Cambridge Economics

Cambridge Faculty of Economics
Alumni Newsletter

In the year that the University is celebrating its 800th Anniversary, it is a pleasure to introduce the Economics Faculty's second alumni newsletter. We were delighted by the reception of the first one last year, and particularly pleased that it prompted interesting comments and reminiscences. Please feel free to let us have your thoughts on this one. You can contact us by email at: econalum@hermes.cam.ac.uk

Having been Chair of the Faculty from 1992 to 1996, I have been elected Head of the School of Humanities and Social Sciences of which it forms a part, from 2009 to 2012. Although I filled a comparable role in the 1990s, the subsequent devolution of budgets to the University's six Schools has increased the demands of the job substantially. In common with all higher education, Cambridge University is entering a period in which public spending will be under pressure. A major part of my task will be helping colleagues to generate more income through their teaching and research. In recent years the Economics Faculty has practiced what it has preached by taking a lead in innovative income generation. We are determined to continue to do so.

William Brown

Vince Cable - An Economist in Politics

The Westminster Village is in a frenzy of self-recrimination and speculation. In the centre of it all, Vince Cable (Fitz. 1964 and President of the Union 1965) is calm and ready to reflect on Economics and his time in Cambridge. He has represented Twickenham in Parliament since 1997 and is the Liberal Democrats' spokesman on Treasury matters. In that role he has earned a well-deserved reputation as one of the few to foresee the looming financial crisis, and as a scourge of political opponents at the highest level.

Having first read Natural Sciences, he switched to Economics for Part II of the Tripos. He stood in awe of the big figures who had emerged in Keynes' wake – the list includes Joan and Austin Robinson, Richard Kahn, Frank Hahn, Richard Stone, Ken Berrill, James Mirrlees and James Meade. Their discourse was that of Keynes' disciples, addressing issues of efficiency, equity, employment, and economic growth. And, while acknowledging the current vitality and diversity of Economics in Cambridge, he points to the absence of such a clear public voice today.

But Keynes' liberal economics was soon to be captured and distorted by politicians whose main aim was to promote, or dispute, the case for intervention in the mixed economy. Meade's nuanced balancing of the open market economy on the one hand with the need for selective initiatives to compensate for market failure on the other, was not acknowledged until it was too late.

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By that time, Economics had become a branch of mathematics, largely impenetrable to the uninitiated. In his view, the inability of sophisticated economic models to cope with shocks and persistent dis-equilibrium has contributed to their loss of credibility among policy makers and the public alike.

But now the financial crisis is demanding a fresh approach. Economics, in the process of constructing a new architecture from the rubble of micro- and macro analysis, has become interesting, controversial and exciting. Vince takes up the challenge in his latest book, 'The Storm', arguing for a global regulatory framework that will encourage, and not impede, innovation and growth.

In developing his economic commentary, he values discussion and dialogue with leading economic journalists – he mentions in particular Martin Wolfe and Gillian Tett of the Financial Times – and with think tanks, including the National Institute and the Institute for Fiscal Studies. But, sad to say, he gains less from academic economists, whose dialectic commitment and cautious even-handedness tends to obscure clear policy analysis and prescription.

After gaining his doctorate from Glasgow University, Vince's economic thinking was shaped first by work in Africa on development policy and then as part of Shell's renowned team of scenario builders. In Kenya, where he worked in the government service, he used the power of cost-benefit analysis to evaluate capital investment projects in the public realm that had significant spillover effects. At Shell he found unbridled intellectual curiosity and a radical approach to the multi-disciplinary analysis of major energy and environmental issues that was not constrained by reductive economic models.

But he attributes his success as an economic commentator in the maelstrom of political debate to a simple, if challenging, technique: start from first principles and think clearly. It is a good axiom for us all.

Tony Cockerill

Incentives to borrow are what matter

"Never again" is the popular response to the financial crisis and a seasoned observer might well be excused for thinking "never again yet again". The government is proposing to prevent any recurrence by better regulation of financial institutions. But better regulation, to be successful needs to be combined with measures to reduce incentives for people to borrow if the chance of a future crisis is to be significantly reduced. Why, one might wonder, do mature and profitable businesses borrow at all, instead of relying on retained profits to fund their activities? Presumably because they or their shareholders like borrowing. Business may like it because they get tax relief on debt but not on equity. Shareholders may like it because businesses borrow on terms more favourable than they have access to themselves, perhaps because they cannot offset debt interest against their own share portfolios or because it is easier for limited companies than individuals to escape debts through bankruptcy. If tax relief for debt interest were removed, there would be less incentive to borrow and less corporate gearing. Ideally debt finance would be tax-penalized because it raises the risk of bankruptcy. The result would be a more stable banking system.

Why do people borrow to buy houses but not normally to invest in their pension funds? Housing investment is tax favoured compared to other forms of investment. There is no gains tax and people can enjoy the benefit of their investment without paying tax, simply by living in it. If housing were properly taxed, for example by an annual tax on house values, house purchase would seem much less attractive and people would be less likely to take out large mortgages.

Why are financial institutions like banks particularly keen on debt rather than equity finance? Generous bonus arrangements mean that equity investors risk having their return appropriated by management. So they insist on terms which make equity seem expensive and favours debt. A tax surcharge on non-contractual salary payments such as bonuses would make remuneration more transparent and equity finance cheaper. If governments address incentives to borrow and not simply ways of limiting excessive and risky lending, then the chance of a future crisis will indeed be seriously reduced.

Martin Weale
National Institute of Economic and Social Research

A Graduate Training Experience

I came to Cambridge by accident. Finishing an undergraduate degree in psychology, I was disturbed to learn that GDP failed to account for natural capital depletion. A World Bank economist working on this told me that "The World Bank hires from five universities: Cambridge, Oxford, Harvard, Stanford and Yale". However absurd in retrospect, it was a short list. Discovering that the US schools charged application fees shortened it further - again, absurd in light of the life cycle income considerations that I had yet to learn about. The final filter, at least, was sound: Cambridge had a year long diploma and masters, more flexible than Oxford's two year masters. On arrival, I was surprised by the reading lists: accustomed to merely a recommended textbook, Cambridge's extensive reading lists offered no such illusion of Truth: knowledge was a living, human endeavour. Cambridge's physical presence reinforced this sense: stone steps worn by centuries' use reminded us that we stood in a long human project of inquiry. Even the collegiate structure fostered this: I could take any question puzzling me to graduate drinks on Friday and find someone – a biologist, historian or classicist - able to help answer it. But - my Cambridge training forces me to ask - is this economically or statistically significant?

Colin Rowat

My First Time at Cambridge

I first went to Cambridge through a conspiracy between my Ph.D. advisor Kenneth Arrow and his old friend Frank Hahn, who was visiting Harvard during my last year there as a graduate student. Together, Frank and Ken determined that I was "uneducated" and that the only remedy was for me to sit at Frank's feet for a year or so. So in the autumn of 1975 I was duly dispatched to Cambridge -- first as a visitor at Darwin, then as a junior research fellow at Jesus.

It was an exciting period for Cambridge economics. Angus Deaton, Mervyn King, Gordon Hughes, Roger Witcomb, Oliver Hart, and Douglas Gale were all Young Turks, enlivening both the Faculty seminar and the evening seminar that Frank had started at Churchill. I could eavesdrop on legendary figures like Joan Robinson and Richard Kahn in the tearoom. And one memorable night at the Hahns, I had the opportunity to hear Nicholas Kaldor assert (rather surprisingly) that "prices play no allocative role in a modern economy."

Cambridge was also a good place to work and get one's work assessed. Frank didn't care much for social choice theory, but he would carefully read and critique my papers on that subject - while never failing to point out that "Of course, dear boy, it's all nonsense." David Newbery too was a generous mentor and introduced me to other helpful people and the two of us started our joint paper on dynamically consistent tariffs after a conversation with Churchill mathematician Peter Whittle.

As Frank has always reminded me, "Cambridge is the center of civilization." And for that reason it turned out to be a good place to meet non-Cantabridgians too. I first got to know Amaryta Sen, Jim Mirrlees (then at Oxford), and Terence Gorman because they came to Cambridge to deliver papers in the Faculty seminar. Then, there was the momentous afternoon when I got into conversation at tea with Partha Dasgupta, who had stopped by Sidgwick Avenue on his way home from the L.S.E. We hit it off immediately - and soon started work on the first of a series of projects that continues to this day.

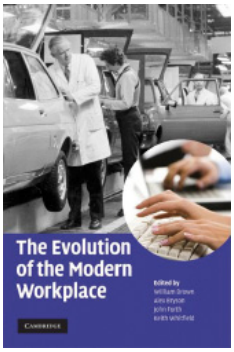
That was long ago, and I have since returned to Cambridge on many occasions, including stints as an overseas fellow at Churchill and St. John's. But for whatever reason—the dazzling first impression Cambridge made on me, the colorful and eccentric characters I encountered, or perhaps just because I was young—that initial Cambridge sojourn has the rosiest glow of all in my memory.

Eric Maskin
Nobel Laureate in Economics 2007

Books

The Evolution of the Modern Workplace

Edited by William Brown, Alex Bryson, John Forth, Keith Whitfield



The last twenty-five years have seen the world of work transformed in Britain. Manufacturing and nationalized industries contracted and private services expanded. Employment became more diverse. Trade union membership collapsed. Collective bargaining disappeared from much of the private sector, as did strikes. This was accompanied by the rise of human resource management and new employment practices. The law, once largely absent, increasingly became a dominant influence. The experience of work has become more pressured. The Evolution of the Modern Workplace provides an authoritative account and analysis of these changes and their consequences. Its main source is the five Workplace Employment Relations Surveys that were conducted at roughly five-year intervals between 1980 and 2004. Drawing on this unique source of data, a team of internationally renowned scholars show how the world of the workplace has changed, and why it has changed, for both workers and employers.

Graduate Student Conference

Thanks to generous funding from the Faculty, a Graduate Student Conference on the topic "Macroeconomic and Financial Linkages: Theory and Practice" was organised on December 15th and 16th, 2008 at Peterhouse College.

The organising committee of doctoral students screened and finally accepted 17 papers from a number of PhD students at universities and central banks in the UK, Europe, and Malaysia.

The key note speakers were Lord Eatwell, President of Queens College and Director of Cambridge Endowment for Research in Finance, and Professor Tony Cockerill, Leverhulme Emeritus Fellow.

There was high level of participation from doctoral students from both the Faculty of Economics and the Judge Business School. Feedback from the last day of the conference as well as email correspondence after the conference indicated that people found the event extremely useful and well-organised. Representatives from the Bank of Italy have already proposed the idea of the next conference being held at the Bank of Italy.

Lord Eatwell

Kamiar Mohaddes
Sergejs Saksonovs

Geoff Harcourt on Cambridge Economics' First Century

The Economics Tripos at Cambridge celebrated its centenary in 2003 with a number of brief lectures and, as is usual at Oxbridge, with food and drink. My brief (in two senses) was to discuss some academic highlights of those first 100 years. What follows is a shorter version of my lecture. As background, may I point out that over this period, Cambridge economists made seminal, often classic contributions to welfare economics, employment and monetary theory, the theory of the firm and economic history, including history of economic theory?

I started with Pigou's Wealth and Welfare (1912) reviewed by Edgeworth in the March 1913 Economic Journal. "Originality", Edgeworth writes, "has set its unmistakable mark on Professor Pigou's work. [This is] not inconsistent with some resemblance to great predecessors … The good which philanthropy and statesmanship should seek is defined in accordance with Sidgwick's utilitarian philosophy". Pigou's theoretical means to achieve that end are "the methods perfected by Dr. Marshall". Pigou's "most sublime" theoretical contributions assumed "the form of mathematical reasoning", but with practical importance attached to other arguments taking the classical form of deduction from psychological generalisations.

Edgeworth, a wise old bird, writes that to assess the value of theory we should use the "Aristotelian doctrine [of attending to] the … pronouncements of the practically wise, who have acquired by experience a certain power of mental vision". He poses the question: "How far do our author's theories belong to the category of practical wisdom, or to that higher kind of science [which is] wonderful … difficult but not useful for human purposes?" Mathematical economics is certainly useful but do further elaborations "imply a correspondingly large contribution to the Art of Political Economy"? The analogy of mathematical physics does not help us to answer [so much for our physics envy]. Edgeworth therefore "leaves to posterity the decisive answer".

Cannan reviewed the first edition (1920) of The Economics of Welfare in the June 1921 Economic Journal. (Remember that he had been a candidate for the Chair of Political Economy that Pigou held). Cannan started with a complaint: "In the presence of a thousand pages a reviewer feels somewhat of a worm … like that despised being … inclined to turn". "The sage who observed that of the making of books there is no end was a child in these matters. In … Pigou's paradise an author will scrap his magnum opus … superseding it with another twice its size every eight years". Cannan sighs for "a little of Malthus's 'prudential restraint'". He closes graciously, "a valiant effort by a very gallant gentleman to increase our economic welfare". Remember, though, that Captain Oates vanished into the Antarctic night, never to return.

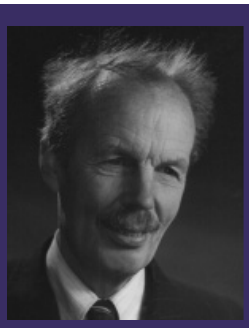
A personal and professional tragedy was the intellectual falling out of Maynard Keynes and Dennis Robertson in the 1930s. Before this occurred, thank goodness, Robertson published in 1926 a seminal study – "a theoretical skeleton" – of the relationship between real and monetary factors in the making of the cycle. Banking Policy and the Price Level was the "horrible little younger son [surely brother?]" of A Study in Industrial Fluctuations (1915). The book was deliberately difficult and concise; the author thought it had merit because, as it was short, it was "quickly over".

Frank Ramsey's two famous papers, "A contribution to the theory of taxation", in the March 1927 Economic Journal and "A mathematical theory of saving" in the December 1928 Economic Journal were 40 years ahead of their time, spawning the later literature on optimum taxation and growth. Maynard Keynes in the March 1930 Economic Journal wrote of the second paper: "[It was] one of the most remarkable contributions to mathematical economics ever made, both in respect of the intrinsic importance and difficulty of its subject, the power and elegance of the technical methods employed, and the clear purity of illumination with which the writer's mind is felt by the reader to play about its subject". Keynes referred to Ramsey's "modesty". This is borne out by Ramsey's assessment of the paper. "Of course, the whole thing is a waste of time". It had distracted him from "a book on logic" … [because] it [was] much easier to concentrate on than philosophy and the difficulties that arise rather [obsessed him]".

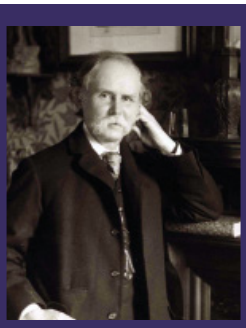
I turned next to Joan Robinson's The Economics of Imperfect Competition (1933), noting that it was preceded by Piero Sraffa's 1925 and 1926 articles. Richard Kahn's "The Economics of the Short Period" (1929), Gerald Shove's lectures and writings and Austin Robinson's classic, The Structure of Competitive Industry (1931). Keynes probably came closest to a correct assessment. He referred "to the very considerable development of the theory of value in the last five years" and to the fact that there is "no convenient place [to find] a clear statement of the nature of modern technique, or a summary of recent work … Mrs Robinson aims at filling the gap … has done it very well … The book will be for a little while to come … essential … for any serious student of the modern theory of value".

The major landmark of Cambridge's contributions was The General Theory, published on 4 February 1936, the day after the Arts Theatre opened, "two projects, linked by a common feeling, converging at a single moment in time" (Robert Skidelsky). When the Faculty celebrated its publication 50 years on, our's not being an exact science, we chose the wrong day in February. The General Theory is indisputably Keynes's work, but he was much influenced by the members of the 'circus' and by Kahn's 1931 multiplier article, "Mr. Meade's relation", and Kahn's scepticism concerning the quantity theory, which still characterised A Treatise on Money (1930).

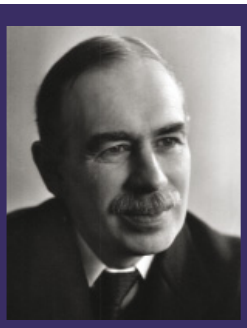
I drew on two reviews, one by Austin Robinson in The Economist, 29 February 1936, the other by John Hicks (JR as he then was), chosen by Keynes to review it for the June 1936 Economic Journal. Austin's was the only signed review ever to appear in that august journal (even then it only ran to initials, "E.A.G.R."). Austin complained to Keynes about the narrowness of the title chosen – "Mr. Keynes on Money" – and other alterations. Keynes told him it served him



Arthur C. Pigou (1877–1959) © Peter Lofts



Alfred Marshall (1842–1924) © Elliot and Fry



John Maynard Keynes (1883–1946) © Peter Lofts

Frank Ramsey (1903–1930)

Joan Robinson (1903–1983) © Peter Lofts

Richard Kahn (1905-1989) © Peter Lofts

right for publishing in the Yellow Press. Austin's perceptive review has stood the test of time. He approved of Keynes's polemical passages: "Like Horace's schoolmaster Mr. Keynes whips his pupils into agreement". He deplored the comparative absence of the masterly, clear style of Keynes's earlier writing, the possession "in usual bounty [of] the gift of translating theoretical ideas into realities … conveying them in words of one syllable". Austin used plain language to describe the existence of under employment rest states and the processes by which they may or may not be reached, drawing on his keen sense of industrial behaviour by explaining that the sub-profitable levels of output as a whole away from the rest states meant that the situations were not sustainable. He also had a clearer view of the equality of S and I and the roles it played than perhaps even the author.

Hicks's review article, though entitled "Mr. Keynes' Theory of Employment", immediately evades this constraint by bringing in output, shifting equilibrium and money. Hicks chose employment (or rather unemployment) because it was then the most practical problem to which "this sort of theoretical improvement" was relevant. It was a theory of output in general, Marshallian in inspiration in method but not confined to a single industry; "a theory of shifting equilibrium vis-à-vis the static or stationary theories of general equilibrium … of Ricardo, Böhm-Bawerk or Pareto"; "a theory of money [in so far as it brought] money out of its isolated position as a separate subject into an integral relation with general economics". For Hicks making S=I by definition was an important change in point of view – "The changing, progressing, fluctuating economy has to be studied on its own … it cannot usefully be referred to the norm of a static state." "From the standpoint of pure theory, the use of the method of expectations is … the most revolutionary thing about the book". Hicks identifies "a proposition of fundamental importance" – *cet. par.*, the marginal efficiency of capital *(m.e.c)* will be lower, the greater the amount of capital goods already possessed – on which Keynes based his theory of trade crisis and a new theory of long-period unemployment, even more novel and startling.

Hicks concluded: "[We have] to change, not so much our methods of analysis, as some … elements in the outlook … inherited from the classics. [We] can have too much, even of economic virtues … the nineteenth century could only afford Ricardo because it sinned so luxuriantly against Malthus. Today we must find a new sin, if it can give us a century before the day of reckoning it will have done well." I must also mention the precociously insightful reviews by two of Keynes's pupils at King's, life-long friends and colleagues, David Champernowne and Brian Reddaway.

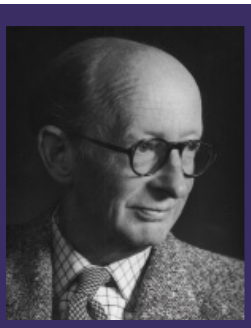
I closed the 1930s with two of my favourites – Maurice Dobb's Political Economy and Capitalism (1937), a classic that pays rereading, and Brian Reddaway's The Economics of a Declining Population (1939), the lucid arguments of which are becoming more relevant by the day.

For the 1940s I singled out James Meade's and Dick Stone's 1941 Economic Journal article on the national accounts of the United Kingdom. It was a by-product of Austin Robinson's favourable reaction to How to Pay for the War (1940), which convinced him of the need for reliable estimates of national income and expenditure on a continuing basis. He recruited James "to get the logic right" and Dick "for his remarkable familiarity with British economic statistics". Austin always regarded this "as his chief contribution to the war". I also mentioned Joan Robinson's 1942 Essay on Marxian Economics which led Gerald Shove (in 1944) to give her an α on Marx but only β- on Marshall; and elicited a letter from Keynes addressed to "Mrs. Austin Robinson", starting "My dear Joan". Keynes thought it "as well written as anything you have done … despite the fact that there is something intrinsically boring in [attempting] to make sense of what … is not sense." Keynes was left with the feeling that "[Marx] had a penetrating and original flair but was a very poor thinker indeed". So now we know.

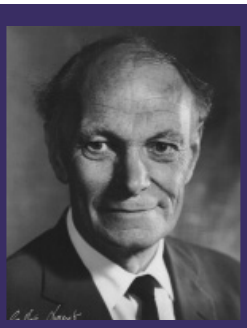
The 1950s saw at least four milestones: the Sraffa (in collaboration with Dobb) edition of Ricardo's works and correspondence (1951-55) for which Piero received the then equivalent of the Nobel Prize; the publication of volume I of Dick Stone's "Red Books" on consumer expenditure in the United Kingdom, a magnum opus and veritable tour de force – Angus Deaton (1987) singles out for praise the explicit description of data, the "masterly exposition of the theory of demand and revealed preference and [the] chapter on economic methodology which reads like a text until one realises that this is where the texts originated"; Joan Robinson's "generalisation of the General Theory to the long period"; The Accumulation of Capital (1956), published 20 years on from The General Theory when Joan was the same age as Keynes in 1936; and Jan Graaf's Theoretical Welfare Economics, (1957), based on "a Ph.D. thesis largely completed around 1951".

Tibor Barna's review in the September 1957 Economic Journal was the most favourable and knowledgeable review of Joan's magnum opus. Using "The Keynesian apparatus of thought and her reflections on competition and monopoly [she] applied them to classical problems and to the testing of classical answers". For Abba Lerner in the 1957 American Economic Review, though, the "most important parts are the errors and ingenious confusions which can give such first class exercises to graduate students (and professors) who could do with a tough work out and who can stand the tough cuteness of Mrs. Robinson's style". For him "[the book] constitutes a pearl whose most conspicuous product is irritation". For Lawrence Klein, writing in the 1980s, the introduction remains "a truly masterful statement of economic principles [serving to lay bare] the fundamental aspects of our subject to beginners".

Paul Samuelson described Jan Graff's book as "a classic in our own time written by a brilliant South African [who] left his impress on the Cambridge environment but subsequently revealed a preference to be a non-economist". Graaf concluded that "the greatest contribution economics is likely to make to human welfare … is through positive studies … rather than through normative welfare economics". For Samuelson Graff's nihilism was "partly a matter of temperament … one who [accepted] the universe in a cheerful David Hume way might state the same conclusions … yet give quite a different impression".



Maurice Dobb
(1900–1976)
© Peter Lofts



Brian Reddaway
(1913–2002)
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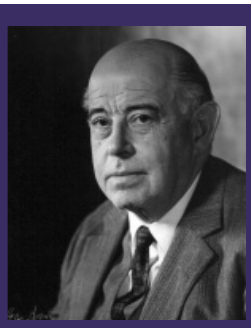
James Meade
(1907–1995)
© Peter Lofts

Richard Stone
(1913–1991)

Piero Sraffa
(1898–1983)



Nicholas Kaldor
(1908–1986)
© Godfrey Argent

1960 saw fundamental contributions to theory and to theory coupled to applied work, exemplified by Sraffa's Production of Commodities and Wilf Salter's Productivity and Technical Change (based on his Ph.D. of the early 1950s supervised by Brian Reddaway). For Ronald Meek, writing in the Scottish Journal of Political Economy in 1961, Piero's slim volume was "a magnificent rehabilitation of the classical (and up to a point Marxian) approach to certain crucial problems relating to value and distribution … [implying] rehabilitation of the labour theory of value in something … like the form it assumed … in Marx." After following a similar intellectual pilgrim's progress to Piero, Krishna Bharadwaj perceptively entitled her review article in a 1963 edition of Economic and Political Weekly *(EPW)*, "Value through exogenous distribution". Mourning Salter's tragically early death at the age of 34, Trevor Swan described his work as "unfulfilled renown". I still continuously meet people who are inspired by his book, superb intelligence and lucid analysis.

Robin Marris's highly original but difficult to read book, the Economic Theory of Managerial Capitalism (1964) was reviewed in the June 1965 Economic Journal by Charles Carter. Carter felt that Marris deserved "much credit for a resolute attempt to write the theory of the firm in terms not wholly repugnant to common sense". He worried that Marris's style obscured his "essentially simple though powerful ideas", so that "Mr. Marris's work … will not have the influence which the originality and power of his ideas justifies". Time has proved Carter's fears to be groundless; the book is a classic.

In December 1964 the Hahn-Matthews survey of growth theory, the role model for survey articles ever since, appeared in the Economic Journal. I also cited Nicky Kaldor's last will and testament to our trade, the 1984 Mattioli Lectures, Causes of Growth and Stagnation in the World Economy (1996) (published 10 years after his death, edited by his biographers Tony Thirlwall and Ferdy Targetti). In them Nicky, the most obvious successor to Keynes in Cambridge, set out the reasons for his growing dissatisfaction with orthodox economics (Arrow-Debreu general equilibrium was his target), and with early and mid Kaldor, including his period as Jean-Baptiste Kaldor in the 1950s and 1960s developing macroeconomic theories of distribution and growth (this explains, not excuses, my omission of "Alternative Theories of Distribution" in the "Green Horror" in 1955-56). He then presented his latest (and, sadly, last) "vision" of how the world works, emphasising complementarity, increasing returns, and the accompanying processes of cumulative causation that he derived from Smith, Allyn Young, his LSE teacher and mentor, and Myrdal. He closed with a "package deal" of policies to save the world. That Nicky was ever an orthodox economist, albeit an internally critical one, is a mystery for the idea of a constraint on anything, especially himself, was completely foreign to his nature.

An important aspect of Keynes's influence is the seminal contributions of economic historians – Phyllis Deane, Charles Feinstein, W.J. ("Ian") MacPherson and Brian Mitchell – to our understanding of the first Industrial Revolution and to development generally, including in Phyllis's case, the evolution of economic ideas. Another major strand, to my mind, the wave of the future in theory, is the development of cyclical growth and multi-sectoral dynamic structural growth models by Michal Kalecki, Dick Goodwin and Luigi Pasinetti. Luigi is now the senior living heir to what I regard as the Cambridge Tradition.

There I stopped (except for brief mentions of our Nobel Prize winners and Marshall lecturers), not because there have not been major contributions by Cambridge economists since then, but because time and space are scarce resources and maintaining friendships is a prudent choice, especially on gala occasions.

Geoff Harcourt

Marshall Lecture: Daron Acemoglu

For society to achieve enduring and sustainable democracy, power among the people must be accompanied by self-generating and self-renewing coalitions of common interest. This was the ultimate message from this year's Marshall Lectures, which were given in the Lent term by Daron Acemoglu, Professor of Applied Economics at Massachusetts Institute of Technology (MIT).

His quest is to identify and understand the economic origins of democracy. The lectures reported on his formal economic analysis and modelling of the factors influencing the persistence through time of institutional arrangements – broadly, societal aims, customs and practices – and of the triggers for change. His starting point was that constitutional change intended to promote democracy often does not lead to institutional change. His examples, drawn from history and from developing countries today, included cases where the shift from colonial to post-colonial rule has not ensured the abolition of autocracy, repression and corruption.

The initial model is of a society composed of an élite (the minority with power) and the citizenry (the majority without power). A significant shift away from autocracy can lead to democracy dominating choice over the two alternatives he specifies of constitutional monarchy and 'non-democracy'. But a smaller shift towards democracy may, in terms of a two-stage game, induce the élite to take pre-emptive action and so retain effective control.

The game-theoretic framework is built around differences between groups in the distribution of power and in expected pay-offs. The second lecture added complexity to the analysis of the first by considering the influence of different and conflicting interests within groups, and the forces that both drive and inhibit the formation of stable coalitions. Technically, the completion of the model is a Markov perfect equilibrium in which coalitions are formed endogenously.

Daron holds the distinguished Charles W. Kindleberger Chair of Applied Economics at MIT and is the recipient of many citations and awards, including the John Bates Clarke Medal from the American Economic Association. His current work on the persistence of institutions is being enriched by inter-disciplinary collaboration, in particular with James Robinson, Professor of Government at Harvard. Their book* gives an absorbing perspective of their work so far.

Tony Cockerill

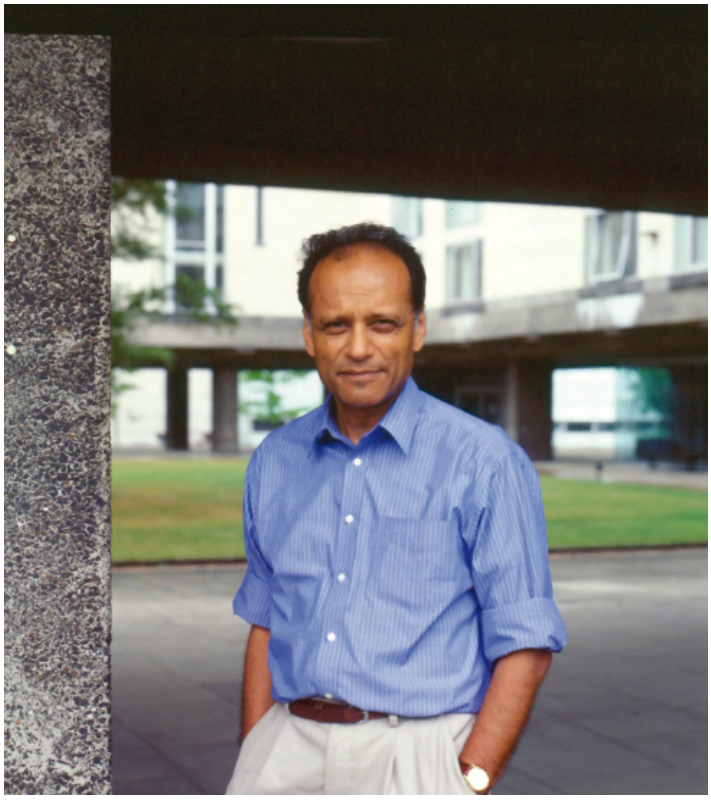
* Acemoglu, D. and J. Robinson (2006). Economic Origins of Dictatorship and Democracy. Cambridge University Press.

Profile: Professor Sir Partha Dasgupta

At once one of the most distinguished yet most self-effacing members of the Economics Faculty, Sir Partha – he was knighted by Queen Elizabeth II in 2002 – holds trenchant views about the theoretical foundations of modern welfare economics and the challenges facing Economics in Cambridge.

His range of publications and research interests is vast, covering welfare and development economics, the economics of technological change, population, environmental and resource economics, the theory of games, and the economics of under-nutrition. The breadth of interest and volume of output are due mainly, he says, 'to my short attention span.'

The linking theme amongst the diversity is the quest for, and application of, rigorous analysis in understanding human welfare. What motivates him is an abiding curiosity, rather than the search for policy prescriptions which drives many researchers in development economics. He is pleased if his work gives socially useful outputs that can help improve the human condition – as it has done, and no doubt will go on doing – but it is the intellectual challenge that excites him.



Partha currently holds the Frank Ramsey (he of the monopoly pricing rule) Chair of Economics and is a Fellow of St John's College. He has been a Faculty member in Cambridge since 1985, following appointments at the London School of Economics. Born in Dhaka, which was then in India and now is in Bangladesh, he graduated in Physics from the University of Delhi before reading Mathematics and then working for his doctorate in Economics here in Cambridge. He has held a number of prestige visiting appointments, including Chairs at Stanford and, currently, at Manchester. Exceptionally, and reflecting his breadth of interests and achievements, he is a Fellow both of the Royal Society (FRS) and of the British Academy (FBA). Although he is reluctant to let personal matters intrude, he is married to James Meade's daughter, Carol and Partha has played a leading role in obtaining funding for the eponymous lectureship.

The citation for his knighthood reads: 'For services to Economics', a recognition gained by standing for most of his career outside the mainstream of economic thought and analysis. It has been at times, he says, 'a lonely journey.' It started with curiosity about why society manifests such diverse patterns of organisation and behaviour when humans are characterised fundamentally more by similarities than by differences. His approach ran counter to the prevailing orthodoxy of the 1970s which favoured the analysis of individuality and 'rational' behaviour. His work was enriched then, as now, by drawing on the methods and insights of other disciplines, in particular evolutionary biology and cultural anthropology.

The 'limits to growth' debate, which focused on the economic impact of the depletion of non-renewable resources at the time of the first energy crises, led to Partha's fruitful collaboration in the Faculty with Geoff Heal. 'The Club of Rome' had expressed Malthusian concern about the dire consequences of policies that were favouring continued and unequal economic growth. Partha's analysis identified and resolved the inconsistencies in the debate and largely settled the argument by developing and applying capital growth theory.

But his interest soon shifted to the challenges and opportunities presented by renewable, rather than non-renewable, resources for sustainable economic development, which is his present field of research. As always, his approach is based on unremitting depth of thought and analysis to produce a rigorous and robust framework in which economic and social phenomena can be analysed, and their underlying causes identified and explained.

This work's applications are mainly in development economics. And it is here that Partha takes issue with current research and methodology, whose emphasis is on description and prescription, rather than dispassionate analysis. Making sense of, and explaining, the complex socio-economic pathways that lead to the accumulation of wealth on the one hand and enduring poverty on the other is difficult, demanding the use of concepts and methods, many to be drawn from outside Economics, that go beyond naïve statistical models.

But not all of his work is at the frontiers of Economics. He is also a gifted communicator, as his recent contribution to OUP's 'very short introductions' confirms*.

Partha is no stranger to debate and controversy. He defends his corner vigorously. Recently he has taken issue with the analysis and findings of the Stern Review of the Economics of Climate Change, challenging the choice of the long-term social time preference rate and the calculation of the aggregate saving ratio. He suspects the absence of sensitivity tests in the Review's estimates of the impacts on global economic growth if action is taken to combat change, and if it isn't, can be accounted for by politicians' unspoken anxiety that concern about environmental issues might rise too high on the policy agenda at a time of global recession.

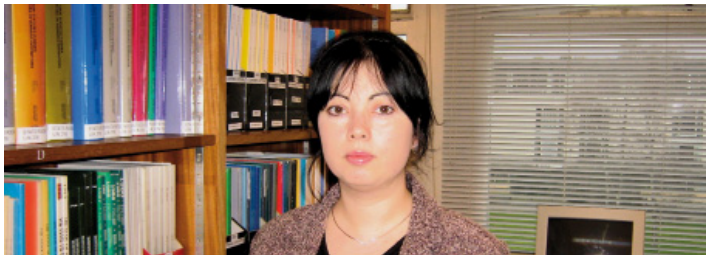
But if you want to spend a diverting and enjoyable hour or two away from studying, researching or teaching Economics, read the argument between Partha and Hilary Putnam (of Harvard) and Vivian Walsh on the ethical foundations of Economics, in Economics and Philosophy**. While perhaps lacking a knock-out blow in this boxing match, Partha definitely wins on points.

Tony Cockerill

* Economics: A Very Short Introduction. OUP 2007.
** See Economics and Philosophy, vol. 21, no.2, 2005 and vol. 23, no.3, 2007.

Exploring European diversity

How far are per capita output and incomes converging across the European Union regions? Research on the Microeconomics of Growth in Europe, conducted in the Faculty by Dr Luisa Corrado is being funded under the European Commission's Marie-Curie Fellowship scheme. The project has been able to identify regional 'convergence clusters' through a novel technique, developed with Dr Melvyn Weeks, which corrects potential problems arising from the short time horizon of the data. This permits the analysis of sector productivity across the European Union regions over the past 30 years.



The four sectors examined - agriculture, manufacturing, market and non-market services - reveal many regional convergence clusters, suggesting that there is no single EU-wide convergence process, but rather that there are different convergence paths in different economic sectors across different parts of the EU. While geographical factors appear to explain results reasonably well in agriculture, they do less well in manufacturing. The findings are of policy interest because they suggest that increasing economic integration in the EU may not be intensifying the spatial agglomeration of economic activity, but rather is being accompanied by geographical dispersal. These techniques have also enabled Luisa to explore the much more human issue of what, beyond income and material conditions, plays a role in determining individual well-being across Europe. It appears that the social attributes of those closest to us regionally and locally explain individual well-being far better than national economic trends. In Europe, as elsewhere, neighbours matter.

Luisa Corrado

Neural Basis of Market Instability

Financial market bubbles and crashes destabilise the global economy, yet a scientific explanation for their occurrence remains elusive. Research led by Professor Aldo Rustichini and funded by the ESRC will attempt to provide an explanation based on the neural and endocrine substrates of risk taking. The experiments his team have designed will examine how financial decision-making is influenced by endogenous steroid hormones. They will explore the ways in which fluctuating levels of these steroids contribute to financial market instability, and the extent to which men and women differ in their endocrine reactions to economic risk and return. The main hypothesis emerged from data collected on a trading floor in the City. Elevated levels of endogenous steroids may impair rational choice and systematically shift risk-preferences across the market cycle. Field work will be carried out on trading floors to evaluate whether traders' testosterone levels rise during a bull market, increase risk-taking, and thereby amplify the market's upward momentum. Another hypothesis is that traders' cortisol levels rise during a bear market, increase risk-aversion, and thereby amplify the market's decline. The field work will be complemented with laboratory experiments using functional neuroimaging and pharmacological manipulation of testosterone, cortisol, and dopamine signalling in order to see whether risk seeking behaviour will increase with testosterone and risk aversion with cortisol administration.

Sir Richard Stone Annual Lecture

The Centre for Research in Microeconomics (CReMic) recently instituted the Sir Richard Stone Annual Lecture. It is to be a major event in the annual calendar of CReMic whose primary aims are to provide a focus in the Faculty and more widely in Cambridge for first class research in microeconomics. The Lecture provides an opportunity for a leading scholar to discuss issues of particular current research interest. The Lecture also honours Sir Richard Stone, the founding Director of the Department of Applied Economics, a Nobel Prize winner, and a major contributor to developments in microeconomics especially the theory and empirics of consumer behaviour.

Richard Blundell

The inaugural lecture was entitled "How Revealing is Revealed Preference? The Stone Legacy and the Analysis of Consumer Behaviour". It was presented by Richard Blundell, the David Ricardo Professor of Political Economy at University College London, at Gonville and Caius College where Sir Richard Stone was an Honorary Fellow. Using a non-parametric approach, his Lecture addressed two key criticisms of the empirical application of revealed preference theory to consumer behaviour. The first is that, when it is not rejected, revealed preference theory does not provide precise predictions. The second is that, when it is rejected, it is unable to characterize either the nature of consumer irrationality or the degree or direction of changing tastes.

Next year's lecturer will be Professor David Laibson of Harvard University.

Richard Smith

Obituaries

Two distinguished alumni have passed on during the year. Sir Kenneth Berrill (above) was a lecturer in the Faculty, as well as Bursar at both St Catharine's and King's Colleges, throughout the 1950s and 1960s. He moved on to a remarkable career in both public service and the City as, among other roles, Head of the Government Economic Service and as Chair of the Securities and Investment Board. Lord 'Eddie' George served most of his career at the Bank of England, culminating as Governor for an eventful ten years up to his retirement in 2003.

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