Economic Schools of Thought: Crash Course Economics #14
Crash Course: Economics
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=====Introduction (00:00)=====

Adriene: Welcome to Crash Course: Economics, I'm Adriene Hill.

Jacob: And I'm Jacob Clifford.

Adriene: Now, believe it or not, we actually read many of your comments on YouTube.

Jacob: First!

Adriene: Some are productive and others, not so much.

Jacob: This guy looks like Mark Cuban, but not as attractive...or rich.

Adriene: We've noticed some people are disappointed we haven't covered the different economic ideologies.

Jacob: You're ignoring the Austrian School. What's this Keynesian trash?

Adriene: Well, guess what? Today, we're going to talk about other schools of economic thought.

[Intro Plays]

=====History of Economic Theories (0:32)=====

Jacob: To understand these economic theories, we're gonna have to jump into a little bit of history. In 1798, a British economist named Thomas Malthus argued that population growth would outpace food production, so eventually humans would run out of food and starve. You wonder why some people call economics the dismal science. Well, Malthus was wrong. Dismally wrong.

The world population has grown from one billion in his time to over seven billion today. And it turns out that the famines we have seen are largely man-made disasters that have very little to do with our ability to produce food. But Malthus was writing at the beginning of the Industrial Revolution. He didn't factor in advancements in technology, agriculture production or transportation. So with the information he had, he was kinda right, but he was still wrong.

Economic theories are constantly being proven, disproven and revised. The problem is, when these theories are wrong, millions of people can be adversely affected. Take Malthus. Some scholars combined his ideas with those of Charles Darwin and concluded that giving assistance to poor people and social programs like welfare are actually immoral. This is called Social Darwinism and it's completely wrong.

Now, economics is not an exact science. It aims to draw conclusions about human behavior without the benefits of labs or perfect control groups. Economic theories reflect different attitudes about human nature and those are likely to change over time. Let's go to the Thought Bubble.

=====Thought Bubble (1:44)=====

Adriene: The founder of modern economics was a Scottish philosopher named Adam Smith. In 1776, his book *The Wealth of Nations*, was published. It was an organized discussion about production, markets and economic theory, and it was tremendously influential. Smith introduced the idea that a person following their own self-interest could end up serving the common good. He also advocated free trade. Many countries at the time had heavy tariffs which protected their domestic manufacturers at the expense of trade.

A generation later, British economist David Ricardo expanded on Smith's ideas by introducing the theory of comparative advantage: the idea that two people or countries can both benefit from trade, even if one of them can produce more of everything. When both focus on what they're best at and then trade, everyone benefits.

Anyway, the field of economics grew, advancing ideas like private property and free markets. And then along comes *The Communist Manifesto* in 1848. Rather than examining individual behavior, German philosophers Karl Marx and Friedrich Engels looked at economic classes and argued that history was explained by the conflict between workers and property owners. This process would inevitably lead workers to overthrow their bosses, ushering in a new stateless and classless system, called communism.

Marx followed this up with *Das Kapital*. Political movements spawned by Marxist economics challenged Adam Smith's view that individual self-interest serves the common good. The end result was two main camps: free market capitalism, supporting private property, and communism, advocating collective ownership of the means of production. Thanks, Thought Bubble.

=====Classical Economics (3:25)=====

Despite Marx's challenge, market-based economic theory continued to dominate through the end of the 19th century, with contributions from French, British, and American economics. This body of thought is called Classical Economics, and it was embodied in a book called *Principles of Economics*, published in 1890 by English Economist Alfred Marshall. Marshall organized and defined concepts we still use today, like supply and demand and marginal utility, which we're gonna get to soon.

But as capitalism was expanding around the world, Marxist movements were too. By the early 20th century, this battle for hearts and minds, along with political and social unrest in Europe, led to the establishment of the Soviet Union in 1922.

Jacob: As Communism was maturing in the Soviet Union, the Great Depression crushed the market economies of the world's richest countries, it also dealt a devastating blow to Classical Economics. The theories of Smith and Marshall didn't have much to say about how something like this could happen, or how to fix it. The British economist John Maynard Keynes proposed new answers in his 1936 book *A General Theory of Money, Interest, and Employment*, which basically launched the field of macroeconomics.

=====Keynesian Economics (4:32)=====

Along with John Hicks, James argued that market economies don't self-correct quickly because prices and wages take time to adjust. They claimed that during recessions, it is necessary for the government to get involved by using monetary and fiscal policy to increase output and decrease unemployment. Keynes wasn't supporting Communism, but his views directly challenged classical economists who saw government intervention as universally harmful for the economy. Now eventually Keynesian Economics became part of mainstream economic theory. See? I told you, economic theory changes over time, and all it took in this case was a catastrophic global depression.

Keynes's ideas, combined with the ever-present Marxist critique, opened the door to more and more government involvement. Since the Great Depression, many nations have pursued a political and economic ideology called Socialism, although Socialist ideas and policies have been around since the 19th century. In most cases, these economies allow for private properties and markets, but also have government ownership of industry, significant regulation, and big public programs like universal healthcare. In Scandinavian countries like Norway and Sweden, they love these socialist policies.

Now the US has rejected many of these socialist ideas, but the US government, or at least economists that advise politicians, are clearly in favor of Keynesian economic policies when the economy's in trouble.

=====Hayekian economics (5:40)=====

Adriene: But as Socialism and Keynesian economics expanded, other groups continued to forcefully push for private property and free markets. The most vocal was often the Austrian school of economics, they also have a very vocal fanbase in our comments section. Friedrich Hayek and Ludwig Vunmises, who were unsurprisingly from Austria, argued that heavy state involvement has never produced the results it promised, and that regulation and government tinkering is actually a problem, not a solution. Rejecting nearly all forms of fiscal and monetary policy, the Austrian school today argues the economy's just to complicated to manipulate.

This backlash against government intervention was carried forward in the US by Milton Friedman. Like the Austrians, Friedman advocated privatization of many functions that had been assumed by government, famously proposing school vouchers and deregulation of the economy. He also concluded that the depression could be blamed on botched monetary policy rather than some inherent fault of capitalism.

The theories of Friedman and his followers at the University of Chicago came to be called the Chicago School of economics. Friedman's views got a huge boost in the 1970's. At that time, inflation soared while output stagnated. Remember stagflation? A combination that Keynesian economics had trouble reconciling. Some macroeconomists drew on the insights of the Chicago school to claim that these events disprove Keynesian economics.

Building on the ideas of Friedman, another idea of economics gained traction: monetarism. Whoo, Stan, so many -isms. Monetarists focused on price stability and argue the money supply should be increased slowly and predictably to allow for steady growth. At about the same time, another theory called supply-side economics, or sometimes called trickle-down economics entered the mainstream. Supply side economics advocated deregulation and cutting taxes, especially corporate taxes.

=====Modern economics (7:37)=====

Mainstream economics today takes ideas from both classical economics, including monetarism, and Keynesian economics. This unified theory is sometimes called the New Neoclassical Synthesis. And yeah, economists are bad at naming things, too. But debates about how and when to implement policies continue. And remember, these are more than just intellectual classroom spats, these policies affect millions of people.

The different reactions to the global recession in 2008 are a good example of this. Some economists suggested using Keynesian policies, namely deficit spending. Other economists suggested the more classical approach of reigning in excess spending to reduce budget deficits, something called austerity.

Believe it or not, economists are still fighting about which of these policies is the right approach and when to use them. We can all agree that Keynes was right about at least one thing, when he said, "Ideas shape the course of history." So where are all these economic theories and ideologies gonna take us in the future? Most countries that once supported strict Communism like China and Cuba have moved toward Capitalism. The only country that's really sticking with it's North Korea, but they're too isolated to be a real test case for an economics system.

But this doesn't mean that Marxism is dead. Many capitalist countries have adapted socialist looking programs. It appears the world's economies are converging towards the middle. but in the end, it turns out it's just really hard to predict the future, especially when we're talking about something as complex as the world economy. Remember Malthus's belief that we're all gonna starve? Well like Malthus, we don't know what kind of changes humanity's gonna face in the future. If history has proven anything about economic thought, it's that we should expect surprises that will upset our current economic models, just like Malthus couldn't imagine that we'd all be alive today.

Thanks for watching, we'll see you next week.

=====Credits (9:30)=====

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