

Chapter 14

Q & A on “The Political Business Cycle” by William D. Nordhaus (1975)

Historically, and systematically, catching most difficult subject

William D. Nordhaus (1975). The Political Business Cycle. *Review of Economic Studies* Vol.42, No.2 (April): 169-190.

Pertinently connected W. Nordhaus with J. Tobin (1982). Is Growth Obsolete? pp.360-451. In: J. Tobin (edited.), *Essays in Economic Theory and Practice*. Cambridge, MA: MIT Press. x+ 684p.

An answer from the viewpoint of purely endogenous:

We live in a balanced state, dynamic and static, and beyond both space and time. Second by second, unbalanced is balanced as it is. Trade-off already expresses past results. Negative and positive principle prevails in this world. The other side is also true from its side and vice versa; we do not blame each other neither fight each other by nature. This truth is evidenced by hyperbolas in two-dimensional plane, where two extremes are united by a universal philosophy, beyond religions and races, and money.

Money is indispensable yet, money is neutral to economic activities. It implies that the real assets have its rule and role, where the best is politics-neutral and spirituality-neutral, as the author proved theoretically and practically the essence of ‘purely endogenous.’ Purely endogenous measures all the possible parameters, variables, and equations, under no assumption and/or under perfect competition, where marginal productivity of capital equals the rate of return and marginal productivity of labor equals the wage rate; $MPK = r = r^* = r_0$ and $MPL = w$, as measured by the absolute and relative price level of $P = p = 1.0000000$ and accordingly measured by marginal rate of substitution = $\sigma = 1.0000000$. All the policies are integrated by the real assets policy and fiscal policy of $\Delta D = (S - I) - (S - I)_{PRI}$, where an assumption of government assumption necessary for cash flows-in and cash flows-out is thrown away. Causes = results simultaneously holds, second by second and the initial data turn to be endogenous data.

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Q & A from Q_{N1} to Q_{N9}:

Start Q_{N1} and A_{N1}:

Q_{N1} (p.169, *ibid*); The macroeconomic framework:

What problem does the MIT-FRB (i.e., the FRB-MIT-Penn-Economic Model, 1972 (8)) fall into?

A_{N1}: As shown in Figure 1 (p.171) of private nonfarm deflator and unemployment rate, even this model remain illustration and cannot express actual data on the same two-dimensions. It is natural since the model holds under the market principles so vertically distinguished. Deviation of related equations can solve problems but, separately from the illustration, which holds commonly to the literature and ‘purely endogenous’.

Q_{N2} (p.171, *ibid*); Individual preferences and aggregate behavior:

Are ‘individual preferences’ approach and ‘maximum utility’ righteous even in the macro level?

A_{N2}: Individual preferences are estimated by individual utility in the micro level. It is natural since no way but individual preferences is possible under the market principles. Aggregate behavior is well asked by Nordhaus.

Q_{N3} (p.175, *ibid*); Optimal inflation and employment:

As shown by Figure 2 *Contours* of aggregate voting function (176p.), rate of inflation and unemployment rate are mathematically analyzed. Is there any possibility to express contours of aggregate voting function?

A_{N3}: No, no possibility is there. Figure 2 indispensably shows a limit, thoroughly to the extreme.

Q_{N4} (p.177, *ibid*); Long-run choice in democratic systems, (1) geometric analysis and (2) reservation:

As shown by Figures 3 and 5 for Long-run policies (177p. and 180), these figures exactly express long-run theoretical choice in democratic system and how to improve democratic systems, such that Nordhaus is one of geniuses. Do long-run policies solve problems in democratic systems?

A_{N4}: Yes, theoretically but not always in reality. Why not always in reality? This is because people by country must know this fact in reality.

Q_{N5} (p.181, *ibid*); Short-run behavior: the political business cycle:

As shown by Figures 4 and 6 for Short-run policies (179p. and 181), these figures exactly express short-run theoretical choice in democratic system and how to improve

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democratic systems step by step. Do short-run policies solve problems in democratic systems, now step by step?

A_{NS}: Yes, theoretically but not always in reality. Why not always in reality? This is because people by country must know this fact in reality and freely have spirited decision by individual, followed by openness and disclosure periodically by country.

Q_{N8} (p.185, *ibid*)¹: Historical evidence:

As shown by Figures 7 and 8 towards the political business cycle (183p. and 185p.), these figures exactly express the democratic system target of people by country (note of the author; we cannot find Subjects 6 and 7 here but Figures 7 and 8 were not abbreviated). Figure 8 of 'The political business cycle' historically presents an invaluable evidence that inflation rate and unemployment rate move match by year but adversely. Table 1 of 'Unemployment trends before and after elections' further presents an statistics evidence more concretely, by applying 'probability of a rise or fall is one-half and independent,' each to eight advance countries. Are these evidences justified historically?

A_{NS}: Yes, these evidences are justified historically. Note that actual world change minute by minute and is never repeated so that we say no guarantee in the future.

Q_{N9} (p.187, *ibid*); Conclusions and remedies: The 9th subject asks for remedies for indispensable biases in democratic systems, after citing J. K. Galbraith's 'theory of social unbalance.' (Nordhaus here indicates 'theory of social unbalance' is very plausible on theoretical grounds as discussed by others. Nordhaus (pp.187-188, *ibid*) here states five remedies by item:

1. It is clearly unrealistic to ask each citizen to carry a full-scale econometric model of the wage-price-unemployment nexus in his head. We question that practical possibility of the "classical" solution in such complicated matters.
2. There remains only a "second-best" solution. And, more important is the length of the election period.
3. The costs and benefits of independent policy, monetary, fiscal, and Central Banks (e.g., FRS and the Bank of England), determination are difficult to weight.
4. A different kind of solution is an "income policy." This removes the political business cycle by making the underlying trade-off disappear. There is little doubt that if we could cure the disease its symptoms would disappear.
5. A final approach is to broaden the base of participation in policy-making, as in the tradition of indicative planning. As evidence, we note that among advanced countries

¹ It seems that **Q_{N6}** & **Q_{N7}** and their corresponding **A_{N6}** & **A_{N7}** are missing. However, the author of this book found that, on page 181 is "5. Short-run behaviour" and on page 185, "8. Historical evidence" appears following section 5.. The author of this book believes that two sections, 6. and 7., of Nordhaus (1975) are missing by some reason.

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showing the highest cyclical variety are the unplanned economies of the US, Canada, Japan, and West-Germany; while those showing the least cyclical variation are the planned economies of France and Sweden.

Do these remedies all justify how to upgrade the level of democracy by country?

A_{N9}: Yes, certainly. Moreover, the above five contents by item clarify everlasting truth.

Why do these statements highly so much? The five statements include all the possible limit of theory and practice under the market principles as follows:

1. Related to the size of government: ‘Nothing to do’ the base as shown by the laissez-faire.
2. Yes, the length of the electoral period will lead to more responsible politics.
3. The costs and benefits of independent policy are indispensable under market principles and most wasteful to all the parties.
4. Trade-off between Phillips curve and inflation and, between any others is indispensable under the market principles.
5. Yes, participation is a base for communicate with each; from family, relatives, small society, to large society, local government, broader area, country, and universally in this world. Learning by doing is the base for society and human beings in this world. And, each country can enjoy national taste, and preferences, culture, and history, which are independent of technological progress by country, even under less populated and resources, since the Nature is organic by nature. We are relaxed and bright in the future.

Q&A on Gregory N. Mankiw

The Macroeconomist as Scientist and Engineer

Citations per paper are far and away the best.

Mankiw, Gregory, N. (2006). The Macroeconomist as Scientist and Engineer. *Journal of Economic Perspectives* 20 (May, 4): 29-46.

Easily connectable with “Mankiw, Gregory, N. (2013). Defending the One Percent. *Journal of Economic Perspectives*, 27(3,Summer): 21-34.”

Q & A from Q_{M1} to Q_{M10}:

Let's start from Q_{M1} and A_{M1}:

Q_{M1} (p.29, 2006); Introduction:

What is the difference between the science and engineering of macroeconomics? This cut end shows one of Mankiw's broad insights.

A_{M1}: The author (Kamiryō) is confident in a fact that nature, God, natural science, and social science are close to each other. Macroeconomics is one aspect of social

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science, which is involved in human life and human decision-making. We human always approach this direction, back and forth.

Q_{M2} (p.30, *ibid.*); The Keynesian Revolution:

Why was the IS-LM model proposed by John Hicks (1937) and Franco Modigliani (1944) so early?

A_{M2}: The author understands that macroeconomics in the market principles condense into the IS-LM model. Conclusively macroeconomics cannot completely finalize the IS-LM model. This is because the price level is shown by amount and vertically (by goods and services) while macroeconomics must be whole as a system.

Q_{M3} (p.32, *ibid.*); The New Classical:

What does mean by Milton Friedman (1957) and Friedman and Schwartz (1963)? What was the trade-off between inflation and unemployment? After Robert Lucas's (1976), why do the real business cycle theories appear so many?

A_{M3}: If monetary policy is independent of the real assets policy, macroeconomics cannot be integrated since vertical combination is not wholly acceptable. Trade-off between inflation and unemployment occurs since inflation is independent of unemployment, both being external. Trade-off will disappear if inflation and unemployment are united within a whole system.

Q_{M4} (p.34, *ibid.*); The New Keynesians:

Why did Lawrence Klein (1946) appeal 'macro econometrics'? Why does 'one market' fail in clearing influences supply and demand in related markets? What do mean by general equilibrium, the assumption of market clearing, and a sticky-price equilibrium?

A_{M4}: Macro econometrics is developed to solve problems in macroeconomics. Macro econometrics is free from rules in economics and holds without equations and unavoidable assumptions to justify equations in macroeconomics. Macro econometrics can approach phenomena of equilibrium, independently of rules in economics.

Q_{M5} (p.37, *ibid.*); Digression and Vitriol:

Empirically bad symptoms and results of depression, inflation, unemployment and inequality are repeated. Policies hold in the long-run.

A_{M5}: Policies and results are not in the same wavelength. It implies that theory is independent of practice. Distance between theories and practices must be buried towards better matching.

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Q_{M6} (p.38, *ibid.*); A New Synthesis, or a Truce?

A_{M6}: By the accumulations of theories and practices by country, economists and researchers intend to integrate or synthesize both. Each school has its own cut end. Nevertheless, it is difficult to attain synthesize theories and practices in the market principles, due to vertical combinations in methodologies.

Q_{M7} (p.40, *ibid.*); The View from Central Banking:

Central banking policy is independent of monetary and market policies. Each policy is free from other ranges of policies, even in macro economies. A range policy is not always cooperative with others.

A_{M7}: A range policy is short-sighted and fights with other range policies. It accelerates a notion that individuals differ from a country.

Q_{M8} (p.41, *ibid.*); The View from Fiscal Policy:

What range does fiscal policy belong to? Why does fiscal policy not belong to real assets policy? What assumption does fiscal policy need? Is the Jobs and Tax Relief Reconciliation Act of 2003 effective or efficient?

A_{M8}: Fiscal policy needs an assumption that deficit estimated by cash flow -in and -out is equal to real asset deficit. This assumption is sham and does not justify cash flows deficit. The Jobs and Tax Relief Reconciliation Act of 2003 remains naturally within a narrow range solution.

Q_{M9} (p.43, *ibid.*); Inside the Classroom:

Now for summary of classroom that is composed of typical schools, Keynesians, and neoclassical, old and new. A generation ago, the three leading texts for this course were those by Robert Gordon; Robert Hall and John Taylor; and Rudiger Dornbusch and Stanley Fischer. Today, the top three sellers are those written by Olivier Blanchard; Andrew Abel and Ben Bernanke; and Gregory, N. Mankiw (myself). Why Keynesians originally prefer no use of the Cobb-Douglas production function to the use of that production function?

A_{M9}: Keynesians and econometrics are free of the rules of economics: Nevertheless, Keynesians, econometrics, policy-makers, and leaders by country, have not solved problems in macroeconomics and have repeated depression, deflation, inflation, and unemployment. Classroom is not open to other school such as purely endogenous and simultaneous system, or the *EES* (Earth Endogenous System) classmates. The *EES* is green cycling society-oriented and is most fitted for people' organic policies.

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Q_{M10} (p.44, *ibid.*); Not a Dentist in Sight:

“New Keynesian economists have supplied better models to explain why wages and prices fail to clear markets and, more generally, what types of market imperfections are needed to make sense of short-run economic fluctuations. The tension between these two visions, while not always civil, may have been productive, for competition is as important to intellectual advance as it is to make outcomes.”

A_{M10}: The author proves a fact that wages and prices are measured and solved under perfect competition, by using Marginal Productivity of Capital=the rate of return, and Marginal Productivity of Labor=the wage rate, where no sticky-price exists and clear markets holds, erasing its assumption.

Q&A on Avner Offer 1997:

Between the Gift and the Market: the Economy of Regard

Social and mathematical explanations of unique Avner Offer' (1997) gift price and market price framework, simultaneously with philosophy behind.

Avner Offer (1997). Between the gift and the market: the economy of regard. *Economic History Review* L (3): 450-476.

Historical researches to investigate the literature broadly and deeply; the number of citation is 153.

Q & A from Q_{AOI} to Q_{AOIX}:

Start Q_{AOI} and A_{AOI}:

Q_{AOI} (p.451, 1997); Historically; reciprocity, unconditional hospitality, sympathy, maximum price, equilibrium, money, and a pseudo-regard:

The writer (Avner Offer) shows his range of philosophical connections with market prices strictly in the market principles.

A_{AOI}: The author (Kamiryo) understands the writer's intention clearly and that the writer's Figures, particularly, Figures 1 and 4 mathematically expresses the gift and market prices, traditionally following two-dimensional common coordinate axes; price of the y axis and quantity of the x axis. The author has not found such a unique paper as the writer's before.

Q_{AOII} (p.457, *ibid.*); Empirically, reciprocity, equality matching, and permanent income: The writer pursues his expressions not only theoretically but also empirically.

A_{AOII}: The author first is able to confirm a rule that actual data realizes equality matching as an exchange between equals and second understand Figure 2 that compares three data in the US, Australia, and the UK; GNP, DCI (gross consumer

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income), and TISA (total incomes system of accounts), citing Eisner’s tab. A. 15, 73p, 1989. The author’s *EES* (“*Earth Endogenous System*,” lxviii+568, 2013) indispensably measures national disposable net income, $Y = C + S = W + \Pi$.

Q_{AO III} (p.462, *ibid.*); Discretion, an element of gifting, and reciprocal:

The market principles produces vertical markets such as labor and financial. Labor markets, as a result, allow discretion, where gifting must be taken into consideration. Yet, the writer never loses a righteous direction towards reciprocal.

A_{AO III}: Nevertheless, it is still difficult for economists to step into causes-effects relationship in respective markets.

Q_{AO IV} (p.463, *ibid.*); Farming, capitalism, moral claims, and agrarians:

The writer approaches essentials lying background, farming versus capitalism and step into moral claims.

A_{AO IV}: These phenomena are superficial results. Philosophy is used for connecting phenomenal results with concrete system by industry.

Q_{AO V} (p.464, *ibid.*); Gifting, from outside, regard, the impersonal market, personal obligation, advertising and sales promotion, and consumer preferences:

Now the writer focuses price systems under the market principles and looks for pertinent concepts and definition. The writer’s question: What is the impersonal market good for?

A_{AO V}: The writer perceives and presents the importance of organic and organism as a goal of empirical costs by goods. The writer digs the motives of decision-making to buy and sell and clarifies a fact that the impersonal markets inevitably shrink and retreat.

Q_{AO VI} (p.468, *ibid.*); Common identity and face-to-face relations :

The writer historically and broadly among countries indicates that ‘a common identity can substitute for face-to-face relations.’

A_{AO VI}: The author confirms that the above processes are natural under the market principles and no others.

The author proposes that there exists one unique methodology that directly connects the common identity with its philosophy and pricing as a whole system by economy.

Q_{AO VII} (p.469, *ibid.*); Loyalty, reciprocity, and rule of the game:

The writer takes a fact that ‘loyalty and reciprocity can be used effectively for anti-social ends.’

A_{AO VII}: The author pays attention to the writer’s small groups and societies, free and planned. Here we stand at the entry to a gift economy.

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Q_{AO VIII} (p.469, *ibid.*); Reciprocal exchange and boundaries of the gift and the market:

Figure 4 is a highlight of the writer's expressions towards gifts and markets. Figure 4 shows marginal costs and the difference between the gift price and the market price. On the x axis of quantity, the gift market's range is smaller (to the left) than the market price. On the y axis, the price level of the gift price decreases faster than that of the market price and result the gift price is higher than the market price.

A_{AO VIII}: The supply and the demand lines and the quantity and the price simultaneously hold in an economy. Accordingly, average and marginal costs and profits are expressed in a graph. No one can deny this figure commonly drawn in the texts. The author indicates that this figure has its own original limit, due to vertical price systems.

Q_{AO IX} (p.471, *ibid.*); Regard, incentives, personal relations, gift exchange, the cost of information, the cost of time, public policy, authenticate, personalized gift, and discretionary delay:

The writer arranges for and authenticates the whole background of Figure 4.

A_{AO IX}: The author cannot deny the writer's authentication processes. The author declares that Figure 4 is alternatively expressed by purely endogenous figure or hyperbola and recollects the essentials of the *EES*. Simultaneous causes=results, actual data=endogenous data in a certain range, and no assumption under perfect competition or $MPK=r$ and $MPL=w$ and $p = P = \sigma = 1.0000000$.

These implies that average=marginal cost, discretionary=natural or no arbitrary, and micro=macro movements in an economy.

Challenges: Magazine of Economic Affairs 31 (July/August, 1988): 32-52
In the Beginning: by Paul A. Samuelson

The following invaluable literature reminds us importance of historical facts:

1. Paul A. Samuelson (pp.32-34, *ibid.*) : In the Beginning;
 2. James Tobin (pp.35-41): A Revolution Remembered;
 3. Martin Feldstein (pp.42-46): Counterrevolution Progress;
 4. Benjamin M. Friedman (pp.47-52): Evolution Prevails.
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1. Paul A. Samuelson (pp.32-34, *ibid.*) : In the Beginning
A) We realize that a fact that academic revolution has been bravely repeated when traditional notions prevailed and there appeared no new ideas. The author (Kamiryō) accepts this fact as if history is organic or organism is the essence of history. Human makes its history by aspect or by cut end.

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2. James Tobin (pp.35-41): A Revolution Remembered

B) In his subtitle, ‘Conservatism reigned,’ Tobin states that Schumpeter did concede the existence of ‘widespread suffering and needless waste and saw some role for temporary public ‘expenditure to blot out the worst things without injury to the economic organism.’ The author is impressed by Tobin’s use of economic organism. In terms of the *EES*, Schumpeter’s technological progress is expressed by the qualitative coefficient, with minimum net investment and under a constant capital-output ratio.

C) In his subtitle, ‘Arrival of Hansen,’ Tobin states that Hansen’s change of heart and mind about Keynes’ new book altered the climate at Harvard in academic year 1937-38,’ with John Williams.

D) In his subtitle, ‘Macroeconomics comes of age,’ Tobin states that macroeconomics as a distinct subject of theory and empirical research did not really exist before 1936.’ The author could confirm that macroeconomics is as young as the author’s age.

3. Martin Feldstein (pp.42-46): Counterrevolution Progress

E) In his subtitle, ‘Deficit spending,’ Feldstein states that lifetime lag between spending and enjoying is significant. Feldstein stresses that ‘just paying the interest on the national debt requires 40 percent of all personal tax revenues: without that interest obligation, our tax rates would be 40 percent lower today and the incentives of after-tax compensation that much more favorable.’ Further, Feldstein indicates that ‘Unfortunately, several decades of Keynesian instruction on the virtues of budget deficits have left the public and our political leaders confused about the costs of running persistent deficits.’

4. Benjamin M. Friedman (pp.47-52): Evolution Prevails

F) In his subtitle, ‘Image vs. reality,’ Friedman states that because public perceptions of any institution typically lag behind the reality, the prevalent external view today is that this research focus, which gained momentum through the 1970s, remains predominant at Harvard now. The facts are otherwise.

The author of this book adds to the above results a fact that actual results appear beyond space and time, not separately but simultaneously, as proved in the *EES*.

G) In his subtitle, ‘Anti-Keynesian disappointments,’ Friedman states that the ability of many of the modern economy’s markets to move quickly to positions of supply-determined equilibrium are themselves often highly limited.’

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The author of this book adds to Statement G) a fact that endogenous equilibrium is one, where supply-determined equilibrium completely overlaps demand-determined equilibrium.

The author's viewpoint for Challenges: Magazine of Economic Affairs 31 (July/August):32-52

First, for Alvin Hansen (1887-1975):

- (1) Requirement of net investment at enterprises or the private sector is partially right. Government and company net investments, however, should be respectively limited to minimum. Without erasing real assets causes, enterprises cannot promote net investment by themselves. Government cannot press unfair fiscal policy on enterprises since enterprises have their own profits maximization principle.
- (2) A view of low investment due to delayed technological progress is wrong. An endogenous rate of technology is managed by the qualitative investment coefficient, which is independent of population and public policy.

Second, from the AXIOM viewpoint in the *EES*:

Nature-oriented or nature-neutral is purely endogenous, with no assumption in thousand endogenous equations. Six nature-neutrals are explained as the essence of the *EES*: money-neutral; consumption-neutral to growth and returns; the relative share of capital-neutral to macro inequality; deficit-neutral, politics-neutral; and spirituality-neutral.

The unique AXIOM is a constant capital-labor ratio in an organic system as a whole by country. A constant-labor ratio robustly guarantees organic system as endogenous organism, by country, year, sector, and year and over years. As a result, green cycling society realizes simultaneously under the market principles cooperatively in the global world.

- (3) Six organic aspects in endogenous equilibrium by country and sector (see 'Notations' in the *EES*) are measure-oriented. Six organic aspects are simultaneously measured with 'Seven endogenous parameters' hidden in an endogenous Cobb-Douglas production function solely used for the *EES*.

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1. Avner, Offer (1997). Between the gift and the market: the economy of regard. *Economic History Review* L (3): pp.450-476.
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3. Friedman, Benjamin M. (1988). Evolution Prevails. *Challenges: Magazine of Economic Affairs* 31 (July/August): pp.47-52.
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