

Book Review

21st Century Economics: Economic Ideas You Should Read and Remember.
Edited by Bruno S. Frey and Christoph A. Schaltegger. VoxEU.org Book:
CEPR Press, 2020. 115 pp.

This edited volume is the result of an inquiry into what is the content of modern economics that one should read and remember. Basically, the book is a collection of insightful contributions by a wide array of economists. Out of which, at least twenty ideas and contributions stand out as fitting to the theme of this journal.

The first recommended literature is entitled *Mostly Harmless Econometrics: An Empiricist's Companion* by Joshua D. Angrist and Jorn-Steffen Pischke. In a nutshell, the book identifies causal effects in a concise and reader-friendly manner, that is, it begins with a question on whether hospitals make people healthier to demonstrate the selection problem researchers face when dealing with observational data. This is followed with discussions on alternative methods for causal inference and concluding with support for more transparent research designs that lead to credibility in empirical economics and policy relevance. Besley and Burgess view that politicians' need to take the well-being of the citizens into account, especially if their actions are monitored by free media, in *The Political Economy of Government Responsiveness: Theory and Evidence from India*. The authors introduced a new field of media economics after an in-depth study of how the media can mitigate the principal-agent problem, leading to a central hypothesis that politicians pay more attention to citizen's interest when the prevalence of media is larger. The critical question is how the watchdog function is changed by the advent of social media, while economic reasoning suggests that the role of the fourth estate is strengthened with a bigger, better accessible and more competitive market for information.

The Nobel Laureate Amartya Sen's latest masterpiece *The Idea of Justice*, is the next pick. Sen argues that even when the limits of the concept of happiness is broadened to the idea of fulfillment or human flourishing, it remains to just one dimension of life. Keeping happiness within the boundaries of common sense means that priorities could stretch well beyond the narrow limits of one's personal well-being, given the dynamic nature

of subjective happiness. Next in order is the work of Hans Gersbach on *Redesigning Democracy: More Ideas for Better Rules*, which comes in two parts. Contractual democracy establishes how the results of policies post-election can be improved for citizens by introducing contracts proposed by competing political candidates. The second part, on rules of decision making and agenda-setting, demonstrates how better political rules and agendas offering a divisible public good lead to optimal outcomes. Another book with a similar line of reasoning but from an institutional perspective is the highly recommended *Why Nations Fail: The Origins of Power, Prosperity, and Poverty* by Acemoglu & Robinson. It offers a brilliant framework on how economic and political institutions collectively drive long-term development. While the former shape incentives, the latter is the deciding factor on which economic institutions a country has in place. The authors differentiate between inclusive and extractive institutions under both categories and explain how the fear of creative destruction acts as the root of opposition to inclusive institutions. Using the European colonialism as an example, they demonstrate the key role of critical junctures driving institutional changes.

Frey and Stutzer, in turn, emphasize that a proper working of institutions has preconditions beyond the narrow economic view in their book on *Happiness, Economy and Institutions*. They focus on institutional effects, in particular the impact of direct democracy on well-being. On an implicit level, the authors address the missing link in the thinking of two Nobel Prize laureates, Buchanan and Hayek. It is an exemplary literature on the connection between constitutional and behavioural economics. *Economics and Identity* by A. Akerlof and Rachel E. Kranton suggests the prominent concepts in Economics, for example fairness rest on the notion of identity. By postulating the existence of identity utility, they show how these ideas contribute to the analysis of economic issues - education, race, poverty, labour market, gender roles, productivity, and wages - affecting economic outcomes. The duo has been developing the concept of Identity Economics since the turn of the millennium, investigating measurements, determinants, and the effects of identity on economic behaviour. Their approach rests on the premise of new assumptions that provide a significantly different view of reality. For example, the proof of individuals' willingness to trade off lower wages against higher social status. At the very least Identity Economics has opened a new field of study and a professional association that highlights the role of groups, norms and narratives to economic models and decisions.

With the view to revising the theory of collective action, Elinor Ostrom raises the question of how potential cooperators provide signals and act conditionally in her book on *Collective Action and the Evolution of Social Norms*. Contrary to traditional economic theories, human behaviour is not assumed in an axiomatic manner. Political institutions facing social dilemmas can now consider endogenous factors to facilitate organizational learning instead of relying solely on rational behaviour. In a similar vein, the need to evaluate policy in terms of citizen preferences is put forth by John Matsusaka in his book on *Public Policy and the Initiative and Referendum: A Survey with Some New Evidence*. The underlying idea suggests direct democracy complementing representative democracy through open, and productive exchange of opinions to facilitate beneficial policies.

Raj Chetty helps explain what one can expect from economic research in his book on *Yes, Economics is a Science*. Given the debate on whether Economics is a science, on the quality of policy decisions based on sound reasoning, he goes on to defend the role of hypotheses development and empirical testing in economic studies. Differences among experts are said to originate from variations in data quality, measurement techniques and interpretation of results, and thus do not point towards the lack of science in Economics. Subjectivities due to implied value judgments and individual biases do not make Economics any less scientific, he concludes. *The Superiority of Economists* by Marion Fourcade, Etienne Ollion and Yann Algan offers a sociological perspective on the economic profession. The trio support Economists' higher market status as a combined result of better financial position and emphasis on mastering quantitative reasoning. Despite the Economists' dismissive attitude towards other social scientists and the field itself being insular in nature, the authors admit that the general mission to maximize public welfare has been relatively successful. The last reading along this strand of thinking is Dani Rodrik's book on *Economics Rules: The Rights and Wrongs of the Dismal Science*. His arguments rest on the understanding of knowledge accumulation in Economics, horizontally and not vertically. At best, he says economic models provide refinement to daily thinking, and the search for making sense of the world one cause at a time.

Not surprisingly, Thomas Piketty's book on *Capital in the Twenty-First Century* made the list of readings on economic ideas that should be remembered. In addition to putting economic inequality back on the agenda, the author addresses the issue of wealth distribution in relation to socio-

economic growth and stability. Using statistical data dated from the 18th century for the United States (US), he demonstrates how progressive taxation of capital moderates the differences in rates of return between capital and economic growth over time. *Saliency and Taxation: Theory and Evidence* by Raj Chetty, Adam Looney and Kory Kroft highlights the relevance of fiscal illusion, tax neutrality, tax incidences and deadweight losses in public economy. They show the evolution in the theoretical foundation of policy making, applying saliency in value-added tax in the US. While low saliency appears to reduce excess burden, it also distorts individual optimization causing welfare losses. Consequently, the degree of attention individuals pay to aspects of a choice or a lack of it significantly affects their actual decision. Yet, Allan H. Meltzer presents three key messages showing favour of the only system that maximizes long-term growth and personal freedom, in his book on *Why Capitalism?* He argues against the widespread tendency to think of financial crisis as the end of capitalism, and for realism as compared to idealism. All moral criticisms of capitalism confound structural deficiencies and personal vices, and therefore capitalism is not responsible for what goes wrong, but the people in powerful positions are, according to the author.

The concluding part of this volume includes two relevant chapters. *A Model of Social Identity with an Application to Political Economy: Nation, Class, and Redistribution* by Moses Shayo, in which the author argues that political preferences are shaped by social identities. In identifying themselves to adapt and fit in with social groups, individuals gravitate towards demographic similarities, and consequently become altruistic toward the group's political beliefs and policies. Ultimately the interaction between political identification and policy choices renders it a source of indeterminacy. Exploring these issues empirically is imagined to be revolutionary to political economy. Daron Acemoglu's and James A. Robinson's book on *Economic Backwardness in Political Perspectives* illustrates the importance of political institutions, political commitments, and credibility of oppositions to economic development. Their model shows proof of the trade-off faced by the elite in supporting market-enhancing policies due to divergent interests between the incumbent government and citizenry at large, using a simple surplus maximizing economic efficiency analysis.

The rest of the volume contains short chapters on topics ranging from the harmlessness of Econometrics, Bitcoin, importance of financial literacy,

auction theory, mindful Economics, crime, inequality, poverty traps, network structure of social capital, the Lucifer effect, and human economy, amongst others.

Shafinah Rahim

Faculty of Economics and Business

Universiti Malaysia Sarawak

94300 Kota Samarahan

Sarawak

Email: barshafinah@unimas.my