LAW AND MACRO: WHAT TOOK SO LONG?

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I

INTRODUCTION

Why has the development of law and macroeconomics lagged so far behind law and microeconomics?[1] In this Article, I consider three hypotheses:

1. Microeconomics fits better with law and legal reasoning than macroeconomics.
2. The Great Moderation of 1980–2007, in which western economies mostly avoided the twin perils of high unemployment and high inflation, lowered the stakes of macroeconomics relative to microeconomics, which encouraged the spread of law and microeconomics. The failure of price controls to thwart the high inflation rates of the 1970s, by contrast, discouraged the development of law and macroeconomics.
3. Law and economics' intellectual origins at the University of Chicago, a place of libertarian leanings and hostility to Keynesian macroeconomics, encouraged the development of law and microeconomics rather than macroeconomics.

I mostly reject the first hypothesis. Hypotheses two and three, by contrast, prove more compelling.

There are some areas of law, such as contract law, that are seemingly well-tailored to microeconomic analyses of incentives without focus on economy-wide general equilibrium effects. However, there are many other areas of law and regulation inextricably intertwined with macroeconomics, contradicting hypothesis one. The key constitutional question of the early U.S. republic—the establishment of a national bank—was fundamentally a question of macroeconomics. Today, it is (or should be) impossible to analyze such fundamental areas of law as financial regulation, central banking, bankruptcy

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1. I am not the first to ask this question. *See generally* Mark Kelman, *Could Lawyers Stop Recessions? Speculations on Law and Macroeconomics*, 45 STAN. L. REV. 1215 (1993). Kelman mostly concluded that lawyers could not stop recessions. *See id.* at 1285–86. I will refer to Kelman's speculations throughout this Article.

law, tax law, the law of government benefits, intellectual property, and international economic law without considering macroeconomics. And even contract law has had crucial (if rare) moments of interaction with macroeconomics, such as when Congress amended most U.S. credit contracts in the Great Depression with an eye towards stimulating the economy.[2]

The macroeconomic history of the period 1970–2007, law and economics' era of heady growth, offers a more plausible explanation for the predominance of law and microeconomics, supporting hypothesis two. During the 1970s, law was used for macroeconomic purposes. In fact, the primary initial policy response to the "Great Inflation" of the 1970s was the introduction of wage and price controls under the Economic Stabilization Act of 1970.[3] Price controls failed, tarnishing the use of law for macroeconomic purposes.[4]

After the conquest of the Great Inflation via a prolonged period of monetary policy tightness and unemployment, western economies enjoyed the Great Moderation, with relatively mild recessions and stable, low inflation. In 2003—the heart of the Great Moderation—the American Economic Association's president, Robert Lucas, asserted that macroeconomics' "central problem of depression prevention has been solved, for all practical purposes, and has in fact been solved for many decades."[5] If macroeconomics was a solved problem for economists in developed nations, then there was little if any need for lawyers in wealthy countries to consider the effects of law on the business cycle, especially given the checkered experience of law and macroeconomics during the 1970s. In other words: let the economists handle it. This position was no longer tenable after the Great Recession, explaining the rising subfield of law and macroeconomics.

The importance of intellectual fashion also played an important role in the underdevelopment of law and macroeconomics (hypothesis 3). From the 1960s to the 1980s, law and economics was most closely associated with the University of Chicago (Chicago), home of seminal law and economics scholars like Ronald Coase, Richard Posner, Gary Becker, and Aaron Director, as well as the first two journals in the field. Association with Chicago practically guaranteed that law and economics would avoid macroeconomics. At the time, Chicago's leading macroeconomists first rejected Keynesian business cycle management in favor of

2. *See generally* SEBASTIAN EDWARDS, AMERICAN DEFAULT: THE UNTOLD STORY OF FDR, THE SUPREME COURT, AND THE BATTLE OVER GOLD (2018) (describing Congress's abrogation of standard terms in debt contracts giving the creditor the option of demanding repayment in gold rather than currency).

3. *See* Gene Healy, *Remembering Nixon's Wage and Price Controls*, WASH. EXAM'R (Aug. 15, 2011), https://www.washingtonexaminer.com/remembering-nixons-wage-and-price-controls [https://perma.cc/Z355-6UW6].

4. *Id.*

5. Robert E. Lucas, President, Am. Econ. Assoc., Macroeconomic Priorities, Presidential Address at the One-Hundred Fifteenth Meeting of the American Economic Association (Jan. 4, 2003), *in* 93 AM. ECON. REV. 1 (2003).

exclusive reliance on monetary policy[6] and then rejected the argument that high unemployment during recessions was a problematic phenomenon.[7] Neither school of macroeconomics leaves much, if any, room for law and regulation to affect macroeconomic policy productively. As a result, law and economics as produced at Chicago was naturally dominated by microeconomics.

Law and economics' early libertarian and deregulatory associations also played a role in the relative absence of law and macroeconomics. Microeconomics—before the development of behavioral economics—assumes individual rationality. Under a microeconomic lens, intrusive legal interventions tend to be disfavored. Only the presence of externalities justifies legal intervention, and many externalities can be internalized without law via Coasean bargaining.[8] Law and microeconomics therefore offered an attractive framework for scholars with a libertarian and deregulatory bent—and for the philanthropists interested in funding a research program producing laissez-faire policy recommendations.

Keynesian macroeconomics, by contrast, begins with a market failure—the presence of excess unemployment due to a lack of aggregate demand in the economy. Mitigating this market failure requires government intervention, in the form of state control over the currency, fiscal policy, or some other mechanism. Evaluating law from a macroeconomic perspective is therefore just as likely to favor government intervention as deregulation, making it less attractive than law and microeconomics to the early funders who helped popularize the field and spread its teachings.

History and ideology therefore worked in tandem to delay the development of law and macroeconomics within law and economics generally. The prolonged Great Recession that followed the Financial Crisis of 2008, however, indicates the need for a shift in direction.[9] The Great Recession showed emphatically that the problem of recession prevention has not been solved. We should therefore not be surprised if legal scholars and economists explore law and regulation as a tool for mitigating the worst recessions and preventing the asset price bubbles that often precede these recessions. Indeed, I predict that macroeconomic performance over the next generation will play the most important role in determining the future of law and macroeconomics. If many countries experience anemic growth rates and low interest rates akin to Japan's lost decade(s), heightening the need for new tools of macroeconomic management and further

6. The theory of "monetarism" was advanced most prominently by Milton Friedman. *See generally* MILTON FRIEDMAN & ANNA JACOBSON SCHWARTZ, A MONETARY HISTORY OF THE UNITED STATES, 1867–1960 (1963).

7. This argument is known as the "real business cycle" theory and is associated with Robert Lucas, among others. *See infra* note 59.

8. For an introduction to the Coasean approach to mitigation of externalities, see generally Steven G. Medema & Richard O. Zerbe Jr., *The Coase Theorem*, *in* ENCYCLOPEDIA OF LAW AND ECONOMICS 2000, at 836–92.

9. Macroeconomics is undeniably fond of the adjective "great." The last century has witnessed the "Great Depression," "Great Inflation," "Great Moderation," and "Great Recession."

undermining the argument that the economy is capable of self-regulation, then law and macroeconomics will—and should—flourish. But this flourishing will require law and economics to embrace a methodological diversity that has been missing heretofore.

II

WHAT IS LAW AND MACROECONOMICS?

To ask why law and macroeconomics is relatively undeveloped, we first need to define what it might be. Macroeconomics is the study of how the aggregate economy behaves, examining phenomena like inflation, growth, unemployment, money, and interest rates. While microeconomics seeks to understand how one market behaves, macroeconomics focuses on the links between markets. At times, the links between markets create phenomena that could not exist in a single market. For example, a widespread desire to hold on to money or a reduction in the supply of money may push other markets, such as the labor market, out of equilibrium for an extended period.

Macroeconomics may be further categorized as either short-run or long-run macroeconomics. Short-run macroeconomics studies the prevention and mitigation of recessions. It is primarily concerned with preventing the periodic shortages of spending ("aggregate demand") that cause excess unemployment. Long-run macroeconomics, by contrast, studies persistent differences in growth and output levels. It is primarily concerned with increasing the economy's ability to produce at full employment ("aggregate supply"), which is determined by forces such as technological change and capital formation.

Law and macroeconomics studies how law affects these aggregate variables of interest, and how fluctuations in these aggregate variables affect law.[10] It offers a different perspective from conventional law and microeconomics. In microeconomics, a law that improves the functioning of an individual market is efficient and therefore desirable. In macroeconomics, however, the law's generalized effects must be considered. A law that improves the functioning of one market may have negative spillover effects on other markets and on the overall economy by impacting aggregate demand or aggregate supply.[11] As a result, macroeconomic perspectives should often produce different policy recommendations than conventional law and economics. For example, a

10. For more extensive discussions of law and macroeconomics, see generally YAIR LISTOKIN, LAW AND MACROECONOMICS: LEGAL REMEDIES TO RECESSIONS (2019); Yair Listokin & Daniel Murphy, *Macroeconomics and the Law*, 15 ANN. REV. L. & SOC. SCI. 1 (2019).

11. *See, e.g.*, Gauti B. Eggertsson, *Was the New Deal Contractionary?*, 102 AM. ECON. REV. 524, 549–50 (2012) (showing that the formation of cartels, which inefficiently reduce output in a single market, can raise inflationary expectations and therefore increase aggregate demand and thus overall output); *see also* Robert Cooter & Aaron Edlin, *Law and Growth Economics: A Framework for Research* (Berkeley Program in Law & Econ., Working Paper Series, 2011), https://escholarship.org/uc/item/50t4d0kt [https://perma.cc/Q8QR-GTSY] (demonstrating how intellectual property creates microeconomic distortions for the purpose of enhancing innovation and increasing long run aggregate supply).

microeconomically inefficient mandate to install pollution scrubbers on power plants may be macroeconomically justified during a recession because the mandate increases spending and lowers wasteful unemployment. However, this macroeconomic perspective has rarely been explored by law and economics.

III

IS MACROECONOMICS ILL-SUITED TO LAW?

In 1993, Mark Kelman asserted that "macroeconomists have not traditionally addressed the types of institutional-design issues that concern lawyers."[12] If it were true that there is relatively little nexus between law and the macroeconomy, we should not be surprised at the underdevelopment of law and macroeconomics.

This assertion is flawed. One of macroeconomists' principle concerns is the money supply, which is critically determined in part by precisely the "types of institutional-design issues that concern lawyers." Central banks exist to help guarantee the stability of the money supply: their powers and limitations are fundamentally legal. Examples abound. The status of the first National Bank of the United States was the subject of intense constitutional dispute.[13] The international monetary policy regime established by the Bretton Woods system in the wake of World War II entailed elaborate institutional designs involving many lawyers and administrators.[14] During the Financial Crisis of 2008, one of the most important decisions was the non-bailout of Lehman Brothers by the Federal Reserve, attributed to an absence of legal authority from the detailed Federal Reserve Act.[15] And a group of German plaintiffs challenged the European Central Bank's (ECB's) solution to the European crisis as exceeding the ECB's legal authority.[16]

The establishment and maintenance of the money supply—a core macroeconomic issue—is a subject deeply enmeshed in law. Lawyers and macroeconomists share this common interest.

The connections between law and macroeconomics do not end with money. As Steven Ramirez has demonstrated, nearly every administrative agency (for example, the Securities Exchange Commission, National Labor Relations Board, and National Recovery Administration) established during the New Deal began

12. Kelman, *supra* note 1, at 1216.

13. *See* GORDON S. WOOD, EMPIRE OF LIBERTY: A HISTORY OF THE EARLY REPUBLIC, 1789–1915, at 143–45 (2009) (discussing the intense debate between Federalists and Republicans in 1791 over the constitutionality of a law authorizing the Bank of the United States).

14. *See generally* John W. Pehle, *The Bretton Woods Institutions*, 55 YALE L.J. 1127 (1946) (describing the institutional design and legal relevance of the newly developed International Monetary Fund and World Bank).

15. *See* TIMOTHY GEITHNER, STRESS TEST: REFLECTIONS ON FINANCIAL CRISES 83, 186 (2014) (explaining that the Fed "didn't believe [it] had the legal authority to guarantee Lehman's trading liabilities, even using [its] 'unusual and exigent' powers under 13(3)").

16. *See* Mehreen Khan, *German High Court Rejects Case Against ECB Crisis Tool*, FIN. TIMES (June 21, 2016), https://www.ft.com/content/ac3a89c2-f382-388f-b4e6-d1b657361db8 [https://perma.cc/4J82-VN9Z] (describing the constitutional controversy over the ECB's programs).

with macroeconomic motives.[17] During the Great Depression, the institutional design questions considered by lawyers were an integral part of macroeconomic policy. Nor was law and macroeconomics merely a subject of regulation. Congress went so far as to amend most contracts between debtors and creditors by suspending "Gold Clauses"[18]—and the Supreme Court upheld the intervention as constitutional.[19] And during the 1970s, the Nixon and Ford administrations (with grudging support from their economic advisers) attempted to mitigate the Great Inflation through the formation of Wage and Price Stability Boards—regulatory bodies with legal power.[20] Although Nixon's price controls, implemented through the Wage and Price Stability Boards, may have failed, they show macroeconomics deeply enmeshed with law.

Even if macroeconomics and law are mutually interdependent, it could be argued that macroeconomic reasoning is simply ill-suited to law relative to microeconomic reasoning. Many areas of law, such as common law, for example, proceed case-by-case. In these areas, law addresses incentive problems between the parties to the case—the domain of microeconomics. Case-by-case reasoning, by contrast, cannot easily solve systematic social ills like widespread unemployment. If law and economics only applied to case-by-case reasoning, then this hypothesis for the dominance of law and microeconomics would look compelling. Using case-by-case adjudication to remedy recessions would be a heroic task—far better to rely on more systematic responses to macroeconomic problems offered by expert agencies such as central banks.

Law and economics, however, does not limit itself to case-by-case reasoning. Microeconomic reasoning is regularly applied to the systematic regulatory and statutory solutions offered to complex multi-polar questions. Tax law, for example, helps determine the fiscal stance of the entire economy. Tax law is regularly used as a tool of macroeconomic policy—it is rare for a recession to occur without a reduction in tax rates and change in tax rules. And yet tax law casebooks focus exclusively on microeconomic efficiency concerns in describing the economics of tax, ignoring macroeconomics.[21]

Tax law is no outlier. There are other regulatory regimes designed to solve systematic social problems that are almost exclusively examined from a microeconomic perspective within law and economics. These regimes include antitrust law, the law of utility regulation, financial regulation (though this is

17. *See generally* Steven A. Ramirez, *The Emergence of Law and Macroeconomics: From Stability to Growth to Human Development*, 83 LAW & CONTEMP. PROBS. no. 1, 2020, at 219.

18. Gold clauses in business contracts allowed a creditor to demand payment in gold rather than currency. For a description of the controversy surrounding the suspension of these gold clauses by law, see EDWARDS, *supra* note 2.

19. *See generally* Norman v. Balt. & Ohio R.R. Co., 294 U.S. 240 (1935); Nortz v. United States, 294 U.S. 317 (1935); Perry v. United States, 294 U.S. 330 (1935); United States v. Bankers Tr. Co., 294 U.S. 240 (1935).

20. *See generally* Healy, *supra* note 3.

21. *See* Yair Listokin, *Equity, Efficiency, and Stability: The Importance of Macroeconomics for Evaluating Income Tax Policy*, 29 YALE J. ON REG. 45, 58 (2012) (arguing for an increased emphasis on macroeconomics in teaching and research on tax law and policy).

rapidly changing), regulation of consumer finance and bankruptcy law, environmental law, securities regulation, and land use regulation, among many others. Decisions in these areas have important macroeconomic effects because of their systemic perspective. Yet these effects have been overlooked until very recently.

Some, including Kelman, argue that "macroeconomics may be less accessible and illustrable by the use of 'commonsensical analogies' than microeconomics."[22] Subtle macroeconomic argumentation requires an understanding of the interaction between the money market, markets for goods and services, and markets for saving and borrowing. As a result, sophisticated law and macroeconomics is undeniably difficult.

But this sets the bar for law-and-macroeconomic arguments too high—and well above the standard we set for law-and-microeconomic arguments. For law and microeconomics, we expect arguments that explain why certain laws and regulations are more or less likely to distort behavior and lead to efficient outcomes relative to other laws. The fact that distortions can only be defined relative to a Pareto optimum that is ill-defined and essentially unreachable does not prevent engagement with these more tractable microeconomic considerations. Similarly, short-run law and macroeconomics, at its core, concerns itself with aggregate demand. And long-run law and macroeconomics, at its core, concerns aggregate supply—the economy's total capacity to produce. A successful short-run law-and-macroeconomic argument needs to explain why a certain law or regulation is likely to encourage more spending in recessions and less spending in booms than alternative policies. A successful long-run law-and-macroeconomic argument should similarly explain why a certain law or regulation is more likely to raise the economy's aggregate supply capacity than the alternatives. While more detail than this is certainly welcome, law and macroeconomics should not be held to a higher standard than law and microeconomics.

Indeed, law and economics has not demanded more than this level of explanation from "Law and Finance," which explains how law determines the size and structure of a country's financial sector and output capacity—traditionally macroeconomic outcomes. The mechanism linking law to the size of the financial sector in the Law and Finance literature is ambiguous, to say the least. Nevertheless, this primarily empirical literature has flourished in spite of its ambiguous theoretical grounding.[23]

In total, a lack of affinity between macroeconomics and law is not a compelling explanation for the underdevelopment of law and macroeconomics. The Great Moderation, by contrast, offers a better explanation.

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22. Kelman, *supra* note 1, at 1217 (error in original).

23. *See* Steven Kaplan & Luigi Zingales, *How "Law and Finance" Transformed Scholarship, Debate*, CHICAGO BOOTH REVIEW (Mar. 5, 2014), https://review.chicagobooth.edu/magazine/spring-2014/how-law-and-finance-transformed-scholarship-debate [https://perma.cc/2EBU-ZY4E] (describing the influence of research taking a law and finance perspective).

IV

THE GREAT MODERATION AND THE UNDERDEVELOPMENT OF LAW AND MACROECONOMICS

Law responds to pressing social problems. In the Great Depression, when insufficient aggregate demand was perhaps the dominant policy problem, law responded. And when inflation reared its head in the 1970s, law responded again. Price controls, implemented by the Wage and Price Stability Board, attempted to mitigate high inflation, again putting law at the heart of macroeconomic policy. Then came the Great Moderation.

A. The Great Moderation and the Law

No one described the legal trends of the Great Depression era as "law and macroeconomics"—perhaps because law and economics had yet to be seriously developed.[24] Yet as law and economics grew and thrived in the 1980s and 1990s, the salience of macroeconomic policy problems in the United States and Europe decreased—a development known as the Great Moderation. With macroeconomic policy problems fading into the background, there were relatively few laws and regulations passed with macroeconomic policy goals for law-and-economics scholars to analyze, and even less need to encourage the development of novel legal instruments to solve non-existent macroeconomic policy problems.

The term "Great Moderation" describes the "striking decline in the volatility of aggregate economic activity" experienced by most advanced economies between the early 1980s and the Great Recession of 2008 and beyond.[25] In the United States, for example, the standard deviation of annual output growth (one measure of economic volatility), declined from 17.8% from 1954–1983 to only 7.7% from 1984–2005.[26] Annual inflation rates also became lower and more stable during the later period.[27]

24. Even though no one described the Great Depression era macroeconomic policy as law and macroeconomics, some appreciated the desirability of such a field. In the late 1950s, Guido Calabresi taught his first law and economics course at Yale Law School. Interview with Guido Calabresi, Professor Emeritus, Yale Law School, in New Haven, Conn. (Sept. 4, 2019). The course explored law from a microeconomic perspective. *Id*. Yale Law School's dean during this period, Eugene Rostow, was puzzled by Calabresi's microeconomic emphasis on microeconomics. *Id*. Finding Calabresi's area of economic emphasis puzzling, Rostow asked Calabresi to consider a class on law's role in the prevention of recessions and depressions—law and macroeconomics: Rostow considered depression prevention the primary task of economics. *Id.* Calabresi declined the request. *Id*. Rostow then asked Robert Bork to consider teaching law and macroeconomics. *Id*. Bork declined as well. *Id.*

25. Steven J. Davis & James A. Kahn, *Interpreting the Great Moderation: Changes in the Volatility of Economic Activity at the Macro and Micro Levels*, 22 J. ECON. PERSP., no. 4, Fall 2008, at 155, 155.

26. *Id.* at 161.

27. *See id*. at 163.

The causes of the Great Moderation are the subject of considerable debate. Some attribute the trend to good luck,[28] others to economic shifts towards more stable sectors (such as the growing role of services versus manufacturing),[29] and still others attribute the trend to improvements in monetary policy.[30] Whatever the cause, stable output and inflation diminished the motivation for legal and regulatory fixes to macroeconomic problems. If the "central problem of depression prevention ha[d] been solved, for all practical purposes,"[31] then why complicate law by attempting to solve a non-problem? In such an environment, there was little practical push for the development of law and macroeconomics. Law-and-macroeconomic policy interventions on the scale of New Deal agencies or wage and price controls were nowhere to be found during the Great Moderation.[32]

The Great Moderation also limited the urgency of macroeconomic analysis of legal topics with clearly macroeconomic origins. Programs and agencies such as the Federal Housing Administration (FHA), Federal Deposit Insurance Corporation, and Federal Reserve have transparently macroeconomic motivations. But evaluating the efficacy and boundaries of the legal framework of these institutions assumes less urgency when they are operating within a steady state. As a result, the fields of law most connected to macroeconomics often became backwaters of law-and-economic analysis before the Great Recession. Indeed, financial regulations with macroeconomic motivations, such as the Glass-Stegall Act's limitation of financial institutions, drew "heavy criticism as a Depression-era relic."[33]

The Great Moderation's powerful impacts on intellectual trends in macroeconomics more broadly are exemplified by the steadily decreasing role attributed to fiscal policy within macroeconomics. Fiscal policy stabilization—lowering taxes and increasing spending during recessions and eliminating deficits during booms—was long a standard part of the post-World War II macro policy toolkit. By the end of the Great Moderation in the mid-2000s, however, conventional macroeconomic wisdom dictated that "discretionary fiscal policy [was] dominated by monetary policy as a stabilization tool because of lags in the

28. *See, e.g.*, James H. Stock & Mark W. Watson, *Has the Business Cycle Changed and Why?*, 17 NBER MACROECONOMICS ANN. 159, 162 (2003).

29. *See* Davis & Kahn, *supra* note 25, at 160.

30. Richard Clarida, Jordi Galí & Mark Gertler, *Monetary Policy Rules and Macroeconomic Stability: Evidence and Some Theory*, 115 Q.J. ECON. 147, 148 (2000).

31. Lucas, *supra* note 5, at 1.

32. This is not entirely true. In the wake of the Asian Crisis of 1997, some Asian nations adopted laws and regulations, such as capital controls, with macroeconomic motivations but little microeconomic justification. *See, e.g.*, Ethan Kaplan & Dani Rodrik, *Did the Malaysian Capital Controls Work?*, *in* PREVENTING CURRENCY CRISES IN EMERGING MARKETS 393, 422–23 (Sebastian Edwards & Jeffrey A. Frankel eds., 2002).

33. Dan More, *The Virtues of Glass-Steagall: An Argument against Legislative Appeal*, 1991 COLUM. BUS. L. REV. 433, 433 (1991).

application, impact, and removal of discretionary fiscal stimulus."[34] If the intellectual case for an orthodox Keynesian tool like fiscal policy lost its mojo during the Great Moderation, then we should not be surprised that academics did not consider a less conventional alternative—law and regulation—during the same period. Nor should we be surprised that legal analysis of the institutions of fiscal policy, tax, government benefits, and government procurement law—among others—emphasized microeconomic questions rather than macroeconomics.

B. The Great Recession and Financial Regulation

The Financial Crisis of 2008 represented the "worst financial crisis in global history"[35] and led directly to the Great Recession—the worst global recession since the Great Depression.[36] The macroeconomic turmoil brought an emphatic end to the Great Moderation. If the Great Moderation hindered the development of law and macroeconomics, then we would expect the Financial Crisis of 2008 and the Great Recession that followed to stimulate the field because it deals with aggregate demand issues This is indeed what we have found—but only in limited fields.

Many legal and regulatory changes followed the Financial Crisis of 2008.[37] A combination of extraordinary Federal Reserve actions such as emergency lending and stress tests, combined with Congress's passage of the Emergency Economic Stabilization Act of 2008 and the establishment of the Troubled Asset Relief Program, restored calm to the financial sector.[38] In 2010, Congress passed the Dodd Frank Act, "the greatest legislative change to U.S. financial regulation since the explosion of financial legislation in the 1930s."[39] Examining these legal and regulatory developments without considering macroeconomics would not pass the smell test. Law and economics has risen to the occasion. Economic analysis of financial regulation and the housing market now regularly considers

34. Jason Furman, *The New View of Fiscal Policy and Its Application*, VOX EU (Nov. 2, 2016), https://voxeu.org/article/new-view-fiscal-policy-and-its-application [https://perma.cc/Q2X2-7HX6].

35. Tim Worstall, Opinion, *Ben Bernanke: The 2008 Financial Crisis Was Worse than the Great Depression*, FORBES (Aug. 27, 2014), https://www.forbes.com/sites/timworstall/2014/08/27/ben-bernan/ke-the-2008-financial-crisis-was-worse-than-the-great-depression [https://perma.cc/M2GR-89NX].

36. *See, e.g.*, Josh Bivens, *Worst Economic Crisis Since the Great Depression? By a Long Shot*, ECON. POL'Y INST. (Jan. 27, 2010), https://www.epi.org/publication/snapshot_20100127 [https://perma.cc/86FV-4Y5H].

37. This Article focuses on the American policy response to the Financial Crisis of 2008 and the Great Recession that followed. The European policy response to the Financial Crisis of 2008 was similarly robust, with national governments stepping in to rescue many failing financial institutions and the ECB playing an extraordinary role. For a review, see generally EUROPEAN COMM'N DIRECTORATE-GENERAL FOR ECON. & FIN. AFFAIRS, ECONOMIC CRISIS IN EUROPE: CAUSES, CONSEQUENCES, AND RESPONSES (July 2009), http://ec.europa.eu/economy_finance/publications/pages/publication15887_en./pdf [https://perma.cc/2SQF-D5XE].

38. Emergency Economic Stabilization Act, 52 U.S.C. §§ 5201–61 (2012). For the Troubled Asset Relief Program, see 52 U.S.C. §§ 5211–41.

39. Randall Guynn, *United States*, *in* INT'L BAR ASS'N, TASK FORCE ON THE FINANCIAL CRISIS, A SURVEY OF CURRENT REGULATORY TRENDS 25, 39 (2010).

"systemic risk," a concept rarely explored in the pre-2008 literature. Many of the contributors to this issue of *Law and Contemporary Problems* are, quite appropriately, specialists in these areas.

Even though the Great Recession was severe, its magnitude was limited by several decisive policy responses. In addition to the heroic efforts to rescue the financial sector just described, the U.S. (and international) economy was supported by unprecedentedly loose monetary policy and, in the short-run, significant fiscal stimulus.

C. The Great Recession and Monetary Policy

In ordinary economic times, central banks stimulate the economy by lowering interest rates to encourage investment and consumption. At the outset of the Great Recession, central banks lowered interest rates significantly to stimulate their moribund economies. However, when nominal interest rates fall to zero, as they quickly did during the Great Recession, conventional monetary policy loses traction. To cope with this "zero lower bound" on interest rates, central banks adopt unconventional monetary policy measures, including quantitative easing. In quantitative easing, central banks buy longer term assets that they normally shun, seeking to affect rates on these assets, which remain above zero. Because markets for these assets are much larger than the market for short-term bonds usually targeted by central banks, quantitative easing necessitates a much greater role for the central bank in the economy. Between 2008 and 2017, for example, the five largest central banks increased their balance sheets four-fold—effectively printing roughly fifteen trillion dollars in money and reserves over this period.[40] These extraordinary actions almost certainly mitigated the Great Recession.[41]

Whatever its effects, quantitative easing does not represent central banking as usual. Quantitative easing brings (unrealized) risks of inflation and may create asset bubbles.[42] It expands the role of central banks in the economy and often stands in tension with legal restrictions on central banks, such as the Treaty of Lisbon's limitation on ECB monetary financing.[43] As of yet, no central bank has successfully unwound quantitative easing.

40. Tyler Durden, *A Problem Emerges: Central Banks Injected a Record $1 Trillion in 2017 . . . It's Not Enough*, SNBCHF.COM (May 11, 2017), https://snbchf.com/2017/05/durden-emerges-central-banks-trillion-2017 [https://perma.cc/7X5H-QZXU].

41. *See, e.g.*, Arvind Krishnamurthy & Annette Vissing-Jorgensen, *The Effects of Quantitative Easing on Interest Rates: Channels and Implications for Policy* (Nat'l Bureau of Econ. Research, Working Paper No. 17555, 2011), *reprinted in* BROOKINGS PAPERS ON ECON. ACTIVITY, Fall 2011, at 215.

42. For an expression of inflation concerns, see, for example, Cliff Asness et al., *An Open Letter to Ben Bernanke*, WALL ST. J. (Nov. 15, 2010), https://blogs.wsj.com/economics/ 2010/11/15/open-letter-to-ben-bernanke [https://perma.cc/J2VZ-34JA]. For concerns about massive central bank bond purchases causing asset bubbles, see Jean-Michel Paul, Opinion, *Why We Have to Talk About a Bubble*, BLOOMBERG (Jan. 11, 2018), https://www.bloomberg.com/opinion/articles/2018-01-11/why-we-have-to-talk-about-a-bubble [https://perma.cc/2NZC-ASHU].

43. Case C-62/14, Gauweiler v. Deutscher Bundestag, http://curia.europa.eu/juris/celex.jsf?celex=/ 62014CJ0062 [https://perma.cc/Z2C6-RNPR] (June 16, 2015).

Consequently, legal limitations on central banks constitute an increasingly important subject for law and macroeconomics. The field has partially taken up the challenge.[44] But the field of administrative law has curiously ignored central banks in spite of their importance. The problem for administrative law scholars may be that the study of central banks plainly requires macroeconomic sophistication, yet very few administrative law scholars have the macroeconomic background necessary to evaluate specific monetary policy or financial regulatory decisions on their own terms.[45] Over time, however, the study of central banks as legal actors is likely to be a growing part of law and macroeconomics.

D. Fiscal Policy and Law and Macroeconomics

The Great Recession overturned the macroeconomic consensus against fiscal stimulus that formed during the Great Moderation.[46] During 2009, the G20 engaged in coordinated economic stimulus, which had substantial mitigating effects on the Great Recession.[47] After the Great Recession, the new conventional wisdom, expressed by the Chair of the Council of Economic Advisers in 2016, held that "(1) [f]iscal policy is often beneficial for effective countercyclical policy as a complement to monetary policy. (2) Discretionary fiscal stimulus can be very effective and in some circumstances can even [increase] private investment."[48]

In this environment, law-and-economic analysis of fields touching on fiscal policy—which includes tax law, the law of government benefits, government procurement law, and government insurance and lending programs such as the FHA's mortgage insurance program—needs to consider the macroeconomic effects of laws. With limited exceptions,[49] however, the study of these areas does

44. See, for example, the work of Peter Conti-Brown, Robert Hockett, Kathryn Judge, Katharina Pistor, Morgan Ricks, and Annelise Riles on this subject.

45. In a recent working paper, my co-authors and I explore an alternative hypothesis. We argue that the judiciary rarely reviews Fed monetary policy because plaintiffs lack standing. In turn, the absence of case law makes Fed monetary policy relatively invisible to administrative law scholars. *See generally* Peter Conti-Brown, Yair Listokin & Nicholas Parrillo, *The Administrative Law of Central Banking* (Yale Law Sch. Working Paper, Dec. 2019) (on file with author).

46. For a review of the effects of fiscal stimulus on output during the Great Recession, see generally Olivier J. Blanchard & Daniel Leigh, *Growth Forecast Errors and Fiscal Multipliers*, 103 AM. ECON. REV. 117 (2013).

47. For a description of stimulus efforts of G20 countries in late 2008 to early 2009, see Eswar Prasad & Isaac Sorkin, *Understanding the G-20 Economic Stimulus Plans*, BROOKINGS INST. (Mar. 15, 2009), https://www.brookings.edu/research/understanding-the-g-20-economic-stimulus-plans/ [https://perma.cc/99BC-BST4].

48. Jason Furman, Chairman, Council of Econ. Advisors, Expanded Version of Remarks Prepared for the Global Implications of Europe's Redesign Conference: The New View of Fiscal Policy and Its Application (Oct. 5, 2016), https://obamawhitehouse.archives.gov/sites/default/files/page/files/2016/1005_furman_suerf_fiscal_policy_cea.pdf [https://perma.cc/728P-AQN7].

49. *See, e.g.*, Andrew Hayashi & Daniel P. Murphy, *Savings Policy and the Paradox of Thrift*, 34 YALE J. ON REG. 743 (2017); Yair Listokin, *Equity, Efficiency, and Stability: The Importance of Macroeconomics for Evaluating Income Tax Policy*, 29 YALE J. ON REG. 45 (2012).

not do so, focusing on microeconomic aspects of the law almost exclusively. The near-complete absence of macroeconomic analysis in these fields, more than ten years after the advent of the Great Recession, implies that developments in macroeconomic history alone do not fully account for the relative absence of law and macroeconomics within law and economics.

E. Law and Macroeconomics Outside of Regulating the Money Supply and Conducting Fiscal Policy

Monetary and fiscal policy, examined in the last two subparts, are the most conventional tools in the macroeconomic policy toolkit. Laws and regulations in other areas offer additional tools to combat recessions, despite being underutilized. For example, as I describe elsewhere,[50] regulated utility prices have similar effects to taxes. If utility prices were held down in recessions and allowed to rise more in booms, then overall spending would likely increase when unemployment is high—exactly what Keynesian policy prescribes. Many other areas of law, such as bankruptcy, the law of remedies, land use law, environmental law, and labor and employment law, show similar promise as tools of Keynesian aggregate demand management.

Law and macroeconomic analysis of these fields is in its infancy—even after the Great Recession. Although the academic study of law and macroeconomics outside of financial regulation and fiscal policy is underdeveloped, many different jurisdictions have implemented such policies. In China, for example, business-cycle-sensitive regulation is a core part of macroeconomic policy.[51] And, as described above,[52] regulation and debt forgiveness formed an essential part of the U.S. government response to the Great Depression and the Great Inflation. To improve the effectiveness of these interventions, law and economics scholars will need to address them for what they are—macroeconomic interventions—rather than simply pointing out their microeconomic weaknesses.

But the frequency of these policy interventions, and thus the urgency of law and macroeconomic analysis, will likely depend on future macroeconomic events.

V

THE ROLE OF CHICAGO AND IDEOLOGY

Although the Great Moderation explains the lack of interest in law and macroeconomics in the 1980s, 1990s, and early 2000s, law and economics first

50. *See* LISTOKIN, *supra* note 10.

51. *See* Dena Sadeghian, Graham White & Patrick D'Arcy, *Macroeconomic Management in China*, *in*, RESERVE BANK AUSTL., BULLETIN: JUNE QUARTER 2013, at 11, 12–13 (Sept. 19, 2013), https://www.rba.gov.au/publications/bulletin/2013/jun/pdf/bu-0613.pdf [https://perma.cc/UZ4K-GWW4] ("The operation of macroeconomic policy in China differs from that typically used in developed economies, reflecting China's particular institutional and economic environment. Macroeconomic policy is implemented in a coordinated manner with authorities using a range of monetary, fiscal and regulatory policy instruments to achieve economic objectives.").

52. *See supra* Part I.A.

developed in the 1960s and 1970s. In this early period, the memory of the Great Depression and the prominent role of Keynesian macroeconomics remained fresh.[53] And in the 1970s, of course, the Great Inflation kept macroeconomics in the spotlight. In examining law and economics in the 1960s and 1970s, we cannot ascribe the lack of development of law and macroeconomics to stable macroeconomic conditions.

What, then, explains why law and microeconomics, and not law and macroeconomics, took off? The University of Chicago was the place more responsible for the growth of law and economics than any other. The University of Chicago Law School was the home of many of the field's founders, including Ronald Coase, Richard Posner, and Aaron Director. In addition to being intellectual pioneers, Coase, Posner, and Director were also intellectual entrepreneurs who helped popularize law and economics analysis. Director founded and Coase co-edited the first journal in the field: the *Journal of Law and Economics*.[54] Posner then founded and edited the field's second forum, the *Journal of Legal Studies*.

Coase, Posner, and Director examined law from a microeconomic perspective. Their proclivities were likely enhanced by the sustained interest in law demonstrated by two prominent Chicago micro-economists and Nobel Prize winners, Gary Becker and George Stigler. Indeed, Stigler was one of the colleagues who drew Posner to Chicago from Stanford.[55] Future Nobel Prize winners with considerable credibility within economics, Stigler's and Becker's support lent instant credibility to the nascent field.

If any would-be Posners at Chicago had developed an interest in the macroeconomics, by contrast, then their economics department colleagues likely would have discouraged rather than encouraged them. The dominant macroeconomist in the Chicago economics department at the time was Milton Friedman—also a future Nobel Prize winner. Friedman espoused "monetarism": the view "that monetary policy is more potent and useful than fiscal policy for stabilizing the economy."[56] If fiscal policy was unnecessary for macroeconomics, then law and regulation were beyond the pale. Indeed, monetarists harshly criticized the most important experiment in 1970s law and macroeconomics—Nixon's wage and price controls—"because these would create market distortions."[57] Instead, monetarists like Friedman argued for limitations to the money supply as the best cure for the Great Inflation.[58] To monetarists, using law for macroeconomic ends was a harmful sideshow, doomed to distort markets

53. *See supra* note 24.

54. *Aaron Director, Founder of the Field of Law and Economics*, THE UNIV. OF CHI. NEWS OFFICE (Sep. 13, 2004), http://www-news.uchicago.edu/releases/04/040913.director.shtml [https://perma.cc/Z6YH-KMEY].

55. WILLIAM DOMNARSKI, RICHARD POSNER 57–58 (2016).

56. Bennet T. McCallum, *Monetarism*, ECON. LIB., https://www.econlib.org/library/Enc/Monetarism.html [https://perma.cc/XQY9-VCL4].

57. *Id*.

58. *Id.*

without improving outcomes.[59] Chicago, the hotbed of early law and economics, was thus far more conducive to the development of law and microeconomics than law and macroeconomics from an intellectual perspective.

Macroeconomic history also played a role. The primary macroeconomic problem of the 1970s—inflation—was ill-suited to legal and regulatory solutions. As the failure of price controls demonstrated, the approaches of law and regulation do not offer a long-term solution to inflation. Law and macroeconomics thus proved naturally unattractive to scholars writing in the 1970s. Law and regulation, however, can stimulate economies and reduce unemployment when monetary policy proves unable to stimulate due to the zero lower bound or other constraints, as occurred during the Great Depression and Great Recession.[60] Today's more Keynesian-friendly macroeconomic conditions are thus a much more plausible ally to the development of law and macroeconomics than the macroeconomics facing the early law and economics scholars working at Chicago.

Ideology contributed to the spread of the law and microeconomics initially developed at Chicago. Chicago law and economics, with its emphasis on the elimination of market-impeding imperfections, proved attractive to conservative philanthropic organizations such as the Olin Foundation.[61] As one scholar of philanthropy explained:

> Staff members at the Olin Foundation noted that lawyers tend[ed] to play influential roles in various segments of society. The Foundation consequently provided substantial funding to shape the intellectual climate in the legal realm to embrace free market insights through the study of economic implications of law . . . . [L]aw and economics and economics was an accepted paradigm in legal scholarship in the 1970s, but its use was limited. The Foundation perceived an opportunity to spread its adoption in legal scholarship and among current and prospective legal practitioners.[62]

The Olin Foundation contributed more than $50 million to support microeconomic analysis of the law.[63] This support played a critical role in expanding law and economics' influence. For example, the Olin Foundation and the similarly-minded "Liberty Fund" funded free multiday law and economics education seminars that helped spread microeconomic reasoning throughout the

59. From the late 1970s onward, macroeconomics at the University of Chicago was dominated by the "real business cycle" approach, often associated with Chicago macroeconomist Robert Lucas (another Nobel Prize winner). The real business cycle approach attributes the business cycle to "technology shocks" that stimulate changes in labor supply and capital accumulation. In real business cycle theory, recessions are not inefficient. Therefore, there is no reason for policy to mitigate them. As a result, there is no place for macroeconomically motivated changes to law, which will cause microeconomic harm for no macroeconomic benefit. For a review of real business cycle theory, see generally N. Gregory Mankiw, *Real Business Cycles: A New Keynesian Perspective*, 3 J. ECON. PERSP., no. 3, Summer 1989, at 79.

60. *See* Listokin, *supra* note 10, at chs. 9–11.

61. *See* Steven Schindler, *Revolutionizing Legal Discourse: Law and Economics*, *in* JOEL L. FLEISHMAN ET AL., CASEBOOK FOR THE FOUNDATION: A GREAT AMERICAN SECRET 148, 150 (2007).

62. *Id*. at 150.

63. *Id.* at 149.

legal academy and judiciary.[64] And it is almost impossible to imagine the Olin Foundation or the Liberty Fund providing similar support to law and economics had it been focused on macroeconomics, which emphasizes a fundamental market failure (widespread unemployment) at the heart of modern economies and so cannot avoid market regulation.[65]

VI

CONCLUSION: THE FUTURE OF LAW AND MACROECONOMICS

The remarkable success of law and microeconomics provides another obstacle to the development of law and macroeconomics. Law and microeconomics enjoys the benefit of a large foundation of knowledge. Many legal scholars have invested the time to acquire basic microeconomic skills. They understand the language of law and microeconomics. But this base of knowledge does not extend to macroeconomics, which asks different questions and requires a different skill set. Law and macroeconomics will therefore require scholars to develop new skills—always a hard task when the benefit is uncertain.

I thus conclude with a prediction. Law and macroeconomics' future depends on three things: The subfield will thrive (1) if macroeconomics remains an urgent part of the economic policy discourse, (2) if the field receives support and recognition from macroeconomists seeking to understand the role of law in their fields, and (3) if macroeconomic education for lawyers (which should likely also consider the role of inequality) receives the kind of sustained support that so benefited law and microeconomics.

64. *Id.*; *see also* Henry Manne, *How Law and Economics Was Marketed in a Hostile World: A Very Personal History*, *in* THE ORIGINS OF LAW AND ECONOMICS: ESSAYS BY THE FOUNDING FATHERS 309, 318–20 (Francesco Parisi & Charles K. Rowley eds., 2005); Elliott Ash, Daniel L. Chen & Suresh Naidu, Ideas Have Consequences: The Impact of Law and Economics on American Justice (Mar. 20, 2019) (unpublished) (describing the effects of these free seminars on judicial decision-making).

65. For an in-depth discussion of the Olin Foundation's role in funding the rise of law and economics, see STEVEN M. TELES, THE RISE OF THE CONSERVATIVE LEGAL MOVEMENT 181–219 (2008).