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Theodore W. Schultz [**Ideological Profiles of the Economics Laureates**]

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Abstract

Theodore W. Schultz 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.

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Theodore W. Schultz

by E. C. Pasour, Jr.⁶⁷

Having grown up on a 560-acre farm in South Dakota, Theodore Schultz (1902–1998) maintained his farming roots throughout his economics career (University of Chicago 1998). His early work on the economics of U.S. agriculture was published mainly between 1932 and 1951 (Gardner 2006, 326). This work laid the foundation for his later work in economic development and human capital, particularly in agriculture, for which he was awarded the Nobel Prize (W. Arthur Lewis was a co-recipient). Schultz is the only agricultural economist to be awarded a Nobel Prize in economics.

Schultz stands out among Nobel laureates in economics in terms of his pre-college formal education. He completed elementary school but never went to high

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school.⁶⁸ While farming on his home farm, he attended a short course at South Dakota State College, where he showed such promise that he was encouraged to enter the college as a regular student, which he did (Johnson 1998, 212-213). Schultz earned his bachelor's degree from South Dakota State in 1927 and his Ph.D. in agricultural economics from the University of Wisconsin in 1930. In his short autobiographical essay for the Nobel committee, Schultz wrote:

I managed to enter college in 1924 and I was permitted to complete my college work in three years. The unorthodox economics of the University of Wisconsin during those years appealed to me. Despite my lack of proper credentials I was accepted by the graduate school. My intellectual debt to Professors Commons, Hibbard, Perlman and Wehrwein is large. (Schultz 1992a/1980).

Schultz's first teaching position was at Iowa State College, and within two years of his arrival in 1930, he was made acting chair of the Department. As head of the Department of Economics and Sociology, Schultz built a national reputation by introducing quantitative statistical techniques to American agricultural economists and "threw himself" into the new discipline of econometrics, testing economic theory with data (Burnett 2011, 376-377).⁶⁹

Schultz's domestic agricultural policy views, especially early on, were highly interventionist. In his work on domestic agricultural policy during WWII, Schultz was quite critical of the decentralized price system and envisaged a large role for government in U.S. agriculture. Moreover, government intervention continued to play a key role in his approach to domestic farm policy following the war. But Schultz's views shifted notably in the classical liberal direction in his economic development work, which emphasized distortions by government programs affecting farmers in low-income countries. Although Schultz's view of the role of government evolved over time, focusing more on problems that arise whenever government action is substituted for markets, he never became an adherent of a strong presumption of *laissez faire*.

Schultz's early interventionist views on the role of the state affecting U.S. agricultural policies are spelled out in his book *Redirecting Farm Policy*, published during WWII. The book proposes that "parity prices," the linchpin in im-

68. Many farm workers were in the military during WWI and Schultz's father wanted him to help with farm work. Further, his father's view was that if he left the farm and continued his education, he wouldn't return to the farm (Graves 2004).

69. Agricultural economists and other economists were in the same department at Iowa State, and agricultural economists there emphasized economic theory more than in most other departments of agricultural economists in land-grant universities.

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plementing New Deal farm policies, be replaced with “fair prices”—“that rate of payment which a farmer laborer, or capitalist receives for his services and use of his property is sufficiently high to provide each with an adequate income” (Schultz 1943, 14). The following quotations from the 1943 book describe the purported advantage of central controls in U.S. agriculture by the U.S. Department of Agriculture.

A highly decentralized farm price system administered, in the main, by private agencies has many serious shortcomings. (Schultz 1943, 39)

There is no reason why Congress should not be advised and possibly approve each year the production goals that best reflect the amount which agriculture is capable of producing and the requirements of society. This having been done, the Department should be authorized to use its administrative machinery to attain the production goals as established. . . . This procedure in all probability will give results which, taken as a whole, will be much superior to what takes place when private individuals make estimates, usually acting on fragmentary information and all too often on hunches. . . . The second step in employing the farm price mechanism to allocate farm resources is to establish a system of forward prices. . . . Forward prices are a gigantic futures market operated to coordinate and direct agricultural production. (Schultz 1943, 42-44)

Schultz’s forward pricing idea emerged in the 1973 farm bill (P.L. 93-86) as target prices with compensatory payments. Price supports, including Schultz’s forward pricing that affect output or prices are not consistent with free trade. Despite the inconsistency, Schultz even early in his career, was a firm believer in the beneficial effects of international trade and sought to educate the public about the principles of trade following the disastrous effects of the Smoot-Hawley Tariff Act (Burnett 2011, 376).

It is difficult to know how much of Schultz’s interventionist thinking at this time was colored by the exigencies of wartime. In a paper published shortly after the war, however, he continued to envisage a large role for government in U.S. agriculture and to promote a wide range of government policies:

Can conservation be left solely to market forces? The answer, of course, is no. Will a market economy provide stocks and storages necessary to stabilize our gigantic livestock industries? Again the reply is in the negative. What about credit, housing, farm ownership, medical facilities, education, research and experimental work, old age and

retirement opportunities? None of these can be left wholly to the market economy. (Schultz 1946, 26)

In 1943, after 13 years at Iowa State, Schultz left in the wake of the widely publicized oleomargarine affair—a bitter battle over academic freedom. In 1942 the U.S. Secretary of Agriculture requested that Iowa State publish a series of publications on government food policy pointing out problems with current farm policies. One study in the series, “Putting Dairying on a War Footing” (Brownlee 1943), a study approved by a committee of which Schultz was a member, attracted the ire of the butter producers. The work argued that margarine compared favorably with butter in nutritional value and palatability; it argued against legal restrictions on margarine production and marketing and on margarine use during the war. When the dairy industry fiercely objected, the controversy became a national story and farm groups called for Schultz’s resignation. The College administration attempted to block publication of the pamphlet and the President of Iowa State failed to back Schultz. Schultz managed to get the research published but, he resigned from Iowa State and accepted a position in the Department of Economics at the University of Chicago (Passell 1998).

“That incident provoked some serious soul-searching,” recalled D. Gale Johnson, a long-time colleague of Schultz (quoted in Passell 1998). One might conjecture that Schultz’s personal experience with politicizing the production, marketing, and use of margarine and butter had an effect on him. While at Chicago, Schultz became much more cautious about recommending government action. Schultz was on the executive committee of a group, including Milton Friedman, that met in 1946 to begin work on sponsoring a “Free Market Study” with the objective to promote scholarly arguments as to how a modern society might be organized to maximize individual liberty (Burnett 2011, 39). That same year, Schultz became head of the economics department at Chicago and would remain in that position until 1961—formative years for the so-called Chicago School. All told, I surmise that shortly after age 40 Schultz underwent a pronounced ideological shift toward classical liberalism, reflected in his later work.

At Chicago, Schultz studied the process of economic development for farmers in low-income countries—the work for which he received the Nobel Prize. He began to emphasize the harmful effects of government policies on agricultural producers. His contribution rested on two major points: (1) farmers in developing countries, though often illiterate, were rational and made efficient use of their resources; and (2) his work increased understanding of human capital and its role in production (Johnson 1998, 209). David Henderson summarizes Schultz’s conclusion:

[P]rimitive farmers in poor countries maximize the return from their resources. Their apparent unwillingness to innovate, [Schultz] argued, was rational because governments of those countries often set artificially low prices on their crops and taxed them heavily. ... A persistent theme in Schultz's books is that rural poverty persists in poor countries because government policy in those countries is biased in favor of urban dwellers. (Henderson 2008)

In contrast to the stress on government planning seen in his early work on U.S. agricultural policy, Schultz's work in economic development emphasized the importance of entrepreneurship—even by small producers in low-income countries—and the distortions in production and marketing stemming from government programs of various kinds.

First, *economic disequilibria are inevitable*. ... [T]he function of farm entrepreneurs in perceiving, interpreting, and responding to new and better opportunities cannot be efficiently performed by government. (Schultz 1978, 15, emphasis in original)

[T]he unrealized economic potential of agriculture in many low income countries is large. ... [F]or want of profitable incentives, farmers do not make the necessary investments, including the purchase of superior inputs (for example, seeds, fertilizer, and machinery). I argue that...interventions by government are the primary cause of the lack of optimum economic incentives. (Schultz 1978, 17)

In short, Schultz saw governments as harming producers in low-income countries by obstructing market incentives and discouraging technological advancements, thereby impairing the profitability and success of agriculture (Schultz 1978, 16-17). The emphasis on government failure in analyzing the effect of government policies on producers in low-income countries stands in bold contrast to his earlier, statist approach to U.S. agricultural policy during WWII. In the later years, Schultz elaborated an idea of entrepreneurship as “the ability to deal with disequilibria,” and published an article in the *Journal of Economic Literature* entitled, “The Value of the Ability to Deal with Disequilibria” (Schultz 1975; see also Schultz 1990).

Schultz also used agriculture as an area for applying Chicago notions of ‘political markets.’ Political markets are said to function to benefit individuals and groups who have access to and can influence the political process. Examples include export taxes on farm products, the use of state marketing boards for farm

products at the expense of the farmer, and import restrictions on farm inputs (Schultz 1978, 21).

Although Schultz's skepticism of government increased as he studied poverty in low-income countries, he continued to find an important role for government in funding agricultural research, primary education, and some welfare activities (Schultz 1993, 37-38). Further, in Schultz (1961, 14), he supported subsidizing rural workers to move to urban areas in order for their children to have better employment options.

Schultz had a lifelong dedication to the importance of developing human capital—capital produced by investing in knowledge—and he helped introduce human capital and the importance of education to development economics (Ranis 1979, 1389). His theory of human capital focused on the effects that investing in health and schooling had on population quality; he emphasized that education accounts for much of the improvement (Schultz 1992b/1980).

Schultz's work on the importance of education for low-income producers focused on the importance of knowledge rather than on the appropriate role of the state in financing and producing such knowledge. That is, despite the often shocking state of government-run schools in some low-income countries he did not analyze governmentally generated distortions in the financing and production of educational output as he did in the production and marketing of farm products in low-income countries. But on the basis of more than half a century of experience in agricultural economics and the administration of research, Schultz concluded: "It is true even in the United States that the more heavily the University is dependent on the patronage of government, the less is the freedom of inquiry in the social sciences" (Schultz 1979, 464). In the same paper, Schultz expressed his sense that rent seeking by groups throughout the economy means that government efforts, ostensibly to correct market failures, are more likely to make matters worse:

There is a pervasive intellectual and popular commitment to the belief that the failures of the market are the primary source of that which is wrong with the economy. Each interest group has its own list of such market failures. To overcome them, an increasing number of organized groups seek protection and redress by means of public programs and institutions created by government. Business groups have a long history of serving their special interest by this means. Organized labor and organized commodity groups have been doing this on behalf of their special interests for decades. This pluralistic process is currently confounded by the politics of health, of the aged, of poverty, of income transfers, of energy, of environmental politics, and others. The resulting modifications of the political economy in

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general do not correct actual market failures but tend to bring about other forms of economic failure. (Schultz 1979, 467)

Despite Schultz's ideological evolution as his work shifted to economic development and human capital in low-income countries, his views on U.S. agricultural policy did not shift as much as one might have expected in view of his stress on harmful interventions by government in his later work. In 1974 he looked back three decades at his work on U.S. farm policy, focusing particularly on his war-time book *Agriculture in an Unstable Economy* (1945), written, Schultz says, while he "was, no doubt, influenced all too much by Keynesian thinking" (Schultz 1974, 2). Schultz described his old policy proposals, including his compensatory payments approach for farm commodities—the latter described as "both brilliant and naïve" (Schultz 1974, 9). Schultz suggested that, as a younger man, he did not well understand how his work would be put to use by those who demand economic research:

On policy I am less sanguine than I was in 1945, partly because of more doubts about economics and partly because of the fragmentation of policy. Economic policy is a tricky business. The demand for it is ever so fickle; what is in fashion today is old hat tomorrow.... . . . Each new public agency has a claim to a small fragment of economic policy and old agencies with their entrenched programs seldom fade away. Both demand justification for their respective programs and economists promptly supply models to satisfy these demands. . . .

Young economists have a marked comparative advantage as suppliers of policy proposals. They are bright and adjustable to the changes in demand; they are well equipped to produce the models that are demanded; and entry into this business is easy. . . .

Out of my analysis of economic fluctuations, there emerged the idea of compensatory prices for agriculture. It was a new idea. . . .

Although the underlying economic analysis is solid, it has not been a feasible policy proposal. Herein lies an important lesson about policy. I was fully aware that my compensatory payments entailed governmental intervention. I devoted several pages to three difficulties that could be anticipated. One of these pertains to our government viewed as an institution. I noted, "there is always the question whether in our democratic form of government such a proposal can be put to good account. Will not pressure groups use compensatory payments to raid the public treasury?" I argued that compensatory payments were less vulnerable than alternative policies. Although experience

since 1945 is ambiguous on this point, what I said reveals the naiveté of my youth. The moral is clear: economists are like mice putting a bell on the cat. The cat has its own taste for mice and economists are caught by their commitment to preferences as given. (Schultz 1974, 8-9)

One can read parts of Schultz's substantial oeuvre, as in the work just cited, and find ample evidence to support the view that he was a strong supporter of government action, especially in his early work in domestic agricultural policy. He continued to support some interventionist domestic farm programs throughout his career. On the other hand, his later work on economic development emphasized government failure problems and is supportive of decentralized markets. Thus, there is substantial evidence to support the conclusion that he migrated ideologically in the classically liberal direction during the second part of his career as his work shifted from U.S. agricultural policy to the economic development process in low-income countries. It is ironic that he was viewed by most agricultural economists as a strong advocate of the free market when his support for government intervention was strongest in domestic farm policy. Despite his mixed record, he is remembered as a defender of markets and one who stressed government failure in his research in economic development.

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Reinhard Selten

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

Reinhard Selten (1930–), born in Breslau, a German city in what is now Poland, was raised in a troubled period of German National Socialism, anti-Semitism, and war. His father, who was Jewish, blind, and an entrepreneur, operated a successful “reading circle” business. He eventually was forced to sell it under Nazi law. After the war, Selten’s life was marked by avoiding the Soviet army, international migration, poverty, physical farm work, and a stay from official school work. However, when he returned to school, he excelled. Selten had a knack for