Input Output Analysis, quo vadis?

Topic:
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INPUT-OUTPUT ANALYSIS QUO VADIS?

As early as in his Presidential Address to the American Economic Association in 1970 Wassily Leontief had warned the economics profession of being in danger of taking the wrong road. His warnings were echoed by several contemporary commentators who argued that parts of modern economics share some responsibility for the current financial and economic crisis. Severe economic crises request the economics profession to reconsider its doctrines, abandon views that can no longer be sustained, return to views that can, or create new ones appropriate to the situation under consideration. As an integral part of economics, input-output analysis cannot possibly avoid to respond to this request. It is argued that input-output analysis is a child of the classical approach to the theory of production, income distribution and relative prices. This is illustrated in terms of two papers by Leontief: In his 1928 maiden paper he adopted a circular flow framework and explained relative prices in terms of the distribution of the surplus product amongst different social classes. In his 1985 paper he dealt with the problem of technological change and the involved choice of technique problem in strictly classical terms. It is shown that in such a framework there is no presumption that the amount needed of a particular input per unit of a particular output will fall with an increase of the price of the input, or at most stay the same. Hence the conventional concept of "substitution" between inputs need not hold and the equally conventional downward sloping demand function for an input cannot generally be sustained. It is argued that this fact has nothing to do with the well-known phenomena of "reswitching" of techniques and "capital reversing", but is of much wider importance. This has important consequences for economic theory and applied economics, including input-output analysis.