



INSTEP-WFU Cambridge

ECONOMIC THEORY: THE CAMBRIDGE TRADITION

Prerequisites: *Introductory Microeconomics and Macroeconomics*

This course brings to life a number of key economic concepts, by setting them in the historical context which inspired their creators while they worked at Cambridge; and by exploring their continuing relevance to some of the major economic questions of today. – from the optimal size of national (private and public) debt, to stabilisation policy, to the exchange rate regime international financial architecture, to the nature and purpose of economic development.

It could be argued that the “Cambridge tradition” began with Thomas Malthus (1766-1834) and his most celebrated book, *An Essay on the Principle of Population* (1798). Malthus was a graduate, and ultimately a Fellow, of Jesus College. The gloomy analysis and predictions of this book were not popular, and the term “Malthusian” took on a rather pejorative significance. Malthus did not found a school of thought in Cambridge, so we had to wait until the arrival of Alfred Marshall (1842-1924) who can truly be said to be the father of the Cambridge Tradition. He was a founding father of the neo-classical school, and his famous *The Principles of Economics* (1890), became the most seminal work of this school. Marshall was succeeded in the Chair of Political Economy, the only professorship in economics in Cambridge at the time, by A.C. Pigou (1832-1959), a young Fellow of King’s College, who had come to economics through the study of history, philosophy and ethics. Pigou’s most important contribution to economics was his formulation of what we would nowadays call the discipline of “welfare economics” in his greatest book, *The Economics of Welfare* (1920). Pigou was a devout Marshallian, and defended Marshall’s ideas against all-comers, most conspicuously the onslaught on standard neo-classical ideas launched by another of Marshall’s protégés, John Maynard Keynes (1883-1946), also a Fellow of King’s College. This was born out of a deep disillusionment with neo-classical ideas, in particular its inability to come to terms with the mass unemployment of the inter-war period. He had no quarrel with Marshallian microeconomics. That still made sense to him. But on a macroeconomic level the neoclassical school was helpless. Keynes founded the discipline which we know today as “macroeconomics”, and with it the concepts of “aggregate demand” and its policy counterpart “demand management”. Demand management played a vital role in the formulation of macroeconomic policy in the Western world for most of the post-war period. The Keynesian Revolution evolved into the Keynesian Consensus. This consensus was challenged and apparently overthrown by the monetarist counterrevolution led by Milton Friedman and his colleagues and students at the University of Chicago and its offshoots.

But the events following 2008 and the Great Recession which ensued changed all that. The inability of the monetarist model to explain what was happening led to a surprisingly rapid reinstatement of Keynesian ideas.

On a microeconomic level concern about the environment and global warming have given rise to a debate about the desirability of a carbon tax, an idea directly traceable to Pigovian welfare economics.

Economics is in a state of flux once again, and one of the purposes of this course is to clarify some of the issues which are being discussed currently.

READING LIST

Essential Reading

J.A. Trevithick, *Inflation: A Guide to the Crisis in Economics*, Penguin, 1980

J.A. Trevithick, *Involuntary Unemployment: Macroeconomics from a Keynesian Perspective*, 1992

D. Begg, R. Dornbusch and S. Fischer, *Economics*, latest edition.

Background Reading

Clarke, P. *The Keynesian Revolution in the Making 1924-1936*

Deane, P *The Evolution of Economic Ideas*

Eatwell, John and *Keynesian Economics*
Milgate, Murray

Heilbroner, R. (1999) *The Worldly Philosophers: the Lives, Times, and Ideas of the Great Economic Thinkers*.

Samuelson, Paul Anthony *Economics* (1980)

Skidelsky, R *John Maynard Keynes v 3* Skidelsky, R. (2003) *John Maynard*

Keynes 1883-1946 Skidelsky, R *Keynes: the Return of the Master*

METHOD OF ASSESSMENT

1. Weekly readings
2. Class presentations and participation in the general discussion
3. Mid-term and end-of-term papers, consisting of one essay in each case and (as part of the final assignment) a selection of quotations from the readings, each accompanied by the student's comment.