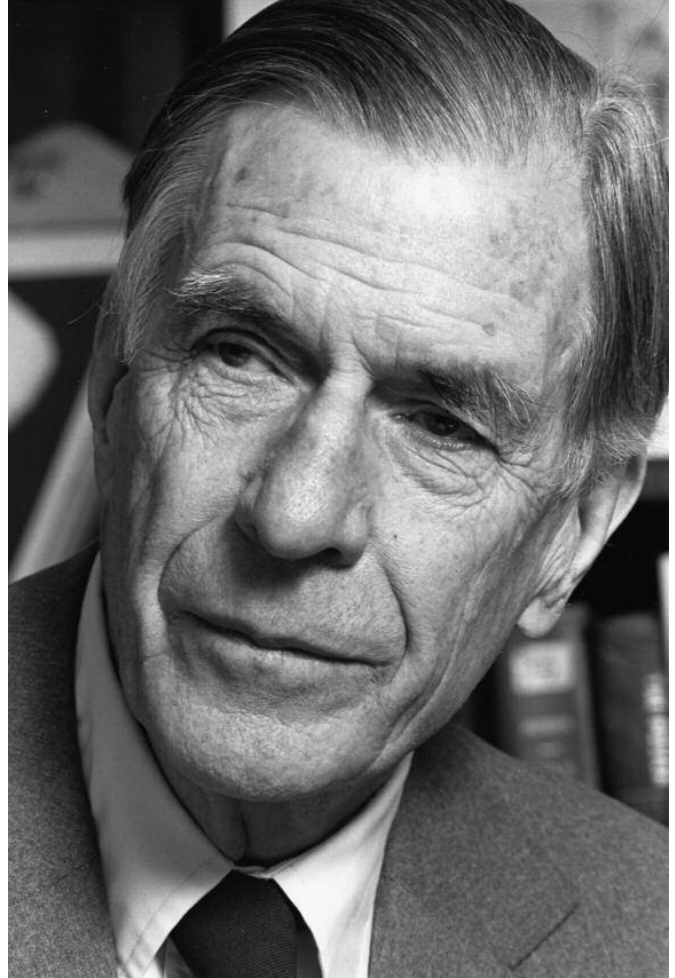


# Unconventional Wisdom

Interview with John Kenneth Galbraith

*John Kenneth Galbraith has been writing best-selling books about economics for many years. Those books—of which there are literally dozens—have earned him the reputation as the best-known economist in America, and perhaps even the world. His classics include American Capitalism (1952), The Affluent Society (1958) and The New Industrial State (1967). More recently he has written The Culture of Contentment (1992) and The Good Society (1996). But Galbraith's views, however popular when measured by book sales, are certainly not uncontroversial. He is famous for challenging standard doctrine within the mainstream economics profession and for challenging the value system implicitly reflected by both public and private decisions. Galbraith is currently an Emeritus Professor in the Department of Economics at Harvard University. He was interviewed by Christopher Ragan, Editor of World Economic Affairs, at his home in Cambridge, Massachusetts.*



**W**ORLD ECONOMIC AFFAIRS: **Who have been your greatest intellectual influences, and how is this influence evident in your writings and ideas?**

**Galbraith:** Well, I began with Alfred Marshall. He was my great introduction to economics. With much of his work I eventually came to disagree, but you had to know what was wrong before you could know what was right. I was also very much influenced, in the 1930s in California, by Thorstein Veblen, and in the latter half of the 1930s, after I came to Harvard, by John Maynard Keynes. He was a great opening of the window in 1936. Up to that time, I had adhered to

the notion that the Great Depression, for example, was the result of the control of prices and output, an aspect of imperfect competition. I went through a major transformation that year when I read Keynes' *General Theory*.

And then there were many others. Alvin Hansen, who was the voice of Keynes here at Harvard, was very influential. I was, early on, instructed in the connection between economics and government action by people both at Harvard and in Washington—by John D Black at Harvard and Henry Wallace in Washington. I concluded, from their work, that there was a natural bridge between economic theory and practical action.

**WEA:** **Some people would argue that your main contribution to economics over the years has been in altering our underlying value system rather than in developing precise, convincing theories of the structure of the economy. One example is that your views may have increased the attention paid to poverty and to the appropriate provision of public goods, whereas your views on “countervailing power” may not have been well accepted by the economics profession. Would you agree that your contribution has been mainly in terms of changing values rather than in precise theory-building?**

**Galbraith:** I would agree. My interest in the minor refinements of economic theory has been very low. Or, rather, it has not been low, but subject to control. On the other hand, countervailing power—the notion that the institutional structure of the economy works by the creation of opposing systems of power—has been, in my view, surprisingly influential. The book in which it appeared [*American Capitalism*] is still in print, it's still discussed. I keep encountering references to countervailing power in my reading and I am, by no means, disappointed by the reception of that book.

**WEA:** If nothing else, you have certainly been a successful producer of terminology—"the affluent society", "countervailing power", and "the conventional wisdom" are a few examples.

**Galbraith:** The conventional wisdom has been my best.

**WEA:** Lester Thurow described you in *The New Palgrave's Dictionary of Economics* as "an economist out of the mainstream of economic thought but in the mainstream of economic events". Do you agree?

**Galbraith:** I would broadly accept that observation. Lester Thurow is a very close friend of mine and was once my student. His judgement on such matters is pretty good.

**WEA:** You once described your approach to economics as "the lower economics" with an emphasis on big ideas and prose rather than on technical details and mathematics. Do you lament the fact that your writings have not been adopted by the mainstream of the academic economics profession, or do you think that your ideas have spread further precisely because of your "lower economics" approach?

**Galbraith:** If I had been rigidly orthodox, I think by now I would be well forgotten. Only as you emerge to influence the course of economics, to see flaws in its development and correct them, do you have any hope of continuing recognition. Though I do not want to exaggerate the point, I have never felt all that

outside of the broad current of economics. I served my term as president of the American Economic Association which is not something that is accorded to outsiders, and I have had a large number of close friends in the economics profession, at Harvard and all over the country. So I have never had the sense of exclusion.

When my appointment as president of the American Economic Association was under discussion, there were some objections to it on the grounds that I was not strictly orthodox. Someone made the terrible mistake in the discussion of pointing out that Thorstein Veblen had never been president of the American Economic Association, had never been similarly recognised. And that, I have always been told, was the reason that I was immediately appointed.

### Markets Versus Planning

**WEA:** Let me now turn to the topic of markets versus planning. One of the central themes in your writing has been that government has a role to play in economic planning, and that economic planning has a role to play in successful economies. The past half-century has seen significant changes in this regard, the most dramatic of which was the collapse of the Soviet Union—an event viewed by some as proof that market economies are superior to planned economies.

What do you take as the important lessons regarding markets versus planning from the fall of the Soviet Union?

**Galbraith:** I have no doubt on that point. This is not a matter of ideology. Ideology here is a blanket over thought.

The question is one of the pragmatic mix. There are some areas where the market system—the word capitalism has now gone out of fashion—is absolutely indispensable; and there are others where the role of the state or the restraints imposed by the state are

absolutely essential. One cannot have a general theory covering all situations; one must have an open mind as to the particular situation. In Canada and the United States, some of the greatest achievements have been by government. We have the best university systems in the world, largely the product of government action. Canada would not have been a country if it hadn't been for the government intervention in the field of transportation, once of central importance. So I repeat: this is a question of application

of intelligence to the particular situation and not something to be guided by formula, sometimes called ideology.

**WEA:** Let me follow up on that point because you discuss it thoroughly in your latest book, *The Good Society*. You argue there that, too often, both liberals and conservatives are prone to escaping into ideology from thought. You argue instead that policies ought to be evaluated on a case-by-case basis. Do you think there is much hope that the liberal/conservative "jump to ideology" will be reformed?

**Galbraith:** Oh, the escape into the formula, the escape into the ideology and the pride that is involved in that is very strong. I would have hoped for a pragmatic revolution, but my expectations are not too high.

**WEA:** Some people would argue that much of the success of the East Asian economies comes from a judicious use of government planning rather than complete *laissez-faire*. Do you agree? What important lessons do you draw from the rise of the Asian Tigers?

**Galbraith:** I draw the conclusion that, on the whole, the Asians—Japan, Korea, Singapore—have been less governed by theory, less governed by doctrine than the United States, Canada, and the West, and that three important things have happened as a result. First, a substantial investment—let's take Japan as the leading case—in needed infrastructure. Second, a strong sense that the bureaucracy is allied with business and in its support. And third, a government regu-

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latory structure that is governed—going back to our earlier point—by practical utility rather than by theory.

**WEA:** I once saw reference to the fact that your books have sold even better in Japan than they have in the United States. Your answer to the last question suggests that your ideas may simply be more in tune with the way people think in Japan. What do you think?

**Galbraith:** My books have always been very well received in Japan, but I just attribute that to general Japanese intelligence.

**WEA:** Do you think the increasing trend toward globalisation—increased capital mobility, freer trade and instantaneous communications—places limits on the role of government in the economy?

**Galbraith:** Well, let me begin by saying that I am conducting a one-person and hopeless crusade against the word “globalisation”. It’s an awkward and inaccurate term; let’s talk instead about internationalisation. I don’t think it sets any limits on public action but it does shape public action. It means that there must be co-operative steps of a much more comprehensive sort than would otherwise be the case. Internationalisation I regard as inevitable. It is a force growing out of international trade, growing out of the international corporation, and particularly growing out of intellectual life—sciences, arts, and travel. This is going to continue. I want to see this continue with protection, particularly the welfare system of the individual states, and, of course, one has to expect that it will involve some co-ordination of fiscal and monetary policies.

**WEA:** Do you see internationalisation as putting any constraints on the amount of income redistribution that the government is able to effect?

**Galbraith:** This is not a central point, but there will be—inevitably and usefully—comparisons as to the state of income distribution. One of the factors that is affecting the discussion of the

American economy is that our income distribution is so much worse than that of the other countries.

### Income Distribution in America

**WEA:** Let me go right on to discuss income distribution. In the past two decades, there appears to have been a clear widening of the income gap in America; certainly the share of national income going to the bottom 40% of the population seems to be declining. Are you surprised to see this, and what do you think are the primary reasons for this deterioration of the US income distribution?

**Galbraith:** This is something I certainly didn’t predict. But the causes, I think, are reasonably clear. First, we’ve had this war against the poor, the general attack on the welfare system, which has been particularly damaging for the lowest income groups. This goes back in turn to what I discussed in *The Culture of Contentment*: the rise of a large community of people whose income is reasonably satisfactory, and who, for better or for worse, are very much opposed to public policy on behalf of the poor. Second, we have a strong source of inequality of income in the modern corporate structure. The large managerial class has extensive power over its own income. The corporate executives who appoint the people who set their income are a very important factor in the distribution of income, coupled with the continuing importance of the structure of finance which conveys very large rewards.

**WEA:** Let me take you back to your mention of *The Culture of Contentment* because in that book you argued that many and perhaps most policies are designed to benefit the middle- and upper-income households implicitly at the expense of the low-income households. Given the size and polit-

ical power of the middle class, is there any reason to expect this to be reversed and, what sort of policies that are politically acceptable to the middle class can bring about such a reversal?

**Galbraith:** I’m not widely optimistic. The notion that an economist should always see an improved goal is something which I have reluctantly denied. On the other hand, here in the United States the situation is made worse by what can only be called an imperfect democracy—one in which those who are contented and rich vote and the poor do not. If we had 100%

turnout in our elections, we would have many more politicians cultivating the welfare vote, the vote of the big cities, and the situation would be much better. I’ve argued very strongly that the essential for improvement is bringing the poor into the political system. The problem is not democracy but imperfect democracy. We see that also, in a spectacular way, in the case of the allocation of government expenditures, particularly to the military. The military in the United States has developed an independent power in the executive as well as an independent power in the Congress and establishes its own share of the income that goes for its purposes. So we come to the end of the Cold War, but the military expenditure goes on just the same.

**WEA:** You argued in *The Good Society* that even the middle- and upper-income people, even people that consider themselves conservatives, ought to be in favour of improving the income distribution if for no other reason than that it buys social peace and tranquillity. Why don’t people appear to buy that argument?

**Galbraith:** My statement on that is somewhat optimistic. My obvious answer is they haven’t read my book. I would hope that, as the society matures and becomes more sophisticated, it will be seen that greater equality in income distribution is a source of social tranquillity and that such tranquillity is important for the rich as well as for the poor.

**WEA:** There has been a revival of interest, both among policy-makers

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and academic economists, surrounding the minimum wage. Do you favour raising the minimum wage as a means of improving the distribution of income?

**Galbraith:** Absolutely. And I don't buy the notion that the question turns on unemployment. It could be that an increase in the minimum wage enlarges the flow of aggregate demand and has an affirmative role in the economy. I don't push that point very strongly, but it's at least as good as the argument that the minimum wage increases unemployment.

**WEA:** You generally seem to be an advocate of letting markets allocate resources; on the other hand, you want to temper the use of markets by redistributing income and having government involved in some regulation. As a means of improving the distribution of income, do you see any advantage in using minimum wages rather than just more direct income transfers?

**Galbraith:** Oh, I would use both. I don't see them as alternatives. The minimum wage has its own particular role for its own particular clientele, but that doesn't exclude the progressive income tax, for example, as a very central instrument for income redistribution.

**WEA:** How do you feel about an idea that Milton Friedman, among others, has advocated for many years—the negative income tax?

**Galbraith:** When Milton Friedman makes a step into liberal policy, I naturally applaud. The negative income tax, however, runs into major political difficulties. The notion that you remit money to people who don't need it, which was part of that idea, is perhaps politically unsaleable. While I was once attracted to it, I have been repelled by the political difficulties.

**WEA:** Many years ago in *The Affluent Society* you discussed the tendency of market economies to underproduce public goods such as museums, parks, and clean rivers. And it is certainly easy to see in America and in other countries, especially in large cities, that some of the public infrastructure is literally crumbling

beneath our feet. One solution, greater spending on public goods, seems obvious. But what is the key to bringing about this solution? Is there something fundamental about the US political system that precludes such a solution?

**Galbraith:** Well, I've no easy cure. I have hoped that by a better understanding of the situation one would do something about it. And to that end, I invented the phrase "private affluence and public squalor", which perhaps had some influence in the right direction. But I see no alterna-

tive to popular understanding coupled with much larger political assertiveness by those who most need the public goods. It is the poor who suffer from the poor public housing. It is the poor who suffer from the crumbling schools. It is the poor who need libraries. So I come back to my basic point—what is needed is strong political assertiveness by the poor.

**WEA:** If the lion's share of the solution is to get the poor, or even lower-middle income groups, more actively involved in the political process, how do you do that?

**Galbraith:** My only answer is the one that I have pursued myself: develop the point, talk about it, urge it, and hope that somebody is listening. It is unduly optimistic, but it is the only answer that I have.

### Inflation and Unemployment

**WEA:** I'd like to steer you now toward the topics of inflation and unemployment. Much of your writing over the years has contained concerns about inflation. Indeed, Milton Friedman, who has been nothing if not one of your fiercest intellectual opponents, has credited you with viewing inflation as a serious problem, a concern that is often not shared by other so-called liberals. What do you think are the main costs of inflation? I am thinking

here about the costs associated with moderate inflation, say 8% or 10% per year.

**Galbraith:** First, we have to talk a bit about the extent of the inflation of which we are speaking. I have spent quite a large part of my life in the less developed world, where the problem of hyperinflation can be devastating. I have had no tendency to minimise that problem. Second, there is no doubt that you have an equanimity in the economy if you have reasonably stable prices. And to that end, I have argued, for example, for the European model of wage-price stabilisation, which takes account of the microeconomic thrust of price increases. On the other hand, I see no decisive danger in the kind of inflation which we have had over the last 30 or 40 years. A modest increase in prices every year and some imperiling of the position of the rentier class seems to me to be quite satisfactory. I don't argue for absolutely stable prices.

**WEA:** I'm sure that many people would understand you arguing that today's inflation rate of about 3% is no particular problem. But you go further. You just said that the inflation America experienced over the past 20 years has been no particular problem.

**Galbraith:** That's right. We survived it and there was no particular invasion of economic well-being.

**WEA:** Many years ago you wrote *The Theory of Price Control*, a detailed discussion and defence of wage and price controls. And until at least the 1970s, you were a fairly strong advocate of the active use of wage and price controls as a means of reducing inflation. In particular, you saw this way of inflation fighting as superior to the "mainstream" method of using a monetary contraction to induce a recession. Have your views changed about wage and price controls?

**Galbraith:** Well, I have to explain a little bit. *The Theory of Price Control* was in some sense a retrospective justification of the policies for which I was responsible during the Second World War—I was

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in charge of price control. I did not carry that recommendation over into peace time. I go back to what I said before. In a society of strong trade unions and strong corporations, I'm in favour of microeconomic negotiations to limit the wage-price spiral. But I would not urge universal wage and price controls. That goes farther than, as a purely practical matter, as a purely theoretical matter, I would go.

**WEA:** By microeconomic negotiations do you mean an attempt to "talk down" wage demands?

**Galbraith:** Negotiate wages within the existing structure of prices. This has been commonplace in Europe, and I have always thought it was a good thing.

**WEA:** There is some controversy these days, among both academic economists and policy-makers, about the usefulness of the concept of NAIRU or the "natural" rate of unemployment. Do you think this concept is—or ever was—useful?

**Galbraith:** No. I've never had any support for that. The notion that we can have people suffer unemployment in the interest of price stability is definitely cruel and uncivilised, and therefore I want to see full employment as the basic goal. And if it is necessary to have wage-price restraints of the sort that I've talked about as you approach full employment, I am in favour of that. I do not think, in a civilised country, that one can ask for price stability at the expense of a substantial body of unemployed men and women.

**WEA:** What do you think of the proposed policy of achieving price stability in the United States? Do you see any particular reason why the drive for price stability ought to increase unemployment?

**Galbraith:** Speaking as a purely practical matter at the present moment, I would leave the situation alone. I would not, out of the fear of inflation, go for tighter monetary policy.

**WEA:** In your latest book, *The Good Society*, you argued that full employment and price stability are incompatible.

**Galbraith:** No, I say that some modest increase in prices may be inevitable. That's a little different.

**WEA:** Do you think there is something special about zero inflation? Do you think it is possible for America to have full employment and 2% inflation but not full employment and zero inflation?



**Galbraith:** We will always have some price increases, there is no question. I am prepared to accept it. To have zero inflation at the price of substantial unemployment is unacceptable.

### The Great Crash of 1997?

**WEA:** I would like to turn now to discuss the stock market. You have expressed some concerns about the huge financial flows into mutual funds. Can you explain the problems that might result from the enormous popularity of mutual funds?

**Galbraith:** I think the explosion of mutual funds has exceeded the intelligence available to manage them. There is a hubris there, from which we may one day suffer. One sees a certain nervous-

ness already in the stock market. The day before yesterday [March 13], the Dow went down by 100 points or more, so this is a situation of inherent instability.

**WEA:** Why can't we view mutual funds simply as a low-cost way for ordinary people to have well-diversified portfolios?

**Galbraith:** Oh, I wouldn't exclude mutual funds, but I would say that there has been an explosion of mutual funds far beyond any necessary outlet for middle-class investment.

**WEA:** But what is the actual source of the concern? Is it that there is too much capital going into equity investment or that there is too much capital going into equity investment from unsophisticated investors?

**Galbraith:** Both. The danger we face is that there will be a crack-up on the market. It's been going up partly because people think it's going up and so act, and that pushes it up even further. It has a self-propelling aspect which we have seen in history many times, going back to the Tulip-mania of the 17th century. And when the balloon is punctured—and balloons that are punctured don't subside gradually—there will be a restraint on consumer expenditure by people who have had the sense of wealth from increasing stock prices, and there will be some depressing effect on the economy. I don't think it will be as serious as anything after 1929,

but one should not imagine that one can have a major stock-market correction, as it is called, without some damage to the economy.

**WEA:** I want to come back to that point in a few minutes. You wrote about the causes of the Great Depression in *The Great Crash*. Do you see similarities between the current long-lived bull market and the one in the 1920s?

**Galbraith:** I wouldn't stress the similarities, but there is a common factor which has extended over hundreds of years. This is the euphoria that causes people to invest and, in turn, shoves up the market and justifies the expectations. So you have an automatic incentive to err here, which is part of economic life.

And I would say that is certainly happening now.

**WEA:** Alan Greenspan, the Chairman of the US Federal Reserve, raised the market's eyebrows earlier this year when he spoke about the market's "irrational exuberance". Do you think his efforts to carefully prick the stock-market bubble were sensible?

**Galbraith:** I rather welcomed that comment of Alan Greenspan's—the first of his comments in some years that I thought was in order. I think such a public warning of excess optimism and institutional exuberance in the stock market was well-taken.

**WEA:** Let me take you back to your concerns about a possible crash and the implications for the economy. Suppose a crash occurs tomorrow. Given the Fed's response to the 1987 crash and the subsequent solid performance of the US economy, why should we worry about these crashes?

**Galbraith:** We have had a longer, more exuberant increase this time than we had prior to 1987. No question about that. We have a consumer economy that is based heavily on credit cards and credit, and is sustained by the feeling that people have of increasing mutual fund returns, increasing stock-market returns. All of this would have a depressing effect on consumer expenditure—we shouldn't doubt it.

**WEA:** But why didn't it follow in 1987? Simply because it wasn't the same size of drop in the stock market?

**Galbraith:** There wasn't then the same depth of pessimism that would happen now.

**WEA:** Because of the size of the drop?

**Galbraith:** Yes.

### The State of the Economics Profession

**WEA:** You arrived at Harvard in 1934. In the 60 years that followed, you have witnessed significant changes in economic doctrine. In your view, what have been the most powerful and influential ideas in economics in the past half-century?

**Galbraith:** John Maynard Keynes and his emphasis on aggregate demand. I would have no doubt about that.

**WEA:** Do you think there have been any similarly influential developments in microeconomics?

**Galbraith:** The microeconomics that I taught when I first came to Harvard and joined the community of Frank Taussig and that which now appears in the modern textbooks, which I look at from time to time, are not all that different. The competitive theory of supply and demand, to an extraordinary extent, resembles that of 50 years ago.

**WEA:** Do you think the academic economics profession is currently addressing the right issues? Are there some important neglected problems?

**Galbraith:** Yes, I think there are neglected topics. There is still the enthusiasm for the technical precision associated with mathematical models. I do not deplore that—I think there is a certain discipline that is involved there. And if all economists talked about the problems that I'm interested in, I wouldn't be heard. But I would like to see a much larger concern about income distribution, the problems of the poor, the institutional structure of our great cities and the poverty there. And I would like, not surprisingly, much more discussion of the unequal role of our public services as compared with our private goods.

**WEA:** Can you offer an explanation as to why the academic economics profession doesn't seem to worry about poverty or income distribution as much as the importance of the problems suggest they should? Is it simply because they don't lend themselves well to technical sophistication?

**Galbraith:** No. There is a long tradition which, in some substantial measure, excludes this subject—and I regret it. We all have a tendency to escape the unfortunate and what, at first glance, may seem the unsolvable. The refinement of mathematical models is something anyone can do with skill and grace. The argument about what you do to reduce poverty in the South Bronx is by no means so pleasant.

**WEA:** John Cassidy, in his recent article in *The New Yorker*, chastised the economics profession for failing to produce many new ideas. Do you agree with his assessment?

**Galbraith:** No, I don't agree with that. The ideas are there, the basic structures of ideas are present. It is the problem of what we have just been talking about—an emphasis on theoretical refinement and precision is much more attractive, and maybe professionally more rewarding, than the microeconomic problems of the poor or the macroeconomic problems of the public-private relationships. That would be my criticism rather than his.

**WEA:** So you don't see the profession as having declined in its ability to produce new, good ideas?

**Galbraith:** I think it may be as good now as it ever was.

**WEA:** What do you see as the role of academic economists in the policy-making process?

**Galbraith:** I have already made that clear. I want to see much more concern about the public well-being and much more emphasis on what brings political and social tranquillity.

**WEA:** Let me finish by asking about the title of your most recent book, *The Good Society*. Do you think we are getting there? How optimistic are you that you'll see *The Good Society*?

**Galbraith:** Well, I suppose if we were getting there, I wouldn't be writing about it.

**WEA:** Thank you very much for taking the time to meet with me today. ♦

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