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Narrative Economics: How Stories Go Viral & Drive Major Economic Events

by **Robert J. Shiller**

Princeton University Press, 2019.

When the author of the book is Robert J. Shiller, it is impossible to set expectations too high. He is a celebrated academic economist, winner of the Nobel Prize for his seminal work in the area of financial markets - specifically "for the empirical analysis of asset prices" - and the author of *Finance and the Good Society*, an outstanding book that provides a rich and very balanced view of the financial markets. When the book's intriguing title is also taken into account, the reader expects an eventful intellectual adventure, a joyful analytical ride with numerous rich insights and an abundance of food for thought. The only problem with great expectations - not in a Dickensian sense - is their management: sometimes they are not met.

The book starts with definitions of all the terms that are quite new for the conservative reader who is not used to linking narratives with economics. Shiller sticks to the *Oxford English Dictionary* for the definition of narrative: "A story or representation used to give an explanatory or justificatory account of a society, period, etc." (p. xi). For the author: "A story may also be a song, joke, theory, explanation, or plan that has emotional resonance and that can easily be conveyed in casual conversation" (p. xi), emphasising emotions and being conveyed. The next logical step is to define economic narrative and it is considered: "A contagious story that has the potential to change how people make economic decisions, such as the decision to hire a worker or to wait for better times, to stick one's neck out or to be cautious in business, to launch a business venture, or to invest in a volatile speculative asset" (p. 3). So, the conservative reader concludes that this is just another input for the economic agent's decisions under uncertainty, just another brick in the wall of business decisions based on expectations, since nothing else is available. Nonetheless, this brick is the central topic of the book, as suggested by the very title of the book, *Narrative Economics*, specified as. "The study of the viral spread of popular narratives that affect economic behavior, can improve our ability to anticipate and prepare for economic events. It can also help us structure economic institutions and policy" (p. 3).

Now the stage is set for the aim of the book. Curiously, at the very beginning of the book the author specifies the outcome, rather that the aim. "This book offers the beginnings of a new theory of economic change that introduces an important new element to the usual list of economic factors driving the economy: contagious popular stories that spread through word of mouth, the news media, and social media" (p. 3). So, the reward for the reader will be "a new theory". The first road test of the new theory is - Bitcoin. What are the insights of the new theory regarding Bitcoin? Instead of the theory, the reader gets a lot of, well - narratives. What is missing in the first road test of narrative economics - and is missing thought the book - is the theory and explanation of the causality from narrative to the economic outcome. Instead, the reader is given the normative proposal that the insights from other disciplines - primarily humanities - should be incorporated into economics. There is no insight about the huge methodological problems that such an inclusion would create. The reader wonders why such endeavour has not already taken place, taking into account the benefits for the economics that Shiller advocates. Perhaps insights from Gary Saul Morson and Marton Schapiro (2017) on the substantial methodological problem in linking economics and literature can shed more light on the issue.

The reader is then immersed in the epidemiology issues with epidemic curves, contagion rates, recovery rates, etc. The rather sinister connotation for the reader in the midst of COVID-19 pandemic is somewhat relaxed by focusing to the next question: Why do some narratives go viral? Unfortunately, although a chapter is devoted to this question, there is no answer. Actually, there are many stories about narratives in it, but no conclusion whatsoever. The case study of two 1980s narratives - the Laffer curve and Rubik's Cube - are equality futile, let alone the puzzling economic relevance of the Rubik's Cube. The answer to the question why some economic narratives go viral ends with this bottom line: "In both evolutionary biology and narrative economics, some kind of ornament or display can become popular for no more reason than the fact that it randomly began to be popular" (p. 65). A very helpful conclusion! Perhaps a more honest way to put it would be: "Nobody understands the process and causality".

After all that intellectual artillery preparation, the time comes to the light cavalry charge. The author spells out (p. 103, italics in the original) seven propositions of narrative economics: "(1) *Epidemics can be fast or slow, big or small*. The timetable and magnitude of epidemics can vary widely. (2) *Important economic narratives may comprise a very small percentage of popular talk*. Narratives may be rarely heard and still economically important. (3) *Narrative constellations have more impact than any one narrative*. Constellation matter. (4) *The economic impact of narratives may change through time*. Changing details matter as narratives evolve over time. (5) *Truth is not enough to stop false narratives*. Truth matters, but only if it is in-your-face obvious. (6) *Contagion of economic narratives builds on opportunities for repetition*. Reinforcement matters. (7) *Economic narratives thrive on human interest, identity and patriotism*. Human interest, identity and patriotism matter".

There is no effort by the author to provide empirical verification of these proposals, save some anecdotal evidence, such as, for example, the story that the communist slogan "from each according to his ability, to each according to his needs" was formulated by socialist philosopher Louse Blanc, not by Karl Marx (p. 102). The reader wonders which of the seven proposition is ostensibly empirically supported by this insight. Furthermore, Shiller does not provide any hint about strategy of empirical or any other verification of these proposals. No wonder, the reader ponders, since most of the propositions are insights that are so trivial, such as, for example, "epidemics can be fast or slow, big or small", that they merit no empirical verification. The author emphasises that he will "use these seven propositions as a framework to look at historically important economic narratives, to identify what we can learn from economic narratives and their consequences in the real world" (p. 103). The reader hopes that perhaps lessons from economic history would shed some light on the economic effects of economic narratives, if not on the causality between the narratives and the economic outcomes.

The first economic narrative to be considered is panic *versus* confidence. It is not quite clear what is the content of this narrative, even when Shiller specifies its constituent narratives: financial panic narrative, business confidence narrative and consumer confidence narrative. Then new terms are added to the pot: crowd psychology, suggestibility and autosuggestion. When all the ingredients are simmered and stirred, Shiller's stew is ready to be served: "We can use the concepts of crowd psychology and suggestibility to understand depressions, such as the Great Depression of the 1930s. In doing so, we should look not only at the direct applications of these concepts but also at the ways in which people *think* that these concepts help explain the depressions" (p. 120, italics in the original). In short, no analysis whatsoever, no insights about the ways that narratives impact the Great Depression, no evidence that the narratives explain the Great Depression, no hint about the way that the causality from narratives to the Great Depression should be explored, apart from the rather strange suggestions that it is relevant what people, who have no knowledge of scientific methodology, simply think about the causality - without any research.

In a rare moment of going back to proper economics, the author reviews the analysis of the roots of the Great Depression, emphasising the somewhat conflicting insights of academic economists. On one side, Barry Eichengreen and Peter Temin (2000) argued that the national commitment to the gold standard - despite changes in the labour market - made wages downward rigid and demonstrated that the countries that abandon gold standard recovered earlier. On the other side, Milton Friedman and Anna Jacobson Schwartz (1963) blamed the Federal Reserves and its control of the money supply, i.e. its policy not to offset declines in the money supply caused by the money withdrawing actions of economic agents, such as bank runs. Both sides provided explanations and supported them with empirical evidence. Once the reader is encouraged that the book will finally be about economics and explanations, the author introduces Marx - Groucho, not Karl - and his insights about stock market investment tips that he and his brothers overconfidently bet on (p. 133). A conservative comment would be that Marx - Groucho, not Karl - provided no explanation, so the explanations provided by Friedman and Schwartz (1963) and by Eichengreen and Temin (2000) cannot be contested by Groucho's. A more relaxed comment would be that it is reassuring that nobody asked Friedman et al. to be comedians and make movies, and that it is pity that the Marx brothers, after *A Day at the Races* did not shoot *A Day at the Stock Exchange*. That would have been fun. The fun that is completely missing from reading the Shiller's book.

The other eight economic narratives are treated in the same way. The *frugality versus conspicuous consumption* narrative provided insight that the decrease in consumer confidence decreases private consumption, especially in the case of durables, i.e. that private consumption is cyclical, but this is 101 of Keynesian economics and aggregate demand management. Yes - people who expect that they may become unemployed do buy new cars. But it is hardly understandable how the narratives are connected to this and how narratives can explain this kind of perfectly rational and reasonable expectations-based behaviour. Nonetheless, the author insists on being distinctive from those boring explanations already given by economics. “The modest economic recovery that started at the bottom of the Great Depression in 1933 occurred, at least in part, because people were spending more because poverty was no longer so chic!” (p. 149). So, monetary policy, gold standard, budget deficit, fiscal multiples, New Deal measures - all this is not so chic anymore.

The gold standard *versus* bimetallism narrative discusses the highly controversial development in last quarter of the 19th century in the US, when the gold standard was challenged by bimetallism, with a substantial political economy background. The author provides a number of narratives on both gold standard and the proposed bimetallism, but it is unclear what his contribution is, since there is not even an attempt to explain the triumph of the gold standard by those narratives. Instead, the reader learns that the yellow brick road in *The Wonderful Wizard of Oz* is a metaphor for gold and the gold standard, which has already been explained in detail by Hugh Rockoff (1990)[1]. As in the case of many insights in this book, the reader’s response is: So what?!

The narratives related to labour-saving machines replacing many jobs, automation and artificial intelligence replacing almost all jobs, real estate booms and busts, stock market bubbles, boycotts, profiteers and evil business, and about the wage-price spiral and evil labour unions receive similar treatment. Many words, many stories, i.e. narratives, but no explanation of how these narratives influenced economic outcomes. As a lesson to the policy makers, Shiller emphasises: “We should (…) consider that certain stories that recur with mutations play a significant role in our lives. Stories and legends from the past are scripts for the next boom or crash” (p. 238). If only the key for reading these scripts was provided.

Undoubtedly, the author is aware of all the shortcomings of the accomplishments of this approach, so the last part of the book discusses advancing narrative economics. Consequently, the reader wonders what the research agenda is, what kind of methodological breakthrough should be expected and what are the conditions for them, what are the main theoretical hypotheses that are testable, which should be carefully formulated and then empirically tested. Instead of the answers to those question, the author still points out the importance of narrative economics, hence: “It is very important, if we are ever to have a substantial understanding of the kinds of big economic events that have surprised us so often in the past, that we have some scientific methods

[1] Michael Watts (2003), in his rich and well-balanced selection of the literature pieces that can be of assistance in teaching economics, does not list *The Wonderful Wizard of Oz* as a something that can be helpful. Obviously, his view is that this metaphor is not quite compelling. His choice for the “Barter, Money and Inflation” section includes only Charles Frazier, Erich Maria Remarque, Johann Goethe and Gertrude Stein.

of studying the narrative element of these, even if the science is not complete and still involves some human judgment” (pp. 275-276). This is the bottom-line of the book. The reader expects from the author - who is advocating new economic discipline, and especially from a Nobel Prize laureate - at least some hints, some outline of the scientific method that this approach should be based on, if not an itemised research agenda. In short, it is committed scientific leadership that is expected from the Nobel Prize recipients. None of this is provided by the author.

Shiller complains that: “We can already today learn something about popular economic narratives by counting words and phrases in the digitized texts that are available, but there has not been enough organized research to measure the strength of the competing narratives that combine and recombine over time to cause major economic events” (p. 276). Just noting that counting words is definitely not science, this sentence actually demonstrates that Shiller simply *believes* that narratives cause major economic events. The problem is that he has provided no evidence of this. There is no analysis, no model, no research on the causality mechanism, no identification of the causality, no empirical evidence, since the random anecdotes that he provided are not evidence of any kind. The same point about Shiller’s attitude - though from a different angle - is made by Jonathan Portes (2020, p. 63) by quoting Shiller: “It must be the case that attention-getting narratives drive those decisions” and poising out that; “The ‘must’ is assertion, not analysis”. The problem is that science is not about believing, but about demonstrating; not about assertions, but about evidences.

The book ends (save the quite useless appendix on applying mathematical epidemic models to economic narratives) with guidelines for data collection. It remains a mystery what the data will be used for, without any proper methodology, testable hypothesis or insight on the causality mechanism. But this is a kind of safe shoot in the game of pool. When you do not know what to do - collect data. It will take time and people will forget the purpose of the data collection.

There are books that are long, such as F. M. Dostoyevsky’s *Crime and Punishment*, to borrow examples from literature, but the reader moves swiftly from page to page and after the last sentence has a desire to read it again, and would not remove a single sentence, a single word from the book. There are books that are short. Like, Albert Camus’ *L’Été*, but it is overwhelming with so many deep insights on human existence, their thinking and behaviour, that the reader is truly unhappy when the last page comes. There are books that are *too* short. To return to economics, such a boom, is Branko Milanovic’s *Capitalism, Alone: The Future of the System That Rules the World*, reviewed in the previous issue of this journal[2]. It is too short, because there are so many issue that are mentioned that there was no room for the in-depth analysis of them. Shiller’s book is definitely *too* long, because there is a void between the first and the last page. Its main insights can be limited to just a few sentences, nothing more. Everything else is just, …, well, narratives.

Reading this book is just like riding the train across a steppe: quite an eventless voyage with a huge, monotonous, grey-brown landscape. A good book is a must for such a ride. Alas, the reader is in the midst of the book that provides such a landscape.

[2] Boris Begović (2020) provides more information about Milanovic’s book.

This book provides very little if any food for thought. But it provides energy-packed food for the reader's anger, who has suffered the horror of turning the next page and the punishment of reading the book through to the last one. Why such a prominent economist - a Nobel prize winner, one of the best of the best - has written such a book is well beyond the scope of this review.

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