GENERAL DISCUSSION Four presenters—Maurice Obstfeld, John Van Reenen, Donald Kohn, and Thomas Philippon—spoke in turn. After the conclusion of Philippon's presentation, Van Reenen spoke first. He wondered about the political question of why people vote the way that they do. He did not buy the argument that economics has nothing to do with how people vote; people have a whole mixture of reasons for voting as they do. Identity was a main factor in why people voted as they did regarding the United Kingdom's decision to leave the European Union, as were strong feelings toward immigration. But economics was also important, Van Reenen argued. For most people, what matters materially to their well-being is important; and for economists, thinking about how the message gets out about the economics is key. He was not convinced that the voters did not know that there was an academic consensus on Brexit. Speaking about the economists in the room, he noted that "we think there is a consensus because we read these things all the time; but when I go around and talk to people, they do not hear the same things." The information they get does not have such a strong signal. There is a real issue about information and the media, which plays into this debate, and economics does matter, he concluded.

Responding to Van Reenen, Narayana Kocherlakota pointed to research by Paola Sapienza and Luigi Zingales that asked respondents what they thought about specific economic issues *after* priming them with a statement that nearly all economic experts agreed on the issue.[1] Respondents' answers to a wide range of economic questions did not change significantly when confronted with the economists' consensus. This research suggests that the public's mistrust of experts is not a phenomenon new to Brexit. Just because economists say something is true does not mean that everyone immediately believes them.

Further building on the points made by Van Reenen and Kocherlakota, Raquel Fernandez noted that the wide heterogeneity in what economists were forecasting about Brexit makes it more than just a problem of the media. Economists' quantitative, macroeconomic models, she suggested, are more of an art than a science; and economists diminish their own credibility when they do not admit this up front. And as for the political economy of Brexit, according to Fernandez's recollection of the poll evidence, the United Kingdom's vote to leave the European Union was not concentrated in those regions of the country with necessarily a larger stock of

1. Paola Sapienza and Luigi Zingales, "Economic Experts versus Average Americans," *American Economic Review* 103, no. 3 (2013): 636–42.

immigrants, but rather where there were more *newly arrived* immigrants. She wondered if there was some sort of failure of the state with regard to the public provision of services. Was it true that the state had to some extent abdicated some of its role over the last 10 to 15 years? And for better or worse, was this being blamed on globalization and, more concretely, on immigration?

N. Gregory Mankiw noted that, according to a body of political science literature on voter attitudes toward trade and outsourcing, what makes one opposed to trade is not a concern about being particularly hurt by it, but rather one's psychological worldview—particularly one's sense of nationalism. In the United States, there is a belief among some that Americans are in a sense better than other people, and therefore that Americans should stick to themselves; this is a sense of isolationism, broadly speaking—of not wanting to coordinate not only on trade issues but also on all global issues. These issues are also correlated with education, Mankiw added; people with less education are more likely to have this psychological worldview. He believed that this same sort of thing happened with Brexit. For instance, there is a very strong correlation between education levels in the regions of the United Kingdom and how people voted; people with lower levels of education were much more likely to vote to leave the EU, and people with higher levels were most likely to vote to remain. He suspected that those voters with lower levels of education had more xenophobic, nationalist, or isolationist worldviews, and that they were probably not the kinds of people who were most likely to say that they really wanted to know what economists thought of the issue.

Valerie Ramey contended that the average voter thinks about migration differently than how he or she thinks about trade, and that migration was the more important issue in the U.K. vote to leave the European Union. Even if, on balance, migration has very positive effects, people often have future political effects in the back of their minds. For example, the unfettered migration of Europeans to North America starting in the late 15th and early 16th centuries worked out badly for Native Americans, and the encouragement of U.S. migration to Texas in the mid-1800s eventually led to the annexation of Texas, which worked out badly for Mexico.

Carol Graham was in the United Kingdom at the time of the Brexit vote, and she noticed marked similarities between the attitudes there and the desperation of poor white people in the United States. There is a winners-versus-losers phenomenon vis-à-vis globalization that is not yet fully understood by policy experts. People are voting with the fear of downward mobility in mind; they are not looking at GDP growth rates, for instance.

Support for Brexit in the United Kingdom and support for President-elect Donald Trump in the United States came from places with fewer migrants. In the United States, mortality rates are rising in the least diverse places—hollowed-out, white, poor and middle-class places—and there seems to be a sense that the more diverse, more educated parts of the population are getting ahead. In the United Kingdom, there was also a voting divide between young and old; a whole generation of young people grew up being part of the European Union, and now this will be gone. These sorts of disconnects are not fully understood by policy experts, and the political implications are frightening, she concluded.

Betsey Stevenson believed that the situation might be even worse than people not *caring* what economists think: People do not *trust* economists. Trust in institutions now is quite low, she noted, and it fell a lot during the Great Recession. Although one would have expected this trust to have begun rising as economic conditions have improved, this has not been observed in the United States. Mistrust in institutions appears to have extended to mistrust in economists, which has led to a rebellious attitude. She was worried that this mistrust of economists is going to continue if trust in the institutions that govern does not recover.

Justin Wolfers took issue with the notion that Brexit was somehow an embarrassment for economists and for economics as a whole. Instead, what Brexit revealed was people's preferences about their willingness to pay for loyalty—what he called their "tribal identity." In Ann Arbor, Michigan, just as in the United Kingdom, there is a dislike for people across the border—that being Ohio State University, he joked. Tribal identities matter so much that people are willing to pay $500 to see a football game between Ohio State University and the University of Michigan. For a middle-class family, this could constitute almost 3 percent of annual income, just to sustain the hate. He stated that this all fits perfectly with the characteristics Mankiw described; the people who do this are less educated and more isolationist. Suppose a man of average means pays $400 for front-row seats to an Ohio-versus-Michigan football game. Many economists might judge this decision to be foolish; and the public understands this but supports the decision anyway. The point is not that the man was not a credible messenger; it is that people are very willing to pay for this particular tribal identity.

Frederic Mishkin shifted the conversation to the question of financial stability, which was the focus of Donald Kohn's presentation. In a situation like Brexit, an important determinant of this stability is what central banks do in response. He noted that the Bank of England's response to the Brexit vote was a classic example of a central bank being ahead of the curve; as soon as the vote was announced, the Bank of England indicated that there would be a backstop to the system. This announcement had a huge impact, and it was one of the reasons Mishkin thought the vote's very short-term macroeconomic effects had been mild. In a nod to Kocherlakota's paper in the present volume—"Rules versus Discretion: A Reconsideration"—Mishkin stated that the Bank of England's response to the vote was a classic example of why slavishly following monetary policy rules—or even being encouraged to do so by legislation—is such a bad idea. In the face of a highly consequential economic event such as Brexit, the central bank needs to react very quickly; and the faster it reacts, the less it needs to do. If the Bank of England had been subordinate to a Taylor rule, Brexit's economic consequences might have been much worse, he concluded.

Alan Blinder recalled that when the news of the Brexit vote hit, the first thing that occurred to him was the pervasive uncertainty created by its outcome. Since the final negotiations for Brexit were presumably still about two years away, this should in principle cause things to freeze in place. He wondered what the effects of this uncertainty would be on investment and foreign direct investment. He pointed to early research by Ben Bernanke that examined the potentially large effects relative to the steady state.[2]

Robert Gordon stated that in talking about Brexit, there is a tendency to ask what is going to happen to tariffs on U.K. exports to the European Union after the renegotiations have been completed. But he thought another angle to this story had not been sufficiently considered. There is a view that the dominant force in the U.K. trade balance is the capital account, and that the current account adjusts endogenously in response to the capital account, with the lever whereby this happens being the exchange rate. He contended that it would be very likely in some future world for an increase in tariffs imposed by the European Union on the United Kingdom to be offset by a depreciation of the British pound, and thus there would not be significant employment effects; rather, there would be reductions in U.K. consumers' standard of living due to higher import prices. The United Kingdom has a particular problem that is not confronted by, say, Norway: London's enormous exports of financial services to the rest of the European Union. In the event of a full Brexit, Gordon believed that the major effect on these exports would be quantitative restrictions on financial services, rather than tariffs on goods.

2. Ben S. Bernanke, "Irreversibility, Uncertainty, and Cyclical Investment," *Quarterly Journal of Economics* 98, no. 1 (1983): 85–106.

Following up on Gordon's comments, Martin Baily wondered if any of the presenters had a view on Brexit's impact on the future of the financial services sector in the United Kingdom, and in London in particular, which is seen as the hub of Europe's financial services sector. Financial services account for about 10 percent of Britain's GDP and about 10 percent of its tax revenue. It seems likely that the financial services sector would be reduced in size due to the Brexit decision—probably not right away, but gradually. Where will these financial services go? And what will the effect be on U.K. living standards? He suspected that some financial services activity would relocate to the United States, but the European Union might want to establish an alternative financial hub.

Gert Peersman expressed some optimism about Brexit, citing the problems associated with the eurozone's common currency, the euro, which is used by most EU members. The common currency has not functioned well because of anti-integration sentiments between the different member countries, and the United Kingdom—of course, not a euro user—has always been against more integration within Europe. And now that the United Kingdom has voted to leave the EU, Peersman wondered if this might present an opportunity for the remaining member countries to improve integration. If they did, then the EU might function better than it now does.

Caroline Hoxby also had a more optimistic view that others in the room. Without doubting many of the economic analyses that cause concern among economists, she wanted to talk through some of the logic of Brexit. First, she contended that the average quality of U.K. economists and policymakers is at least as high as, if not higher than, in the rest of the European Union. Second, she argued that regulation of labor markets and financial markets in the United Kingdom is arguably superior to that in the rest of Europe. Third, she believed that U.K. political institutions enjoy a lot of confidence around the world. This does not mean they are perfect, she noted; but people tend to have more confidence in them, on average, than in the parallel institutions of many other EU countries. Fourth, she contended that no continental EU financial industry enjoyed as much confidence as the City of London's. Fifth, she argued that with the vote to leave the EU finalized, U.K. policymakers would presumably be freed up to be wholly oriented toward U.K. economic interests in a way that they had not been before the vote.

Hoxby objected to the assumption that U.K. economists and policymakers would respond inoptimally to the post-Brexit environment. Just as the Bank of England responded well to the Brexit vote, so would U.K. economists and policymakers on other matters. Why shouldn't they conduct trade negotiations cleverly? Why shouldn't they do everything possible that they can unilaterally do to maintain trade? Why can't they unilaterally adopt laws and regulations that make the financial industry most likely to stay in the City of London? Hoxby refused to believe that U.K. economists and policymakers are going to act stupidly simply to ensure that their dire predictions about Brexit are borne out. Moreover, she believes that policymakers in the European Union will get over their current angry, punitive mode and make decisions that are mutually beneficial, such as maintaining free trade. Gains from trade benefit both the United Kingdom and the rest of the European Union. A trade war initiated by grumpy EU countries would be self-punishing.

Steven Davis joined Hoxby in "sounding a few notes of discord." First, it was not obvious to him that the European Union has been an exemplar of good governance and policymaking. For instance, there have been protracted difficulties in responding to the sovereign debt and banking crises in Greece—which are connected in part, but not entirely, to the common currency—to the immigration crisis, and so on. From the perspective of a U.K. voter, it is not obvious why he or she would want Britain to be an EU member long term. Second, Davis did not hear much discussion of any clear evidence that, thus far, the Brexit referendum has had much in the way of negative economic consequences. Has one seen—even in firms that should theoretically be especially exposed to Brexit's risks—declines in price–earnings ratios? Have such declines persisted? Has one started to see a withdrawal of investment or foreign direct investment in sectors that would be especially exposed to Brexit? Perhaps there is such evidence, Davis noted, but he has not seen much of it. Third and finally, he thought that economists and policymakers alike should seek to better understand voters' motivations so they can frame their arguments in ways that address them.

Maurice Obstfeld reiterated that there should be no doubt that the main issue for the U.K. voters was migration and its perceived consequences—and there is a broader problem for the rest of Europe that serves as a lesson here. An essay written back in 1996—historian Tony Judt's "Europe: The Grand Illusion"—warned that many people in Europe could perceive the pan-European institutions as good for mobile elites but not for others, those he described as "the linguistically, educationally, or culturally disadvantaged, underprivileged, or despised Europeans who don't live in golden triangles along vanished frontiers."[3] This tension will eventually cause a

3. Tony Judt, "Europe: The Grand Illusion," *New York Review of Books* 43, no. 12 (July 11, 1996).

backlash. Obstfeld did not think that economics does not matter, but he did believe that this cultural tension and backlash potential alter the cost–benefit evaluation of policies and institutions in a fundamental way, so that concerns about migration, sovereignty, and the like are very important. He encouraged everyone to read or reread Judt's very prescient essay.

Van Reenen made two points. First, in response to the optimism of Hoxby and Davis, he did not believe that the benefits of Brexit would be great for the United Kingdom. On the regulatory front, the United Kingdom successfully opted out of some of the EU's most onerous regulations, and thus it already has the most flexible labor market in the world next to that of the United States. The degree to which Brexit could make the U.K. labor market even more flexible, then, is limited. In terms of the negotiations, he noted that the United Kingdom has a disadvantage in its leverage; about 45 percent of U.K. exports go to the European Union, while only about 9 percent of EU exports go to the United Kingdom. He believed that this shortage of negotiating leverage by the United Kingdom would affect the final deal.

Second, on the broader political aspects of Brexit, Van Reenen noted that around the world—including in the United Kingdom—there has been a huge hit to the wages of average people since the Great Recession; between 2008 and 2014, the average real wage fell more than 8 percent, the biggest sustained fall since the 1920s. This is a huge hit for the average person who is relatively wealthy, and has made people angry. This anger, he believed, had been successfully manipulated by many politicians and thus directed toward immigrants, despite the fact that the huge wave of immigrants into the United Kingdom has actually been a benefit. Because average European immigrants are educated and likely to be able to work, they typically pay more in taxes than they take in welfare; in fact, immigrants to the United Kingdom actually pay more into the welfare system than the average U.K. citizen. Van Reenen noted that since about 2010, the United Kingdom has been subject to severe austerity measures, which have made seeing a doctor or getting one's child into school more difficult. These effects have been successfully blamed on immigrants, he explained, in the same way that people feel that unemployment is high or wages have fallen because of immigrants; but in reality, these things have nothing to do with immigrants and everything to do with the financial crisis. He believed that populist politicians in the United Kingdom were able to influence the vote somewhat by heaping the blame on immigrants, and that this theme of rising populism around the world is cause for concern.

Following up on the theme of rising populism, Kohn thought that populism is partly a response to a sense that the people in power are making decisions for which the voters had not voted. With respect to the United Kingdom, people thought that EU leaders in Brussels were making decisions that affected them, and they did not have a say; this sovereignty, they believed, should reside in the national governments. On Peersman's point about integration, Kohn thought that increased integration without fundamental political reform and political buy-in by the people of Europe would end up being counterproductive by feeding the populist revolt against the elites who make decisions in which the people have no say. On Blinder's question about uncertainty and the effect on foreign direct investment and investment in general, Kohn stated that there was much emphasis by experts—many of whom referenced Bernanke's work—on how uncertainty postpones investment decisions. There is some anecdotal evidence—at least in commercial real estate, and particularly in cities—that major investments have at least been put on hold, but hard data on the matter are not yet available.

Despite the optimism of some of the discussants, Thomas Philippon was not convinced. On Peersman's point, he stated that there simply is no appetite for an ever-increasing European Union. The United Kingdom will certainly see more fiscal integration, but the best one can hope for is more tax harmonization, which is already in the remits of the European Commission. Europeans actually do want more integration vis-à-vis security, but they do not want any kind of supernational economic policy. Philippon agreed that the United Kingdom has a superior regulatory system; from the perspective of financial stability, the United Kingdom's staying in the European Union would have been preferred. However, the political class in the United Kingdom is a disaster; the political left has completely disappeared, and the political right has been split down the middle. He feared that the U.K. Civil Service might be put in charge of the Brexit negotiations, which would make it very clear that the United Kingdom would not have access to the Single Market, since it would be against the Treaty of the European Union; other European countries would need to revise the treaty so that the United Kingdom would have access to the Single Market, which he believed was implausible. There would not be a soft option either, because that would mean needing to accept migration, which is one of the key reasons the United Kingdom voted to leave in the first place.

Besides the fact that the United Kingdom has been delaying Article 50, which may be annoying for the European Union in the short term, Philippon did not believe there was any mood of punishment or punitive reaction against the United Kingdom within the European Union, as Hoxby had suggested. In response to Baily's question about what Brexit means for the City of London and its financial services sector, Philippon said that this is hard to know; but he believed there was no possible scenario whereby London would not remain Europe's main financial center. A significant number of financial services will probably migrate out of London to cities like Frankfurt, Paris, and Dublin—and the extent of this migration is unknown—but Philippon was confident that London will remain the continent's main financial center.