

A little disorder is a good thing

Nobel Prize-winner Edmund Phelps tells **Ralph Atkins** why Europe is doomed to lag behind America economically

As befits a combative, septuagenarian American economics professor known for his distinctly cynical view on Europe's growth prospects, Edmund Phelps is conservative in his choice of New York restaurant for lunch. Isabella's, at the base of a red-brick Upper West Side building with metal fire escapes, is filled with parents and children enjoying its American cuisine. The bright dining room overlooks the school opposite.

Last year's economics Nobel Prize winner arrives exactly on time. Born in 1933, Phelps is tall and lanky with a big smile. He is wearing a pale green checked summer jacket and brown tie; his white hair is neatly trimmed. After much international travel recently – he is just back from São Paulo – “it's kind of nice to re-establish contacts with my roots,” he says, referring to the menu.

As he happily accepts the waitress's proposal to start with a glass of Californian white wine, my hopes rise that this will be a convivial rather than intellectually challenging lunch (I had been worried: his 20-page online autobiographical notes had slipped into mathematical formulae by page five). Phelps lives on the Upper East Side, and “before I became very busy” – before winning his Nobel prize – would take the M4 bus across 110th street and then north to Columbia University. So, in fact, Isabella's – 30 blocks south of Columbia – is a radical departure. “This is out of my bus route,” he laughs. “But I'm a venture-some person. I've often gone out of my bus route.”

Traditionally, the Nobel Prize for economics recognises work that was carried out many decades ago but still has relevance today. Phelps won his for work in the late 1960s that overturned the then-conventional wisdom that a stable relationship existed between

inflation and unemployment – thus challenging the idea that politicians could pick an acceptable length for jobless queues and the rate of price increases. But he is also renowned for his criticism of continental European “corporatism”, which he believes hampers interaction between entrepreneurs and financiers and results in Europe relying on the import of ideas and techniques from the US.

Since 2001, Phelps has been director of the Center on Capitalism and Society, based at Columbia University. This is an economic forum for discussing what it is that allows commercial ideas to blossom into economic success for a country.

The waitress is back to take our order. We both choose corn chowder as a starter. He then selects the Maryland crab cake sandwich, a regular choice of his. I follow his recommendation and opt for a Cobb salad, in this case a chicken and Roquefort mixture.

Phelps feels he is at the stage in his career “where I

‘Europeans have all these attitudes that get in the way of an effective economic system’

can afford to be as radical as I want to be. And so I am having a lot of fun thinking about capitalism and trying to imagine how economics would have to be rewritten to capture the heart of that kind of system.”

Traditional economics, he explains, sees the world as if it were a plumbing system. “It's basically rooted in equilibrium – things work out as people expect them to do.” Capitalist reality, however, “is a system of disorder. Entrepreneurs have only the murkiest picture of the future in which they are making their bets, and also there is ambiguity, they don't know, when they push this lever or that lever, that the outcome is going to be what they think it is going to be – there is the law of unanticipated consequences. This is not in the economic text books, and my mission, late in my career, is to get it into the text books.”

As the creamy-white soup arrives, I switch the conversation to Europe, which, Phelps believes, is doomed always to trail behind the US. The lack of innovation

makes jobs dull and unsatisfying into the bargain. “I don't begrudge Europe waiting to see what works in America before expending the resources to adopt this or that new good or technique,” he says. “I just think the Europeans are depriving themselves of a high-employment economy and they are depriving themselves of intellectual stimulation in the workplace – and personal growth – by sticking to the stultifying, rigid system that I call corporatism.”

Phelps says Italian friends tell him that things have changed, that “we're virtually like America now”. But notwithstanding Europe's impressive growth rebound lately, he sees too much backsliding. “In Germany, for example, many companies invite trade union representatives to sit on supervisory boards and give advice on investment decisions – hardly unadulterated capitalism.

“Of course, corporations in Germany found a way out. You know what they did? They started bribing the union officials to go along with what they did – [look at] the Volkswagen scandal... The fact that they had to bribe gives the lie to those who say: ‘Oh, it doesn't matter, these unions are toothless, this is just all show.’ Well, if it is all show, then how come the union leaders are receiving such large payments?”

He concedes that comparisons with the US have to take account of Europe's ageing population, and that the rise of capital markets, hedge funds and private equity may be forcing change across the continent. But the important venture capitalists in Germany are American, he points out. “Perhaps that speaks volumes about how much of a handicap it was for German businesses to operate under the old *Landesbanken* [the country's public banks] and all those old, decrepit, giant investment banks. Now the Germans are getting the benefits of some good features of globalisation.”

We are into our main course – my salad fills a large plate, he attempts to build a tower out of a crab cake and his bun. Is there anything he admires about Europe, I wonder? He laughs loudly again. Another question to ask him that question, he says, was Larry Summers, the former US Treasury secretary and, more recently, former Harvard president. “I thought it very strange. It implies that

there is nothing I like about Europe... There are lots of things I like about Europe. I go there all the time, I must like it.” He cites as an example that Europe has “a great deal more interest in philosophy than is the case in the US, I enjoy that very much”.

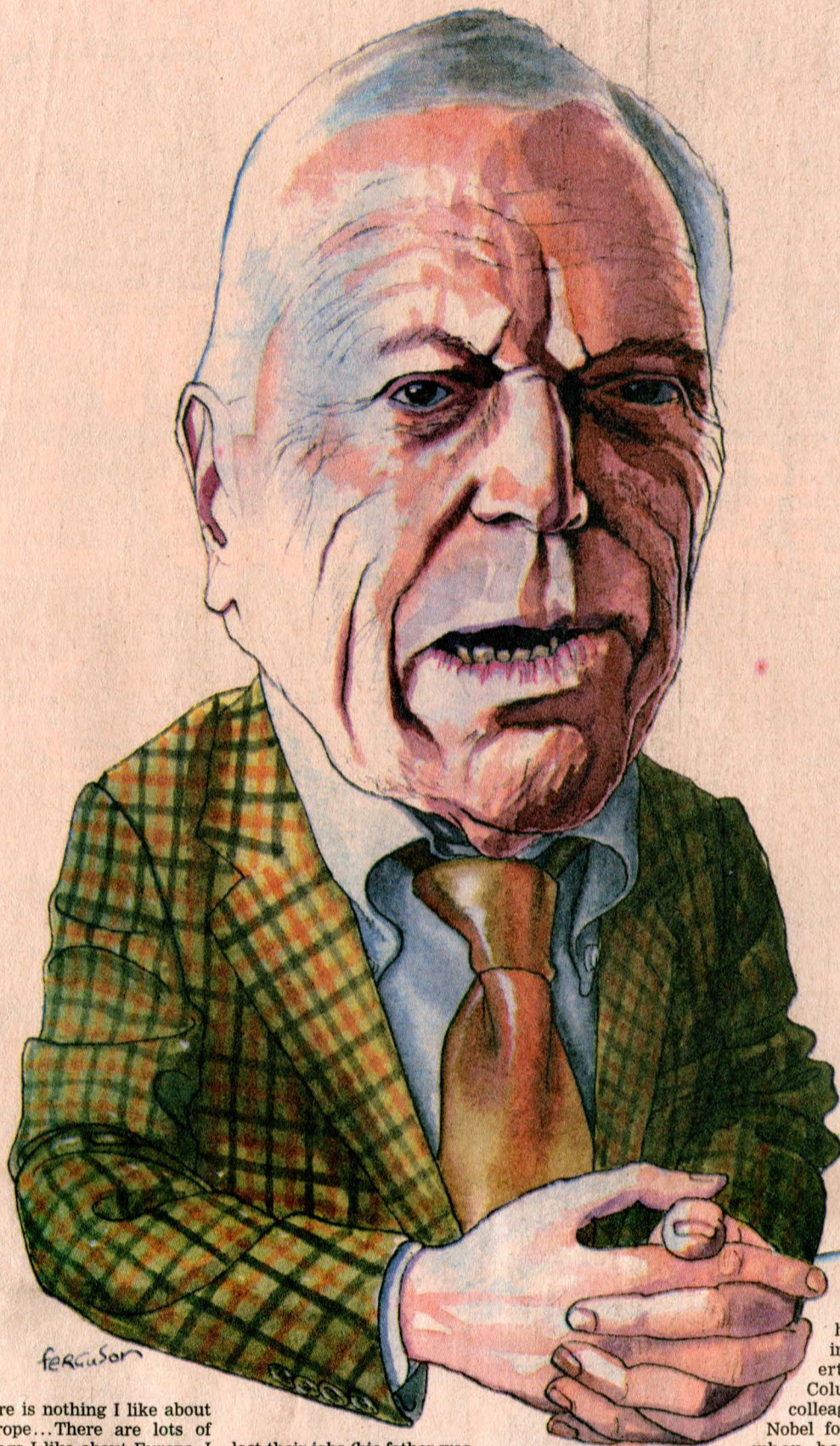
Phelps is anxious to make it clear that he “is not one of those American economists” who say that Europeans object to wealth creation. “My God, I don't know anyone who likes to accumulate their wealth more than the Europeans. I used to live near the Palazzo Farnese [in Rome] with my wife. Looking for a parking space, [I'd be] totally exhausted at 10 minutes to 7pm. And there would be the Italian artisans still working away, as they had been since 8am. Europeans like to work. They like to be wealthy. But they have all these other attitudes that get in the way of an effective economic system.”

Might his distinct view on capitalism and the necessity of embracing change result from his having been born during the Great Depression, in which both his parents

lost their jobs (his father was in advertising, his mother a nutritionist)? Phelps is emphatic. “I was a little kid at the time. It wasn't formative at all.” He tells me about an interview on Swedish television after winning the Nobel Prize: “The interviewer so much wanted me to say that I had been so affected by the unemployment of the Great Depression years. It was very difficult to make him understand that I was just a kid.”

More important for him, he explains, was his time at Amherst college in the early 1950s, a time when he read *inter alia* the Greek heroic epics, Cervantes's *Don Quixote* and Ralph Waldo Emerson on self-reliance. “Without being aware, I think I was being indoctrinated into what was called Vitalism, the idea that what makes life worth living, the good life, consists of accepting challenges, solving problems, discovery, personal growth, personal change.”

His reading of philosopher David Hume taught him



his seminal work relatively late in his career – he was in his mid-30s. Robert Mundell, a Columbia University colleague, received his Nobel for work published when he was a decade younger. “It just took a long time for me to mature and have anything to say that was of any originality,” he says.

I pay the bill but, as we leave the restaurant, Phelps wants to linger. After hesitating, he asks if I would like to walk a few yards north to the American Museum of Natural History. In the park outside, there is a pink stone monument inscribed with the names of all American Nobel Prize winners since Theodore Roosevelt won the peace prize in 1906. At the bottom of the second side is Phelps's name, added only a few days previously. Phelps points to some of his contemporaries. He is touchingly proud.

Ralph Atkins is the FT's Frankfurt bureau chief

Phelps reflects that he did

Isabella's, Columbus Avenue, New York

2 x corn chowder
1 x crab-cake sandwich
1 x Cobb salad
1 x cappuccino crème brûlée
1 x dark chocolate 'bag'
2 x glass Californian white wine
2 x double espresso
1 x bottle still water

Total: \$100.25