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# BOOK REVIEWS

**László Csaba**
***Crisis in Economics***
*Studies in European Political Economy*
*Budapest: Akadémiai Kiadó, 2009, 223 pp.*

Who would dare to question the significance of the never ending quest for a better match between theory and practice science in general and in economics in particular. The global crisis of the last two years with its devastations of earthquake dimensions on financial and labor markets has again marshaled enough justification for claims that venture to question the scientific values of the economics profession. No wonder that calls for creating a new brand or new versions of analyzing economic phenomena are gaining more acceptance in established journals of the profession. What is more, calls for a complete quit or, mildly put, for a well-defined separation from the 150 years of tradition in analytical socials sciences also have started to abound. Joining this new crowd of critics is László Csaba's new book in which he has found it timely to ask some fundamental hard questions about the economics profession in general, and about its relevance and applicability to the real world in particular. His recent monograph is indeed a genuine and remarkable effort to improve our understanding of the economic profession from a bird's eye view. The work, beyond the slightest doubt, offers a commendable set of valuable fresh insights into the complex world of economic ideas at crisis times. Does anyone doubt it? The dramatic events from The Great Depression are haunting us, and so are the depression-easing, macro policy adjustment steps of the early 1930s, which, be good or bad, are frequently recalled and reanalyzed these days. In our deeply troubled, globally determined times, as witnessed over the last 2 years, clear economic vision, a proper historical perspective and methodological soundness are all being vehemently and simultaneously sought after.

This is especially so when it comes to discussing the sharply observable "disconnect' between global economic issues and its interpretations by modern economic theory. Against these high expectations, Csaba's book is no disenchantment by any measure, since it offers reliable guidance in all these departments to any reader who has kept somewhat abreast with the recent developments in mainstream economic literature. Much of the subjects covered in the volume are strongly related to some often revisited macro concepts of economic integration in general, and to a handful of key issues of globalization a growth and development in particular. Thus, they all need well informed academic readers who were relentlessly swimming in the main currents of the profession. Those who have, will surely enjoy the fresh angles and the wealth of new propositions, especially on the EU-enlargement related matters. When it comes to the EU political economy, beyond a shade of doubt, Csaba is at his best. The real strength of the author and his book is in its integrating-synthesizing capacity to compress seemingly far fetched most modern research ideas, thinking patterns and facts just to accompany them with a sharp vision of what is and will be relevant for leading economic research to better understand global – and more emphatically European development trends. The review that follows is not wishing to be exhaustive by any means, it only offers some reflections on issues that mattered the most to this particular reader.

In the introductory chapter, the work strongly kicks off with a vivid discussion that manages to firmly capture the reader's interest with the unusual theme: Why European Political Economy in an Americanized Discipline? The philosophy-of-economic science type chapter convincingly elaborates on why methodological exclusionism emerged in the first place, and why and how it is desirable to get to a more moderate and cooperative approach in the post crash era. A major source of his pro- methodological-pluralism argument is a Frydman – Goldberg (2007) study, which has blamed modern economic research for its exclusive focus on micro foundations and for its obsession with precise predictions; and – as was aggressively demonstrated by the current crisis – for the misfit between high brow theoretical application that had dismal delivery (p. 33). Yes, indeed, the current global crisis has taught us hard lessons in a most rapid fashion, as it has been handing out painful punishments across the globe for millions of laid off workers, for bankrupt companies and for hard pressed governments alike. It has demonstrated that the reliance on traditional academic output in economics is less and less productive, and that the limitation of the rationality principle gets stronger and stronger real world confirmations. This line of reasoning gets most of the emphasis in the main thrust of Csaba's argument on the questionable omnipresence and omnipotence of the rationality postulate, the one that is widely propagated by the bulk of the mainstream, by the efficient market theory in particular, (by the one which has visibly failed in the current crisis). Over the last 10 years, the limitations of rationality postulate have been demonstrated with ample evidence by many, among them was George Soros (2006), an active financial mega-player, who himself – by his genuine concept of reflexivity – even theoretically has contributed to our understanding of the nature of global money and credit markets.

On the same score, Csaba appears to be in agreement with an even stronger statement, namely with that of Nobel Prize winner Akerlof (2007: 17–29), in which Akerlof went as far as calling for a "*revision of the exclusiveness of the positive economics paradigm, in which statistical testing is everything, while studying cases and intentions is discarded as anecdotic evidence."* Moreover, *"when nonlinear dynamics become important as in contemporary physics, mathematics, biology, chemistry, meteorology and even in financial economics, predictive power alone in the usual sense of foretelling the future in exact quantitative terms, can no longer serve as the measure of what true science is."* (p. 41)

If one wishes to account for the value added of Csaba's exhaustive overview on this topical subject of the rationality postulate and methodological exclusionism, then, perhaps, as a final stand, the following more moderate conclusion can be reached: Csaba seems to be in almost full agreement only with Colander et al. (2007/2008) in that a Kuhnian paradigm shift of the current mainstream in the medium run is highly unlikely, despite the challenges that came from many angles against the most valued methodological foundations. Yet, change is already in the making, and much of it may come from within, as implied by the author, it can be deciphered from Robert Solow's view appearing in his recent addendum to his Nobel autobiography, *"economic growth theory my be coming back to a historic view",* a strong trend Csaba has also tried to document. In other words, the excessive methodological focus which led to exclusionism and intellectual arrogance of the past two decades, is likely to be overcome both in terms of promotion and academic appreciation and access to major journals alike. That is exceptionally good news for many in the profession. *"The traditional delineation between hard facts and soft interpretations can no longer be sustained, not even in introductory textbooks"*(p. 43.) – encapsulates the author his less encouraging main message on this line of reasoning.

Summing up, he is clear and firm in his conviction that methodological pluralism must already be taken as given, while the reemergence of the $19^{th}$ century ideal of grand social science is highly unlikely. The necessity for across-the-board methodological innovation in economics and not just in its mathematical formalization is more than pressing. Also is the need that there should be incorporation of new perplexing insights of other sciences even if these undermine previously axiomatic views such as rationality or the symmetry of loss and gain. (pp. 43–44).

Transition or spontaneous disorder? This is the focal research question in part II for Csaba, where his laborious efforts enable him to foretell, with some trust, the fortunes of post transition change in old and new Europe. The main hypothesis of the third chapter is that public choice is though quite important, in shaping policies, and institutional reforms it is much less relevant, especially in the long run, than most theories of systemic change and political economy of policy reforms would have it (p. 54). For a reliable explanation of this proposition Hayek's wisdom is being referred to, indicating that systemic transformation is *"the outcome of human action, not however of human deliberation".* In explaining why there are lastingly different trajectories for the development of post communist states, Csaba reaches conclusions that largely, yet not necessarily in every respect, contradict earlier findings of the comparative economic literature. For him, communality of the past is neither immediately nor directly decisive for the future development patterns. As the variants of capitalism (VoC) approaches would have it, social and economic implications of the lasting differences among macroeconomic, macro-social coordination mechanisms are considered as constituents of the competing models, rather more variants of the similarly structured market economy (as indicated and advocated by Iversen 2005).

There will be lasting differences between normatively projected and actually forecasted developments both in quantitative and qualitative sense. An unfortunate outcome of this prediction of this chapter will be that Central European growth is *unlikely to follow the overoptimistic growth paths to be forecast from the unconditional acceptance of models of convergence*.

Likewise, there is not much good news associated with the freedom of choice for system designers and citizens, too. All their freedoms will be much less for many years to come than thought at the down of systemic change. Behavioral norms and the tradition of muddling through are strong factors to remain.

In chapter IV, entitled *"Causes and Consequences of a new variety of macro-economic populism"* Csaba attempts to decipher the sources of macroeconomic derailment and institutional stagnation that followed the 2004 enlargement of the European Union.

Of particular interest is the case of Hungary, the author's homeland, a small open economy with a forerunner label for many years, which has "managed" to show how the first can be the last. The sad saga of a new member country is presented in the analysis showing how Hungary has been gradually relapsing into the stagnant continental model of Italy, France and Germany where the political economic rationalities regularly clash. I (I. M.) add, that Hungary is way short of the envied levels of productivity and efficiency and can ill-afford the stagnating status of the of respective countries. The short answer to why it happened is indeed straightforward: in Hungary, hard choices were not made by the governing parties for almost two decades. Following the wisdom of Jean Paul Sartre no choices are also choices, Csaba reminds us. Inaction has led to dramatic endings and there was little surprise in the outcomes: severe deterioration of macroeconomic performance and a relative loss of position against the rest of the new EU members, not to speak of the top ten countries, in the World Economic Forum Rankings. Major factors of growth, capital, R&D and EU funds, were not put to galvanizing functions for a good many wasted years.

The diagnoses of macroeconomic derailments for other countries, the Baltics, Poland, the Czech Republic and Slovakia are also instructive and fit the pattern of general observations for the causes of derailment. Namely, it was shown as a typical set of common features of the largely distorted development paths of the countries at hand that, a) the governing parties tended to disintegrate, the social redistribution moved back and force; b) the stick and carrot mechanism for long term measures was lost; c) the EU as an external disciplinary agent malfunctioned due to its own implementation crisis; d) there was a general loss of credibility and transparency in economic and political affairs, which was coupled with populist discourse; e) there was loss of control over monetary policy amidst mounting disequilibrium, both external and domestic; euro adoption created a false sense of security (pp. 110–111).

Csaba does not accept a typical conclusion of the enlargement literature. He rejects all theoretical attempts to generalize the positive impact of EU membership on growth. Also, he finds non-conclusive the explanations of the currently foreseeable slowdown either immediate or owing to a bust, way before neoclassical theories of convergence would suggest. Also more emphatic, and is clearly not in line with the basic tenet of the literature, is his argument on the real significance of the external anchor, the single currency, *"The availability of the external anchor and favorable expectations for joining the single currency do not replace, as they are not event meant to replace, responsible, timely and informed policy action, based on insights from academic economics."* (p. 113)

*"Premature enlargement? How long a consolidation period is needed?"* These are the focal questions of Chapter V in which, on balance, Csaba appears to share the skeptical view, which the present reviewer tends to co-share. Namely, it is to be firmly stated and restated that on issues of the visible and quickly attainable tangible results of the enlargement, the euro-skeptic trend is still hard to be overlooked. One of the many reasons why this outcome is to be reflected upon with more rigour is that the assumption of the old members about the self propelling nature of marketizing reforms and conversion to fiscal orthodoxy in new members proved to be overly optimistic. Popular, consumption driven booms enjoyed by most of the new members will not be, we can agree, the way to go, especially until large external/internal disequilibria exist. The multi-causal and

multi-dimensional nature of stagnant reforms in the economic and non economic areas alike render it probable that overcoming the impasse of the 2000s is likely to take significantly longer time than postulated at the time of eastward enlargement. Likewise, meeting the EMU criteria will take at least a decade. These are some of the key points of Csaba's mainly dismal conclusions on the delicate matters of the maturity case.

*"Revival or all problems swept under the carpet? Visionary prospects and myopic reality"* carries the heralding title for Chapter VI. In fact, the main finding, or claim rather, of this chapter is more down to earth and less exiting than the title would suggest: the EU has managed to cope, despite a number of inconsistencies with three very different enlargements basically with success. (p. 138). No matter however controversial this claim maybe in the eyes of many, especially against the frequent complaint that the EU is in crisis, the general thrust of the chapter's underlying argument is still positive and forward looking. To the author' full credit, he is non-hesitant in discrediting the traditional federalist idea that to spend ever more funds (in GDP terms) is an established and good measure of how to create efficient and relevant joint policies for the EU-27 (p. 145).

Chapter VII, *"The future of the EU: Between high and low politics*" is aiming at working on the puzzle that emerges from the drift between high politics and low politics in the EU. The former is trying to politicize the EU by pushing ahead through means of elaborate formulations of public law. The latter has drawn attention to the very different mostly economic and social concerns of the median voter and translates into the Euro-skeptic stances of several governments. Csaba appears to show no mercy, he invokes Shakespeare and soon labels the sad fate of the Treaty renewing efforts as "Comedy of Errors". Csaba reminds us that many obvious facts are being neglected. More precisely: the EU is not meant to equalize the level of development across members (community budget capping reassures that). A net inflow amounting to a maximum of 1–1.5 % of GDP is by definition unfit to trigger overall growth. Since EU money is typically for competitive bidding, there are no contingents as in CAP, earmarked for individual needs, thus the calculated sums should not be treated as entitlements. Also, structural funds are earmarked for a variety of purposes from education to environmental protection, thus indirect internal patterns of money distribution render EU funds as inadequate means to counter major economic lulls. This warning of the author merits special attention amidst the strong and long lasting gravity of down phases of the business cycles omnipresent in the years of 2008–2009 across the entire EU.

The EU is unfit to impose any rule on its unwilling members. Csaba finds no indication of two popular misperceptions, i.e. intensive penetration of ludicrous EU rules in Hungary and the exploitative nature of EU membership. On the contrary, he has shown that the median voter and the man on the street has been tremendously benefitting from the gradual implementation of European standards into a rather unstable post-communist environment. The EU related complaints are either macro-economically insignificant or simply false (p. 173).

Economic transformation and the process of Europeanization is the main subject of chapter VIII. A political economy perspective is applied to assess how constitutional change has influenced economic change and how to improve policies and institutions. On the term Europeanization Csaba understands an overrated promise in the sense that for much of the academic and policy analyses of the last 20 years, the early promise developed into an axiom that Europeanization is likely to represent a fundamental molding factor for all countries engaging in the systemic change, but particularly for the new members.

Constitutional progress in terms of new political economy can and may help economic performance in several channels. Even monetary policy can get positive impetus from well defined division of labor of institutions and mandates of central banks. Notwithstanding that the top down controlling and guiding function of the EMU arrangements could not exert their influence either in law or fiscal policy (p.185). The EU is still more an association of compound states rather than a federal arrangement that can enforce legal norms, in which bad examples are easy to emulate.

One must agree on a crucial point which is anything but trivial: exchange rate policy and interest rate policy, a major deliberative component of the old members, is no longer meaningful.

In Hungary, expectations to the speediest adoption of the euro has been rational but the opposite has happened. Contrary to ECB, the National Bank of Hungary (MNB) has been following a pronounced inflation targeting (IT) path, while ECB was sticking to a two-pillar strategy. Little wonder that inflation targets were regularly missed in eight consecutive years, in the 2001–2008 period. Monetary policy was forced to give up the entry date to the euro-zone largely due to the inescapable tolerating of fiscal laxity and severe exchange rate volatility.

Summarizing part 3, *"Theories of Europeanization",* the following can be emphasized. On the one hand there is a mixed bag: Csaba has managed to show the superiority of EU induced reforms and policies against the realistic alternatives that were on the cards of various layers. On the other hand, Hungary has been confronted with a series of constraints emanating from the tiptoeing of intra-EU reforms (at the level of high politics). Formally powerful EU-arsenal has often proven ineffectual on the ground both against old and new trespassers. The weakness of the intergovernmental and the thin and shy supranational institutions and policies were in line with what was expected on the ground of the neo-institutionalist brand economic theories.

Part IV *"Towards a theory of sustainable economic growth and prosperity"* is a stand alone study attempting to formulate tentative answers to major challenges posed by policy crises to economic theory. Although the collected empirics and learned experience are from transition countries they indeed may have broader applications. Out of the many, most applicable new and fairly concrete suggestions which are carrying a fresh perception of this chapter – at least to the present reviewer – the section on the *"Public policy with short bottlenecks"* deserves special mention. Here, Csaba provides a set of new normative requirements for good governance, as he calls them *"simple and commonsensical maxims"*. Without giving the exhaustive list, it makes sense to briefly indicate some of his top priorities. These are: a) Support small business and make them capable to cooperate with the transnational sector. This is a task long overdue in Hungary, for sure. b) Reorient and remedy the drift in the system of education, vocational training needs to be reintroduced. c) A new system of social transfers needs to be retailored on early retirement and disability schemes that featured overgenerous payoffs. Strong incentives to work must be reestablished. d) Further privatize pension schemes. Re-channel funds to the health sector to services of the elderly. e) Strengthen the actions of competition policy towards more efficient workings of single European market.

Overall, this book has been a remarkable success in its argument for the use of a return to a broader political economy approach to social and economic matters. At the same time, Csaba's main findings have supported the broad understanding of the standard economic paradigm rather than joining old institutionalism that has been traditionally hostile to any version of modern macroeconomics and analytical social science. He is absolutely clear on one of his final current crisis related verdicts: our *insights have not led to the revival of a naïve libertarian belief in the night watchman state. On the contrary, our analyses of crises, have called on more regulation at the transnational level* (p. 220).

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