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Address for Correspondence:

Professor Geoffrey M. Hodgson, The Business School, University of Hertfordshire, Hatfield, Hertfordshire AL10 9AB g.m.hodgson@herts.ac.uk

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Her Majesty the Queen
Buckingham Palace
London SW1A 1AA

Madam

We are writing both in response to the question you posed at the London School of Economics last November – concerning why few economists had foreseen the credit crunch – and the answer to you from Professors Tim Besley and Peter Hennessy dated 22 July.

We agree with many of the points made by Professors Besley and Hennessy, principally those summarized in the next paragraph, but we regard their overall analysis as inadequate because it fails to acknowledge any deficiency in the training or culture of economists themselves.

Their letter rightly mentions that 'some of the best mathematical minds' were involved in risk management but 'they frequently lost sight of the bigger picture'. Many believed that risks had been safely dispersed and 'virtually removed' through 'an array of novel financial instruments ... It is difficult to recall a greater example of wishful thinking combined with hubris. ... And politicians of all types were charmed by the market.' In summary, they conclude, 'the failure to foresee the timing, extent and severity of the crisis and to head it off, while it had many causes, was principally a failure of the collective imagination of many bright people, both in this country and internationally, to understand the risks to the system as a whole.'

In addition to the factors mentioned in their letter, we suggest that part of this responsibility lies at the door of leading and influential economists in the United Kingdom and elsewhere. Some leading economists – including Nobel Laureates Ronald Coase, Milton Friedman and Wassily Leontief – have complained that in recent years economics has turned virtually into a branch of applied mathematics, and has been become detached from real-world institutions and events. (We can document these and other complaints fully on request.)

In 1988 the American Economic Association set up a Commission on the state of graduate education in economics in the US. In a crushing indictment published in the *Journal of Economic Literature* in 1991, the Commission expressed its fear that 'graduate programs may be turning out a generation with too many *idiot savants* skilled in technique but innocent of real economic issues.'

Far too little has since been done to rectify this problem. Consequently a preoccupation with a narrow range of formal techniques is now prevalent in most leading departments of economics throughout the world, and notably in the United Kingdom.

The letter by Professors Besley and Hennessy does not consider how the preference for mathematical technique over real-world substance diverted many economists from looking at the vital whole. It fails to reflect upon the drive to specialise in narrow areas of enquiry, to the detriment of any synthetic vision. For example, it does not consider the typical omission of psychology, philosophy or economic history from the current education of economists in prestigious institutions. It mentions neither the highly questionable belief in universal 'rationality' nor the 'efficient markets hypothesis' – both widely promoted by mainstream economists. It also fails to consider how economists have also been 'charmed by the market' and how simplistic and reckless market solutions have been widely and vigorously promoted by many economists.

What has been scarce is a professional wisdom informed by a rich knowledge of psychology, institutional structures and historical precedents. This insufficiency has been apparent among those economists giving advice to governments, banks, businesses and policy institutes. Non-quantified warnings about the potential instability of the global financial system should have been given much more attention.

We believe that the narrow training of economists – which concentrates on mathematical techniques and the building of empirically uncontrolled formal models – has been a major reason for this failure in our profession. This defect is enhanced by the pursuit of mathematical technique for its own sake in many leading academic journals and departments of economics.

There is a species of judgment, attainable through immersion in a literature or a history, that cannot be adequately expressed in formal mathematical models. It's an essential part of a serious education in economics, but has been stripped out of most leading graduate programmes in economics in the world, including in the leading economics departments in the United Kingdom.

Models and techniques are important. But given the complexity of the global economy, what is needed is a broader range of models and techniques governed by a far greater respect for substance, and much more attention to historical, institutional, psychological and other highly relevant factors.

In summary, the letter by Professors Tim Besley and Peter Hennessy overlooks the part that many leading economists have had in turning economics into a discipline that is detached from the real world, and in promoting unrealistic assumptions that have helped to sustain an uncritical view of how markets operate.

We respectfully submit that part of the problem lies in the additional factors that we have outlined above. As trained economists and United Kingdom citizens we have warned of these problems that beset our profession. Unfortunately, at present, we find ourselves in a minority. We would welcome any further observations that Your Majesty may have on these problems and their causes.

We remain your most humble and obedient servants,

Sheila C. Dow

Professor of Economics, University of Stirling and author of *Money and the Economic Process* and *Economic Methodology*

Peter E. Earl

Associate Professor of Economics, University of Queensland, Australia, and author of *Business Economics: A Contemporary Approach*

John Foster

Professor of Economics, University of Queensland, Fellow of the Academy of the Social Sciences in Australia and President Elect of the International J. A. Schumpeter Society

Geoffrey C. Harcourt

Emeritus Reader, University of Cambridge, Emeritus Professor, University of Adelaide, Academician of the Academy of Social Sciences, Fellow of the Academy of the Social Sciences in Australia

Geoffrey M. Hodgson

Research Professor of Business Studies, University of Hertfordshire, Academician of the Academy of Social Sciences and Editor-in-Chief of the *Journal of Institutional Economics*

J. Stanley Metcalfe

Emeritus Professor of Economics, University of Manchester and former member of the Monopolies and Mergers Commission

Paul Ormerod

Academician of the Academy of Social Sciences and author of the *Death of Economics, Butterfly Economics,* and *Why Most Things Fail*

Bridget Rosewell

Chairman of Volterra Consulting and Chief Economic Adviser to the Greater London Authority

Malcolm C. Sawyer

Professor of Economics, University of Leeds and Managing Editor of the *International Review of Applied Economics*

Andrew Tylecote

Professor of the Economics and Management of Technological Change, University of Sheffield