1 Why I am an Economist*

I turned to economics because I wanted a framework for thinking about the problems of society. I was already in my early 30s, so it was quite a decision. But I was not disappointed.

As an undergraduate I had read history and then begun a part-time masters’ degree in sociology while teaching in a comprehensive school. I remember well at that stage thinking that I understood how society and the economy worked. In fact I even began to write a sixth-form textbook on the subject.

But then I was asked to become the research officer for the Robbins Committee on Higher Education, which was to launch the great university expansion of the 1960s. In the first few weeks of our work, a memorandum came from the Treasury asking ‘Should extra public money be spent on higher education or on renovating the decaying cities of the North?’ I realised I had no framework at all for thinking about such a question.

So, when the Committee’s work was done, I set about learning economics – not easy at any age and certainly not at 31. I was comforted to be told that James Meade had not understood the subject for the first five years, until he suddenly realised what it was all about. Fortunately I was well motivated and I already had questions I wanted answering.

It was a real culture shock. Though I had always believed in the mixed economy, I had never much liked the profit motive. To be among people who thought it wonderful was at first quite uncomfortable, but I soon took it on board. The majority of the British intelligentsia did not do so until quite recently. What they perceived as a new philosophy of ‘market economics’ was in fact the stock-in-trade of mainstream economists throughout my working life.

But what I really liked about economics was the breadth of the issues it could handle – from taxation and transport to education, health and crime. Since many people question this universalism of economics, let me try to explain what I think economics can and cannot do. I shall do it in the form of seven propositions, beginning with positive economics and moving on to policy.

* Prepared for this volume.
Tackling Unemployment

WHAT I BELIEVE

Economics is about rational choice and about systems

Economics is about two things – rational choice and systems. Positive economics begins with rational choice which tells us how individuals and companies will change their behaviour if faced with different alternatives. These responses can be predicted because to a degree individuals and companies are maximising some objective function subject to constraints. When altered circumstances change the constraints, behaviour changes in predictable ways. In common parlance, people compare the benefits and costs of different actions and adjust until there is no scope for increasing the excess of benefit over cost.

From this approach to the different agents in the economy, we then model the working of the system when all the agents interact. When they come together in a ‘market’, this determines the terms (‘prices’) which constitute the opportunities for the individual agents. Thus the ‘market’ determines the prices and also the allocation of resources – of which the most important is the use of human time. There can be no coherent economic analysis of any problem without an equilibrium model of how agents interact to determine a set of prices and quantities.

Too much of empirical economics is conducted without a theory of how the system is working. People run wage equations which show that house prices affect wages without reference to what causes house prices. And so on. There has to be theory, but the theory must be driven by facts.

Positive economics should start from facts

When we set up the Centre for Labour Economics in 1980, we discussed what were the big issues we should investigate. One distinguished theorist said we should investigate ‘why unemployment was too high’. But most of us jumped on him, saying we should investigate first why unemployment was what it was. Only if we understood that could we fruitfully discuss whether it was too high.

This means that we must start from facts. Of course some facts are more interesting than others – and generally the things we want to explain will be things which have a big impact on human welfare or on people’s ability to make money. But that is a matter of motivation. The research strategy must be driven only by facts – many facts. And the aim of the research is to find an explanation which is as consistent as possible with all of them.

Thus economics which starts with one fact and looks for a theoretical explanation of it is unlikely to be fruitful. I once taught a labour economics course jointly with a distinguished theorist, who claimed to have revolutionised