Macroeconomic Don Quizotes

What do macroeconomic equilibrium, The Fountain of Youth, and El Dorado all have in common? People have spent years looking for them only to realize that they don’t actually exist. Abstractly believing in nonsense doesn’t have to hurt anyone, but if the belief in nonsense causes people to take harmful actions, we have a problem.

I’m not saying that a water source that kept you young forever wouldn’t be cool. Nor would I pass up on the opportunity to obtain massive amounts of gold. But, if the belief in The Fountain of Youth or El Dorado causes you to forsake your family and your health to wander aimlessly around Spain, then it is no longer just nonsense. I find Don Quixote to be so fundamentally annoying not because he has mistaken beliefs, but because he actively harms innocent people based upon his mistaken beliefs.

Don Quixote’s apprentices account for the vast majority of macroeconomics professors in existence. The macroeconomic textbooks they write are not only full of nonsense, but they are actively harmful. They create a false world of macroeconomic equilibrium in order to suggest solutions that are internally logical to their model, but inherently false to reality.

The Don Quixotes love to assume that there is some type of macroeconomic equilibrium that sits around just waiting for “shocks” to knock it out of equilibrium. The world is full of shocks, and even more surprises. Every day is a shock to some economic actor. No shop keeper knows exactly how many customers she’ll have the next day. No consumer knows exactly what they will buy over the next year.

People are responsive beings. They respond to the world around them. Disequilibrium is the norm rather than the aberration. Prices of products constantly change. People move from one job to the next. Product lines get added and deleted. The economy is in motion and will continue to stay in motion as it is constantly battered by a myriad of forces reacting against each other.

Purveyors of macroeconomic equilibrium are often one and the same who advocate intervention in the economy to bring it back to equilibrium. They act as if not only there is equilibrium, but that they know where it is. If anyone knows exactly how many ice cream cones the US needs to produce tomorrow, please raise your hands. What no hands? No one can know the “appropriate” amount of ice cream cone production for today let alone for tomorrow. The $15 trillion US economy makes a lot more than just ice cream cones.

There is no appropriate level of consumer spending. Therefore, there can never be over or under consumption. There is no set percentage of an economy that needs to be devoted to investment. Therefore there is never any over or underinvestment. What can exist are bad investment decisions due to imperfect information about the future. Policies that aim to increase consumption, investment, government spending, or exports are not only based on a belief in fictitious equilibriums, they do damage to long run economic growth by misallocating resources.

The next time you hear someone suggest that the US economy needs to be stimulated, picture a guy chasing a rainbow in hopes of finding a leprechaun hoarding a bunch of gold at its base. People are already engaging in actions that they believe to be in their rational self interest. Unless someone out there knows how many ice cream cones the economy is supposed to be making, the appropriate price to sell them at, and who gets the cones, I’ll leave it up to the dairy farmer to determine his milk output, the ice cream company to determine their ice cream output, and the individual ice cream consumers to determine how much ice cream is “appropriately” consumed.

I’m willing to bet that individuals wouldn’t put themselves into $14 trillion of debt to buy ice cream. That kind of economic damage can only be done by someone mistakenly trying to fix that which was not broken, thereby breaking it in the process. How many people must the macroeconomic Don Quixotes hurt before they are held accountable?