Economics in the 21st Century: A Critical Perspective on the Work of the John Bates Clark Winners

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Abstract

Economics has the awkward distinction of being both the most influential and most reviled of the social sciences. The economic crisis that started in 2008 does not appear to have caused the discipline's influence to wane, but it has expanded the number of its critics. Broadly speaking, the growing criticism from outside (and occasionally inside) economics centered on how the discipline lacked realism and used technique as an end in itself, instead of engaging with concrete economic realities and accepting a pluralism of approaches adapted to the complexity of economic problems. A fundamental component of the lack of realism is the lack of attention by the mainstream of the discipline to the economic influence of the most powerful people, institutions and corporations that dominate the decision making of the 21st century. This paper explores whether this criticism should be applied to the work of Daron Acemoglu, one of the new generation of economic superstars, who have won The John Bates Clark (JBC) medal, given to the American economist under forty "judged to have made the most significant contribution to economic thought and knowledge," and is generally considered the second most prestigious in the profession (after the Nobel Prize, which it sometimes foreshadows). Acemoglu and

the other winners of the JBC are significant because they represent the future of economics as defined by the discipline itself.

Introduction

Economics has the awkward distinction of being both the most influential and most reviled of the social sciences. The economic crisis that started in 2008 does not appear to have caused the discipline's influence to wane, but it has expanded the number of its critics. Even the Queen of England memorably entered the fray, enquiring how it was possible that no one in the profession noticed the down turn coming[1]. The original, understandable, indictment of the profession's lack of ability to predict or explain the economic meltdown rapidly spread to a wider criticism. Students were walking out of first year economics courses and signing petitions lamenting the poor quality of their economics education. Respectable media outlets like the *New York Times* in the US and Canada's *Globe and Mail* were conducting scathing investigations into the discipline under headlines like "Economics has met the enemy, and it is economics."[2] Broadly speaking, the growing criticism from outside (and occasionally inside) economics centered on how the discipline lacked realism and used technique as an end in itself, instead of engaging with concrete economic realities and accepting a pluralism of approaches adapted to the complexity of economic problems. A fundamental component of the lack of realism is the lack of attention by the mainstream of the discipline to inquire about the economic influence of the most powerful people, institutions and corporations that dominate the decision making of the 21st century.

This paper explores whether this criticism should be applied to the work of Daron Acemoglu, one of the new generation of economic superstars, who have established significant influence both inside and outside the discipline. The John Bates Clark (JBC) medal is given to the American economist under forty "judged to have made the most significant contribution to economic thought and knowledge," and is generally considered the second most prestigious in the profession (after the Nobel Prize, which it sometimes foreshadows). We will focus on the work of Daron Acemoglu in this paper, but we have examined the work of all those that have won the award from 2001 to 2013 in *Economics in the 21st Century*. The winners of the JBC are significant because they represent the future of economics as defined by the discipline itself. It reveals the type of methods and subject areas that the discipline deems meritorious. This might not be of particular importance if economists had no sway on the world outside the "academic scribblers" beavering away in ivory tower obscurity, but this is not the case. Economists significantly influence both broad public opinion and public policy.

The "Old" Mainstream

Up until this generation of economists, the "old" mainstream rested on four pillars. First, rational self-interested maximization is the assumption that people use the information available to weigh the costs and benefits of every activity and undertake those that are the most beneficial. To take one example (to which we will return) people decide to commit crimes by calculating the costs, like incarceration and loss of legitimate income, and the benefits, like the income from a theft or the satisfaction of a murder. This is the often derided *homo economicus* the rational calculator who attempts to maximize their own benefits.

Second, mainstream economics has focused on the individual as the center of inquiry. Economic predictions are made based on how individuals respond to their constraints and incentives. So, for example, consumer behavior can be predicted by how individuals respond to price changes given their preferences for a product. This emphasis on the individual can be contrasted using class as the unit of analysis, as was done by classical economists like Adam Smith, Thomas Malthus and David Ricardo and is currently done by non-mainstream economists like those who work in the Post-Keynesian and Marxist traditions. Focusing on class stresses that individuals can be combined into groups with similar economic interests and that these groups can be expected to absolutely and relatively prosper or suffer depending on economic trends and policies.

As an example of an analysis that focuses on classes in society differs from old mainstream analysis, we can look at the theory of comparative advantage in international trade. Most old mainstream economists argued that if nations specialize by producing what they can make most efficiently, and trade with other nations for the goods that they are less capable of producing, all trading nations will be better off than if they did not trade and produced things that are more expensive to make. It is this theory that underpins the mainstream economics' support of free trade between countries. A concrete example of this is when Wal-Mart sources its products from low wage nations, like China, reducing consumer prices in the U.S. Yet, this simple model abstracts from the winners and losers in free trade. Trade specialist Paul Krugman argues that competition from low wage nations has driven down the incomes of less educated American workers. "And no, cheap consumer goods at Wal-Mart aren't adequate compensation."[3] On the other hand, free trade helped Wal-Mart become one of the largest and most profitable corporations in the world by allowing them to purchase their products from the lowest cost countries in the world. According to the Economic Policy Institute, free trade has contributed to rising income inequality, suppressed real wages for production workers, weakened unions, and reduced fringe benefits.[4] There is a "class effect" from free trade. Business owners benefit and workers, especially those who are in occupations that compete with low wage countries, lose.

Third, mainstream economics relies on formal mathematical modeling. This is justified by its ability to produce rigor, by which economists mean logically consistent conclusions derived from an explicit set of assumptions. A contentious issue with formal modeling is that it must, by definition, choose which aspects of reality to include and which to exclude. When abstracting from a world of infinite potential variables, the theorist must decide which are the most salient and which it is possible to exclude without significant cost to the ability to predict or explain. Old mainstream economics has typically chosen to model human behavior as individuals with no class or power, who behave in a rational manner to maximize their interests, and who do not make systematic errors when making economic decisions. In these models, the owners of Wal-Mart, the Walton Family, and John Q. Public have similar goals and behave in a similar manner. The only real difference is that the Waltons' income permits them a greater range of consumption choices. However, in reality the Waltons' wealth does not only stem from cheap sourcing from the developing world, but also the tremendous power that comes with the massive scale of their operations, which they have used to dictate prices and alter the terms of trade with their suppliers and workers. Despite the fact that the Waltons have considerable political and economic clout both because of their sizeable financial resources and the inherent power that comes from the fact that business decisions have a massive impact on the broader economy, most mainstream economics models abstract from the fact that the Waltons (and other large corporations) have more influence on how the economy works than their customers or employees.

Finally, the quest for scientific truth is undertaken using econometrics – using statistical techniques to determine whether variables are related to each other. If economists want to determine whether the minimum wage impacts unemployment, the researcher would over time, or across different regions (or both in panel data), use unemployment as the dependent variable to be explained by the appropriately named explanatory variables (things that could reasonably be expected to influence unemployment), one of which would be changes in the minimum wage. If changes in the minimum wage are statistically related to changes in unemployment, independently of the other explanatory variables, then economists conclude that the minimum wage influences unemployment rates. This appears straightforward, but after numerous econometric tests, economists still disagree about the impact of minimum wages on unemployment.[5] The problem is that discovering incontrovertible evidence based on the very messy real world is inherently difficult even with advanced econometric techniques. Further, as was the case with modeling, the conclusions from econometric testing depend a great deal on choices made by the investigator - the choice of econometric technique to be used, what to use as explanatory variables, the choice of data to name but a few. Economics is hardly the only social science to engage in these kinds of statistical techniques. They have become commonplace in most of the other disciplines as well. However, it was economics that largely introduced these techniques that put the science in social science. It also has a centrality in economics that it does not hold in other social sciences. Indeed, as economists expand beyond their traditional subject areas, it is this method of enquiry that may come to define the discipline.

Critics of the Economic Mainstream

The old economic mainstream, and its four pillars, has been subject to longstanding criticisms. One stream of criticism revolved around the economic method. Broadly speaking, the concern of these critics focused on the perceived tendency in economics to lose itself in abstract modeling, econometric technique, and unrealistic assumptions that rendered it incapable of addressing real world economic issues. The problem here is one of emphasis. Critics in this tradition are not arguing that all modeling is useless. Modeling can illuminate real world phenomena, but in economics it has evolved into an end unto itself. This is a concern that has been long expressed but remains unaddressed. A 1988 Commission to review graduate training set up by the American Economic Association expressed concern that it was churning out, "*idiot savants*" that were narrowly brilliant in terms of technique but were completely ignorant of actual economic issues[6]. One of the more longstanding critics in this vein is Tony Lawson of Cambridge University who argues that what he considers to be the disciplines' numerous failings stem from its insistence on "mathematical deductivist reasoning" as the benchmark language[7]. The inability of almost all the mainstream economists to foresee the economic crisis of 2008 (or in many cases actively argue that the policies in place made an economic crisis nigh on impossible) brought some big economic names into the Lawson camp. Columbia University economist Jeffrey Sachs, argued that the reliance on modeling has distracted economists' attention from the "underlying mechanisms in the economy."[8] Willem Buiter, who taught at the London School of Economics and Yale and is currently the chief economist at Citigroup, argued the emphasis on mathematical rigor, and the unrealistic assumptions that were needed to make models solvable left macroeconomists woefully unable to address the 2008 crisis, describing the state of the discipline as "self-referential, inward-looking distractions at best." As a result of the emphasis on modeling and mathematical tractability, concern with anything approaching the actual economy, especially the possibility of the economy under stress, meant that the profession was unable to predict the crisis.[9]

An alternative criticism of mainstream economics is that, at least since the 1980s, it has grown increasingly enamored of free markets and suspicious of the state[10]. The "free market" criticism gained increased traction after the 2008 economic crisis, which many commentators attributed, at least in part, to a withdrawal of state oversight in the financial sector, a policy justified by economic theory.[11] Even Alan Greenspan, one of the champions of deregulation of the U.S. financial system leading up to the 2008 crisis in his capacity as the Chair of the Federal Reserve, declared partial culpability on this front admitting that his faith in free markets was "a flaw."[12] Critics who argue that economics has developed a free market bias have been provided with ample evidence to bolster their argument. Even in the aftershock of the 2008 crisis, which tragically demonstrated the dangers of laissez faire policy in the financial sector, mainstream economics has not only continued to insist on its usefulness, but to confer economics' highest award to the more dogmatic proponents of free markets. In 2013, Eugene Fama, the originator of the efficient markets hypothesis, which "demonstrated" the impossibility of asset market bubbles (the flashpoint of the 2008 crisis), was one of the winners of the Nobel Prize. This would be akin to astronomy awarding its highest prize to someone who "proved" that the sun revolved around the earth.

While both the technique and free market criticisms do reveal considerable flaws in the economic discipline, they do not explicitly acknowledge the most fundamental gap in how the discipline of economics understands the economy.

What is Really Missing? The Economic System

In the late 1990s and early 2000s critics of mainstream economics like Sheila Dow[13] and Robert Heilbroner & William Milberg[14] argued that the problem with economics' reliance on the four pillars is that they lead to a lack of attention of broader social forces, or macrofoundations, on the individual. People do make choices, but a focus on individual choice, rather than the powerful social and economic institutions that shape those choices, pulls a veil over what actually determines economic reality. Humans do not form preferences in a vacuum. They are not handed down by a divine being. Rather they are formed from their earliest moments of infancy through exposure to social conventions and shaped by the dominant institutions. A focus on the individual ignores the fact that this individual is significantly influenced by its social surroundings and influences. According to Heilbroner and Milberg economics, and all social sciences, should strive to "penetrate the façade of 'the individual' to its social roots."[15] Perhaps most important among these macrofoundations that were being neglected was the role of the economic system itself in shaping behavior and creating power relationships in society. While the methodological critique mentioned earlier in the chapter does contain an important element of truth the focus on econometrics and mathematical modeling is particularly problematic in so far it is focused on the individual as the primary explanatory agent without an exploration of the social and economic context.

We would argue that the most damning of the four "old" mainstream pillars is the use of the individual as the centre of analysis, which ignores what Heilbroner-Milberg describe as the "social forces" that influence the individual. In particular, the question is whether the approach to those crucial issues investigated in the research of the JBC winner, from poverty in the developing world to the merits of progressive taxation, contain an analysis that incorporates the systematic role of the power, particularly, although not exclusively, that of the corporation in an economic system dependent on private investment for employment, innovation and growth.

As authors like Lawson point out, the methods of modern economics do not make for hospitable ground for an analysis of power in the economic system. It is here that we can see the interrelationship between the method and the free market critiques which were presented as distinct earlier in the chapter. One strain of the methodological critique (associated with people like Lawson) is that the economic insistence on mathematical rigor and tractable models does not merely abstract from reality, but creates a specific kind of bias in economic analysis, toward free market results and away from concerns about power and broader social forces on the individual. This connection is identified by those who favor a more ideological explanation for the direction of modern mainstream economics like Dow. In comparing the approaches of the old mainstream and newer game theoretic approaches with a feminist, political economy method, Dow argues that simplifying assumptions allow the former to, "yield sharp definitive results," while the latter emphasize, how the individual is influenced by the social, the evolution of social convention and how economic and social structures influence each other[16]. Ignoring social forces, conventions and economic structures is not ideologically neutral. It ignores the power relationships that exist in an economic system, hiding the impact of broader social forces in the cloak of individual choice. [17]

This is not to say that economics should not be commended for its commitment to seeking chains of reasoning as well as the mathematical and statistical quest for a rigorous understanding of how the world actually works. However, we will investigate the extent to which Acemoglu's work on development tethers his technical chains to something that resembles a capitalist economy - something that was not accomplished in the "old" mainstream. To borrow a phrase from Anwar Shaikh, in economics mathematical formalization has not resulted in rigor, so much as "rigor mortis."[18]

Acemoglu: Time Inconsistency

Acemoglu is a professor at the Massachusetts Institute of Technology. As of 2014 he was one of the most cited economists in the world. His 2012 book *Why Nations Fail: The Origins of Power, Prosperity and Poverty* was shortlisted for the Financial Times and Goldman Sachs Business Book of the Year Award. Acemoglu is prolific, writing on a wide range of topics, but his most influential work is on development. We will focus on his most famous theory, on the connection between colonial rule and development from his article (along with Simon Johnson and James Robinson) "The Colonial Origins of Comparative Development: An Empirical Investigation"[19] and the book "*Why Nations Fail*?"[20] as well as a recent paper on global innovation in an interconnected world "Can't we all be more like Scandanavians"

Acemoglu argues that the roots of economic success or failure can be found deeper than what he claims are the surface causes that previous researchers had identified, like agricultural productivity, education levels or savings rates. These things may be important, but they are not causes. Rather, they are caused by the appropriate institutional structure. For Acemoglu, good institutions, like those in South Korea or the US, are inclusive. They "feature secure private property, an unbiased system of law, and a provision of public services that provides a level playing field in which people can exchange and contract; it must also permit the entry of new business and let people choose their careers."[21] Poor economic performance is caused by failure to follow this straightforward policy prescription. Africa is a cautionary tale: "Property rights have been insecure and very inefficiently organized, markets have not functioned well, states have been weak and political systems have not provided public goods.[22] The greatest threat to property rights and markets is a predatory state in which government levies high and arbitrary taxes or expropriates land and property. This uncertainty reduces individuals' willingness to save and invest and is the root cause of low productivity, saving and growth. Low educational attainment can be explained by the lack of incentive for people to get educated and the unwillingness of an extractive government to fund education.[23] The root of poverty is found in rapacious states that enrich their member elites at the expense of their population. The question, then, is how did these kinds of destructive states come about? Much of the blame lies with the lasting legacy of colonialism.

While extractive institutions certainly existed in today's impoverished nations before the arrival of Europeans, colonial states often created rules designed to dispossess the native population and transfer resources from the colony to the home nation. This is not true of all colonies, however. Acemoglu argues that there is a crucial distinction between "settler" colonies, which had large European populations, and those where Europeans faced high mortality rates, and would not settle. In settler colonies, like the US, Canada, Australia, and New Zealand, the settlers set up institutions that enforced the rule of law and encouraged investment (At least for themselves. They were less committed to the property rights of the native populations). In the other extreme, as in the Congo or the Gold Coast, they set up extractive states with the intention of transferring resources rapidly to the colonizing nation.[24] Further, the detrimental, predatory institutions set up by colonizers persisted well after independence because colonialism created political structures that inhibited growth and heterogeneous nations that were difficult to govern.[25]

The wealthy European nations, by contrast, owe their success to institutions that are beneficial to economic growth. “Political institutions placing limits and constraints on state power are essential for the incentives to undertake investments and for sustained economic growth.”[26] Acemoglu and his co-authors note that the rise of Europe between 1500 and 1850 was concentrated in the Atlantic ports. They argue that this was not only due to the obvious mechanism of an increase in profits because of the lucrative colonial trade, but also, crucially, that the growing political strength of the emerging merchant class in the non-absolutist nations of the Netherlands and England resulted in increasing protections of private property rights from expropriation by the monarchy. In the English example, during both the Civil War and the Glorious Revolution merchants sided with those who wished to decrease the rights of the monarchy. Anti-monarchy victories in these conflicts resulted in “major checks on royal power and strengthened the rights of merchants.”[27] In countries in which strong merchant classes were able to protect property rights by limiting the monarchy’s privileges to grant monopolies and impose arbitrary taxes, economic growth followed.

The list of inclusive, non-extractive states is long and remarkably diverse, able to encompass widely varied development paths such as the US, South Korea and Lula’s Brazil. Although Acemoglu’s stress is certainly on the security of property rights, this should not be mistaken for a free hand for business. Part of what constitutes inclusive economic policy is a limit to the power of large business, especially in the crony capitalist form that Acemoglu sees emerging in the US currently. Markets are, therefore, not sufficient to ensure inclusiveness. They can tend to concentration, resulting in the rise of political and economic elite. One of the more inclusive, and therefore, beneficial periods in US development was when the anti-trust movement of Progressive period in the early 1900s limited the power of the robber barons.[28] More currently, the rise of the Worker's Party in Brazil, from its creation of "participatory budgeting" in Porto Allegre to Lula's presidential election in 2002, was based on a broad coalition of social movements that sought to remove political and economic power from the hands of the military elite and their business allies and return it to Brazilians. Acemoglu notes that the rise of the Worker's Party corresponded to a period of strong economic growth, declining inequality and much higher educational attainment in the country.[29]

Yet equality is not unequivocally beneficial. In a more current twist on the importance of incentives and private property rights, Acemoglu argues that, what he terms, "cutthroat" capitalist nations (the US), with greater inequality, are more innovative than "cuddly" countries (Scandinavia) with stronger redistributive institutions. The argument is that the greater the gap between successful and unsuccessful entrepreneurs, the greater the innovation. For an individual country, redistributive institutions, like unions or social democracy that improve the consumption of those at the lower end of the income distribution, may result in increasing welfare. However, although cuddly Scandinavian capitalism may be appealing to an individual nation, since it is the U.S.'s version of cutthroat capitalism that drives innovation in the world economy, the comfort of the cuddly is only possible through free riding on the inequality of the cutthroat. Acemoglu's evidence is that in the much more unequal US, people work longer hours and the file more patents per capita than Scandinavian countries.[30] Therefore, if we were all Scandanavians, the world would be a poorer place.

An Evaluation of Acemoglu: Current International Events and The Innovative State

Arguing that colonialism has been a problem for the colonized is a welcome improvement on much economic analysis of the problems of development, which has often been ahistorical and free of context. Acemoglu is no doubt correct in arguing that the colonial experience left much of the developing world at a considerable, and persistent, disadvantage. However welcome Acemoglu's focus on the pernicious institutional legacy of colonialism may be, it overlooks much of what is currently hindering impoverished nations and places too much emphasis on property rights as the driver of economic success.

First, as an explanation of "why nations fail" it omits the more current external factors that have had a detrimental impact on developing nations. While Acemoglu is very clear that the current predatory governments are a lasting legacy of colonization, the reason that nations fail appears to be the shortcomings of the state in the former non settler colonies. Yet it is not only the governing elite that siphon off wealth from the impoverished citizens of the developing world. Nor is it often true that the governing elite are a result of a political process, democratic or otherwise, internal to former colonies. A variety of post-colonial institutions from MNCs, to developed country governments and their military, to international institutions have played a crucial role in hindering the growth of poor nations. However, to illustrate why this point in so important we might use one of Acemoglu's own examples - Mobutu's reign in the Congo.

Acemoglu argues that the precolonial Kongo was ruled by an absolutist king whose personal wealth stemmed from extracting income from his unfortunate subjects through slavery and arbitrary, exorbitant, taxation. The extractive institutions created no incentive for the population to save and invest since any increases in income would simply be taxed away. The negative impact of the king was such that people moved as far away from established roads and markets as possible to avoid the reach of their grabbing ruler. The arrival of the Europeans replaced the domestic despot with an even more gluttonous foreign one – most famously the Belgians under King Leopold II. According to Acemoglu, on achieving independence, the extractive, "institutions, incentives and performance reproduced itself" under the rule of Mobutu.[31] So it is extractive institutions that keep the Congo poor.

It is true that extractive institutions kept the Congo poor, but confining the post-colonial extractive institutions to the obviously parasitic domestic elite headed by Mobutu leaves much of the tale untold. Mobutu came to power after the previous democratically elected Prime Minister, Patrice Lumumba, was overthrown following a civil war in which the mineral rich province of Katanga, supported by the Belgian government and mining companies like Union Minière, fought for independence. Lumumba's overthrow and subsequent death by firing squad was actively sought, financed and supervised by not only the Belgians but also the UK and the US (who attempted a CIA inspired assassination using poisoned toothpaste). The US then supported Mobutu during his reign from 1965 to 1997, during which he managed to amass a personal fortune of somewhere between $50 million, by his own reckoning, and $5 billion, according to the US State Department (one could argue that not all this money was squandered - Mobutu was the financial backer of the famous 1974 "Rumble in the Jungle" heavy weight championship between Muhammad Ali and George Foreman), while the average income in his country was 60 cents a day.[32] Not only was the US involved in financing Mobutu's lengthy stay in power, in the late 1980s it also pressured the IMF and World Bank to extend $275 million in additional loans to the Congo over the objections of the senior staff who correctly predicted that there was very little chance that the country would ever be able to repay the loan given the rapacious nature of its current government.[33] Mobutu's predatory regime was not merely a legacy of colonial institutions but put in place and supported by foreign firms and governments.

The Mobutu example is not an anomaly in *Why Nations Fail*. There is little mention of any post-colonial, negative, external influences on impoverished nations. The *Why Nations Fail* index has no listing for MNCs, foreign direct investment or a role for the US military and espionage in shaping the fortunes of developing countries anywhere in the world. Yet, one could argue that MNCs extracted significant income from the developing world. Further, as was the case in the Congo and so many other countries, MNCs actively intervened in the domestic politics of developing world. It is, therefore, inaccurate to paint the governments of developing countries as the sole culprit in extraction and corruption.

The IMF does merit some mention in *Why Nations Fail* - in five of the four hundred and sixty two pages. The problem with the IMF is that its "sensible" policies were, "not adopted, not implemented, or implemented in name only."[34] The abysmal economic performance of countries that had IMF policies foisted on them in the wake of the debt crisis was not the fault of the policies themselves but because "their intent was subverted or politicians used other ways to blunt their impact."[35] *Why Nations Fail* suggests that the real problem with the IMF was that, as outsiders, they failed to understand that their reasonable policies would be subverted by extractive governments. However, the problem with the IMF was that an external body was imposing free market policies that were much more successful in ensuring that debt repayments continued to flow to creditors than improving the economies of debtor nations. The IMF, and the other current international economic institutions, that have contributed to the poverty of the developing world are largely ignored by Acemoglu. Developed country influence on the developing world is not limited to the admittedly horrific legacy of long dead generations, but a current, ongoing phenomenon.[1] Acemoglu's focus on the persistent detrimental legacy of

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[1] Similarly, Acemoglu and Robinson's *Economic Origins of Dictatorship and Democracy* (2006) seeks to explain which of these two forms of government will emerge in a nation almost exclusively using economic factors internal to a nation. For example, the discussion of the political history of

colonialism is no doubt a component of the explanation for the gap between rich and poor nations. It is also a welcome inclusion of historical and comparative analysis, albeit not one that will be unfamiliar to economists outside the mainstream. Yet, crucially, it ignores the most powerful contemporary determinants of the economic trajectories of developing nations.

Acemoglu's attachment to property rights as the main driver of economic success has been criticized as dangerously one dimensional.[36] It downplays the crucial role that governments often play in innovation and growth. Although Acemoglu certainly advocates for "inclusive" economic and political institutions that level the playing field like those in Porto Allegre, even arguing for rules that would favor strong unions because of their important role in the democratic process,[37] the overarching message is that the role of government is to ensure property rights while avoiding the kind of crony capitalism that results in too much power for too few businesses. Yet other scholars have argued that many successful nations have relied extensively on a much more active state than that which is implied by Acemoglu. Ironically, this is particularly true of the nations that are currently strong advocates of non-intervention like the US and UK. Both of these nations used tariffs and subsidies during their early industrializing period to foster the growth of particular sectors.[38] An active state can also be important in creating innovation according to Mariana Mazzucato's book, *The Entrepreneurial State*. Contrary to the popular myth that the dynamism of the private sector can be contrasted with the moribund, bureaucratic

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Guatemala, El Salvador and Nicaragua makes no meaningful mention of the determining role of US influence.

government, many of the most important inventions, from pharmaceuticals to electronics, owe an often unacknowledged debt to the state. Just to take one example, the high tech poster child, Apple, benefitted substantially from ground breaking public innovation. It was the government that undertook the initial research that created the internet, touchscreens, GPS and voice activated "assistants" like Siri, which are so vital to Apple's products.[39] According to Mazzucato, US venture capitalists waited for the state to take the big risks in research and development, and after companies like Apple adopted these publically funded technologies they hid their profits in tax havens, undermining the capacity for future innovation.

Mazzucato's arguments are a more recent take on those of Lester Thurow, the former Dean of MIT's Sloan School of Management, who argued in *The Future of Capitalism* that private firms in a competitive environment will underinvest in research and development for several reasons.[40] First, research, especially at its more basic levels, is a positive externality. Spillover benefits mean that the social benefits are much greater than the private remunerations to the innovating firm. Second, private firms will not invest in research and development because they tend to have short-term time horizons. Corporations that must maintain shareholders' rates of return in a competitive environment cannot afford to undertake costly current investments for long run payoffs. Since the return to basic, as opposed to applied, science is both longer term and more uncertain, it is unlikely that private firms in the US would undertake this type of research. Because governments tend to be more indifferent as to who reaps the benefits from investments in innovation, nor is it focused on its own rate of profit, it plays an essential role in the long-term investment in capitalist economies. According to Thurow, the claim that innovation occurs due to intense competition in a profit maximizing corporate system is very misleading. In fact, he argues, that it is competition that limits firms' willingness to engage in basic research.

While Acemoglu's choice of exemplar nations includes those that have employed activist governments, the focus on property rights creates the impression that it is the private sector that generates innovation and prosperity, when, in fact, the role of government in most wealthy nations has been far more interventionist, using protectionist policies to foster domestic firms and spending billions in research funding to provide innovative technology for companies.

Finally, it is worth contesting Acemoglu's claim that cutthroat capitalism, with more inequality, is more innovative than the cuddly version. The logic behind this is that innovators need to be provided with the incentive of insecure incomes. The evidence for this is that in one model cutthroat nation, the US, workers put in longer hours and residents have registered more patents per capita than the more cuddly Scandinavian countries.[41] It is true that US workers toil longer than their wealthy country counterparts. By the mid 2000s it was not uncommon in the US for men to work more than 60 hours a week and women to work more than 50. A growing number of people took on two or three jobs. All told, by the 2000s, the typical

American worker worked more than 2,200 hours a year — 350 hours more than the average European, more hours even than the typically industrious Japanese. It was many more hours than the typical American middle-class family had worked in 1979 — 500 hours longer, a full 12 weeks more. Americans now sleep between one and two hours less than they did in the 1960s.[42] However, the connection between working hours and innovation is not immediately obvious. The number of hours worked by an increasingly income constrained US labor force appears to be more a measure of desperation due to stagnant wages and unprecedented personal debt than of innovation. In fact, there are two America's, where a cutthroat existence is the norm for the vast majority and a cuddly one for the corporate wealthy. It is the American business class that is coddled with huge government subsidies, tax incentives, and public sector funded research. They are better off than their fellow classmates in Scandinavia.

Even the superior patent per capita measure is fairly limited. If Acemoglu had chosen an alternative, like the World Economic Forum's (WEF) annual Global Competitiveness Report ranking of nations' innovation, his conclusions might have been different. The WEF is funded and populated by the world's largest corporations. In the 2013-2014 Report, Finland ranked 1st, Sweden 6th, and the US 7th on innovation.[43] Further, to the extent that the US is an innovative nation, one could question whether this should be attributed to its insecure and unequal income distribution, as Acemolgu has done, or the entrepreneurial role of its government, as Mazzucato has suggested. Many scholars - perhaps most famously Richard

Wilkinson and Kate Pickett's *The Spirit Level* – have pointed out that inequality of outcome is a problem. Unequal nations fare more poorly than those that are equal on a myriad of social indicators, including health, education, social mobility and violence.[44] According to Wilkinson, "if you want to live the American dream, you should move to Finland or Denmark."[45] Given the uncertainty associated with both Acemoglu's measures and sources of innovation, it would seem to be an unwise justification for the difficulties that come with pronounced inequality.

Conclusion

In his work on development, Acemoglu departs, perhaps, more noticeably than any other JBC winner from the four pillars of the old mainstream. He often goes without formal modeling. Although he incorporates statistical testing, it is not the focus of his method, which is often much more historical. He does not focus on the individual as the primary unit of analysis. He does pay attention to the broad social and historical context in which individual actors operate and acknowledges the role that power can play, at least the power of colonial powers over their colonies.

Acemoglu's analysis does explicitly focus on the evolution of institutions as an explanation of economic success or failure. He argues that slow economic growth in the developing world is caused by poorly functioning institutions that are an enduring legacy of colonial systems that were set up to extract resources. Yet his view of institutional failure is limited to developing country governments failing to create a strong system of property rights and expropriating income for its own benefit. His analysis does not acknowledge the crucial continuing role of the international economic system in creating impediments for development through contemporary multinational corporations, developed country governments and international institutions like the IMF. Further, his claim that an equal nation can only thrive by free riding on the technological innovation of the more unequal cutthroat fails to distinguish between who is cuddled and whose throat in being cut in the US. It also may not be a very accurate gauge of what promotes growth, prosperity and equality.

It would be difficult to argue that the external power of multinational corporations, the IMF, and current foreign governments did not have a significant, if not determining, influence on the development of many poor countries. Yet it would be difficult to find any mention of these recent external factors in Acemeglu. Acemoglu does not fit nicely into the tradition of neglecting the social and economic macrofoundations that was criticized by Dow, Heilbroner and Milberg. He does pay attention to the big picture. However, his focus on colonialism and its legacy in creating extractive developing country governments neglects the current macrofoundations by ignoring the modern international institutions that create arguably the most significant impediments to the development of poorer nations.

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