On The Margin

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CREDO's Burkhauser Appointed to CEA

CREDO member Richard Burkhauser has been appointed to U.S. President Donald Trump's Council of Economic Advisors. Burkhauser, the Sarah Gibson Blanding Professor of Policy Analysis Emeritus at Cornell University, officially became a Member of the Council of Economic Advisors on September 28, 2017. He started less than a week later.

He joins Kevin Hasset and Thomas Philippson on the President's new council. The three-person council is supported by a staff of economists and acts as the primary source of objective economic advice to the U.S. president. A few days after beginning the job, Burkhauser explained, "Kevin Hassett and Tomas Phillipson are first class applied economists and I am looking forward to working with them."

> "I am comfortable with people knowing that I am a member of CREDO and an economist who is also a practicing Roman Catholic"

Burkhauser has been a member of CREDO since its founding. Indeed, he was on the program of the Lumen Christi Institute's first conference with economists, church leaders, and other scholars on economics and Catholic social thought. CREDO grew

out of the informal community that arose from these conferences.

"I am comfortable with people knowing that I am a member of CREDO and an economist who also is a practicing Roman Catholic," explained Burkhauser.

Burkhauser is a labor economist with special expertise in the area of poverty and vulnerable populations. He received his Ph.D. in 1976 from the University of Chicago and taught at Vanderbilt University and Syracuse University before joining Cornell. Burkhauser also holds positions at the University of Texas-Austin and the University of Melbourne. He has had a prolific publishing career, including co-authoring books on work, disability, social security, and the aging population. His journal articles span an even wider range of topics including obesity and measuring inequality.
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Update from the President of CREDO

Joseph Kaboski
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CREDO has just finished our third year of formal existence this past summer, and this is our seventh issue of "On the Margin". We missed publishing last year, as we were waiting on a contribution from an influential cardinal that never came through unfortunately. I anticipate a bishop's contributions to return in the next newsletter, however.

In its fourth year, CREDO continues to grow. We have nearly 500 members, and membership has already grew over 20 percent in 2017, and has continued to grow this year. We co-sponsored our second mini-seminar on Catholic social thought for faculty and graduate students in economics and finance this past May in Rome. Sponsoring an event in Rome was a milestone. We will host the mini-seminar again at Notre Dame this June, 2018, and we hope to sponsor it in Jerusalem in 2019! We continue to discuss the future of Lumen Christi-sponsored conference , since Cardinal George's passing, and we are hoping to collaborate with the USCCB. Other events are expanding, as members have taken initiative. Kelly Davidson is organizing a Mass and breakfast at the Agricultural and Applied Economics Association in Washington, D.C., while Carola Binder organized the first CREDO sponsored academic session at an economics conference, the Southern Economic Association's meeting. Moreover, CREDO members made their own progress. As we cover in this issue, CREDO member, Richard Burkhauser, was named to President's Council of Economic Advisors, while CREDO vice president, Jesus Fernandez-Villaverde, introduced a course on ethics and economics at a secular, Ivy League university.

It has not been a year of only success and joys, however. CREDO member, colleague, and dear friend, Tim Fuerst, passed away in February, 2017, after a 10 month battle with cancer. Please pray for his soul, and his widowed wife, Toni, and four children.

I learned something quite interesting regarding Catholic social teachings at the seminar in Rome. Mssr. Martin Schlag told me that when Pope Francis talks about "inequality," the word is actually poorly translated. In fact, as I later verified, the Spanish and Italian versions of his writings and talks do not use "inequality" but "inequity". It's interesting because inequity has a sense of unfairness to it, while inequality may or may not be unfair. I've used this to motivate students to think about the causes and consequences of inequality, and think about the extent to which, or the types, that are just or unjust, fair or unfair. In terms of causes, some difference between the rich and poor may be due to virtues such as hard work and prudence, in which case it is just, while others may be due to vices like greed, dishonesty or even fraud and theft, where it is clearly unjust. In the middle, we have things that are less determined by behavior like natural abilities, family background, educational opportunities, and luck. This middle area may be the most important. I also encourage my students to consider the relationship between inequality and the common good, and the ability

how does inequality - in its diferent forms - impact a person's ability to "attain their own perfection," i.e., the person God has called him or her to be.

of individuals to become the people God has called them to be. To apply the words of the *Gaudium et Spes*, how does inequality – in its different forms – impact a person's ability to "attain their own perfection", i.e., the person God has called him or her to be. Some of these dimension

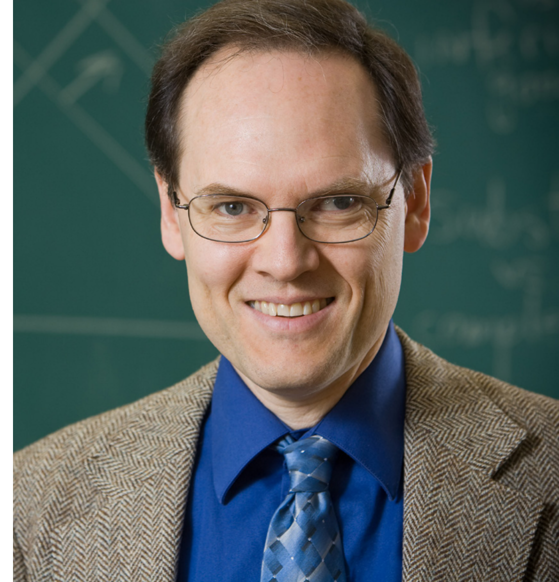
can map nicely into the things we often consider as economists, such as poverty, mobility, income, educational outcomes, institutional stability, political economy, etc., while others stand a bit outside the field (e.g., the impact on solidarity) but are nevertheless important.

I often get asked – usually from people outside economics – whether there is a Catholic economics. Catholicism certainly affects normative judgements, but what about positive research? Personally, I like to think of this through the lens of an empirical regression. I am a mainstream economist, and I have joked that there are no Catholic standard errors. Nevertheless, I think there are left-hand side variables (outcomes) that are more of interest to Catholics. (My own interest in development is motivated by my faith, for example.) What about right-hand side variables? Are there Catholic explanations for economic phenomena? Perhaps there are questions we ask, and hypotheses we consider that stem from out Catholicism. Clearly, theories need to hold up to data, but I think my own thinking of what it is to be human makes me more likely to consider social phenomena, behavioral models of internal conflict, etc. It would be interesting to hear others take on these questions. If you have a contribution, please send it to contact@credo-economists.org.

Photos from the 2017 Summer Seminar on "Economics & Catholic Social Thought: A Primer" in Rome.
Photos courtesy of William Hauk.

The Economics of Pope Francis: An Introduction

Robert Whaples



Robert Whaples
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Pope Francis has invited those concerned about the economy, the environment and the destiny of the world – everyone – to join a dialogue. And there is a clear need for dialogue between Francis and economists, as the pope and many economists don't see eye to eye at a fundamental level on many issues. In the spirit of Francis's call, *The Independent Review* published a symposium, "Pope Francis and Economics" in its Winter 2017 issue (an expanded version will soon be published as *Pope Francis and the Caring Society*.) The symposium's essays are by Andrew Yuengert (Pepperdine) on the writings of Francis and earlier popes on the market economy; Samuel Gregg (Acton Institute) on how Francis's Argentinian background has influenced his economic outlook; A.M.C. Waterman (University of Manitoba) dissecting the arguments in Francis's environmental encyclical, *Laudato si'*; Philip Booth (St. Mary's University (UK)) on the omission of property rights-based solutions in *Laudato si'*; and Lawrence McQuillan and Hayeon Carol Park (the Independent Institute) on how capitalism unleashes private charity. The symposium begins with my own examination of what Francis says about the economy, juxtaposing his first principles with those of economists, attempting to put his ideas into economists' terms.

As Francis sees it, the purpose of the economy, like the purpose of everything else in the world, is to lead all people to God. Francis's concern for the poor is most obvious. Even in his "environmental" encyclical, *Laudato si'* (LS), his focus is as much on the poor as on the environment: "we have to realize that a true ecological approach *always* becomes a social approach; it must integrate questions of justice in debates on the environment, so as to hear *both the cry of the earth and the cry of the poor*" (LS 49). He affirms that the priority must be to eliminate extreme poverty, but argues that money isn't enough – dignity and especially the dignity of work are crucial. Helping "the poor financially must always be a provisional solution in the face of pressing needs. The broader objective should always be to allow them a dignified life through work" (LS 128).

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For all his tender attention to the poor, it's easy to overlook his concern for the rich. Here his message is that wealth and abundant consumer goods and services are dangerous – because they can separate us from God, from our brothers, and from our true nature. He warns that our concern for material wellbeing leads us to make bad choices and in one homily (God's Time) he refers to a possible dialogue between spouses. "No … more than one child, no? Because then we can't go on vacation, we can't go here, we can't buy a house … We are in love with temporal things, while what Jesus offers is infinite. We like the temporary because we are afraid of God's time, the end of time." The riches of the market seduce us into settling for too little – for vacations, rather than children; for an earthly paradise walled away from humanity, instead of God. The market "tends to promote extreme consumerism in an effort to sell its products, people can easily get caught up in a whirlwind of needless buying and spending" of "compulsive consumerism" (LS 203).

A "constant flood of new consumer goods can baffle the heart and prevent us from cherishing each thing and each moment" (LS 222). Despite castigating "the unfettered pursuit of money," however, Francis affirms that "business is a noble vocation, directed to producing wealth and improving our world. It can be a fruitful source of prosperity … especially if it sees the creation of jobs as an essential part of its service to the common good" (LS 129).

After explaining Francis's positions, I point out that they are fundamentally at odds with some of the foundations of modern economics – for example as found in most intermediate microeconomics textbooks where the assumption is made that "consumers always prefer more of any good to less … more is always better, even if just a little better." In rejecting this point, Francis contends that utility declines once a person has too much, so "divesting" ourselves of this excess will make us better off. This argument also implies that the marginal benefit curve for a good is lower than economists generally assume, so the efficient amount is lower and arguments about how the invisible hand efficiently allocates resources are often off base. Similarly, many economic models assert that work is a "bad" to be avoided – ignoring the dignity of work stressed by Francis. My essay closes by pointing out blind spots in Francis's view of the economy – especially its track record of reducing absolute poverty and diffusing power – and examining both the strengths and weaknesses of capitalism for achieving the goals of the Church and Francis in our fallen world.

Burkhauser continued from front page

One of Burkhauser's specific research areas is the minimum wages; he has published 16 papers over the past twenty years on the topic, and testified in front of Congress as well.

In a piece to the first issue of *On the Margin*, he reviewed the empirical research on the impacts of minimum wage laws and argued that they are ineffective in attacking poverty among the working poor. He promoted the Earned Income Tax Credit (EITC) as a more targeted and effective alternative to helping compensate the working poor:

"In the language of the Catholic Church, the goal of the 'just remuneration' is to provide income 'sufficient for the needs of a family', in the words of Pope John Paul II. Pope John Paul saw that grants targeted toward 'the specific needs of families', like 'the number of dependents' were an alternative for achieving the goals of just remuneration (*Laborem Exercens*, 19). In precisely this way, the EITC is a much more effective way to convert wage rates determined by supply and demand in competitive markets into living wages that lift the otherwise working poor out of poverty, all without reducing employment."

On the Sovereign Debt Crisis in Europe

Pedro Teles

Pedro Teles
Professor, Católica Lisbon School of Business and Economics

Following the financial crisis, already ten years old, Europe was hit by a severe sovereign debt crisis that challenged the European institutions. Should the ECB have responded to the crisis with the powerful tools of monetary issuance? Or should instead the solution of the crisis be left to the fragile European fiscal institutions? At the heart of these questions is the issue of whether the sovereign debt crisis in Europe was due to weak fundamentals or to coordinated expectations. Whether the answer is fundamentals or expectations could mean that either the ECB was right in intervening massively, targeting low sovereign debt spreads, or the German Constitutional Court was right in questioning that same intervention. The answer may very well be that both fundamentals and expectations are to blame.

The importance of fundamentals

Portugal, my country, was one of the countries more severely hit by the sovereign debt crisis. And fundamentals did certainly play a role. I could see that role being played as I taught open economy macro at Universidade Catolica, in Lisbon, year after year.

I have been teaching a course in international macro since the early 1990s. I always start by looking at the figures for the balance of payments in Portugal. The first time I taught the course, back in 1993, and looked at those numbers, the Portuguese net foreign debt was -3% of GDP, i.e. net foreign assets were positive (public debt was 55% of GDP).

Foreign deficits started going up in the mid nineties. Foreign debt in 1999, at the start of the Euro, was already 34% of GDP, still quite low, but the current account deficit was close to 10%.

Since then, every year, on the first day of class, I would look at the numbers, and the debt was higher than the previous year deficit, and the deficit was equally high. After a while, I did not need to look at the numbers any longer. The debt would be up by more than 5% of GDP, closer to 10%, year after year.

Then, came the years without growth, and the deficits were even higher. Finally came the financial crisis and with it a sequence of public deficits above 10% of GDP, the debt hidden in public companies or in public-private partnerships adding up to the total public debt (130% in 2013).

By the end of 2009, the foreign debt was close to 110% of GDP and the current account deficit was still 9% of GDP. Then spreads went up.

The potential role for expectations

Portugal was not the only country in Europe with weak fundamentals at the onset of the sovereign debt crisis. But was there also a role for expectations in triggering the crisis? How much of the crisis could have been caused by self-fulfilling expectations on default?

I don't think we can answer these questions without using. There are two main ways in which expectations may matter. One is liquidity (I'll call it Cole and Kehoe). Governments issue short-term debt, and they have long-term assets, their entitlement to tax revenues. This maturity mismatch could induce a sovereign debt crisis driven by a run on sovereign debt, just as maturity mismatches in banking lead to bank runs.

A second way expectations may matter is through interest rates that affect the service of debt (call it Calvo). If expectations are good, interest rates are low, and consequently servicing costs are also low; default does not occur. However, if investors expect high default risk, they ask for high interest rates to compensate for this, which drives up servicing costs and can induce default.

Both theoretic explanations of a role for expectations, Cole and Kehoe or Calvo, are compelling but the modeling of both is remarkably fragile. Whether the models can produce expectation-driven outcomes depends critically on the specifics of

the model, on the timing of moves of borrowers and lenders and on the decisions they get to make. Which theories are correct in terms of these specifics? There is unfortunately no real way to tell directly from data. Still, the large swings in spreads, and the effect of a mere statement of intensions by Mario Draghi are good evidence of multiplicity.

> Considering what caused the crises is important in guiding future policies to avoid them in the future and policy responses when they arise.

In some of my own work, "Self-Fulfilling Debt Crises with Long Stagnations" with João Ayres, Gaston Navarro, and CREDO member, Juan Pablo Nicolini, we argue that the role of expectations is more robust if the world we live in is one with good and bad times, i.e., long periods of high growth followed by long periods of stagnation. During good times, default is unlikely, and expectations can't drive the outcomes, but when countries enter long stagnations default is much more likely, and expectations can be critical. Portugal has faced a fifteen-year long stagnation with high levels of debt both public and foreign. Fundamentals did certainly play a role there. But our work can also help us argue that expectations may have played a key role in triggering the crisis.

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1. Cole and Kehoe (2000) examine this type of crisis.

2. See Calvo (1988).

3. See, for example, Aguiar and Gopinath (2006) or Arellano (2008)

CONTRIBUTORS

Robert Whaples is Professor of Economics at Wake Forest University. He graduated from the University of Maryland in 1983 with B.A.'s in Economics and History, and earned a Ph.D. in Economics from the University of Pennsylvania in 1990. His dissertation, "The Shortening of the American Work Week: An Economic and Historical Analysis," won the Allen Nevins Prize from the Economic History Association. Professor Whaples is the editor of five books; his research focuses on the history of labor markets, with emphasis on the length of the work week, aging, and discrimination; and he has explore consensus among economic historians and economists, especially the widely-cited "Do Economists Agree on Anything?" and "Are Disagreements among Male and Female Economists Marginal at Best?"

Pedro Teles is Professor at Catolica-Lisbon School of Business and Economics at the Catholic University of Portigal. He is also a Research Fellow at the Centre for Economic Policy Research and an Advisor at the Bank of Portugal. He holds an MA and a PhD in Economics from the University of Chicago and a Licenciatura in Economics from the Catholic University of Portugal. Professor Teles specializes in macroeconomics and monatery economics on which he has published numerous articles.