A History of Contemporary Economic Theories

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The Age of Fragmentation: A History of Contemporary Economic Thought by Alessandro Roncaglia, *Cambridge: Cambridge University Press, 2019; pp x + 442, $39.99.*

The increased specialisation visible in economics research has been intertwined with the gradual disappearance of the study of the history of economic thought from universities worldwide. However, perhaps ironically, the fragmentation or super-specialisation of economics research also contains within it the need to understand how these different research agendas might be understood in a coherent manner. Alessandro Roncaglia's *The Age of Fragmentation: A History of Contemporary Economic Thought* (2019), the book under review, provides the readers with a clear analytical lens to understand the seemingly disparate and divergent streams of economics research which emerged after World War II. His previous book *The Wealth of Ideas: A History of Economic Thought* (2009) remains an important text in the domain of history of economic thought (HET hereafter) in particular and economics in general; a concise version of it was published in 2016 as *A Brief History of Economic Thought* (for my assessment, see Thomas 2019).

Theories of Value and Distribution

Roncaglia begins the book by highlighting the two fundamentally different and contending approaches to the theory of value and income distribution—the classical approach of William Petty, Adam Smith, David Ricardo, and Karl Marx and the marginalist approach of Carl Menger, Stanley Jevons, Leon Walras, and later, Alfred Marshall. While the classical economists possess an "objective" theory of value, whether understood in terms of the amount of land and labour used up in production or solely in terms of labour (p 15), the marginalist economists developed a "subjective" theory of value by recourse to the notion of utility (p 24), something which lacks an objective unit of measurement, such as the acres of land or the hours of labour. The fundamental unit of analysis in classical economics is a social class vis-à-vis the asocial individual in marginalist economics (pp 18, 25). In the classical approach, income distribution was "built on the opposition between the main social classes" (p 20), whereas in marginalist economics, the opposition gave way to a harmonious theory of income distribution with each factor of production receiving a remuneration based on their respective contribution (p 24), appropriately called the marginal productivity theory of income distribution.

The differences existing within these paradigms are also attended to in the book. For instance, Roncaglia notes that Jeremy Bentham's "one dimensional view of felicific calculus" was criticised by John Stuart Mill because he thought that "quantitative differences between different kinds of pleasures and pains … cannot be reduced to quantitative differences" (p 22).

Knut Wicksell "developed a marginalist theory of distribution between capital, land and labour based on their marginal productivities;" given that capital is a bundle of heterogenous commodities, he oscillated "between an aggregate and a disaggregated notion of capital" (p 33). It was Wicksell who formulated a distinction between the natural rate of interest (determined by the marginal productivity of capital) and the monetary rate of interest (determined in the money market), which was utilised to explain the trade cycle and inflation (p 34). For Wicksell, despite adopting the marginalist theory of value and distribution, monetary variables do exert an influence on real variables.

Marginalist Economics

Objection to the marginalist approach to economics, especially its reliance on methodological individualism—the individual as the fundamental unit of analysis—came from Thorstein Veblen who underscored the role of "social habits and customs" in understanding the society; others who have contributed to this tradition, which works on the "borderline between economics, sociology and history," include Wesley Mitchell, John Kenneth Galbraith, Gunnar Myrdal, and Shigeto Tsuru (pp 35–37).

While Joseph Schumpeter also espoused a cautious view of methodological individualism, he adopted the marginalist supply-and-demand approach towards value but rejected Jevons's identification of value with utility (p 42). Schumpeter identified the following as crucial agents of economic development: the entrepreneur and the banker; the former innovates, and the latter finances the innovation (pp 44–45). However, he also adopted the marginalist assumption that, in equilibrium, there is full employment of all productive resources; this underlies his notion of "creative destruction" in his theory of the trade cycle (p 69).

Alongside and connected to his critical contribution of the principle of effective demand—that panned leakages is brought into equilibrium with planned injections to the circular flow of income via variations in aggregate activity levels—John Maynard Keynes demonstrated that monetary variables influence real variables, such as real output and employment in direct contrast to the marginalist framework. Notwithstanding the (residual) presence of marginalist elements in Keynes's *The General Theory*, interest rate expresses the preference for liquidity and not the marginal productivity of capital as in Wicksell or the rate of time preference as in modern marginalist macroeconomics.

Hayek and Sraffa

The only two economists who get an entire chapter for themselves are Friedrich von Hayek, the "founder of neo-liberalism" and Piero Sraffa, "the revolutionary" (the respective titles of Chapters 4 and 5). At the core of Hayek's economics is the view that "a totally laissez-faire economy tends to grow more than an economy where the state plays an active role" (p 62). After reading his work, Lionel Robbins, now widely famous for his "scarcity" definition of economics, invited Hayek to give some lectures in London and also supported his appointment to an economics chair at the London School of Economics (p 64). While Hayek accepts the marginalist theory of value, he ascribes a significant role to monetary factors in his theory of the trade cycle, a causation which is irreconcilable with the marginalist dichotomy between real and monetary factors (p 70). Revisiting the Hayek–Sraffa debate surrounding the latter's conception of the natural rate of interest and capital (via recourse to the average period of production which he later abandons [p 73]) can provide important insights for contemporary macroeconomics. (It is from Sraffa's intervention that Keynes derived the theory of own interest rates [p 100].) Hayek, unlike traditional marginalists, sees the choices of the economic agent "as an experiment in conditions of uncertainty, the result of which modifies initial knowledge and expectations in a continuous process" (p 77). Roncaglia views Hayek's support for the market as an "able rhetorical exercise, but totally devoid of analytic foundations" (p 78).

Roncaglia's chapter on Sraffa begins by highlighting his significant influence on Antonio Gramsci and Ludwig Wittgenstein.[1] After discussing his early contributions on money and banking, Sraffa's devastating criticism of Marshallian theory is outlined which exposes its "contradiction between increasing returns and competitive equilibrium" (p 97). Subsequently, a section is devoted to Sraffa's work on putting together Ricardo's writings, published in 10 volumes and an index, which continues to be "recognized as a model of philological rigour" (p 101). Sraffa's 1960 book *Production of Commodities by Means of Commodities* revived the classical approach to the theory of value and distribution by providing an analytically coherent value theory wherein one distributive variable is exogenously determined, as was customary subsistence wages in the old classical economists. The criticism of the marginalist theory of value based on its notion of (aggregate) capital as a factor of production also has an important implication for contemporary marginalist macroeconomics: it challenges the notion of "well-behaved demand curves for capital," which monotonically increase as the wage rate increases so as to "guarantee convergence towards full employment equilibrium" (pp 109, 129).

'New' Economics

The next four chapters of the book respectively deal with "new" microeconomics (mainly expected utility and general equilibrium theories), "Macroeconomics of the Neoclassical Synthesis" (Phillips curve and supply-side growth theories), "Neo-liberal streams" (Austrian economics, rational expectations, and public choice), and "applied economics and econometrics."[2]

By treating utility as a "natural phenomenon, capable of objective measurement," John von Neumann and Oskar Morgenstern are drawing from the cardinal utility approach within marginalist economics prior to Vilfredo Pareto's ordinal utility approach (p 115). The degeneration of the notion of equilibrium from long-period general equilibrium (found in Ricardo and Walras) to modern intertemporal and temporary general equilibrium models is visible in Chapter 6 (especially pp 119–25); the correspondence between the actual and the theoretical world, visible in the traditional notion of equilibrium which was understood as a tendency of actual variables to gravitate towards theoretical variables, has been severed with the new notions of equilibrium which represent purely formal solutions and they also suffer from "negative results as far as uniqueness and stability of equilibrium are concerned" (pp 125; see also p 127, note 27). In particular, marginalist economic theory finds it difficult to accommodate two central features of modern economies: increasing returns to scale and non-convexity of production sets (p 125, note 22 and p 127). But then, in the 1970s, research began to be "focused on the specification of circumstances that hinder or render impossible the optimal functioning of the market," most notably the implications from "asymmetric or imperfect information" (pp 144–45). This is also visible in the "new Keynesian" strand of marginalist macroeconomics, which "try to provide microeconomic reasons for the rigidities that at a macro level cause unemployment" (p 158); the various rigidities considered by Joseph Stiglitz, a main exponent of this approach, are "imperfect information, price rigidity, non-competitive markets" (p 158, note 15).

Ludwig von Mises, whom Hayek considers his mentor, initially worked on monetary economics and later developed a "science of human action" (pp 186–88). In his rejection of mathematical formalism, his standpoint was different from that of marginalist economics (p 189). And despite Mises, Hayek, and Schumpeter stressing that their theories of the trade cycle deal with "market processes" and not "market equilibrium," Austrian economic theories "presuppose the assumption of full utilization of productive resources," a key tenet of marginalist economics (p 189). Roncaglia cites the contrasting case of George Shackle, a student of Hayek, who "converted to Keynesianism" and subsequently examined the "complex role of expectations in the decisional process" (p 190, note 21).

The current mainstream in macroeconomic policy and teaching combine "elements of the neoclassical synthesis, monetarism and rational expectations theory" and may be termed the "new neoclassical synthesis" (p 207). Roncaglia is right in expressing concern about the fact that the mushrooming "applied analyses [which] are utilized in search for interpretations of current economic events" mostly do not rely on economic theory and seem "unaware of the theoretical debates, for instance those concerning the theory of value and distribution" (p 230).

Mainstream Economics

Roncaglia also rightly expresses unease over the imperialist nature of mainstream economics which seeks "to bring all aspects of human life within the compass of economic science" (p 114); Gary Becker, drawing on the work of his teacher George Stigler, pioneered the application of the marginalist theory of value, or more accurately one of its elements—that of utility maximisation—"to issues ranging from drug addiction to advertising, from marriage to begging, from discrimination to crime" (p 132). More recently, social identities (such as gender and religion) have been included as an argument in utility functions; however, given the marginalist assumption of independent preference sets, Roncaglia correctly points out that social issues such as "[r]eputation, identity and belonging … may be included only artificially in such theories" (p 133).

James Buchanan extended the application of utility maximisation (by asocial individuals) to political science where politics is not seen as the

> search for optimal *collective* choices, but as an enquiry into decisional rules, finalised to the resolution of conflicts among individuals. (p 209; emphasis added)

This approach falls under public choice theory; a rather misleading title given the absence of any "public" in the real sense of the term. It was subsequently "redefined as political economy" (p 210), creating yet another source of confusion especially vis-à-vis the political economy of Smith, Ricardo, and Marx. The ongoing work of Daren Acemoglu also falls into this "political economy" tradition (p 334).

Challenges

Challenges to the assumption of the rational asocial individual (*homo economicus*), the foundational unit of analysis of marginalist economics, also arose from behavioural economics (Herbert Simon, Daniel Kahneman and Amos Tversky) and experimental economics (Vernon Smith). While the latter conducts experiments in "the search for regularities in the actual behaviour of agents" (p 247), the former challenges the notion of normal behaviour predicted by expected utility theory via the concepts of "bounded rationality and satisficing behaviour" (p 249). Behavioural and experimental economics draw on ideas from psychology and neurobiology, respectively (pp 248–49); such interdisciplinary work has generated new research programmes like neuroeconomics, cognitive economics, and theoretical experimental economics (also known as agent-based models which rely on computer programmes) (pp 255–56). The work of Kahneman and Tversky extended the expected utility theory by incorporating risk and thus the prospect theory was born (p 261). This led to "a long series of empirical studies aimed at confirming, criticising or better specifying the behavioural assumptions" (p 262). In a similar way, utility functions were modified in different ways and the following theories were proposed: regret theory and disappointment theory (pp 262–63). Richard Thaler, whose work falls under the prospect theory, rightly "considers behavioural economics as a development, not an alternative, to the marginalist mainstream tradition" (p 263) and therefore his policy conclusion is not surprising:

> rely on market forces while public authorities should limit themselves to exerting a gentle push (*nudge*) for addressing agents to overcome the deviations from fully rational behaviour. (p 264)

An effective challenge to neoclassical synthesis (particularly the neutrality of financial choices in undertaking investment), monetarism, and Eugene Fama's theory of efficient financial markets arises from the work of Hyman Minsky. Minsky's assumptions of "uncertainty, financial fragility, [and] money manager capitalism" generate an economic theory which underscores capitalism's "systemic instability, namely the predisposition to crises" (pp 280, 284). Therefore, government intervention is required to "establish and enforce a 'good financial society'" (p 285, note 28). Much like Keynes, Minsky favours an active preventive position than "ex post measures" (p 285). From Roncaglia's discussion of mainstream financial economics, financial institutions, and financial regulation policies (pp 269–79) and other issues throughout the book, it is abundantly clear that in the production of economic theories, the ends are not independent of the means. However, given the marginalist theory of value and distribution, it is only by taking recourse to ad hoc assumptions or modifications that the users of the theory can justify government intervention in the economy.

Non-marginalist Economics

To provide students and policymakers with an alternative framework of understanding and managing the macroeconomy, one must look to non-marginalist alternatives, and it is here that the study of economic thought becomes particularly significant. Some of the notable non-marginalist economists in Cambridge, besides Keynes and Sraffa, were Maurice Dobb, Richard Kahn, Nicholas Kaldor, Michał Kalecki, and Joan Robinson. Kalecki had arrived at the principle of effective demand independently of Keynes via the Marxian route. Kaldor's analysis of growth assumed increasing returns to scale and treated technological progress as endogenous (p 297). Post-Keynesian economists, both past (such as Kahn, Kaldor, and Robinson) and present "consider it misleading to represent markets as in simultaneous equilibrium, for commodities as for money, based on well-defined and sufficiently stable demand and supply functions" as in the IS–LM set-up (p 299). Roncaglia devotes a section to the capital theory debates (pp 303–08; for a highly accessible and recently published survey focusing on the second stage of the capital theory debates, see Fratini 2019).[3]

Inspired by the work of Sraffa, Pierangelo Garegnani, Luigi Pasinetti, and Paolo Sylos Labini made significant contributions to the different aspects of value theory, capital theory, growth theory, and firm theory (pp 310–16). To this initial group, I would add the work of Krishna Bharadwaj who made lasting contributions to classical economics, both theoretical and empirical (in her analysis of the Indian economy, particularly the agricultural sector).[4] Rather than Roncaglia's manner of classifying the work of these three economists as falling into three distinct "Sraffian schools," I prefer the classification employed in Aspromourgos (2004) of "Sraffian research programmes" as it is analytically richer and more useful for new researchers.

In the penultimate chapter, Roncaglia presents the other significant non-marginalist research stream of Marxism but devotes inadequate space to it (pp 321–26). Although he includes evolutionism and institutionalism in this chapter, they are not strictly non-marginalist as Roncaglia himself notes, the influence of subterraneous reference to the marginalist tradition within the evolutionary and institutional research streams is often apparent (p 336).

The final chapter is titled "Ethics and the Problem of Power" where Roncaglia discusses "income inequalities as an ethical issue" (pp 360–63), welfare economics, and Amartya Sen's capabilities approach; although, strictly speaking, Sen's work also has marginalist foundations.

Conclusions

I now offer some observations on the overall presentation and nature of the book. The book would have benefited from a concluding chapter which highlights the role of the theory of value in all aspects of economics; as Roncaglia writes while discussing institutionalism, "no economics approach can do without a theory of value" (pp 336, 348). The use of footnotes as opposed to endnotes makes the reading of the book pleasurable as they are variously employed to explain a concept (p 281 for instance), provide further reading (p 250, note 2 on behavioural economics), or highlight additional crucial assumptions (p 117, note 9 on the crucial assumption of probabilistic independence in decision theory). While Roncaglia extensively utilises articles published in the *History of Political Economy* and the *Journal of Economic Literature*, more references to articles published in other professional HET journals, such as the *European Journal of the History of Economic Thought* and *Journal of the History of Economic Thought* would have been welcome.

Some sections serve as good readings in regular courses in economic development (for instance, Section 7.6 entitled "Theories of Economic Development"). In this particular section, Roncaglia provides an overview of an array of "laws" arising from empirical analysis: Engel's law, Wagner's law, Baumol's law, Kuznet's law, and Verdoorn's law (pp 167–69). Chapter 7 which deals with the "Macroeconomics of the Neoclassical Synthesis," may be prescribed as essential reading for an intermediate level macroeconomics course.

Marshall was instrumental in promoting the notion, currently dominant, that knowledge in economics proceeds in a cumulative way and that therefore reading "older" texts is unnecessary. As Roncaglia writes, Marshall viewed Ricardo as "a somewhat imprecise and unilateral precursor of modern theory" and consequently "no reason emerges to waste time on Ricardo's works" (p 101). The rapid rise of the textbook culture in economics education has further solidified the key tenets of marginalist economics by ignoring especially the important critiques posed from those external to its paradigm. This is visible as early as in Paul Samuelson's textbook which ignored Sraffa's critiques although he engaged with it in his other writings (p 130, note 30).

Roncaglia's book provides a magnificent account of the history of contemporary economic ideas by tracing their roots in either the marginalist or the classical theory of value and distribution, highlighting the implicit assumptions of mainstream theories, pointing out important debates and powerful critiques many of which have not made their way to contemporary economics teaching and research, offering alternatives to marginalist mainstream economics, and by situating this history in the relevant intellectual and political climate. In conclusion, the book reaffirms that HET, as a way of doing economics, not only offers a more active way of learning mainstream economics but also provides coherent alternatives to it in the areas of teaching, research, and policy.

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NOTES

1 In a recent biography of Frank Ramsey, a close associate and friend of Keynes, Sraffa, and Wittgenstein, Misak (2020) convincingly argues that Ramsey had a more significant influence than hitherto recognised on Wittgenstein's later philosophy than what can be discerned from the latter's writings (for the dominant interpretation, see pp 98–99 in Roncaglia's book).

2 Krishna (2019) surveys the evolution of econometrics with a section devoted to the developments in India (see pp 229–32).

3 Drawing on the insights from this debate, I had co-authored a critical commentary which showed the theoretical and empirical problems of using an aggregate production function to understanding India's economic growth (Joshi and Thomas 2013).

4 See Omkarnath (2018) for a short intellectual biography of Bharadwaj and especially section VI for her contributions to the analysis of the Indian economy published in a special issue of *Artha Vijnana* devoted to the "Indian reception of Piero Sraffa's economic contributions."

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