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George A. Akerlof – Robert J. Shiller:  
Animal Spirits  
*How Human Psychology Drives the Economy  
and Why It Matters for Global Capitalism*<sup>[2]</sup>

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The professional life of the two authors and the title of their co-work grabbed the attention of the writer.<sup>[3]</sup> He wonders whether the work places particular emphasis on Keynes' "animal spirits". He also wonders whether the path searching of economics in recent years and its growing number of self-examining questions have encouraged the two noted professors of economics to re-read, interpret and think further about the few lines of Keynes' General Theory. Keynes uses the term animal spirit in Part VII of Chapter 12.<sup>[4]</sup> „Even apart from the instability due to speculation, there is the instability due to the characteristic of human nature that a large proportion of our positive activities depend on spontaneous optimism rather than on a mathematical expectation, whether moral or hedonistic or economic. Most, probably, of our decisions to do something positive, the full consequences of which will be drawn out over many

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[2] Akerlof, George A. – Shiller, Robert J. (2011): *Animal Spirits: How Human Psychology Drives the Economy and Why It Matters for Global Capitalism*. Corvina Kiadó, Budapest.

[3] Akerlof's name is widely known by his analysis examining the effect of asymmetric information on market equilibrium (George A. Akerlof (1970)), his study is a basic literature among economists dealing with insurance market; Shiller, professor of economics of Yale University is perhaps well-known for his writing titled *Tőzsdemámor* (Robert J. Shiller (2007)).

[4] We note that before Keynes there are some treatise on the influence of spirit on human decisions and behaviour in different economic and social decision making processes. Without the claim of completeness Plato's tripartite theory of soul (Platon (1984)) and Max Weber's idealized types of rationality are mentionable. Plato argues that the soul is composed of three parts: the logical, the spirited, and the appetitive. These three parts of the soul also correspond to the three classes of a just society. Max Weber proposed an interpretation of social action that distinguished between four different idealized types of rationality. The first, which he called purposive/instrumental rationality, is related to the expectations about the behaviour of other human beings or objects in the environment. The second type, Weber called value/belief-oriented. Here the action is undertaken for what one might call reasons intrinsic to the actor: some ethical, aesthetic, religious or other motive, independent of whether it will lead to success. The third type was effectual, determined by an actor's specific affect, feeling, or emotion. The fourth was traditional or conventional, determined by ingrained habituation. Weber emphasized that it was very unusual to find only one of these orientations: combinations were the norm. (Weber, Max (1967): *Gazdaság és társadalom*. Közgazdasági és Jogi Könyvkiadó, Budapest.)

days to come, can only be taken as a result of animal spirits – of a spontaneous urge to action rather than inaction, and not as the outcome of a weighted average of quantitative benefits multiplied by quantitative probabilities. ... Thus if the animal spirits are dimmed and the spontaneous optimism falters, leaving us to depend on nothing but a mathematical expectation, enterprise will fade and die; – though fears of loss may have a basis no more reasonable than hopes of profit had before. ... But individual initiative will only be adequate when reasonable calculation is supplemented and supported by animal spirits...”<sup>[5]</sup>

After World War II Keynes’ General Theory was very determinant in economic thinking and also in its economic policy and practical reflections all over the world. The questions of interventionist national economic policy and of economic growth were met with keen interest. Growth and wealth were the success indicators of the intense race between the two poles of the world torn into two parts. Although there were some theoretical debates on the rate of statism and of state control, its necessity was hardly queried.<sup>[6]</sup> However, Akerlof and Shiller draw attention to the fact that only some certain parts of Keynes’ theory are widespread, especially those formalised by Hicks; therefore other parts e.g. animal spirits are forgotten. It is an interesting question why the Keynesians, the followers of Keynes, neither emphasised it, nor took it into consideration.<sup>[7]</sup>

In the range of Keynes’ ideas it played a central role – as is properly indicated by the citation – that in uncertain situations economic players might make their decisions by operating and invoking animal spirits. Without this factor the Keynesian model is not what was originally aimed at by its author. According to Akerlof and Shiller, it is for this reason that after a while the theory became undefendable; thus Milton Friedman and his followers queried the adequacy of the Keynesian theory in the 1970s and emphasised once again the almightiness of market in the style of classical economists. By the 1980s neoclassical principles had taken the leading role in the competition of economic theories behind economic policy decisions both in the United States and in the United Kingdom.

The reader who picks up this book is in for a serious and entertaining economic read. By rehashing and rethinking Keynes, Akerlof and Shiller state that economic processes and systems cannot be understood without variations in individual feelings, impressions, passions and human nature and without animal spirits.

[5] Keynes, J. M. (1936): *The General Theory of Employment, Interest and Money*. Part VII of Chapter 12. Elérhető: mercury.ethz.ch/.../Files/.../1366\_KeynesTheory of Employment.pdf.

[6] Augusztinovics Mária (1996): *Miről szól az input-output modell?* Közgazdasági Szemle. XLIII. évf. 4. sz.

[7] According to Csaba László (2011) heterodox traditions (he mentions the Austrian School and the old-line Keynesianism), which were always present in economics, were eradicated all over the world from education and thinking by the shrinking of courses and curriculum regarding the history of theory and by reducing the time spent on theoretical education. (Csaba László (2013): *Kérdőjelek a közgazdaságtanban és oktatásában*. Közgazdasági Szemle. LX. évf. 1. sz.)

The first part of the book specifies and explains animal spirits, whereas the second part tries to explain some significant present day macroeconomic processes with the help of the factors introduced in the first part. The five animal spirits are the followings: confidence, fairness, corruption and antisocial behaviour, money illusion and stories.<sup>[8]</sup>

In connection with the meaning of the term confidence, the authors highlight an implicit belief, which overrides rationality. When making a decision the trusting individual ignores or ill-manages the information. Confidence is impermanent since in a favourable, optimistic environment humans trust and make their decisions spontaneously as they anticipate success by instinct. The authors identify the spill over effects of confidence with a confidence multiplier similar to the Keynesian one, and they state that it affects every other multiplier. They are in no doubt of painting a proper picture of the future development of consumption with the help of the analysis of the data collected on confidence during surveys.

Fairness has been treated in several economic writings and its role in decisions can be as emphasised as other considerations regarded as strictly economic. The authors introduce the role of fairness in economic decisions by using the examples of the findings of questionnaire surveys and experiments. They then present theories regarding fairness and finally deal briefly with the relation of fairness to norms and economy. Although their examples are thought provoking, the definition of fairness is missing, particularly if compared to the chapter dealing with confidence.

According to the authors, the comprehension and the discussion of corruption and antisocial behaviour, or in other words, those of the dark side of economy are essential to correctly interpret collapses, failures and dysfunctions. They mention the three major recessions of the U.S. to represent what problems can be caused by corrupt and antisocial behaviour. They guess that economic and business cycles are not independent on how human commitment to ethical behaviour changes. The intensification of corruption and antisocial behaviour may be affected by more factors, i.e. the probability to discover a crime, the judgement of the measure of punishment, the social acceptance of crimes, the appearance of economic innovations and their regulation and supervision, and the changes in norms and in law-abiding behaviour.

Money illusion, the phenomenon that economic players decide based on nominal value, has a fundamental effect on economic legalities. From the brief presentation of the theories of Fisher, Keynes, Phillips and Friedman it emerges that the authors consider both the pure theory of Fisher and Keynes and its counter pole, the conception of Friedman, according to which money illusion

[8] We note critically that the authors do not emphasize that these spirits are on different levels of abstraction and some elements by way of example stories and the role of past were important in the previous phase of the economic theory from Smith to Samuelson.

does not exist, as naive. Although money illusion can be observed in several fields of economy i.e. in the field of wage and money setting, in case of credit moratoriums and in accountancy, its inquiry and the precise interpretation of the phenomenon requires further investigation.

Stories and the telling of stories have a basic effect on human knowledge. Facts, which we remember, live typically in our minds linked to some story. The authors illustrate the strong influential effect of stories with the help of the very illustrative example of Mexico.

In the second part of the book the authors describe how the mentioned five factors play a role in the evolution of recessions; how central banks can affect economic actors; why there is unemployment. Beyond that, using the idea of animal spirits they analyse the relation between inflation and unemployment, the suddenness of savings, the volatility of the price of monetary assets and that of company investments, the cyclicism of real estate markets, and the continuance of poverty observed among underprivileged minorities.

From the standpoint of the authors macroeconomics has to deal with the reason for the lack of total employment. They think that the theory of Adam Smith does not respond to the existence of economic fluctuations and does not appropriately confirm why there is no need for state intervention. To their mind, although the theory of Adam Smith correctly took account of rational human behaviour, the essence of which is that humans try to make economic decisions in accordance with their selfish interests, it did not take account of the fact that the presence of this behaviour is not exclusive in decisions. It did not take animal spirits into account. At this stage the authors definitely disregard *The Theory of Moral Sentiment*, a book, which provided the ethical, philosophical, psychological, and methodological underpinnings to Smith's later works, including *The Wealth of Nations* (1776), *Essays on Philosophical Subjects* (1795), and *Lectures on Justice, Police, Revenue, and Arms* (1763). Smith's classic work puts forward ideas about moral judgment and conscience and virtue that have taken on renewed importance in business and politics.

The stance adopted by Akerlof and Schiller is admittedly one, which views a better state to be the solution for the observed economic problems. Strengthening the role of state, according to them, is needed to maximise the advantages of capitalism and to minimise its disadvantages. They believe that capitalist societies are able to be enormously creative, thus state should restrict this by its intervention as little as possible. At the same time the self-abandoned capitalist economy is capable of all extremities as we could see and experience in the past years. On this basis the most important is the correctly interpreted role of state and the formation of frames. Regulators and frames should enable the entire evolution of capitalist creativity and at the same time should prevent fluctuations caused by animal spirits. They are not alone in this thought. Wager also argues at length that there is no effective market and welfare surplus without strong, professional and consistent governance.

It is an interesting phenomenon that this thought - according to which approaches based on models applying simplifier assumptions should be forgotten, as these do not allow us to describe complex reality appropriately - has also been increasingly strengthening in the writings of eminent economists since the neoclassical world. Stiglitz encourages the restoring of the traditional relation between aim and means. He does not suggest the rejection of modelling and calculations but their appropriate handling.

Having read the book, the question arises as to which economic theory comes out on top from the decade-long fight against both one another and reality. From the point of view of the wealth of mankind it is uncertain which is preferable: the combination of a complex, unsteady human nature causing economic fluctuations and the need for state intervention, thus reducing the social costs of the previous or the combination of unlimited individual freedom, self-realization and the market performing the necessary corrections. Or perhaps a new determinant theory is about to emerge, which de-emphasises the old ones to the world of historiography? I feel this book is not a new determinant theory but rather part of a new round in the fight, enabling and hoping that in the minds of the authors a new and a (practically) better working theoretical system is set to come into being. It is recommended reading to younger generations studying economics, albeit probably not in the mass education restricted to the basics of both macro- and microeconomics.

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