

# Saving Economics from the Economists

by Ronald Coase

Economics as currently presented in textbooks and taught in the classroom does not have much to do with business management, and still less with entrepreneurship. The degree to which economics is isolated from the ordinary business of life is extraordinary and unfortunate.

That was not the case in the past. When modern economics was born, Adam Smith envisioned it as a study of the “nature and causes of the wealth of nations.” His seminal work, *The Wealth of Nations*, was widely read by businessmen, even though Smith disparaged them quite bluntly for their greed, shortsightedness, and other defects. The book also stirred up and guided debates among politicians on trade and other economic policies. The academic community in those days was small, and economists had to appeal to a broad audience. Even at the turn of the 20th century, Alfred Marshall managed to keep economics as “both a study of wealth and a branch of the study of man.” Economics remained relevant to industrialists.

In the 20th century, economics consolidated as a profession; economists could afford to write exclusively for one another. At the same time, the field experienced a paradigm shift, gradually identifying itself as a theoretical approach of economization and giving up the real-world economy as its subject matter. Today, production is marginalized in economics, and the paradigmatic question is a rather static one of resource allocation. The tools used by economists to analyze business firms are too abstract and speculative to offer any guidance to entrepreneurs and managers in their

constant struggle to bring novel products to consumers at low cost.

This separation of economics from the working economy has severely damaged both the business community and the academic discipline. Since economics offers little in the way of practical insight, managers and entrepreneurs depend on their own business acumen, personal judgment, and rules of thumb in making decisions. In times of crisis, when business leaders lose their self-confidence, they often look to political power to fill the void. Government is increasingly seen as the ultimate solution to tough economic problems, from innovation to employment.

Economics thus becomes a convenient instrument the state uses to manage the economy, rather than a tool the public turns to for enlightenment about how the economy operates. But because it is no longer firmly grounded in systematic empirical investigation of the working of the economy, it is hardly up to the task. During most of human history, households and tribes largely lived on their own subsistence economy; their connections to one another and the outside world were tenuous and intermittent. This changed completely with the rise of the commercial society. Today, a modern market economy with its ever-finer division of labor depends on a constantly expanding network of trade. It requires an intricate web of social institutions to coordinate the working of markets and firms across various boundaries. At a time when the modern economy is becoming increasingly institutions-intensive, the reduction of economics to price theory is troubling enough. It is suicidal for the field to slide into a hard science of choice, ignoring

the influences of society, history, culture, and politics on the working of the economy.

It is time to reengage the severely impoverished field of economics with the economy. Market economies springing up in China, India, Africa, and elsewhere herald a new era of entrepreneurship, and with it unprecedented opportunities for economists to study how the market economy gains its resilience in societies with cultural, institutional, and organizational diversities. But knowledge will come only if economics can be reoriented to the study of man as he is and the economic system as it actually exists.

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