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Economics of Control.

Page 531

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BIBLIOGRAPHY

The *economics of control*, perhaps best represented by Abba Lerner's (1903–1982) 1944 book of that title, based on his 1943 doctoral dissertation for the London School of Economics, is a halfway-house policy approach to capitalist economies between laissez-faire on the one side and socialist economic planning on the other. The economics of control accepts the basic institutional framework of capitalist markets as the organizing principle but recognizes market imperfections, macroeconomic deficiencies, and other problems that require government intervention to improve market outcomes. It was an attempt, in the Page 532 words of Sidney Ratner (1908–1996), at a “reconciliation of liberalism and socialism in welfare economics” (Ratner 1949, p. 133).

John Maynard Keynes (1883–1946), in a letter written at sea on a voyage to the United States during which he read *The Economics of Control*, wrote to Lerner that the latter had “written two books largely distinct ... which you have placed within one cover” (Colander and Landreth 1996, p. 116). The first was dedicated to microeconomic problems analyzed through the neoclassical marginalist approach but infused with a spirit of market socialism that Lerner described as “socialist free enterprise.” This work was part of the debate on socialist planning that has often been viewed as dealing with the question of the viability of a socialist economy but really concerned a more specific, technical issue: whether or not neoclassical theory, in particular general equilibrium analysis, was applicable to a planned economy. Friedrich August von Hayek (1899–1992) and the Austrians said no; Lerner, Oskar Lange (1904–1965), and others claimed that it was (Kirzner 1988).

The second “book” covered macroeconomics and Keynesian theory, which included demonstrating the theoretical justifications for employing Lerner's *functional finance* approach. This approach implied strong fiscal and monetary policies for promoting macro goals, such as full employment, price stability, and stable economic growth, not only for their own sake, but also because full employment was seen as a precondition for the relatively smooth workings of the microeconomy. Keynes called this “second of the two books which you have placed within one cover ... very original and grand stuff,” adding:

I shall have to try when I get back [to England, from his trip to the United States] to hold a seminar for the heads of the Treasury on Functional Finance. It will be hard going—I think I shall ask them to let me hold a seminar for their sons instead, agreeing beforehand that, if I can convince the boys, they will take it from me that it is so! (Colander and Landreth 1996, pp. 116–117)

Keynes does not trust that the heads of the Treasury can understand, because, as Lerner often noted, “Functional Finance is seen to run counter to economic principles” (Lerner 1951, p. 142). Functional finance, or Keynesian economics taken to its furthest logical conclusions (causing David Colander to ask, “Was Keynes a Keynesian or a Lernerian?” [1984]), was, in its application to unemployment, Lerner admitted, “topsy-turvy economics”: “But this is no objection at all. Topsy-turvy economics is just what is appropriate for an economy that is suffering from unemployment. An economy suffering from unemployment is an upside-down economy for which *only* a topsy-turvy economic theory is of any use” (Lerner 1951, pp. 142–143).

By an “upside-down economy,” Lerner means an economy in which strongly held traditional economic principles, such as those regarding thrift and the economical use of scarce resources, do not hold. Lerner noted that when there is unemployment, efficiency becomes inefficient: “an increase in efficiency in any particular productive process does not result

in any increase in efficiency in the economy as a whole. ... The savings due to greater technical efficiency merely go to waste in more unemployment" (Lerner 1951, pp. 143–144). Likewise when there is unemployment, a country has to suffer over its trade balance, because it must worry about rising unemployment stemming from an increase in the value of its imports over the value of exports. Since "the input of the foreign trade industry consists of the effort involved in the manufacture of our exports" and "the output of our foreign trade industry consists of the imports which it yields to us for our use," exports are a cost and imports are a benefit (Lerner 1951, p. 321). Thus when a nation attempts to cure its unemployment problems by reducing its trade deficit, it is promoting costs and restricting benefits.

Other supporters of the economics of control went beyond what they viewed as Lerner's approach, made up as it was between neoclassical welfare economics on the one side and traditional Keynesian fiscal and monetary policies on the other. Adolph Lowe (1893–1995) made the distinction between *primary* and *secondary* controls (Lowe [1965] 1977). Primary controls, or conventional economic policies, take the behavior of the microunits as given, whereas secondary controls, or what Lowe sometimes called *instrumental* controls, seek to shape the behavioral patterns of the microunits themselves, either directly or through creating the structural or environmental contexts that can influence motivations and behaviors (Lowe 1969, p. 33). Examples of the former include a variety of fiscal and monetary policies. The latter would be exemplified by policies that shape expectations (e.g., reducing uncertainty). The line between the two is not always clear, because fiscal and monetary policies can also influence expectations. If business investors know that the state is committed to maintaining a high, stable rate of growth of demand, they will have less uncertainty about future conditions that affect investment and thus output and employment. As Lerner noted, the purpose of taxation is its "effect on the *public* of influencing their economic behavior" (Lerner 1951, p. 131).

SEE ALSO *Economics, Keynesian ; Exports ; Full Employment ; Imports ; Keynes, John Maynard ; Laissez-faire ; Marginalism ; Microeconomics ; Planning ; Policy, Fiscal ; Policy, Monetary ; Socialism ; Socialism, Market ; Taxation ; Unemployment*

Page 533

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