Journal of Economic Methodology

Publication details, including instructions for authors and subscription information:
http://www.tandfonline.com/loi/rjec20

Introduction: Methodological implications of the financial crisis
Kevin D. Hoover

Available online: 10 Dec 2010

To cite this article: Kevin D. Hoover (2010): Introduction: Methodological implications of the financial crisis, Journal of Economic Methodology, 17:4, 397-398

To link to this article: http://dx.doi.org/10.1080/1350178X.2010.525037

PLEASE SCROLL DOWN FOR ARTICLE

Full terms and conditions of use: http://www.tandfonline.com/page/terms-and-conditions

This article may be used for research, teaching and private study purposes. Any substantial or systematic reproduction, re-distribution, re-selling, loan, sub-licensing, systematic supply or distribution in any form to anyone is expressly forbidden.

The publisher does not give any warranty express or implied or make any representation that the contents will be complete or accurate or up to date. The accuracy of any instructions, formulae and drug doses should be independently verified with primary sources. The publisher shall not be liable for any loss, actions, claims, proceedings, demand or costs or damages whatsoever or howsoever caused arising directly or indirectly in connection with or arising out of the use of this material.
FINANCIAL CRISIS SYMPOSIUM

Introduction: Methodological implications of the financial crisis

Kevin D. Hoover

From the end of the second US recession in the early 1980s to the end of 2007, much of the developed and developing world enjoyed an unprecedented period of economy growth, punctuated by only the mildest of recessions. As has happened in the past when the macroeconomy was particularly stable, economists began to congratulate themselves on the strength of their analysis and the wisdom of their policy advice and began to speculate that, if we merely kept it up, the end of the business cycle was at hand. Such hubris seldom goes unpunished and Nemesis came in the form of the US recession, starting in December 2007, and the financial crisis of 2008, whose tentacles reached around the world. By most accounts, the US emerged from the long recession in the summer of 2009, but the recovery has not been robust and the aftershocks of the financial crisis continue to be felt worldwide. Large segments of the public, politicians, and even many economists themselves blamed not only those economists who had directly guided policy, but economists more generally: for failing to predict the crisis, for promoting policies that contributed to it, for employing models and modes of analysis that were out of touch with economic reality, and, consequently, for failing to offer useful advice for counteracting the deep recession. Mainstream economics itself was regarded in many quarters as the source of problem. Older approaches were revived: if only policy had been more Keynesian or more Austrian or more institutionalist, perhaps the collapse could have been avoided. Mainstream economics was charged with backwardness: if only economics incorporated more fully the results of psychology, experimental, and behavioral economics; if only it abandoned mathematical rigor for agent-based simulations; if only it gave up the pretence of being a positive science and adopted a more explicitly normative approach; perhaps, then, it would offer useful guidance in escaping the crisis.

As in past crises, economics turned inward and economists began to reflect on their own discipline. Economists who had previously thought that methodology should be avoided as a diversion from practical knowledge found themselves more or less openly examining their own methodology. Seizing the moment, the International Network for Economic Method (INEM) scheduled a session entitled, ‘Methodological Implications of the Current Financial Crisis: Rational Expectations, Mechanism Design, and Moral Hazard’, for the Atlanta meetings of the Allied Social Sciences Association. This mini-symposium presents the three papers from that session (held on 5 January 2010).

The three papers span the variety of meanings of methodology. Generally, economists distinguish between economic methodology as a general reflection on the nature of economic knowledge and explanation, on the one hand, and the particular methods employed in practicing economics, on the other. Stan du Plessis draws this distinction in his paper, referring to the study of methods as small-m methodology. Economists often treat methodology as encompassing the philosophy of science with economics as a target science or even as philosophical issues in economics taken very broadly. There is, therefore, a
spectrum: philosophy – philosophy of science – highly general reflections within economics itself on the scope, nature, and practices of economics – detailed methods of economic inquiry. The three papers in the symposium can be arranged roughly from the philosophical (Don Ross) to internal economic reflection (David Colander) to specific methods (Stan du Plessis). The division is not perfectly sharp. Don Ross begins with considerations of ethics in relation to economics and with an analysis of the place of social psychology and behavioral economics in the foundations of economic analysis. Yet he ends with practical advice. David Colander’s paper, in part, recounts the 2008 Dahlem Report, ‘The Systemic Failure of the Economics Profession’, which considered, among other things, the role of mathematics in economics. His paper considers the sociology of the profession, as well as the limitations implied by a modeling monoculture. He calls for particular reforms. In contrast, du Plessis’s paper concentrates on the supposed failures of a particular modeling strategy. He argues that the models used by central banks to direct monetary policy are not flawed in themselves; but, because they omit a financial sector in which problems of financial fragility could arise, they need to be elaborated – and he argues that appropriate elaborations are available. His conclusion is, thus, similar to Colander’s in that both call for a richer set of models. But whereas Colander focuses on the range of neglected approaches in mainstream economics, du Plessis calls for a specific program that develops, rather than offers an alternative to, mainstream economics.

This is a rich set of papers. The authors do not address every issue or answer every methodological question raised by the financial crisis. But they have started a provocative conversation.