which structure the economy and to share what economics as a science says given the state of its knowledge”
- *Homo oeconomicus* – economic man – assumed to be rational – we now know this not to be true.

Dani Rodrik, *Economics Rules*, 2016.

- Positive and normative economics – inevitably come together in models (the word itself having both meanings)
- Math is important for consistency
- Different models – even paradigms – are useful in different situations.

We need a palette of models.

Political Economy of the Classics

- Smith: *Wealth of Nations* – statement of economic liberalism
But also a description of nascent capitalism and the invention of economics as a science
- Marx (and Engels): the foundational critique of capitalism and economics
(Ch.1 of the [*Manifesto of the Communist Party*](#) could have been written yesterday)

Markets need rules and institutions

Political economy examines how these are made, and how government policy is made and functions.

Public choice and neo-classical analysis of political process.

Historical and political analyses

Political economy and embedded markets

Karl Polanyi in *The Great Transformation*, 1944.

A self-regulating market demands nothing less than the institutional separation of society into an economic and a political sphere.

[Yet] To allow the market mechanism to be sole director of the fate of human beings and their natural environment... would result in the demolition of society.

Labor, land and money should not be commodified.

2b/ What is capitalism?

What Is Capitalism?

- Michel Albert (heroic and simple). « La fonction historique inouïe du capitalisme a été, depuis environ trois siècles, de commencer à **faire reculer la pénurie**, la famine et l'oppression des tortures sacrificielles... le capitalisme, c'est-à-dire la **libre fixation des prix sur le marché** et la **libre propriété des moyens de productions**... [un ensemble avec] les droits de l'homme et pour commencer la liberté de conscience... »

Mervyn King, *The End of Alchemy*,
London, Little Brown, 2016

- “Over many years, a capitalist economy has proved the most successful route to escape poverty and achieve prosperity. Capitalism, as I use the term here, is an economic system in which **private owners of capital** hire **wage-earners** to work in their business and pay for **investment** by raising **finance from banks and financial markets.**” p17

Marx and Engels

- “**Commodification**” of human activities, of human beings and of nature.
- “The need of a **constantly expanding market** for its products chases the bourgeoisie over the entire surface of the globe.” (*The Communist Manifesto*, 1848)
- Immanuel Wallerstein: expansion of **capitalism seeks labor** (women and countries): the international division of labour is based on race. (*Historical Capitalism*, 1983)

Other characteristics of capitalism

- **Accumulation**
- “Irrational” production: luxuries and penury of basic goods > production for solvent demand and not human needs
- **Credit and Debt (as money)** – the ability to borrow, the willingness to lend – connects future and present
- **Capitalism is crisis prone** – especially in the financial sector
- But it also allows risk management

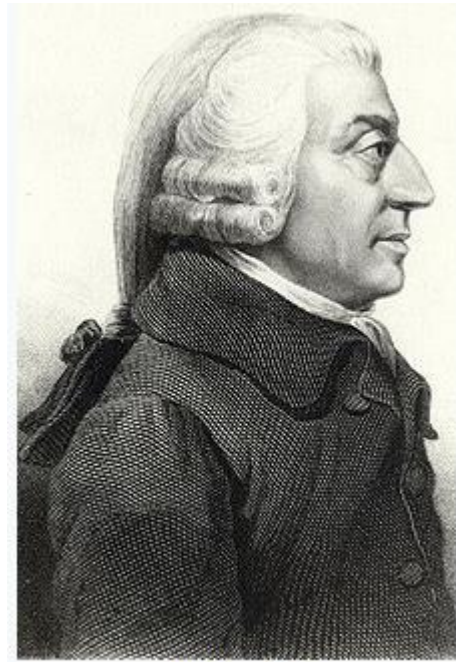
3a/ A return to first principles

Economics born out of the Enlightenment

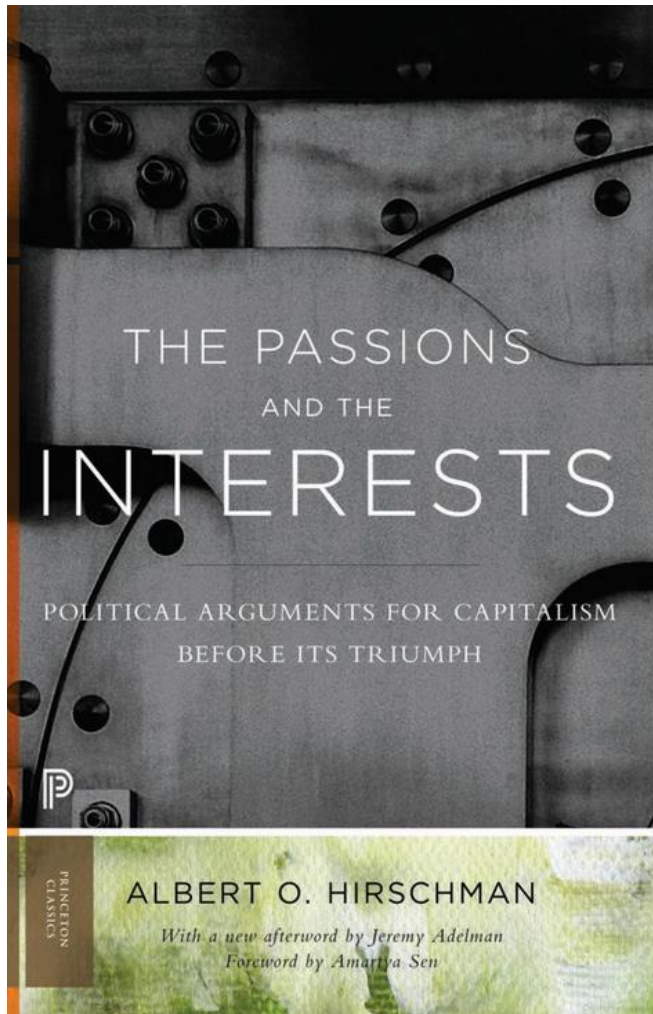
“the Enlightenment figure with by far the greatest global influence today is a moderate, Adam Smith”

O’Hara, p 212.

Competition &
“sympathy”



Reason and commerce over Passion and religion



Hirschman (1977/2013):
for the Enlightenment
money-making was “a calm
passion”.

Quoting Montesquieu:
*Commerce... polishes and
softens (adoucit) barbarian
ways as we can see every
day.*

Business vs. Empire?

The liberal order?



Hard power politics?



My daughter tells me men are apes ☹️

Enlightenment values incorporated into the UN Charter (drafted 1941, signed 1945)

- **WE THE PEOPLES OF THE UNITED NATIONS DETERMINED**
- to save succeeding generations from the scourge of war, which twice in our lifetime has brought untold sorrow to mankind, and
- to reaffirm faith in fundamental human rights, in the dignity and worth of the human person, in the **equal rights of men and women** and of nations large and small, and
- to establish conditions under which justice and respect for the obligations arising from treaties and other sources of international law can be maintained, and
- **to promote social progress and better standards of life in larger freedom,**
- **AND FOR THESE ENDS**
- **to practice tolerance and live together in peace with one another as good neighbours,** and
- to unite our strength to maintain international peace and security, and
- to ensure, by the acceptance of principles and the institution of methods, that armed force shall not be used, save in the common interest, and
- to employ international machinery for the promotion of the economic and social advancement of all peoples,
- **HAVE RESOLVED TO COMBINE OUR EFFORTS TO ACCOMPLISH THESE AIMS.**

Universal Declaration of Human Rights, 1948.

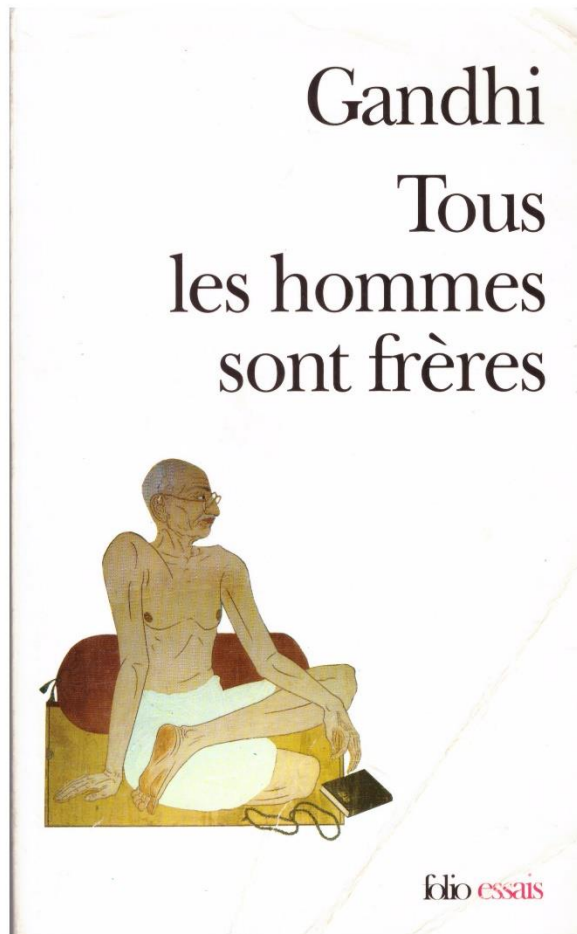


*All human beings are born **free and equal** in dignity and rights. They are endowed with reason and conscience and should act towards one another in a spirit of brotherhood.*

Economic and social rights, as well as political rights

(Coherent with Rawls and Sen)

“What do you think of Western Civilisation?”



Gandhi replied:

*I think it would be a
good idea.*

Human fraternity

Saadi Shirazi (1210-1291)

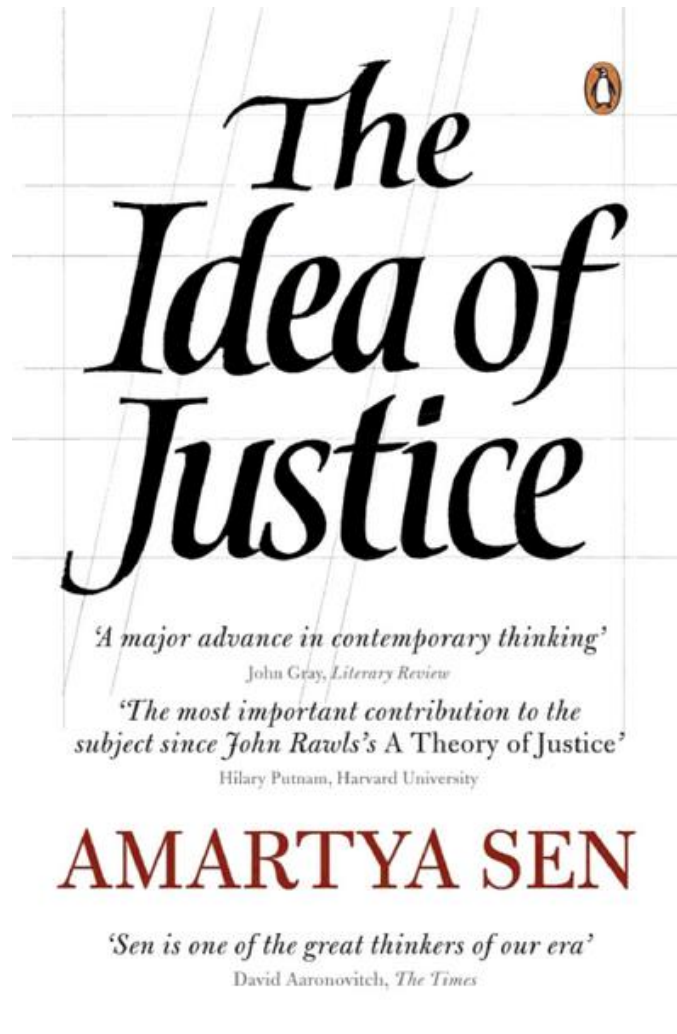
Bani Adam

*Human beings are limbs of one body indeed;
For, they're created of the same soul and seed.
When one limb is afflicted with pain,
Other limbs will feel the bane.
He who has no sympathy for human suffering,
Is not worthy of being called a human being.*



Folio depicting Saadi Shirazi (seated left) and the Salghurid ruler Abu Bakr ibn Sa'd (seated right). Made in Mughal India, dated 1602

Amartya Sen, *The Idea of Justice*, 2009



Sen's capabilities approach is a theory of development and justice that emphasizes the **freedoms people have to pursue their own well-being and happiness**. It is based on the idea that individuals should have **real opportunities to choose the lives they have reason to value, and that society should enable them to do so**.

The capabilities approach is concerned with expanding the range of options available to people and increasing the freedom to choose among them. This approach places emphasis on the capabilities of individuals and communities, their potential, and the resources available to them to make choices and lead fulfilling lives.

Text generated by Openai, *Playground*, 26 January 2023

3a/ Some new perspectives of
economics to explore

Katrine Marçal: *Who Cooked Adam Smith's Dinner?*, 2016.

A whole continent of economic thinking – **feminist economics** – which men have ignored.

And which you have not studied.

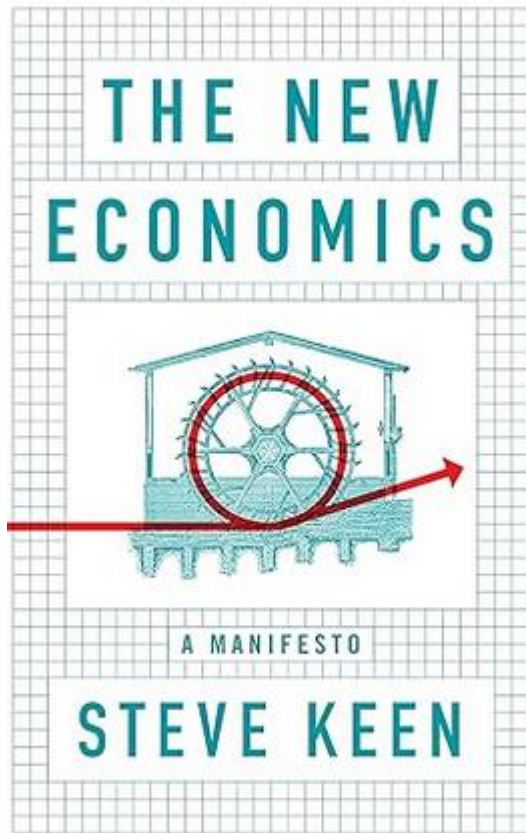
And which may provide key insights into a different approach to economics, needed in this age of global warming.

> Wikipedia: [feminist economics](#)

Narrative economics: from Shiller to Harari?

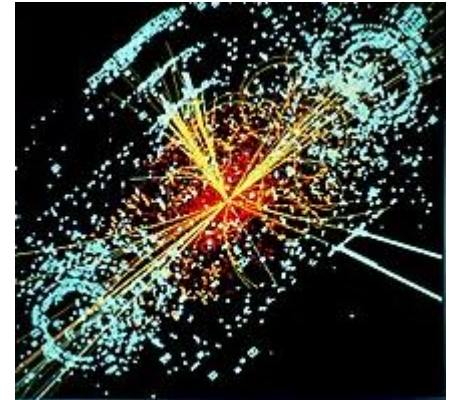
- Robert Shiller: “narrative economics” study of spread and dynamics of popular narratives > economic fluctuations (the Laffer Curve)
([Russ Roberts](#): Laffer curve and Keynesian multiplier, liked by economists and politicians because they suggest possibilities of a free lunch)
- Yuval Harari – [Sapiens](#) – humans succeed because they organize in groups around stories

Beyond a general theory



Keen notes physics has no “[theory of everything](#)”

General relativity
explains gravity



Quantum mechanics explains the strong nuclear, the weak nuclear and the electromagnetic force.

They are incompatible. 😊

Complexity Theory

- Beyond “Newtonian” physics : assumptions
 - (1) relationships between individual components of any system can be understood by isolating the interacting parts,
 - (2) there is a predictability to the relationship among the parts, and
 - (3) the result of interactions and the working whole might eventually be understood by simply summing the parts.
- Monetarism (late 1970s early 1980s): $MV=PT$
- Taylor Rule (early 1990s):

$$i_t = \pi_t + r_t^* + a_\pi(\pi_t - \pi_t^*) + a_y(y_t - \bar{y}_t).$$

Non-Linearities

- Complexity theory seeks to explain non-linearities
- more sophisticated models from physics, biology, ecology and social world (Epple & Rhodes)
- It is not a unified and homogenous theoretical perspective > a dynamic representation of the phenomena (El-Ghalayini)

Big Data and Artificial Intelligence

- Big Data
- Computer power – artificial intelligence
- A quantitative leap in modelling
 - > **solving “restricted complexity”**
(within same epistemological framework)
- But how does complexity connect to policy?
 - A tendency to look for simple ideas

Complexity in Economics

Traditional economics

Complexity economics

Dynamics	<ul style="list-style-type: none">■ Closed, static, linear systems in equilibrium	<ul style="list-style-type: none">■ Open, dynamic, non-linear systems not in equilibrium
Actors	<ul style="list-style-type: none">■ Collectively modeled■ Make decisions using complex deductive calculations■ Comprehensively informed■ Failure- and bias-free■ No learning or adaptation requirements	<ul style="list-style-type: none">■ Individually modeled■ Make decisions using inductive rules of thumb■ Incompletely informed■ Prone to bias■ Capable of learning and adaptation
Structure of ties	<ul style="list-style-type: none">■ Modeled on the basis of actors' indirect interactions through market mechanisms	<ul style="list-style-type: none">■ Modeled on the basis of direct interactions between individual actors
Emergence	<ul style="list-style-type: none">■ Micro- and macroeconomics remain separate	<ul style="list-style-type: none">■ Micro- and macroeconomics are linked■ Macro-level models are emergent results of interactions at micro level
Evolution	<ul style="list-style-type: none">■ No mechanism for renewal of the system or increase in order and complexity	<ul style="list-style-type: none">■ Evolution process based on selection, mutation and amplification provides for renewal of the system and the increase in order and complexity

Jan Arpe, "Globalisation and its Complexity: Challenges to Economic Policy", 2012, Bertelsmann Stiftung

Quoted from:
Belnhocker, 2006, Table 4-1

(Some) Key Concepts

- **Attractors:** elements of order – patterns of replicated behaviour: values, norms and logics Not feedbacks, but influences.
 - **Emergence:** of “bottom-up” behaviour, limits power “top-down” rules and structures
 - **Feedback:** “reinforcing” or “balancing” interactions
 - **Path dependency**
 - **Bifurcation** (paradigm shifts)
 - **Self-organisation:** local responses to system dysfunctions
 - **Scale:** change effects that are not constant
- VALUES – to guide policies**

Open-minded scientific approach

- Falsification defines science as we can only make conjectures about the world (Popper).
- We need to accept that our (individual) knowledge is very limited
- Modesty in approach
- Explanations are partial → pluralism
- That does not mean “anything goes”; all ideas are not equally entitled to be aired: “alternative facts”, etc.

Radical Doubt

Modernity institutionalizes the principle of radical doubt and insists that all knowledge takes the form of hypotheses: claims which may very well be true, but which are in principle always open to revision and may have at some point to be abandoned.

*Anthony Giddens, *Modernity and Self-Identity: Self and Society in the Late Modern Age*, Cambridge, Polity, 1991.*

Takeouts

- **No steady state**: the environment in which agents and policy-makers operate is always changing
- **Neo-classical (mainstream)** economics tends to examine static situations – and assume that the institutional, legal and political environment is given
- The GFC, Covid and wars in Ukraine as well as Israel and Gaza > massive challenges... (global warming)
- Economics as a science and guide to public policy provides only partial responses
- **Power politics** is challenging the international system created after WWII
- We need to be **careful in our assertions**.