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The role of economists in future economic crises

It is realistic to assume that global economic crises will continue to occur. In particular, three such crises are likely to emerge also in the future: 1) *Environmental crises* 2) *financial crises* 3) *migration crises*.

The purpose of this paper is to indicate how crises in these fields may emerge, and how they may be mitigated.

1) In the case of *environmental crises*, economic theory has for a long time provided an appropriate tool box for analyzing the situation. I refer, of course, to the theory of externalities, which emphasizes the possibilities to mitigate negative consequences for the environment of production and consumption that damage the environment by using taxes and subsidies. In this way, it is possible to combine good environmental policy with decentralized decision-making on production and consumption.

An alternative policy approach, which is often advocated by politicians, is based on physical regulations of production and consumption. A weakness of this approach is that open distributional conflicts then emerge among different producer and consumer groups, which makes both agreements and adherence to these conflicts hazardous. This disadvantage is, for instance, illustrated in the failed Paris-agreement concerning CO₂-emissions a few years ago. The distributional effects of general taxes and subsidies are more diffused, and this counteracts an emphasis on distributional issues.

Technicians in firms also argue that it may be possible to remove 90 percent, or even more, of damaging emissions by way of environmental-friendly technological innovation. As we know, technological methods are also developed which remove already existing emissions in the atmosphere and in the seas.

It is better to stimulate environmental-friendly production technology than to push people to choose a new lifestyle. Such technologies can be financed through taxes on emissions but also through general support for research on new

production technology. It is hardly possible to push the environment as much through a change of lifestyles as through a change of production technology.

Emission permits are an alternative to environmental taxes. But I believe that environmental taxes are better than emission permits because the latter are more difficult to explain to the general public.

So much about the possibilities to fight environmental crises.

2. History has taught us that *financial crises* may have damaging social consequences. Therefore, there are strong reasons to create institutions and mechanisms that both counteract the emergence of financial crises and mitigate the consequences of crises that have already emerged. The importance of building such institutions and mechanisms was neglected by many politicians and economists when the financial markets were abruptly liberalized in the 1980s. The result was a series of financial crises with negative effects on other markets than the financial ones.

As we know, politicians have started to create institutions and mechanisms that counteract both microeconomic and macroeconomic instability. This has not yet been completed, and some parts of it do not look very good, but the creation of these institutions and mechanisms continues. The issue remains how to provide a delicate balance between efficiency and stability in financial markets.

But financial stability also requires that monetary and fiscal policy are stable in the long run. A new feature in the Lindbeck commission was to try to achieve such stability using stable rules – in the case of both budget policy and monetary policy.

In the case of suggested budget policy, the Lindbeck commission established a surplus target for the consolidated public sector, for the purpose of reducing the galloping public-sector debt from about 75 to about 35 percent of GDP. Today, the issue is whether the surplus rule should be kept or revised when the debt of the public sector is at an internationally relatively low level. In my view, it would be natural to replace the surplus target by a debt target. I then assume that the policy target is not to abolish the market for public-sector debt by way of permanent surpluses in the public finances.

We can very well ask the corresponding question for monetary policy as for budget policy. It is, for instance, reasonable to reduce the inflation target to one

percent when, in reality, inflation has been less than two percent for a number of years?

3. What about *migration crises*? The deepest driving forces behind an emerging migration crisis are also obvious: the population explosion in low-wage countries, reduced moving costs and armed conflicts. All this takes the form of attempts at mass migration from countries with a relatively low productivity to countries with a relatively high productivity. The positive side of this is increased per capita income both in the world as a whole and among immigrants themselves. The negative side is that developed countries are not able to integrate everyone who wants to move to developed countries. A massive immigration of low productivity workers creates serious social problems in these countries which is reflected in unemployment, benefit dependency and criminality. In this way, many individuals in the domestic population lose the security in their neighborhood and miss part of their network which they have created over the years.

Similar consequences may arise in connection with the liberalization of trade. But the problems are not as serious as the social problems in connection to poorly educated immigrants with often lacking relevant knowledge of the language. Moreover, such immigration results in a concrete confrontation between immigrants and the domestic population. Workers in China who produce products for the Swedish market do not demand social services produced in Sweden!! The confrontation tends to be particularly strong if immigrants are allowed to jump the queues for rationed social services such as housing, health care and old age care. All this means that free international mobility results in more serious social problems than does liberalization of trade.

In the public discussion, it is often asserted that a restriction of immigration leaves the immigrants without assistance. This is not necessarily the case. If rich countries were to give much larger support than today to improvements of the deprived refugee camps, this would help more than ten times as many as the number of received refugees.

It is true that domestic individuals are able to avoid certain negative effects of massive immigration by adjusting their behavior in different dimensions. I refer, for instance, to installing protection against burglary, avoiding being outside after dark, and refusing to appear as a witness before the police and the court. But the consequences are then simply that the immigration costs change

character. Here, the researchers may make a contribution both by clarifying the social consequences of mass immigration and contributing to the integration of immigrants who have the right to stay in the county.

The researcher as adviser

How should we then look at the role of economists as political policy advisers – either as formal advisers to the government or as participants in the open debate? We might look upon the role of the economist as being equivalent to what in medicine is called “evidence based treatment”. But, in many cases, there is not much solid empirical research to draw on. The adviser then has to lean on a combination of established theory and fragmented empirical studies. One example is when a country with a fixed exchange rate has run into a situation with an overvalued currency as a result of rapidly rising wage costs as compared to other countries. Should the adviser then recommend a deflationary policy, discretionary devaluation or a shift to a floating exchange rate? As we know, the Lindbeck-commission chose to recommend the last alternative in such a situation.

A more general problem is if the economist should be concerned about what is regarded as “politically feasible”. Personally, I believe that the economist, in addition to routine advising, should contribute to expand the framework for what is politically feasible. It helps if there are “two legged” economists, who stand with one leg in academia and the other leg in the complex world of economic and political experiences. Therefore, it is important that economists participate in the economic policy discussions. Thereby, they get the chance to extend the borders of what is regarded as feasible policies. It is also important to integrate non-orthodox mechanisms into traditional economic models based on the assumption of the “economic man”. For instance, I refer to mechanisms such as altruism, envy, social norms and trust. In this way, options for innovative research are promoted. Such integration has, in fact, been a connecting thought in my own research over time, also in my most theoretical work.