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Modern Political Economics: Making Sense of the Post-2008 World

by **Yanis Varoufakis, Joseph Halevi, and Nicholas J. Theocarakis**

Routledge, 2009.

This ambitious and all-embracing book is unusual in many respects. The intellectual journey it is inviting us to is very long. On the one hand, the book thematizes paths, or better yet, by-ways, of economic reflexivity from the very beginning. The authors argue for the often made declarations that we should not look back when discussing economic theory stating that those opinions are strictly related to economic history. In other words, they confirm the historical aspect of economic reflexivity and its deep embeddedness in history where something called "inherent error" of economic opinion accumulates. On the other hand, this book offers a collection of diverse narrations starting from 1929; it is obvious that the intention was to tackle the Big crisis in order to draw structural analogies with current flows of the crisis ("We feel that 2008 is a new 1929", p. 7). In fact, this part of the book is the application of the first part as we are presented with all the practical consequences of initial theory and of the affirmation of the basic thesis. By referring to the destiny of economic reflexivity, the authors are alluding to the necessity of practical changes.

Based on common categorization, this book is a heterodox work. Could it be anything else with its half a thousand pages long serving as proof that economic reflexivity is shadowed by "inherent error", which definitely undermines its authority? As the authors use almost every page to demystify economic reflexivity, this book, with respect to established categorization, could not be evaluated any differently. Still, we should ponder the fact that economics is the only science of all the social sciences where this duality prevails and represents the dichotomy between paradigms that follow the "mainstream" or "heterodox' orientation". Naturally, amid seemingly endless books and articles on economic crisis, a questioning of the grounds of economic reflexivity occurred. Crisis, especially one that is deepened and represents structural tendencies, initiates self-reflection. Practical needs force one to immerse into the "metaframes" of his or her own discipline (but there are theoreticians who believe that if changes in the approach to economic reasoning must be made then the purpose of those changes should be to keep everything the same). The comprehensiveness and radicality of this book, however, certainly deserve some attention. The text is highly argumentative with an abundance of constructions (formal, as well) and examples provided to prove the basic thesis; the authors' understanding of economic theory is thorough and they have the knowledge necessary to prove such an ambitious thesis.

The constantly present idea is the objection to the exclusion of political elements from economic reflexivity. Without this idea, the capitalist economy is viewed as a self-regulative system that teleologically slides towards equilibrium. This is associated with the elite economists who devise models as consistent as Euclidian geometry, i.e. every conclusion is compared to the initial assumptions. Instead of elucidating it, the economic reality is obscured. Besides that, incommensurable things like values and prices are set within the same framework for the purpose of model consistency and demonstration of inherent harmony. From an economics aspect, progress could dialectically be understood as regressive because the advancement hampers the understanding that used to be more comprehensive. This could also be understood as the "lost truth": how certain distinguished dimensions were later lost in Aristotle's weak and primitive theory of value. Although Aristotle's teleology cannot withstand the challenge of present day science, it still implies an obscured truth about economics: a coherent theory of value can be constructed only by acknowledging the value of the "telos" of human performance in the world.

We should remember that the authors project an outline of a theory of power. In fact, the paths of economic reflexivity can be envisaged only by relying on the history of power sending the following message:

> "The rulers' social power was, therefore, as much a result of their soldiers' spears as it was founded on the consent of the powerless to their rulers' authority. Dynamic societies built their success on two production processes unfolding in parallel: manufacturing surplus and manufacturing consent regarding its distribution." (p. 22).

The authors call this "Condorcet's Secret," a concept that serves as the explanation of numerous phenomena; Condorcet's Secret suggests that the secret of power does not lie in the "oppressors," but in the "oppressed" (this immensely important principle was even emphasized by Étienne de La Boétie). The authors also present some anthropological assertions: man is a certain kind of pendulum that moves from glorification to a constant destroying of unpredictability. Similarly, man oscillates between accepting the disturbing truths and "luxuriating in blissful ignorance". Economic reflexivity expresses this through clearly separated binary relations: value versus price, economics versus politics, macroeconomics versus microeconomics. Each of these designations is necessarily incomplete and leaves the possibility for "inherent error." The fact that the economists did not prove to be an even match to the crisis in 2008 was not the result of their incompetence, but the result of structural tendencies.

This methodological framework is an explanation of the first steps made by Physiocrats after which an era for economic reflexivity began: the classical period. Special attention is paid to the dynamics of surplus based on the thesis that the most important economic phenomenon can be understood through the process of the creation and organization of surplus. Classicists are faced with the following problem: the explanation of surplus generated not only in the agricultural sector but also in the context of commodification and industrialization. Besides, the profound relationship between surplus and profit should also be observed because it creates the theory of value that is necessary for the thematization of profit. Profit is regarded both as return to capital and as measurement of surplus, which is the source of all problems. Adam Smith offers the theory of growth based on the assumption that wage share of surplus does not change with the growth of economics; he separates the theory of growth from the theory of value. That is his vision of "inherent error" (i.e. "the only scientific truth economics can lead its honest practitioners to is that the study of capitalism is guaranteed to lead to superstition if predicated upon a determination to extract truth from the theoretical models and their empirical applications." (p. XIII)).

The authors discover the loci of indeterminacy in production: acquisition and distribution of surplus. Economic reflexivity opposes this indeterminacy and constantly tries to manage it, thus creating different models that sacrifice constituent elements of complexity for consistency. For example, there are zones in the employer-employee relationship that cannot be specified by any mathematical functions; those are transformation processes of human input in the company's output that can never be subjected to penetrating market codes. Idiosyncratic employment contracts, in general, assume radical indeterminacy because human inputs are immeasurable, unless we turn people into machines in some imaginary Matrix-economics. The impossibility to commodify work completely creates, from an economic point of view, a contract problem. There is a genuine ambivalence of work: it has two dimensions that exist simultaneously, a quantifying and non-quantifying one. This is exactly what economic reflexivity is trying to overcome and, accordingly, it avoids the question of why "human capital" is productive. Mathematically given consistency of economic models impoverishes social complexity. The cost is "inherent error," a closure of the dynamics of economics in the framework of self-referential models. A theory that does not separate labor input and quantifiable input, such as electricity, cannot explain capitalism. The sacrifice for a determinate mathematical model of prices is too big.

Karl Marx was criticized as well. Although the authors expressed positive feedback for his dialectical encompassing of economic problems, the syndrome of "inherent error" was present there, too. Finally, Marx did not go any further than the economic tradition. He exacerbates Smith's problem of supraintentional causality regarding the "invisible hand" of the market: while Smith implies that the motive for profit is eliminated for the general welfare, Marx implies that it leads to a crisis because the accumulation of capital is active until it reaches the moment of self destruction. He clearly shows that the distribution of surplus is determined by the allocation of social power between different social groups. The authors praise Marx for his recognition of tragic dilemmas in capitalism and virtuosity of economic analysis, but the mentioned syndrome influences him too as his political agenda is supported by scientific analysis and is fixed in algebra. Marxian Fundamental Theorem in a multisectoral economy states that the equilibrium exchange between two sectors must be balanced so that the purchasing power of capital goods from a sector that produces the capital goods must equal the value of capital goods in other sectors. Even Marx, however, could not sustain the flux of capitalism and he tried to block it with the closure of system. The key problem is still present: Marx remains in the XIX century.

Even the theory of crisis bears Ricardo's mark in this case: crises annul themselves, increased unemployment decreases wages and decreasing wages restore profit. Yet, a consistent theory on relative values exists, namely the consistent theory of growth and accumulation. *Tertium non datur*. We encounter the phenomenon of lost truth in economics once again. Even though Marx was superior in comparison to Ricardo, he knew that exchange was not conducted according to the embodied labor inputs and followed his basic corn model that made him equalize profit with surplus value on a macroeconomic level. Perhaps he contributed significantly to the process of turning labor inputs into prices with his iterative mathematical procedures, but this loses the scientific basis of the profession. In any case, Marx made the same mistake as economists after 1980 due to financial engineering. If we believe that we can overcome capitalism based on the projection of a society that is scientifically-rationally organized, we will make the same mistake because it is nothing more than the political utilization of determinism. The aim is to offer a unified explanation of value and growth and of distribution and accumulation. Difficulties are avoided by escaping into algebra and into the illusion that the spectacle of mathematical functions can represent dynamic economic reality.

The solution to the hopeless situation exists and it is the impossibility of a simultaneous affirmation of equilibrium values and stable growth. Namely, value can be excluded from the analysis, thereby considering only the physical inputs: that is, for instance, Sraffa's procedure of "production of things by other things" with input that cannot be quantified with work. As the authors pointed out, the Sraffa's model is misinterpreted as a "model" which tends to replace something. The Italian economist intended only to give neoclassical reasoning to the criticism and nothing else, because if Sraffa's procedure is understood as a model then we will go back to Matrix-economics where only machines exist and people are only heat generators that produce surplus. Still, neoclassical withdrawal from the theory of value, from affirmation of price without value, and from the "pre-analytical" vision of price theory based on utility calculus that led the academic community should also be mentioned. More precisely, the authors describe a path that leads from marginalism to neoclassicism, when classical economics inspired by Newton was turned into static architecture, into a calculus of exchange. Classical economics appreciated temporary horizon, neoclassicists froze the time, and the authors blame Leibniz for eliminating time from the analysis of change. This proves that marginal change does not require time and / or consideration of flux. Capitalism now takes the form of Leibniz's vision of God's creation of order: at the beginning of the twentieth century, this vision became dominant in economics. Neoclassicism should be analyzed by means of Leibniz's language of mathematics.

It is not surprising that neoclassicism has been given full attention, its actions and theories are analyzed in great detail, and finally, those discourses are deeply rooted in modern economic reflexivity ("secular religion," as authors wrote it). Time related problems, composition, and scale are presented clearly, and neoclassical political economics and money neutrality are reviewed as well; the reason we are not presented with it in detail here is simply a lack of space. Apart from confirming special and new modus of inherent error for neoclassicists, the authors are particularly interested in the key of their discursive success. Their witty description could be categorized as an orientation concerned with rhetoric effects in economics.

The reason why economic reflexivity could not explain the crisis of 1929 lies in its complexity. This crisis has been studied thoroughly with numerous details and reactions of economic theoreticians. John Maynard Keynes's influence on the authors of this book should be specifically mentioned here. In spite of the praises of Marx who recognized some dimensions of human activity (capital and labor) which cannot be quantified, Keynes is still the would-be hero. He was the first to release himself from the plague called inherent error. Perhaps most remarkable was the simplicity of his conclusion about the epistemic limits of economic theory: "we are damned if we know!" (p. 205). Fluctuations of output cannot be explained by the dynamics of wages. Unlike the classicists, the order is changed: saving is determined by investment, but if we try to clarify what determines the investments, Keynes ignores this: we do not know, we are not able to know. For the first time, a true confession was made about economic complexity and people's desires regarding prices: they cannot be simply framed into mathematically prepared determinations. There is a circle between common beliefs and outputs in economics that is not based on the Matrix principle. Keynes did not only free himself from marginalism, he realized that every model designed to provide a simultaneous theory of value and growth would be a failure. He was brave enough to revitalize a dissident belief that it is possible for capitalism to go through phases and that the "worse scarcity" does not refer to capital or labor, but to commodity demand. Effective demand is indeterminate. The only scientifically supported claim regarding capitalism refers to its radical indeterminacy. Keynes does not claim that man is less rational than it is commonly believed, nor does he claim that crises are escalations of irrationalism; he affirms the importance of rational indeterminacy and the "scarcity of telepathy," which is deeply significant for economics. Besides, there is also the relevance of fallacy of composition: erroneous following of the logic of parts and relating it to the whole, or relating Robinson Crusoe to the United States. Keynes, however, was wrong too; capitalism cannot be rationalized or civilized proving Marx right.

Numerous authors alluded to Keynes after World War II, but it was Keynesianism transformed for the purpose of power redistribution and not an implementation of Keynes's theory. Keynes's theory was pacified by Samuelson's eclecticism. With respect to economic politics, the authors write about a Global Plan that described the dynamics of capitalism up to the seventies. Still, another relevant point that should be explained is the question of how formalism and different equilibrium based models could triumph over the officially established Keynesianism. How could there be a repetition of neoclassicism that is entirely separated from dynamic reality? How could this economic orientation, which is in its self-understanding distanced from the world, become dominant? How can the dominant theory be the one that sacrifices complexity or time? How can the dominant theory be the one which regards production as a form of consumption supported by consumers' preferences? The book analyzes the genesis of game theory, the results and contributions of some theoreticians, relevant additions about mathematics, meta-axioms that are typical of neoclassicism. The authors will always favor John von Neumann's theory, especially because of his precaution. The triumph of formalist theory in economics was not planned, just like many other tendencies that have to be explained by supraintentional processes. Although it was not planned, it does not mean that we did not take part in it: the fiction about formalism's neutrality becomes unrealistic because when it is applied to economics. A political moment is created, i.e. power emanation. On the other hand, when formalism is regularly applied to finances it creates a situation that is self-destructive. This, however, becomes theory that has already started evolving into practice and it represents a variant of neoclassicism regarding the "inherent error." It is a combination of higher mathematics and childish political economics with faith in new financial engineering.

The "Global Plan" represents the first phase of American hegemony where the combination of geopolitical and geoeconomic agendas supported by a transformed Keynesianism can be found. We should not forget that Keynes advocated for a formal international system that would recycle the surplus. This is a contrast to the Global Plan, which was rather a kind of military-financial engineering with corresponding stability and low interest rates. Two similar phenomena, the US trade deficit and the government's budget deficit, changed the constellation after World War II, that is, during the seventies. The newly created situation resembled the mythological scene of sacrifice and it could be called Global Minotaur. In accordance with the already applied methodology that assumes the existence of "Cunning of Reason" and that reality is becoming distant from people's intentions, it is again claimed that nobody projected stagflation, high interest rate and expensive raw materials. Besides, could it be different for a practice that views radical indeterminacy as the absolute horizon of scientific reflexivity of capitalism? This twin deficit gives cutbacks in government spending and a strategy leading out of the demonic circle of twin deficit. In 1971, the Global Plan was discarded as unimportant and the Global Minotaur was created to illuminate the dynamics up to 2008. Everybody is familiar with this mythological scene and the offer of a sacrifice. Now, we should consider the case when economic downturn is experienced, but with systemic flight to the dollar, plus effective global deflation. The mentioned deficits become sustainable, the attracted capital flow provides benefits for some sectors (energy sectors, military related ITC sectors and financial institutions), US growth is enabled through the capital of others (especially the leading surplus economies), while unit of labor cost stagnates. Global capital inflows feed the Global Minotaur.

However, this mythological figure is vulnerable, too; 2008 was nothing else but the year when this basic vulnerability was expressed. A combination of intensive capital inflows and the availability of bank loans increased house prices to an excessive level; Wall Street was raised by this financial dynamic. In effect, capital is channeled in two directions: on the one hand, inflows of capital from the world and on the other, redirecting the capital towards financial entities. Financial expansion is a symptom of these processes; suddenly the planet becomes smaller in comparison to the self-increase in financial derivatives. A trickle-up effect was also recorded:

> "Securitization of the unsafe debts of the poor (e.g. the conversion of subprime mortgages into CDOs) had the effect of making the initial lender indifferent to whether or not the loan could be repaid.... These securitized packages of debt were then sold on

> and resold at tremendous profit.... The rich, in an important sense, had discovered another ingenuous way to get richer by trading on commodities packaging the dreams, aspirations and eventual desperation (once the market crashed and the home foreclosures began) of the poorest in society." (p. 368).

Private money accumulates since, in this constellation, financial institutions have power to make money. Friedrich Hayek could be pleased about this considering his ideas about money, but he did not foresee these consequences. I should also mention the authors' adequate analysis of Europe: they treat the genesis of the European Union in distinctive way in order to conclude that German has become the Global Minotaur's European Simulacrum. This means that the constellation is markedly different although there are certain analogies with the US. This can be proved based on numerous moments. The authors' approach culminates in the analysis of certain cases with regard to the methodology that was developed here: these narrations can explain why the economic "instrumentarium" of the EU was not created based on *esprit communitaire*, but subject to the logic of the Global Minotaur. This also explains why European entities are not ready to face the crisis in the long term.

The authors made an outstanding attempt to develop a political economy that was not infantile. As I said at the beginning, this is a remarkable book considering its narrative structure and metaphorology. In so far, there are certain provocations in this book. We have already seen that it is a two level book whose levels are interrelated in every aspect: criticism of economic reflexivity due to its "inherent error" and criticism of economic politics. There is also ontological indeterminacy that has been consistently denied by economics, thus causing harm to both economics and us. To be more precise, the authors find it necessary to make corrections; there are detailed suggestions concerning economic reflexivity and economic politics. I would also like to make a brief comment on the fact that Marx's books do not have to be read from the perspective of rationalized determinacy of economic order, but from other perspectives as well; I have to admit that this type of reading is also possible. Although Veblen was mentioned as extremely important for the authors, he was not mentioned further in the book, and his works can be taken for the explanation of numerous phenomena. However, those are just partial comments that do not affect the positive opinion of this book that deserves attention.

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