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ECON JOURNAL WATCH
Scholarly Comments on Academic Economics

Thomas J. Sargent [Ideological Profiles of the Economics Laureates]

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Econ Journal Watch 10(3), September 2013: 570-576

Abstract

Thomas J. Sargent is among the 71 individuals who were awarded the Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel between 1969 and 2012. This ideological profile is part of the project called "The Ideological Migration of the Economics Laureates," which fills the September 2013 issue of *Econ Journal Watch*.

Keywords

Classical liberalism, economists, Nobel Prize in economics, ideology, ideological migration, intellectual biography.

JEL classification

A11, A13, B2, B3

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http://econjwatch.org/file_download/764/SargentIPEL.pdf

Thomas J. Sargent

by Daniel B. Klein, Ryan Daza, and Hannah Mead

Thomas Sargent (1943–) was born in Pasadena, California. Sargent has said that in high school he was more interested in football than academics, but his classmates remember him as being very smart (Sommer 2011b). He earned his bachelor's degree from the University of California at Berkeley, where he took his first courses in economics and political science; Sargent remembers going door-to-door for John F. Kennedy, back in "the days when all the Democrats believed in balanced budgets" (quoted in Sommer 2011b). Sargent went on to Harvard University for his Ph.D., then served on the faculties of several universities including Penn, Minnesota, Chicago, and Stanford. He has been professor of economics at New York University since 2002. In 2011, Sargent shared the Nobel Prize in economics with Christopher Sims "for their empirical research on cause and effect in the macroeconomy."

At Minnesota, Sargent, Sims, and others helped establish the so-called "freshwater school" of macroeconomics. A central distinction between the freshwater school and the rival "saltwater school" lies in the emphasis that freshwater macroeconomists place on the idea of rational expectations (Waldmann 2009; Skidelsky 2010, 29-36). Sargent explains rational expectations in an encyclopedia entry:

> The concept of rational expectations asserts that outcomes do not differ systematically (i.e., regularly or predictably) from what people expected them to be. …
>
> The rational expectations version of the permanent income hypothesis has changed the way economists think about short-term stabilization policies (such as temporary tax cuts) designed to stimulate the economy. Keynesian economists once believed that tax cuts boost disposable income and thus cause people to consume more. But according to the permanent income model, temporary tax cuts have much less of an effect on consumption than Keynesians had thought. …
>
> Rational expectations undermines the idea that policymakers can manipulate the economy by systematically making the public have false expectations. … If people have rational expectations, policies that try to manipulate the economy by inducing people into having false expectations may introduce more "noise" into the economy but cannot, on average, improve the economy's performance. …

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> The idea of rational expectations has also been a workhorse in developing prescriptions for optimally choosing monetary policy. Truman Bewley and William A. Brock have been important contributors to this literature. Bewley's and Brock's work…supports, clarifies, and extends proposals to monetary reform made by Milton Friedman in 1960 and 1968. (Sargent 2008)

In a 1998 interview, Sargent described himself and his motivation for adopting rational expectations: "I was just a straight Keynesian economist. And in those days, rational expectations were clearly sort of a next step" (Sargent 1998, 165).

In perhaps their most famous paper, "Some Unpleasant Monetarist Arithmetic," Sargent and Neil Wallace show that, "under certain circumstances, the monetary authority's control over inflation in a monetarist economy is very limited even though the monetary base and the price level remain closely connected. In particular, we will demonstrate that this is true when monetary and fiscal policies are coordinated in a certain way and the public's demand for interest-bearing government debt has a certain form" (Sargent and Wallace 1981, 1).

Sargent has sometimes bristled at attempts to pin down his political persuasion. In the 1998 interview cited above, Sargent claimed: "I don't make policy recommendations" (Sargent 1998, 169). More recently, Jeff Sommer of the *New York Times* reported:

> In telephone conversations last week, Professor Sargent said he felt insulted by people who call him "non-Keynesian" or "right wing," terms that, he said, are based on a misunderstanding of his thinking. And he rejected attempts to categorize his views in simple slogans. He doesn't wear his political opinions on his sleeve. "They really don't matter in my research," he said. (Sommer 2011a)

Sargent then described himself as "a fiscally conservative, socially liberal Democrat" who emphasizes the importance of budget constraints and incentives: "There are trade-offs in efficiency and equality…and they lead to choices that aren't easy" (quoted in Sommer 2011a).

Selections from an interview with Sargent conducted by Arjo Klamer (1984) follow, with Klamer's words shown in italics:

> *Were you political in [your Berkeley undergraduate] days?*
>
> The students at Berkeley had a critical tone at least since the '30s. It was always a place that attracted critical and radical students. I was one in a quiet way. I read a lot of philosophy and political philosophy,

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largely in courses, and I thought a lot about it when we discussed it. I was certainly very liberal, but I wasn't a political activist. I studied hard. (Sargent 1984, 59)

Did you go to Vietnam?

I went through ROTC, was commissioned, and then worked in the systems analysis office of the Pentagon. It changed me in some ways, made me more conservative. I came to understand more clearly the limitations of government actions. It was a learning experience. My conclusions came from seeing the whole decision-making process by which the US got into the war: how we evaluated the situation, how we processed the data from the war, how we understood our options, what we saw as the resources and costs in Southeast Asia, and what we thought was the likely outcome. We didn't do a very good job. There was an incredible volume of inefficient and bad decisions, which one must take into account when devising institutions for making policy. (ibid., 62)

Which other economists have been important for you?

Milton Friedman has been an important person in terms of educating me. I've never taken a class from him, but I've read his stuff. His work and Tobin's are important for me. Trying to figure out what those guys have done has been a continuing source of education for me. (ibid.)

Are the political aspects an important motivation?

I'm not really interested in politics. This rational expectations stuff is clearly not politically motivated. People from all sorts of different political perspectives contribute to it. It's more a technical revolution. One of the early lines of criticism was that this was just a new version of right-wing economics. The trouble with that criticism is that most of the guys were voting for McGovern; they were liberal democrats. More than half of the guys anyway. That's not the issue. These are technical issues about staring at models. If you look at the Keynesian models, if you stare at them hard, you get to the same point that Lucas was at. That means you're on to something.

No, it's certainly not politically motivated. It is technically motivated … I don't dislike government intervention per se. When I came out of Berkeley and Harvard I had a really naïve view of what the government could accomplish. It was my own fault, but I was very pro-

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> intervention: the government should intervene in all sorts of things. I distanced myself from that, but I'm certainly not anti-government. Clearly, you need governments to do things; the question is how are you going to optimally devise institutions for those things. (ibid., 80)

We are inclined to agree with Tyler Cowen (2011) when he says that Sargent should be thought of as being in the "market-oriented" camp, and, given what Sargent says about his own views during his undergraduate and graduate school days, to view him as having grown somewhat more classical liberal. Sargent's works and remarks often have a certain classical liberal tone. Consider, for example, the speech he gave at the Nobel awards banquet in 2011, here reproduced in full:

> Your Majesties, Your Royal Highnesses, Your Excellencies, Ladies and Gentlemen, My Teachers, My Students, and My Students Who Have Become My Teachers:
>
> My good and dear friend Chris Sims and I thank you for recognizing the many women and men like us who use statistics and economic theory to understand how governments and markets can improve peoples' lives. I state 7 practical lessons taught by my beautiful subject, which investigates the consequences of time and chance and cooperation and competition and foresight and incentives.
>
> 1. Many things that are desirable are not feasible. (Carolyn)
>
> 2. There are tradeoffs between equality and efficiency.
>
> 3. Other people have more information about their abilities, their efforts, and their preferences than you do.
>
> 4. Everyone responds to incentives, including people you want to help. That is why social safety nets don't always work as intended.
>
> 5. When a government spends, its citizens eventually pay, either today or tomorrow, either through explicit taxes or implicit ones like inflation and defaults on debts.
>
> 6. It is feasible for one generation to shift costs to subsequent ones. National government debts and the U.S. social security system do that.
>
> 7. Most people want other people to pay for public goods and government transfers (especially transfers to themselves).
>
> I'd like to thank Sweden for welcoming us and for being a country that values learning and education and people who read books and try to write better ones. (Sargent 2011b)

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In a January 2009 *Chicago Tribune* editorial on the "fiscal stimulus package" proposed by the incoming Obama administration, Sargent was quoted as saying: "[T]he calculations that I have seen supporting the stimulus package are back-of-the-envelope ones that ignore what we have learned in the last 60 years of macroeconomic research." In an interview conducted in June 2010, Sargent explained:

> I said something like that to a reporter. I had just read an Obama administration's Council of Economic Advisers document e-mailed to me by my friend John Taylor. I agreed with John that the CEA [Council of Economic Advisers] calculations were surprisingly naive for 2009. They were not informed by what we learned after 1945.
>
> But I suspect that the council was asked to do something quickly, and they did what they thought was "good enough for government work," as some of us said during my days at the Pentagon in 1968 and 1969. Back-of-envelope work can be a useful starting point or benchmark. But it does mischief when it is oversold.
>
> In early 2009, President Obama's economic advisers seem to have understated the substantial professional uncertainty and disagreement about the wisdom of implementing a large fiscal stimulus. In early 2009, I recall President Obama as having said that while there was ample disagreement among economists about the appropriate monetary policy and regulatory responses to the financial crisis, there was widespread agreement in favor of a big fiscal stimulus among the vast majority of informed economists. His advisers surely knew that was not an accurate description of the full range of professional opinion. President Obama should have been told that there are respectable reasons for doubting that fiscal stimulus packages promote prosperity, and that there are serious economic researchers who remain unconvinced. (Sargent 2010, 32-33)

In the same interview, Sargent was asked what modern macroeconomics has to say that is useful in managing and preventing financial crises. He responded:

> A lot. In addition to the formal literature summarized in the Allen and Gale [2007] book, I want to mention the example of the 2004 book by Gary Stern and Ron Feldman, *Too Big to Fail*. That book doesn't have an equation in it, but it wisely uses insights gleaned from the formal literature to frame warnings about the time bomb for a financial crisis set by government regulations and promises. Indeed, one of the

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> focuses of Gary Stern's long tenure as president of the Minneapolis Fed was steadily to draw attention to financial fragility issues and what the government does either to arrest crises or, unfortunately as an unintended consequence, to incubate them. (Sargent 2010, 30)

Also notable is that in his Nobel lecture, titled "United States Then, Europe Now," Sargent suggested that the debt-default history of the United States from 1790 to the 1840s was potentially instructive for modern Europe. The upshot is that when, in the post-revolutionary period, the U.S. central government bailed out the states, it created a precedent that led states again to become over-extended, in particular by funding infrastructure projects, and that it was a good thing that in the 1840s the central government did not bail out the states and left them to default on their debt. The lecture—particularly as delivered in Stockholm in December 2011 (Sargent 2011a), as opposed to the published version (Sargent 2012)—seems to suggest that perhaps the European Central Bank should not bail out member governments.

But Sargent supports some government measures related to the possibility of bank failures, as evidenced in the June 2010 interview:

> I like to think about two polar models of bank crises and what government lender-of-last-resort and deposit insurance do to arrest them or promote them. … So without deposit insurance, the economy is vulnerable to bank runs. The situations where depositors don't run lead to good outcomes, but when there are bank runs, outcomes are bad. The good news in the Diamond-Dybvig and Bryant model, however, is that if you put in government-supplied deposit insurance, that knocks out the bad equilibrium. People don't initiate bank runs because they trust that their deposits are safely insured. And a great thing is that it ends up not costing the government anything to offer the deposit insurance! It's just good all the way around. (Sargent 2010, 30-31)

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Thomas C. Schelling

by Daniel B. Klein

Thomas Schelling (1921–) shared the Nobel Prize in 2005 with Robert Aumann, "for having enhanced our understanding of conflict and cooperation through game-theory analysis." Schelling's most well-known books—books that, in my opinion, can scarcely be recommended too highly—are *The Strategy of Conflict*