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Book Review

[Book Review of] Lucas, Robert E., Jr. : Models of business cycles, Oxford, Blackwell, 1987

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nachvollzogen und kritisiert werden können. Die Untersuchung sollte deshalb vom Leser so aufgenommen werden, wie sich das die Autoren vermutlich gedacht haben: Sie sollte nicht als Offenbarung verstanden werden, sondern schlicht als ein Werkstattbericht.

Klaus-Dieter Schmidt

Lucas, Robert E., Jr., Models of Business Cycles (Yrjö Jahnsson Lectures). Oxford, New York 1987. Basil Blackwell. 115 pp.

The Yrjö Jahnsson Lectures have a long tradition in which distinguished economists (several of them are Nobel-Prize winners) have given a survey on where we stand in a particular field of economic theory. In this book, Lucas takes us, in the true sense, to the frontiers of the theory of business cycles.

The Lectures begin with the description of a very general model that links economic policy to the evolution of the economy (Section II). We arrive at the crucial distinction between the structural and the reduced-form representation of an economy. The message of the "Lucas-critique" is that actions of economic agents are not invariant under changes of nature's (or policy's) actions. In order to make quantitatively reliable statements about the effects of policy changes, decision-rules have to be made explicit, and we may then assume, that "each agent is doing the best he can" (p. 16). Using these model-building principles, we are able to say something about stabilization policy, not in the sense that we will arrive at recommendations about specific day-to-day actions of monetary and fiscal policy, but hopefully at well-defined policy rules which promise to increase welfare.

Lucas continues with a discussion of a specific model for business-cycle analysis; he finds the Kydland/Prescott model[1] most useful for his purpose (Section IV). It represents one of the basic contributions to modern real-business-cycle theory. Certainly, Lucas does not subscribe to this line, but nevertheless uses this model as a benchmark because it applies many of the interesting non-monetary characteristics of neoclassical theory to business cycles. Its performance comes quite close to imitating the actual behavior of the U.S. economy, but not close enough. One way to extend the model would be (most naturally for economists like Lucas) to include monetary factors. Lucas gives two reasons why he thinks that such a synthesis makes sense (Sections VI, VII): firstly, the Kydland/Prescott model would require much larger real shocks to reconcile the actual behavior of the economy with the estimated model (especially for periods of severe contractions); and secondly, Lucas does not want to cast aside the findings of Friedman/Schwartz about the historical relationship between money and economic activity. However, this integration "is, at present, slightly beyond the frontier of what is technically possible" (p. 85). But Lucas continues and describes how this hypothetical ("hybrid") model would behave and illustrates the usefulness of many recent contributions, including his own. He explains why the difference between anticipated and unanticipated money matters and also accepts that nominal wage rigidity can play an important role. Of course, this rigidity has to be properly defined. The classical postulate of the neutrality of money is not given up. Whatever rigidity there may be in the short run is not treated as a "free" parameter; we rather use the

[1] Kydland, Finn E., Edward C. Prescott, "Time to Build and Aggregate Fluctuations". *Econometrica,* Vol. 50, 1982, pp. 1345–1370.

available information, for example, on contract length, in the same way we use the information on lags ("time to build") in the Kydland/Prescott model. As in several of his earlier works, Lucas expresses his optimism that progress along those lines will be possible and fruitful.

If we really learn more about business cycles following this or any other route, what is the additional welfare we can expect from policies that minimize cyclical fluctuations? Lucas provides a benchmark – an upper limit – by investigating the actual variability of total consumption in the United States. Surprisingly, the possible gain in economic welfare is very small; this means that the instability after World War II is a minor problem. If we accept this, we may say that however bad actual stabilization policies have been in recent years – and Lucas has surely been one of their fiercest critics – they have not caused much damage; and if we can devise rules which promise minimal fluctuations of economic activity, we will gain only very little. We may struggle with these results or not believe them. For example, bad stabilization policies might have led to a decline in the growth rates of GNP and consumption by disturbing the signalling function of the price system; in this case, permanent income would be lower than under stable policies. Further, was there not a tremendous waste of resources when many investment projects were undertaken solely for the purpose of hedging against inflation? What about the uncertainty created by stop-and-go policies with respect to inflation, possibly raising interest rates? Finally, how much uncertainty was created by the rise in government debt that was sold as anticyclical policy (which taxes will be raised and when?). But whether we end up with higher estimates of potential welfare gains from good policies or not, we would certainly follow Lucas' statement that we have learned how to avoid big mistakes such as those which have led to severe contractions or hyperinflations.

Lucas has for a long time favored the use of analogue systems, i.e., models with which we can imitate the economy. In these Lectures, he once again demonstrates the advantage of this approach and argues that progress can best be made this way. A further ingredient of his research is the strict application of neoclassical principles. We should analyze all economic problems with one set of economic principles; this approach has by now finally entered textbooks on macroeconomics. One may call his approach "dogmatic", as some will surely do; and it is certainly not satisfying to some that a distinguished economist is so modest to admit that he cannot (yet) explain all relevant phenomena associated with business cycles. But what's the alternative? "If we are honest, we will have to face the fact that at any given time there will be phenomena that are well-understood from the point of view of the economic theory we have, and other phenomena that are not. We will be tempted, I am sure, to relieve the discomfort induced by discrepancies between theory and facts by saying that the ill-understood facts are the province of some other, different kind of economic theory. Keynesian 'macroeconomics' was, I think, a surrender (under great duress) to this temptation" (p. 108). Nevertheless, some will continue to argue today that we do not understand business cycles any better than we did fifteen or twenty years ago, i.e., before the work of Lucas and others. In those days many economists believed that business cycles would become obsolete because of the tools which supposedly gave policymakers power to control the economy.

If we follow the route set out by Lucas, we may wonder how a book like this one will affect policymakers. After all, Lucas takes the "utopian view" (p. 9) that policies can be and should be improved. It is clear that improvement cannot mean picking better numbers for this year's budget, money supply growth, and so on. The role of an economic advisor is limited to, for example, defining rules of conduct. The most pressing problem for policies in Western Europe is the high level of unemployment, and the discussion is confused among economists and among policymakers alike caused, in part, by the widespread use of different labels for this phenomenon (wage gaps, hysteresis, output gaps etc.). What follows from Lucas' Lectures (and especially from Section V on unemployment) is that it does not help unemployed people if anyone tells them that their problem is one of "fine-tuning".

This and all other policy conclusions are not at all "surprising" (contrary to the assertion on the back cover of the book). They are arrived at by powerful economics, and one cannot but agree that this book is essential reading.

Joachim Scheide

Maizels, Alfred (Ed.), „Primary Commodities in the World Economy: Problems and Policies". World Development (Special Issue), Vol. 15, Nr. 5, 1987, 221 S.

Das Sonderheft von World Development zum Thema Rohstoffe enthält 13 Beiträge verschiedener Autoren sowie einen einleitenden Überblicksartikel des Herausgebers, in dem als wesentliche Ziele der Beiträge des Heftes

- eine größere intellektuelle Übereinstimmung über Eigenart und Bedeutung des Rohstoffproblems sowie
- die Diskussion von Optionen für die internationale Politik, die dazu beitragen, den Rohstoffsektor in der Weltwirtschaft und hier insbesondere in den Entwicklungsländern zu stärken,

herausgestellt werden.

Schon die Formulierung „Rohstoffproblem", mehr aber noch die eher politisch-programmatisch wirkende Zielsetzung „Stärkung des Rohstoffsektors" deuten auf Konfliktfelder hin, die sich durch eine große Zahl der Beiträge ziehen. Der Bogen des abgedeckten Themenbereiches ist sehr weit gespannt. Er reicht von Zusammenhängen zwischen der Entwicklung der Rohstoffpreise und der Gesamtwirtschaft in Industrie- und Entwicklungsländern über Fragen der Preis- und Erlösinstabilität, ihren Folgen und möglichen Kuren bis hin zur Rolle und Beurteilung von multinationalen Unternehmen, die im Rohstoffbereich tätig sind. Da eine Behandlung aller Einzelbeiträge den üblichen Rahmen einer Besprechung sprengen würde, soll anhand einiger ausgewählter Themenbereiche beitragsübergreifend versucht werden, einen inhaltlichen Überblick zu geben.

Als erstes Thema drängen sich offensichtliche Unterschiede zwischen verschiedenen Beiträgen in der Problembeschreibung auf, da daraus notwendigerweise Konsequenzen für die abgeleiteten Politikvorschläge resultieren. Die eine Position beinhaltet, daß instabile Rohstoffpreise negative Folgen vor allem für Entwicklungsländer, aber auch für importierende Industrieländer haben. Sie wird vor allem von Nicholas Kaldor (The Role of Commodity Prices in Economic Recovery) vertreten, aber auch Alfred Maizels neigt in seinem Überblicksartikel zu dieser Ansicht. Dagegen kommt Jere Behrman (Commodity Price Instability and Economic Goal Attainment in Developing Countries) in seinem Beitrag auch aufgrund von Modelluntersuchungen zu