The Response to the Response to the Article: A Reluctant Agreement with John Cochrane

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To begin, I believe that being able to read both Krugman and Cochrane's pieces back-to-back is the ideal way to consume these two articles. It makes me wonder if readers at the time were expecting some response from one of the many named classical economists in Krugman's piece, and if it was assumed to be Cochrane, given his vocal reputation. The most interesting thing I found was that, even though I lean towards more of the "saltwater" economist's way of thinking, I discovered that I was agreeing more with what Cochrane wrote than with Krugman. Not because I entirely subscribe to Cochrane's way of thinking, but because he pointed out some fundamental flaws in Krugman's arguments.

I read Krugman's first and found myself agreeing with almost everything he said. That classical economists had it all wrong and their hubris had gotten in the way of their unbiased analysis. Then, after reading Cochrane's response, and learning that most of Krugman's direct personal remarks were taken entirely out of context. As Cochrane pointed out, totally within bound for a political op ed, but has no place in an article that is professing to be about the underlying science. I'll discuss what I liked and disliked about each piece before giving some closing thoughts.

I'll start off with Krugman, which only has two big things going for it, which is my established biases and that I read his piece first. He certainly more closely aligns with my economic way of thinking, but he absolutely ruins any credibility he might have with "strawman" arguments. Yes, the neoclassical economists, the "freshwaters", do believe in a more hands off approach to economic regulation. That the economy will sort itself out because of its various efficient markets. What I find hard to believe is that anyone could be so out of touch and so absorbed in themselves that they believe a recession is good for the economy. This continues for a while, using sound economic arguments ruined with misrepresented quotes and a weak effort to back anything up. At the end of the piece, Krugman's argument distills down to the idea that since Keyes in the 1930's the entire field of study of economics has been a waste. Even his attacks at the "beautiful" mathematical equations comes off as almost petty, in an article that should try its best to remain factual in nature. I do not know if he truly believes his misrepresentations, especially regarding Milton Friedman, but at the end of the day it comes off as disingenuous.

Cochrane, on the other hand, has the benefit of being the response. Had Krugman known he was going to be absolutely picked apart he may have chosen to pull back and stick to factual and empirical analysis a little more. Cochrane does a good job of recognizing the concessions that all economists make when doing empirical analysis, i.e. assumptions. While not perfect in the real world, the Ricardian equivalence is mathematically sound and, until empirical rendered ineffectual, is a good argument for the uselessness of government when it comes to guiding the economy. Cochrane also does a good job of re-using Krugman's arguments against him. In the case of the "noisy trader", Cochrane makes a good point of extending that idea to bankers and politicians. If there are irrational people, then anyone can be irrational. While politicians may have their advisors, I doubt few if any really understand the economic machine as well as actual economists do. Even if fiscal policy was useful in guiding the economy (which empirically is shaky at best), there is little hope that elected politicians, whose main skillset is getting elected, would be able to correctly guide the ship.

At the end of the day, I don't believe I fully side with either of these economist's positions, but if there had to be a "winner", it would go to Cochrane for their well thought out and, most importantly, evidence backed arguments. If I were to align myself with any economic school, it would likely be the monetarists. I do think that the economy can be guided not by fiscal policy, but by monetary policy. Irrationality does exist in the markets, but the repercussions of the "black swan" events can be mitigated by adept helming at the wheel. If anything, the current inflation situation is evidence of this. Had the Fed raised interest rates sooner there is a good argument to be made that the inflation crisis would not be nearly as bad as it has been. Even in the midst of the crisis, which is still ongoing as of writing this response, the Fed is navigating the country through without any strong repercussions on unemployment rates. Nothing will be able to be said definitively until the crisis post-mortem, but monetary policy can and will lessen the impact of economic hardships.