Nothing is sacred: Economic Ideas for the New Millennium
By Robert J. Barro

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The book is written by a noted Harvard professor, economic consultant, and author. The introduction describes why Barro decided to become an economist and attacks J. M. Keynes' advocacy of government spending. He states that the Keynesian model is theoretically and empirically deficient. He admits that when he was a student he appreciated *The General Theory of Income and Employment*, but later he became more impressed by the efficiency of private markets and less attracted by the supposedly curative power of government. He was converted by libertarianism during his first experience at the University of Chicago in 1972. So from the first pages, Barro's market fundamentalism emerges and continues for the rest of the book. The author applies his well honed free market arguments to a varied range of issues.

The introduction is followed by four chapters. Chapter one starts with the author's thoughts on friends and other noteworthy persons through a range of interesting and sometimes ironic essays on famous economists, many of them Nobel laureates. He lauds Milton Friedman's *Capitalism and Freedom*. He reports that all Gary Backer's ideas, about the application of economic principles to a variety of social interaction, are in Philip Wicksteed's book, *The Common Sense of Political Economy*. He defines Robert Mundell as the father of international economics, and he argues that while Adam Smith had brilliant insight his analytical framework was not very good. The philosophy shared by Chicago School and the *Wealth of Nations* permeates Barro's

entire book.

Another outstanding personality is Bono, the rock-pop musician and amateur economist, who fascinates Barro. But Bono, despite his persuasive talents, did not convince the author to put debt relief on the top ten list of growth-promoting policies for poor countries. For Barro more important than "money for nothing" are well functioning legal institutions, promarket policies, sound investments in education and heath and macroeconomic stability. Also Bono's plea for cheap drugs to fight AIDS to spur economic development and save lives in Africa, did not persuade Barro. He is, instead, for providing safe drinking water. It is a cheaper way to save a life, he writes.

The second chapter deals with the economics of social issues, stressing the economics of beauty, abortion, crime, drugs, Napster and meritocracy in higher education. In particular he reiterates Stephen Levitt's strange but convincing arguments that the legalization of abortion in the early 1970's, by reducing the supply of crooks, caused a drop in crime. He argues that the legalization and regulation of drugs would eliminate criminal activity in the U.S. and abroad, while making drugs safer. But his opposition to the Microsoft anti-trust suit, declaring that the suit would not benefit consumers and product improvement, is unconvincing.

The last two chapters are, in my humble opinion, the most remarkable and thoughtful ones.

Barro's third chapter deals with the successes and failures in economic growth, the promotion of democracy and the role of international trade policy. The most important question is whether government policies promote economic development. The author argues that the most favourable government policies for growth, and here an attentive reader can see the influence of his work on economic growth [1997],

include maintenance of secure property rights, promoting the rule of law, fostering of free markets for domestic and international trade, macroeconomic stability and investment in education and health. Unfavourable ones are pursuing environmental protection, elimination of income inequality, high levels of democracy (political rights and civil liberties), and promotion of an array of civic organisations and "social capital".

He emphasizes that democracy, is not always the best way to improve economic growth and he highlights that in Chile, strong economic growth benefited the poor as well as the rich. He also argues that no one has done more than Pinochet and his economic team to demonstrate the superiority of free market capitalism over socialism. Even though Machiavelli's Theory says that "the end justifies the means", humbly, I think that the important end is human rights and liberties not growth. We should never sacrifice human rights for becoming richer. Being poor but free is better than being less poor but oppressed by a dictatorship.

In the same chapter Barro adds that there is an ongoing debate on whether major monetary reforms, such as dollarization, can be successful without preconditions, especially sound fiscal and banking practices. What is interesting is that in Ecuador's dollarization program no precondition existed but dollarization provided the macroeconomic stability that will enhance the impact of such reforms.

In his fourth and concluding chapter, Barro discusses monetary and fiscal policies, and macroeconomics. He argues that cutting tax rates stimulates work and boosts private spending for investment and consumption, contributing to sustained economic growth.

He condemns the 2001 U.S. tax rebate, which gave each family a lump sum because there were no cuts in tax rates that caused people to work harder. But any reduction in taxes is good because it removes revenues from Washington D.C. and thereby keeps

the Congress from spending them.

Barro also explains that spending cuts are more successful than increases in tax revenues in removing deficits because they are more permanent. Therefore he advises cutting welfare and transfers and government wages, which have the strongest tendency to automatically increase. In fact he highlights, referring to the Alesina-Perotti [1997] study, that in cases of successful budget reform 73 percent of the deficit reduction involves less spending, while in the failure cases, only 17 percent of the reduced spending was on transfers and government wages, and a striking 63 percent was in public investment.

In the same chapter, Barro reports that in 2001 the Fed cut interest rates at a pace that was substantially in excess of that predicted from its behavior since mid-1987. He argues that this cut was worrisome because it could be interpreted as a signal that the U.S. central bank was more focused on attempting to prevent an economic slump than committed to maintaining low inflation. But the inflation rate in 2001 was lower than in 2000. So it is easy to see that Alan Greenspan and his board did well in 2001.

In his concluding section the author argues that the stock market is efficient: it is always priced correctly (both when the NASDAQ was at 5,000 and when it was at less than half that level a mere two years later).

The Efficient Market Theory (EMT) states that asset prices in a efficient market fully reflect all available information [Fama 1991]. As a consequence, prices are always at levels consistent with “fundamentals”. Nevertheless, empirical evidence suggests that momentum effects seem to exist [Harney and Tower 2003]. As a result, shares with high returns continue to produce high returns in the short run. The Keynesian notion of “A Bigger Fool”, which efficient market advocates assume away, seem to persist and misalign asset prices. Perhaps the EMT’s proposition stating that all investors are

rational speculators does not always hold. Thus Alan Greenspan's question remains "… how do we know when irrational exuberance has unduly escalated asset values, which then become subject to unexpected and prolonged contractions as they have in Japan over the past decade?"[1996]. Dear Folks nothing is sacred, not even Barro's strong belief in stock market efficiency and market efficiency everywhere.

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