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BOOK REVIEWS

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Rethinking what every economics student needs to know

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1. Introduction

There is a strong case to re-evaluate and change what economics students learn in their introductory courses (see, for example, Bowles & Carlin, in press; Tieleman, de Muijnck, Kavelaars, & Ostermeijer, 2018). Leading textbooks (for example, Mankiw, 2017 [1998]) have been extensively criticised for lagging behind current developments in research, misleading oversimplifications, and providing an emphasis on frictionless free markets.

Komlos' book 'Foundations of Real-World Economics' (2019) provides a timely alternative to what is currently available on the market. Under the banner of 'humanistic economics', which revolves around the central question 'for whom' the economy is doing well, Komlos sets off to expose the differences between imaginary and real markets. The book provides readers with a rich account of actual economic actors and their decision-making processes, how these differ from the frictionless free markets that are most often presented in standard introductory textbooks, and how these simplifications can result in misleading economic conclusions.

Our review is structured as follows. We first present a summary of the contents, then outline the most notable contributions, and finally discuss some points for improvement.

2. Contents summary

The first chapter invites readers to step outside the world of 'blackboard economics' and to accept and appreciate the messiness of real markets. Through the example of Greenspan's famous admission in Congress,[1] readers are made aware, early on, that ideology is unavoidable in economics. That said, Komlos believes that the main task of the economist is to 'verify if particular markets do what we expect […] and improve their functioning so that we ourselves can function better in them' (p. 10). Meanwhile, just as markets are a human construct, so are institutions which should ensure the proper treatment of humans, against pain, suffering and poverty, and enhance human dignity and self-worth. In this sense, Komlos' vision combines a focus on markets with a discussion of values.

Having laid out the characteristics for a 'humane capitalist' economy, the second chapter paints a picture of the power and limitations of markets. On the one hand, markets have been phenomenal tools to spur innovation, increase incomes, and create an abundance of material goods. However, on the other hand, Komlos is concerned that we have made little progress outside the realm of material consumption such as emotional wellbeing, the fight against discrimination, and the persistence of poverty.

The book then splits into two core sections. The first half of the book (chapters 3 through 9) is dedicated to presenting a micro-foundational account of how and why markets often fail. Concepts such as endogenous tastes, bounded rationality, interdependent utility functions, joint-production functions, imperfect information, and imperfect competition are presented as severe limitations of the simplified models present in standard economics textbooks. Komlos outlines market failures as inherent to all market economies and therefore argues that we should view the role of government as complementary to markets, rather than a (imperfect) substitute. That said, Komlos also discusses instances where the government can fail, for example in the face of immense concentration of money, lobbyists can create perverse incentives for policymakers to extract private benefits at the expense of society.

The second half of the book (chapters 10 through 15) is dedicated to macro themes. After presenting a brief history of macroeconomic thought, Komlos goes on to question the often contradictory assumptions between 'micro' and 'macro' models, and discusses methodological issues in official statistics. Komlos is critical of the omission of debt, finance, long-term contracts, and herding behaviour in neoclassical models. He is also concerned that theorising based on representative agents with perfect foresight has created a policy irrelevance in the discipline as crises are (by design) not supposed to happen in these models. While Pareto efficiency is praised in 'micro' analysis, it is 'conveniently' forgotten when it comes to macro concepts, such as technological change and free trade. Along with the issue of converting monetary gains to welfare and the non-trivial issue of compensation in a dynamic economy, he argues that this causes distributional issues which often spill over into the political realm and is evident from the rise of nationalistic parties, such as Trumpism in the US.

In the final chapters of each section (Chapters 9, 14 and 15), Komlos applies the ideas presented in the book to provide a critical evaluation of some controversial and misleading policy conclusions and describes the key factors that contributed to the financial crisis of 2008. He ends by proposing various alternative policy responses to the crisis and reviews the current state of the US economy.

3. Notable contributions of Komlos' real world economics

Komlos' book serves as a critique of two interrelated domains and their relevance for the real world: mainstream economics, and contemporary teaching and textbooks. We first introduce the two main successes of the book, and then, in the next section, give a list of constructive suggestions that might improve it.

The first and most notable merit of the textbook is the distinctive line Komlos draws between imaginary and real markets and the use of examples and evidence from the contemporary world to illustrate this. Komlos convincingly argues that contemporary textbooks paint an imaginary view of people and markets. An 'economic agent' is described as selfish, rational, and acting in isolation. This agent maximises their own utility given exogenous preferences and has infinite wants and desires. Identical agents derive utility *solely* via consumption of market goods which are homogenous. Information is perfect and production is generally sold by identical, competitive firms such that the balance of power is equally shared. There is no time dimension and markets occasionally fail due to externalities, public goods, imperfect information, and market power.

In contrast to that view, Komlos argues that people in real markets act within groups and are subject to societal norms, have bounded rationality, and are guided by emotions, empathy, and fairness. Preferences are endogenous and context-dependent while wants are a cultural construction that can change due to external influences such as advertisement. Consumers are composed of people of different ages, gender, class, wealth, power, race, and impatience. Meanwhile, firms are composed of shareholders, a board of directors, CEOs, as well as employees, and products are heterogeneous along the dimension of branding and quality. Monopoly/oligopoly and monopsony power leads to power imbalances between lender and debtor, employee and employer. Information is asymmetric and incomplete in the presence of uncertainty and imperfect foresight which causes transaction/search costs and speculation. Finally, a key element of markets is that they are dynamic, so long-term decisions can result in path dependency, and rather than market failure being seen as an exception to the rule, it is endemic to all market economies and *also* includes: missing markets, common property, networks, collusion, transaction costs, opportunistic behaviour, corruption, discrimination, illicit activity, and imperfect capital markets.

We agree with Komlos in that '[blackboard economics] presents a caricature of the economy at a level of abstraction that creates a fantasy world and distorts the students' vision' (p. 6). More emphasis needs to be put into properly understanding the implications of the assumptions inherent in economic models and it is 'insufficient to mention the assumptions at the beginning of the course' (p. 14). We need to move on from the notion that 'we know that markets work' to 'admit[ting] at the outset that while markets work well in some circumstances they only do so within an appropriate institutional framework, and not only work inefficiently in others but often tip the stream of benefits towards a few insiders' (p. 1).

A second valuable contribution is the book's extensive emphasis on inequality, poverty, and power. Bowles and Carlin's (in press) findings point towards inequality as 'the most pressing problem economists should be addressing.'[2] Given the emphasis on distributional concerns, Komlos' book appears to be well suited to what students want to be taught.

The distinction between basic needs and wants but also between three types of goods as necessities, comfort goods, and luxuries is important. Komlos warns that some goods such as health care are more essential for life than others, so we should not make the mistake of bundling all goods and services together as this could cause us to severely bias our estimates of welfare. He also argues that in the predominantly oligopolistic structure of current economies, the distribution of income is derived essentially from the distribution of power. Sellers are concentrated and are able to manipulate tastes, preferences and prices. Big corporations, pharma industries, the financial sector, militaries, and lobbies have enormous power that makes a fair distribution impossible. We appreciate that Komlos brings these issues to the forefront of the discussion as students rarely see the word 'power' used in this conext in most textbooks.

4. Points for improvement

4.1. Fair and balanced account of competing views to enable critical and reflective thinking

We appreciate the extensive emphasis that Komlos puts on market failures. We share his sentiment in thinking that economic education should pay more attention to when and why markets do not provide efficient and fair outcomes. However, we also think that a fair critique should aim at a balanced investigation which not only accounts for market failure but also the strength of markets and government failure. For instance, Komlos assigns 'opportunistic behavior' almost exclusively to private sector managers (pp. 144–145). However, state bureaucrats and public sector employees face many of the same problems, such as the principal-agent problem.[3] Lobbying activities are described as harmful to regulations for the 'social good' and are part of 'regulatory capture', which is equivalent to saying that the government is good per se but the private sector does not let it be good by putting the blame solely on the private sector.

Komlos repeatedly expresses the view that people and government should regulate and control the market. The government is introduced to 'represent our collective will—our collective interest-which we cannot adequately enforce as individuals' (p. 27). However, we are concerned that the book portrays the line demarcating people-and-market too thickly, while the people-and-government line is too thin. It even seems that the terms 'people' and 'government' are used interchangeably. Some accounts of government failure are given in several parts of the book; however, these are not as balanced as the discussion on market failures.

Both markets and governments fail, not necessarily in relation to each other but compared to their ideal conceptualisations. For a fair and more complete discussion, we would like to see a more balanced view of market failure and government failure, but also alternative modes of organisation and collective action. We believe that balancing these views in a textbook would improve critical and reflective thinking.

4.2. Substantial pluralism and historically informed narrative of disciplines

Komlos' book provides a wide array of citations which do not often find their way into economics textbooks, such as those of Sigmund Freud, Ivan Pavlov, Erich Fromm, Theodore W. Adorno, and

Aldous Huxley. The book also introduces many schools of thought and methods in economics, so it presents a pluralist perspective. However, though we appreciate this attempt, and understand the difficulty of including all schools and methods, we must admit that their descriptions often come at the very end of a discussion and remain somewhat superficial. We suggest going into more detail and providing a more substantial discussion of them.

Meanwhile, Komlos suggests that economics should interact more with sociology, psychology, political science and philosophy, rather than rely on math in order to avoid ending up with a mechanistic view of the world. We agree that economics should embrace more interdisciplinarity, but would nevertheless like to remind readers that these other disciplines are also the result of historical processes and are not necessarily as they seem to outsiders today.[4] We suggest giving a hint of a historically informed narrative of associated disciplines to provide students with a more realistic view of the development of scientific thought and practice, rather than only comparing the current state of other disciplines to the current state of economics.

4.3. Realism but also ideas and analytical thinking

Komlos provides the reader with many examples, numbers, and rankings. So the book is very rich in real-world examples and most of its argumentation is evidence-based. We appreciate this very much. However, to save the book from crossing the thin line between realistic accounts and unsubstantiated empiricism, we would recommend to have fewer examples with more elaboration. Empirics can sometimes be confusing, or more troublingly, too selective (i.e. cherry picking), while the argumentation of the message gets lost between empirical facts and numbers. So we want realism and evidence, but we also want to avoid the cost of discarding relevant theory and argumentation.

4.4. Clear structure, target audience, and position in the textbook market

Before we conclude, we would like to mention three limitations which hinder this book to reach a wider audience. The first is the book's structure, which is not clear enough to improve readability and reduce confusion. The chapters of the book are currently organised by headers, however the ideas presented do not always link up well and various ideas are repeated in different chapters, such as the discussion of transaction costs and endogenous tastes.

The second limitation is the lack of an explicit account for whom the book is targeted. We are still not entirely sure whether this book is for students or teachers, and if it is for students, what level of knowledge they are expected to have. The book seems to assume some background knowledge of mainstream economics so it may be directed to teachers, economists who know about the mainstream, or second and third-year bachelor students.

The last limitation is that it does not make clear whether the book is to replace or complement current textbooks. The first edition of Komlos' book, 'what every economics student needs to know and doesn't get in the usual principles text' (2014) was included in the World Economics Association's list of alternative texts.[5] However, we are not sure how one would choose only a single book from this list. We think that being open about the aim of a textbook would be helpful for the user. For instance, CORE's *The Economy* textbook, whose aim is to introduce students to what economists currently do and what we know, has started to be used widely since 2017. While we think Komlos' book is not a direct competitor to CORE, due to the more limited scope, set of methods, and target audience, it could be a good complement to it, especially with its elaborate discussion of market failures, distributional concerns and real-world examples.

5. Conclusion

With this book, Komlos has made an important and timely contribution to the economics textbook canon. Not only does it present a critical account outlining the weaknesses of oversimplified economic theory, but it also offers a compelling alternative emphasis with which to study the economy: humanistic economics. Throughout the book Komlos makes a strong case to re-evaluate how economics is taught at the undergraduate level through various references to academic articles and real-world examples. Although the book can benefit from a more balanced account of competing views, an improved structure, and a more targeted audience, we believe that it is nevertheless a great book for anyone interested in the differences between the abstract world of markets drawn on the blackboard and what we see in reality. This book could be useful to broaden and deepen the perspective of students, to spark much-needed discussion in the classroom, and to help lecturers bring in new, relevant material.

Notes

1. 'I made a mistake in presuming that the self-interests of organisations, specifically banks and others, were such that they were best capable of protecting their own shareholders and their equity in the firms', (Greenspan cited in an article by the Guardian (Clark & Treanor, 2008) The article can be found at: https://www.theguardian.com/business/2008/oct/24/economics-creditcrunch-federal-reserve-greenspan.
2. Bowles and Carlin (in press) asked economics teachers to pose the following question to their students: 'What is the most pressing problem economists should be addressing?'. The results from 4442 students at 25 universities in 12 countries over the years 2016–2018, indicates inequality, followed by unemployment, and poverty as the three most pressing issues.
3. The public choice school has a good critique on this. For example, in opposition to the 'fiscal brain' conception that sees the state as a homogeneous entity that has access to the social welfare function without frictions, Buchanan (1949) brings in an 'individualistic view' that suggests and appreciates that it is individuals/human beings that perform governance so imperfections and errors are unavoidable.
4. For instance, mathematics wasn't purely axiomatic and independent of the real world before its nature went into a crisis at the beginning of the twentieth century and became increasingly remote from everyday experience from then on (see the acceptance of non-Euclidian geometry and the role of Bourbakists and David Hilbert). A similar historical argument would also apply to psychology in its movement towards positive psychology which, one might argue, is not necessarily so distinct from the neoclassical school of economics. Or, formalisation in philosophy performs rather similarly with axiomatising mathematics. So we should be aware of the historical processes in other disciplines.
5. The list of alternative texts can be found at: https://www.worldeconomicsassociation.org/textbook-commentaries/alternative-texts/.

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Self-Control, Decision Theory, and Rationality – New Essays, edited by J. L. Bermúdez, Cambridge University Press, Cambridge, UK, 2018, xii + 268 pp., £75.00 (hardcover), ISBN: 978-1108329170

The history of Western philosophy is awash in platitudes championing rationality and self-control. Since Plato, philosophers have cautioned against the iniquities of a weak will and have proffered ever-evolving solutions for circumventing temptation. Today little has changed. Conventional wisdom still holds that practical rationality consists in the judicious exercise of self-control. Yet, the formal study of self-control has progressed from a purely philosophical inquiry to an interdisciplinary endeavor, implicating the cognitive and behavioral sciences as equal stakeholders in the investigation.

Much like the concept of rationality itself, the concept of self-control is a moving target – and the space through which it moves is both normative and descriptive. This is perhaps what makes it such a fascinating if perplexing phenomenon. On the one hand, self-control gives rise to normative paradoxes insofar as it requires one to forego a shorter, sooner reward for a presumably larger, later one. This contradicts classical views in decision theory which identify rational choice as consisting in the maximization of (expected) utility at every node or juncture where choice is possible. On the other hand, self-control gives rise to descriptive paradoxes because it requires persons to make sacrifices for their future selves. The question as to whether different time-slices of a person constitute motivationally disconnected agents depends in equal parts on psychological and metaphysical considerations, neither of which are uncontroversial.

In this collection, J. L. Bermúdez (ed.) draws from a coterie of interdisciplinary experts in philosophy, psychology, and economics to present the newest developments in decision theory about