

Worlds Apart

Alan S. Blinder



There are ways to narrow the gap between economics and politics



The chronic clash between sound economics and good politics frustrates economists who venture near the political world. Much more important, it often blocks the road to better policy. The chasm is wide and won't be fully bridged. But with much effort and a modicum of goodwill, we may be able to shrink it.

Let me start by dispelling a myth. Perhaps because economists are frequently trotted out to support or oppose policies, perhaps because we have a Council of Economic Advisers right in the White House, perhaps because most powerful central banks are dominated by economic thinking, many people believe that economists have enormous influence on public policy. In truth, they don't.

In a book seven years ago, I argue that economic policymaking often adheres to the Lamppost Theory: Politicians use economics the way a drunk uses a lamppost—for support, not illumination. Economists and politicians—by which I mean not only politicians, but the entourage of advisors and message meisters who surround them—hail from different civilizations. They speak different languages. They define success differently. They have dramatically different time horizons. They even employ different logic.

Political logic

I once thought “political logic” was an oxymoron. Many economists still do. But I've learned there is a logic in politics that I'll illustrate with a trivially simple arithmetic example.

Imagine a tax break that would yield \$1 million in gains for each of 10 people but cost 20 million people \$1 apiece. Economic logic clearly counts this as bad policy. To pursue it, there would have to be some persuasive non-economic reason.

But political logic is different. The 20 million people who lose \$1 apiece will barely notice. The 10 million-dollar winners, by contrast, will not only notice this newfound largesse but will be grateful to the politicians who bestowed it. To the politicians, the gains in terms of support, campaign contributions, and the like will dwarf any political losses. Only the most highly principled politician would resist such a trade-off.

This illustrates why so many policy decisions seem so wrong to economists, not just in tax policy, but also in trade policy, regulation, antitrust, and many other areas. It would not help much, by the way, if the politicians understood economics better. Economic and political logic often point in opposite directions, and politicians will follow the latter.

A suggestion for politicians

Can we at least narrow the gap between the two worlds? Can we get politicians to put a bit more weight on the economic merits? Can we get economists to understand the political world a bit better? I think—or hope—we can. I am not naive about this. I realize that economists must do most of the changing. So I'll suggest one change for politicians and two for economists.

Politicians often can't see past the next election, but the truth is far worse. The political pros who advise politicians often can't see past the next opinion poll, or even the next tweet. Their time horizon extends only until that evening's news broadcasts, if that long.

But getting politicians to think longer term may not be hopeless. After all, politicians are adaptable. If they can be persuaded that current political habits are

counterproductive, they may change their ways—not because of a sudden burst of idealism, but because they want to win elections.

One fortunate fact is that a US president's four-year term is long enough for the major effects of most economic policies to be felt. So sound economic policies enacted during, say, the president's first year or two in office are likely to show major benefits before the next presidential election. Within that window, good economics can also be good politics.

Of course, this happy coincidence in time shrinks as the president's term progresses. But that's where the crazy US electoral calendar comes to the rescue. By the 18th month of a new presidency, attention turns to midterm congressional elections. After that, midterm losses typically make it hard for the president's party to push major initiatives through Congress. Instead, political minds turn away from policy and toward the next presidential election. Put all that together, and you see that the policy phase of a new presidential term rarely lasts more than 12–18 months. During that brief period, economic and political time horizons arguably dovetail reasonably well.

And two for economists

What about the minority of economists who wish to get involved in policy? I have two suggestions to offer here. Both cut deeply against the grain. They are *not* what we teach in graduate school.

The first pertains to time horizons again. Political time horizons are too short for sound economic policy. But it's also true that economists' time horizons are often too long for politics.

Economists typically focus on the “equilibrium” or “steady-state” effects of a policy change. What will happen *eventually* after households and businesses adjust to a change in the tax code or a trade agreement? Those questions are important and pertinent to policymaking, but they are close to irrelevant in the political world because people don't live in equilibrium states. We spend most of our lives in one *transition* or another. Economists often brush off “transition costs” as fleeting details of little importance. They shouldn't.

“Economists should pay more attention to fairness rather than doting almost exclusively on efficiency.”

Trade agreements are a good example. With some exceptions, trade theory compares one full-employment steady-state equilibrium with another. David Ricardo taught us over 200 years ago that the free-trade equilibrium is better for society as a whole (although not necessarily better for every person in society) than the equilibrium with trade protection. He was right, which is why almost all economists are free traders at heart.

But adjustment to the superior free-trade equilibrium may be lengthy and painful, involving job losses, reduced incomes for some, decimated communities, and more. Economists know all this but don't pay it sufficient heed. Politicians, by contrast, live in the real world of ever-present transition costs. They may not be in office long enough to enjoy the equilibrium benefits.

Should economists therefore embrace protectionism and the stasis that goes with it? Far from it. I use the trade example to argue a general point: Economists should spend a lot more time and effort thinking about possibly painful transition costs, and how to mitigate them, and think more about what happens before the vaunted steady-state effects arrive.

My second suggestion is that economists should pay more attention to fairness rather than doting almost exclusively on efficiency. In politics, perceived fairness almost always trumps efficiency. Politicos understand that, which is one reason economic policy is often so manifestly inefficient.

In writing this, I risk losing my economist's license. We do, after all, worship at the altar of efficiency for a good reason: Greater efficiency enlarges the economic pie. It's as close as we can get to a free lunch. So I am *not* recommending abandoning efficiency as a guidepost, only that we temper our worship of efficiency with more respect for political feasibility—which often hinges on perceived fairness.

Think of debates over the tax code, which are hardy perennials in legislatures around the world. Economists' beautiful theory of optimal taxation is built around maximum efficiency. But that theory plays no role in legislative debates. Discussions of fairness, on the other hand, dominate the debates. And we get the tax mess that we have.

Nibbling at the edges

So here's my advice to economists interested in actual—as opposed to theoretical—policymaking. Don't forget about efficiency. It matters. We are right about that. But we may have to content ourselves with nibbling around the edges, below the political headline level, to make the details of a complex policy package less inefficient. Call it the theory of the third or fourth best. We may have to settle for that. **F&D**

ALAN S. BLINDER is a professor of economics at Princeton University and a former vice chair of the Federal Reserve. This article draws on a past lecture to the American Academy of Political and Social Science.