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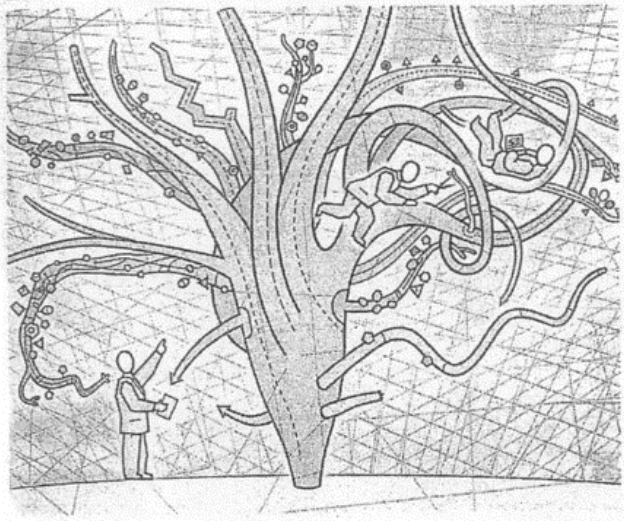
Economists understand little about the causes of growth. The first of a series on the profession's shortcomings



OVER the past decade economists have been intensely scrutinised for their intellectual failings in the run-up to the 2007-08 financial crisis. Yet had the recession that followed been more severe—wiping a quarter off the GDP of every advanced economy, say—those countries would still have ended up four times as rich per person, in purchasing-power terms, as developing countries are now, and more than ten times as rich as sub-Saharan ones. Robert Lucas, a Nobel prizewinning economist, once wrote that after you have started to think about the gap between poor and rich countries it is hard to think about anything else. Economists understand even less about economic growth than about business cycles. But the profession has done too little to address this failure or to understand its implications.

Economists have precious few hard facts about growth. They know that sustained growth in GDP per person only started in the 18th century. They know that countries can become rich only by growing steadily over long periods. They know that in some fundamental way growth is about using new technologies to become more productive and to uncover new ideas. Beyond that, almost everything is contested.

There are three broad lines of thinking. The first dates from 1956, when Robert Solow and Trevor Swan independently developed models based on the idea that growth is a consequence of capital accumulation. Their models explained how poor countries could catch up with rich ones, but not why rich countries had grown in the first place. Mr Lucas and other economists, including Paul Romer, sought to fix that by adding descriptions of how knowledge is developed and disseminated. As simple stories about how growth might work, such models function well.

Yet they share two flaws. First, they are often too vague to be of much practical use. As Paul Krugman, another Nobel prizewinner, once wrote, they "involved making assumptions about how unmeasurable things affected other unmeasurable things". And they leave out most of what matters. Some economies do indeed leap from poverty to riches by mastering state-of-the-art technologies. But most do not, suggesting that formidable obstacles prevent many poor countries from growing in the way that models of knowledge accumulation and diffusion suggest they could. Growth theory is silent about what those obstacles might be.

A second strand of empirical research followed. Economists pored over cross-country economic data in search of factors that might explain differences in growth. Some focused on individual countries and used techniques known as "growth accounting" to quantify the relative contributions of capital and labour. Often, however, much of the growth could be attributed only to an unexplained residual, sometimes interpreted as representing progress in technology but better understood, in the words of Moses Abramovitz, another economist, as "a measure of our ignorance".

Other empirical researchers compared countries, seeking links between economic and political characteristics and rates of growth. Yet, as Mr Solow has remarked, this project has not inspired much confidence. The trouble is the sheer number of variables that might matter, alone or in combination. A study might find that some factor—the rate at which businesses are created, say—is materially linked to growth. But in reality something else correlated with business creation, not included in the study, might be the crucial influence. The world is too complicated to be dissected and examined this way.

A third group of researchers look to history for lessons, examining the Industrial Revolution, the diverging fortunes of former European colonies and so on. They are held back by a paucity of data and have not managed to converge on a shared understanding of the nature of growth. Yet their approach is in some ways the most promising, because it means grappling with the ways in which culture and politics constrain economics. Debates about the origins of the Industrial Revolution revolve around the relative importance of secure property rights, the extent to which cultures tolerate personal ambition and so on. Those about why one European colony ended up rich and another poor focus on why different places ended up with different sorts of institutions, and to what effect.

At bottom, such issues must be the most important ones. An economist might explain China's rapid growth in the 1980s by saying that it began to deploy more capital per worker and to adopt foreign technologies. Yet it was very clearly the result of a political decision to loosen state control over economic activity. It would similarly be accurate to say that China's future growth will depend on how well it develops and deploys new technologies. But that depends on decisions about economic governance taken by its leaders, which will in turn be influenced by social and geopolitical forces that economists scarcely understand and generally ignore. Economists might imagine that if they were put in charge of a poor country, they could get it to grow. But a formula for growth that takes no account of social and political complexities is no formula at all.

Ignore it and it will grow away

A clearer understanding of how growth happens, and why growth-boosting institutions sometimes wither or fail to take root, could raise the living standards of billions of people. The economics of growth should therefore be central to the discipline, even though the questions it poses are objectively hard, and the answers rest more in history and politics than in elegant mathematics. Until they can give better answers in this area, economists should speak with greater humility about how this structural reform or that tax change might affect long-term growth. They have not earned the right to confidence. ■

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