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MACROECONOMICS AFTER KALECKI AND KEYNES

Post-Keynesian Foundations

(Edward Elgar 2023)

Chapter 2

**'INTRODUCTION TO POST-KEYNESIAN
ECONOMICS: METHODS, HISTORY, CURRENT
STATE AND PERSPECTIVES'**

Content

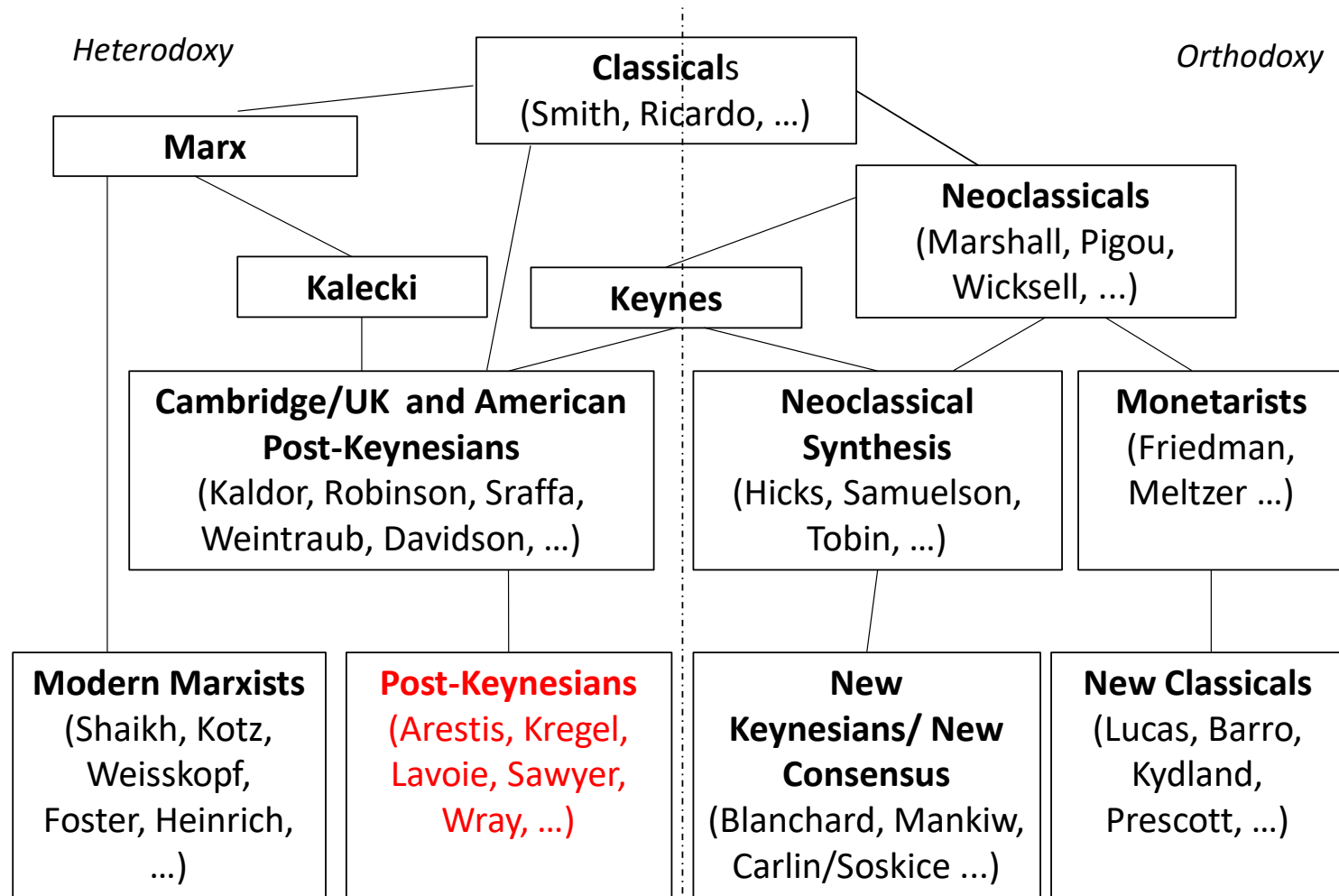


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2.1 INTRODUCTION

Figure 2.1 Heterodox and orthodox schools in macroeconomics



Source: Based on Hein (2019b, p. 240)



2.2 HETERODOX VS. ORTHODOX ECONOMICS



Heterodoxy: Realism

- Objective of economics is to tell relevant stories and to explain actual working of the economy in the real world
→ start with „stylized facts“ (Kaldor) rather than hypothetical idealistic position or assumptions

Orthodoxy: Instrumentalism

- Economic hypothesis is sound, if it allows for calculation of equilibrium and accurate prediction (M. Friedman)
→ start with first principles (utility and profit maximisation, given endowments, perfect competition)

Heterodoxy: Environment-consistent rationality, satisficing agent

- Individuals face severe limitations in their ability to acquire and process information, because the latter maybe simply non-existent (known unknowns, unknown unknowns)
 - expectations based on radical uncertainty (different from probabilistic risk)
 - norms/institutions (conventions, customs, rules of thumb) as rational responses

Orthodoxy: Hyper model-consistent rationality, optimising agent

- Individuals possess quasi-unlimited knowledge and ability to calculate economic outcomes applying the ‚true‘ model (perfect information, rational expectations)

Method

Heterodoxy: Holism/organicism

- Individuals are social beings under the influence of their environment (culture, class, gender, institutions, history)
→ micro-macro paradoxes

Orthodoxy: Individualism/atomicism

- Analysis starts from pre-social individual and his/her preferences
→ representative agent as a utility and/or profit maximiser under constraints
→ microfoundation of macroeconomics (and of institutions)



Economic core

Heterodoxy: Production and growth

- Creation of scarce resources by means of accumulation of (part of) the surplus and technical progress (classicals + Marx), reproduction prices, utilization of resources, because economy usually operates below full utilization (Kalecki, Keynes)

Orthodoxy: Exchange, allocation + scarcity

- Efficient allocation of scarce resources (Robbins), prices reflect scarcity, exchange as the starting point of economic analysis, production + growth as an extensions



Political core

Heterodoxy: Regulated markets

- Individuals markets generate instabilities irrespective of price (in-) flexibility, unacceptable inequalities and inefficiencies; free markets are impossible, tendencies towards oligopoly + monopoly; market regulation and aggregate demand management by the state are required

Orthodoxy: Unfettered markets

- Perfect markets (perfect information, flexible prices) generate optimal results, state intervention generates inefficiencies, exception: external effects, natural monopolies, ...



2.3 STRANDS OF POST-KEYNESIAN ECONOMICS AND BROAD COMMONALITIES

Strands of post-Keynesian economics (‘big tent’)



- **Fundamentalist** (Keynes, older J. Robinson, Minsky, Shackle, Weintraub): fundamental uncertainty, the features of a monetary production economy, financial instability, method
- **Kaleckians** (Kalecki, Steindl, younger J. Robinson): cost-plus pricing, class conflict, effective demand, income distribution and growth
- **Kaldorians** (Kaldor, Harrod, Goodwin, Godley): growth, productivity regimes, open economy constraints to growth, economic and the financial system
- **Sraffians/neo-Ricardians** (Sraffa, Garegnani): prices of production in multi-sectoral systems, choice of techniques, capital theory, long-period positions of the economy, supermultiplier models
- **Institutionalists** (Veblen, J.K. Galbraith, Lerner, Eichner): pricing, the theory of the firm, monetary institutions, behavioural and labour economics



Core claims of PK economics

1. - 5. **presuppositions of heterodox economics**

+

6. non neutrality of money in the short and in the long run the focus on a **monetary theory of production** (Keynes 1933) in which **money is non-neutral** in the short and the long run, i.e. money is not a veil;
7. the dominance of the **principle of effective demand in the short** (Kalecki 1932, 1933, 1935, 1939, Keynes 1933, 1936) **and the long run** (Kalecki 1943, 1954, Kaldor 1957, Robinson 1956, 1962, Steindl 1952), investment creates its corresponding saving via income, growth and/or distribution effects;



Core claims of PK economics

8. the importance of the notion of **fundamental uncertainty**, which is different from probabilistic risk ('we simply do not know', Keynes 1937);
9. the insistence that economic processes take place in **historical and irreversible time** (Robinson 1962)– and are thus largely **path dependent**, hence no pre-determined NAIRU or potential growth ('long run trend is but a slowly changing component of a chain of short-period situations', Kalecki 1971);
10. the importance of distributional issues and **distribution conflict** for economic outcomes (output, employment, inflation, growth).



Table 2.1 Ten main features of post-Keynesian economics

Five pre-suppositions	Five core claims
1. Epistemology/Ontology: Realism	6. Non-neutrality of money in the short and in the long run
2. Rationality: Environment consistent rationality and satisficing agents	7. Principle of effective demand in the short and in the long run
3. Method: Holism and organicism	8. Fundamental uncertainty
4. Economic core: production and growth	9. Historical and irreversible time, path dependence
5. Political core: regulated markets	10. Distribution conflict



2.4 STAGES OF DEVELOPMENT OF POST-KEYNESIAN ECONOMICS



2.4.1 The 1930s and 1940s

- Kalecki's (1932, 1933, 1935, 1939, 1943a) and Keynes's (1933, 1936) revolution in macroeconomics, determination of output and employment, involuntary unemployment and the trade cycle
- Economic policies to overcome short- and long-run effective demand failures, recessions, stagnation and involuntary unemployment (Kalecki 1943b, 1944, Keynes 1943)
- Future of the international currency system after World War II (Kalecki/Schumacher 1943, Keynes 1942)
- Harrod (1939) and Domar (1946): capacity effects of investment and their impact on long-run stability of growth, also Kalecki (1939, 1943, 1954)
- Lerner (1943) functional finance
- Domar (1944) stability condition for government debt dynamics



Table 2.2 Short biography of Michal Kalecki

- 22.6.1899: Born in Lodz, Poland
- 1917: Bachelor's degree in engineering
- 1921: Gdansk Polytechnic, studies in engineering, private studies on Tugan-Baranowsky and Luxemburg
- 1924: Left university without degree, work as a business journalist
- 1929: Research Institute of Business Cycles and Prices, Warsaw
- 1930: Marriage with Ada Szternfeld
- 1933: *Essay on the Business Cycle Theory* (in Polish)
- 1935: Publications in *Revue d'Economie Politique* and in *Econometrica*
- 1936: Scholarship to travel to Sweden and England
- 1937: Cambridge, first meeting with Keynes
- 1939: *Essays in the Theory of Economic Fluctuations*
- 1940: Researcher at the Oxford Institute of Statistics
- 1943: *Studies in Economic Dynamics*
- 1945: Paris, Montreal, New York: Economic Department of UN
- 1954: *Theory of Economic Dynamics*
- 1955: Return to Poland
- 1957: Chairman of the Committee for the Perspective Plan
- 1958: University professor and member of Polish Academy of Sciences
- 1963: *Introduction to the Theory of Growth in A Socialist Economy* (English in 1969)
- 1969: *Studies in the Theory of Business Cycles*
- 4.4.1970: Death in Warsaw
- 1970: *Selected Essays on the Dynamics of the Capitalist Economy, 1933-1970*
- 1972: *Selected Essays on the Economic Growth of the Socialist and the Mixed Economy*

Source: Based on information in Toporowski (2013, 2018)



Table 2.3: Short biography of John Maynard Keynes

- 5.6.1883: Born in Cambridge, UK
- 1897: School at Eton
- 1902: Student at King's College,
- 1905: Degree in mathematics
- 1905: Student of Marshall's
- 1906: Indian Office
- 1909: Fellow of King's College
- 1911: Editor of the *Economic Journal*
- 1913: *Indian Currency and Finance*
- 1915: Treasury, Member of the British delegation in Versailles
- 1919: *The Economic Consequences of the Peace*
- 1920: *A Treatise on Probability*
- 1922: *A Revision of the Treaty*
- 1923: *A Tract on Monetary Reform*
- 1925: Marriage with Lydia Lopokowa
- 1930: Member of the Economic Council of the Prime Minister
- 1930: *A Treatise on Money, 2 volumes*
- 1931: *Essays in Persuasion*
- 1933: *Essays in Biography*
- 1936: *The General Theory of Employment, Interest and Money*
- 1939: Government advisor on war finance and currency issues, Member of British delegation in Bretton Woods
- 21.4.1946: Death in Tilton, Sussex, UK

Source: Based on information in Skidelsky (2003)



2.4.2 The 1950s and 1960s

- PK distribution and growth models of the first generation, Kaldor (1955/56, 1957), Pasinetti (1962, 1974) and Robinson (1956, 1962), in which saving adjusts to investment in long-run growth at normal capacity utilisation through changes in functional income distribution
- Kaldor (1966): applied export-led growth approach focussing on sectoral and regional divergences, dynamic returns to scale, cumulative causation and path dependence in economic development
- Critique of aggregate neoclassical theory in the ‘Cambridge controversies in the theory of capital’, starting with Robinson (1953/54), fundamentally challenging the theoretical consistency of an aggregate neoclassical production, and all the results derived from this, for a more than one-good-economy (Harcourt 1969, 1972)



2.4.3 The 1970s

- ‚Romantic age‘ (Fontana 2009)
- Defining the contours of a ‘post-Keynesian’ paradigm in economics, Davidson (1972), Eichner/Kregel (1975), Eichner (1978)
- Robinson/Eatwell (1973): introductory textbook along Sraffian/post-Keynesian lines
- Foundation of journals: CJE (1977), JPKE (1978)
- Theory of the firm and pricing: Eichner (1976), Harcourt/Kenyon (1976), Wood (1975)
- Thirlwall’s (1979) balance of payments constrained growth model (Thirlwall’s law): long-run growth rate of an economy is limited or even determined by foreign income growth and by the income elasticities of exports and imports
- Minsky’s (1975, 1977): Financial instability theory: tranquility is breeding instability



2.4.4 The 1980s and 1990s

- ‚Age of uncertainty‘ (Fontana 2009)
- Work on methods, publication of some textbook-like monographs on post-Keynesian economics, Arestis (1992), Bhaduri (1986), Carvalho (1992), Chick (1983), Davidson (1982, 1994), Dutt/Amadeo (1990), Lavoie (1992), Lee (1998), Palley (1996), Reynolds (1987), and Sawyer (1985)
- Further journals: IRAE (1987), RoPE (1989)
- Theory of endogenous money (Kaldor 1982, 1985, Lavoie, 1984, 1996a, Moore 1988, 1989),
- ‘Horizontalist versus structuralist’ debate on interest rates, money and credit on the slope of money and credit supply curves (Lavoie 1996a, 1999, Moore 1989, Palley 1994, Pollin 1991, Wray 1990)
- Second generation of post-Keynesian distribution of growth models, based on the works of Kalecki (1939, 1943, 1954) and Steindl (1952), by Dutt (1984, 1987) and Rowthorn (1981): rate of capacity utilisation as an endogenously adjusting variable also in the long run
- Bhaduri/Marglin (1990), Kurz (1990), Blecker (1989): possibility of wage- or profit-led growth



2.4.5 Since the early 2000s

- Integration of distribution conflict into macro, theoretical and empirical/applied works: wage- vs. profit-led demand and growth (Blecker 2016a, Hein 2014b, Chapter 7, Lavoie 2017a, Lavoie/Stockhammer 2013a, 2013b, Stockhammer 2017)
- Kaleckian treatment of the rate of capacity utilisation as an endogenous variable beyond the short run, relevance of Harrodian instability in Kaleckian models (Hein/Lavoie/van Treeck 2011, 2012)
- Non-capacity creating autonomous demand growth, Sraffian supermultiplier process (Serrano 1995a, 1995b), in Kaleckian models (Allain 2015, Dutt 2019, Lavoie 2016a, Hein/Woodgate 2021)
- Wage dispersion and of household income inequality, household debt dynamics (Kapeller/Schütz 2015, Kim/Setterfield/Mei 2014, Prante 2017, Setterfield/Kim 2017)
- Gender and other types of segregation in post-Keynesian macroeconomics (Blecker/Seguino 2002, Braunstein et al 2011, 2020, Hein 2020, Onaran et al. 2019, Seguino 2019, 2020)



- Integrated analysis of money, finance, distribution conflict, effective demand, capital accumulation and growth and its application to changing institutional and historical circumstances, i.e. financialisation (Hein 2012a, Palley 2013, ...).
- Stock-flow consistent models (Godley/Lavoie 2007), both analytical (Hein 2008, 2012a, 2014b, Chapters 9-10) or numerical simulations in richer and more realistic large scale models (Belabed/Theobald/van Treeck 2018, Detzer 2018, ...)
- Different demand and growth regimes, both before and after the crisis, i.e. debt-led private demand boom, domestic demand-led (after the crisis stabilised by government deficits), weakly export-led and export-led mercantilist regimes (Hein 2012)
- Sources and drivers of regimes and regime changes, links with stagnation tendencies since the Global Financial Crisis and the Great Recession 2007-09 (Hein 2019a)
- Several links with CPE and IPE (Hein/Paternesis/Meloni 2021, Hein/Martschin 2021, Köhler/Stockhammer 2021, Stockhammer 2021)



- Minskyan models on financial and economic crises (Charles 2008a, 2008b, 2008c, 2016, Dafermos 2018, Kapeller/Schütz 2014, Lima/Meirelles 2007, Nikolaidi/Stockhammer 2017, Ryoo 2013, 2016, Stockhammer/Michell 2017)
- Ecological constraints and macroeconomic stability (Cahen-Fourot/Lavoie 2016, Fontana/Sawyer 2013, 2016); stock-flow-fund ecological macroeconomic model and socio-economic and – ecological transition (Dafermos/Nikolaidi/Galanis 2017)
- International and development economics: further developments and applications of Thirlwall's (1979) Law (Blecker 2016b, McCombie 2011, 2019, Setterfield 2011, Thirlwall 2011, 2013, 2019)
- Currency hierarchy and development (Fritz/De Paula/Prates 2018, De Paula/Fritz/Prates 2017, Herr/Priewe 2006 Priewe/Herr 2005, Priewe 2008)
- ...



- Further textbooks or textbook-like monographs: Blecker/Setterfield (2019), Dimand/Hagemann (2019), Harcourt/Kriesler (2013), Hayes (2006), Hein (2014b), Hein/Stockhammer (2011a), Heine/Herr (2013), Holt/Pressman (2001), Jespersen (2009), King (2012a, 2015), Łaski (2019), Lavoie (2006a, 2014), Mitchell/Wray/Watts (2019), Prante/Bramucci/Hein/Truger (2020), Rochon/Rossi (2016, 2017b), Tily (2007), Wray (2012).
- Several intellectual biographies: Lopez G./Assous (2010) and Toporowski (2013, 2018) on Michal Kalecki, Davidson (2007), Dostaler (2007), Hayes (2019) and Skidelsky (1983, 1992, 2000, 2003) on John Maynard Keynes, Harcourt/Kerr (2009) on Joan Robinson, King (2008a) on Nicholas Kaldor, Neilson (2019) on Hyman Minsky, Perez Caldentey (2019) on Roy Harrod, and Roncaglia (2009) on Piero Sraffa
- Books on the history of post-Keynesian economics: Harcourt (2006), King (2002), Pasinetti (2007).
- New journals: EJEEP: Intervention (2004 as Intervention: JoE), RoKE (2012).



2.5 THE CURRENT STATE OF POST-KEYNESIAN ECONOMICS



2.5.1 Macroeconomic policy relevance

PK alternative theories:

- Output, employment and unemployment;
 - Distribution, growth and technical change;
 - Money, credit and finance;
 - International money and finance;
 - Financialisation, financial instability and crisis;
 - European economics and economic policies;
 - Development and emerging market economics
-
- Foundations for critique of dominant mainstream NCM since the late 1990s/early 2000s, even well before the 2007-09 crises
 - Full scale PK alternative model and policy mix (Arestis 2013, Hein/Stockhammer 2009, 2010, 2011b)
 - Specified for the special conditions of the Eurozone (Arestis/Sawyer 2011, 2013, Hein 2018a, Hein/Detzer 2015a, 2015b, Hein/Martschin 2020, Hein/Truger/van Treeck 2012)
 - US: MMT (Kelton 2020, Mitchell/Wray/Watts 2019, Wray 2012)



	NCM	PKM
Monetary policy	Inflation targeting by means of interest rate policies, which affects unemployment in the short run, but only inflation in the long run	Target low interest rates which mainly affect distribution, and stabilise monetary, financial and real sectors by applying other instruments (lender of last resort, credit controls, ...)
Fiscal policy	Supports monetary policy in achieving price stability by balancing the budget over the cycle	Real stabilisation in the short and in the long run with no autonomous deficit targets; affects distribution of disposable income
Labour market and wage/incomes policy	Determines the NAIRU in the long run and the speed of adjustment in the short run; focus should be on flexible nominal and real wages	Affects price level/inflation and distribution; focus should be on stable nominal wages, steady nominal unit labour cost growth and compressed wage structure
International economic policies	Free trade, free capital flows and flexible exchange rates	Regulated capital flows, managed exchange rates, infant industry protection, regional and industrial policies
Economic policy co-ordination	Clear assignment in the long run; co-ordination at best only in the short run	No clear assignment; economic policy co-ordination required in the short and the long run, both nationally and internationally

Source: Based on Hein (2017a, p. 154)

Macro-policy debates in post-Keynesian economics



- Monetary policy: ‚activist‘ vs. ‚parking it‘ approach to interest rate (Rochon/Setterfield 2007)? But agreement that current QE is ‚pushing on a string‘ and requires supporting fiscal policies
- Fiscal policy: functional finance? Limits to government debt? MMT (Wray 2012) and their critics (Palley 2015)
- Wage policy: Only nominal stabilisation? Or also re-distribution? Focus on wage structure instead of wage share?
- International economic policy: floating (Wray 2012) or managed/fixed exchange rates?

2.5.2 On micro and macro – and political economy



- Post-Keynesian microeconomics (King 2015, Chapter 5, Lavoie 2014, Chapters 2-3)
- Basic principles of post-Keynesian micro (King 2015):
 - decisions of firms are the driving force
 - oligopolistic or monopolistic competition
 - Fundamental uncertainty, satisficing behaviour

Neither ‘micro-foundation of macro’ nor ‘macro-foundation of macro’: ‘As Kalecki maintained, macroeconomics and microeconomics should be thought of as existing side by side, closely related to and influencing each other but also relatively autonomous and neither constituting the foundations of the other.’ (King 2015, p. 45)

- Integration of changes in micro of firm and households into post-Keynesian macro models of financialisation
- PKs have and should draw(n) on other schools of thought and social sciences: should provide macro for broader political economy

2.5.3 Post-Keynesian institutional academic infrastructure



PK survived as a contested and embattled minority in economics
Managed to develop an academic infrastructure – as part of heterodox economics in general:

- Textbooks/Intellectual biographies (s. Section 4.5)
 - Journals
 - Networks/associations/conferences/summer schools
 - Graduate programmes
- Hein (2014, 2017), Hein/Lavoie (2019), Lavoie (2011, 2014), Stockhammer/Ramskogler (2009), Fontana/Gerrard (2006)

Journals



- *Cambridge Journal of Economics*
- *Journal of Post Keynesian Economics*
- *Metroeconomica*
- *Review of Political Economy*
- *Journal of Economic Issues*
- *International Review of Applied Economics*
- *European Journal of Economics and Economic Policies: Intervention*
- *Review of Keynesian Economics*
- *Review of Radical Political Economics*
- *International Journal of Political Economy*
- *Review of Evolutionary Political Economy*
- *PSL Quarterly Review*
- *Bulletin of Political Economy*
- *Brazilian Journal of Political Economy*
- *Contributions to Political Economy*
- *Panoeconomicus*
- ...

Networks/ associations/conferences/ summer schools



- **North America:** Levy Economics Institute, annual Hyman P. Minsky/PK conferences and Minsky summer seminars in Annandale-on-Hudson, NY
- **South America:** *Brazilian Keynes Association*, annual conferences
- **Australia:** PKs as main organisers of and contributors to the *Australian Society of Heterodox Economics (ASHE)* conferences.
- **Asia:** *Japanese Society for Post Keynesian Economics*, seminars, conferences, *Keynes Society Japan*, annual conferences
- **UK:** *Post-Keynesian Economics Society (PKES)*, annual workshops, PhD seminars and summer schools
- **Denmark:** Nordic post-Keynesian network (conferences)

Networks/ associations/conferences/ summer schools



- **France:** PK conferences at the Universities of Dijon, Grenoble, Lille, partly co-organised by the French *Association pour le Développement des Etudes Keynesiennes* (ADEK), French PKs heavily involved in the newly founded *Association Française d'Economie Politique* (AFEP), conferences and other activities
- **Spain:** University of the Basque Country in cooperation with the Cambridge Centre for Economic and Public Policy, annual conferences
- **Germany:** *German Keynes Society*, small annual conferences for German speaking participant, *Forum Macroeconomics and Macroeconomic Policies* (FMM), annual international conferences in Berlin, biennial summer schools
- **Generall:** post-Keynesians are actively involved in broader associations, as for example the *Association for Heterodox Economics* (AHE), the *European Association for Evolutionary Political Economy* (EAEPE) or the *World Economics Association* (WEA).

Graduate programmes with relevant PK content



- **Brazil:** several universities (Campinas, Rio de Janeiro, ...)
- **US:** American University, Washington, DC, the Colorado State University, the University of Massachusetts Amherst, the New School for Social Research, New York, the University of Missouri, Kansas City, and at the University of Utah, Salt Lake City,
- **UK:** Leeds University Business School, Greenwich University, SOAS London, University of the West of England, Bristol, ...
- **France:** Sorbonne Universite Paris Nord, Lille, Grenoble

Graduate programmes with relevant PK content



- **Italy:** Rome 1, La Sapienza, Rome 3, ...
- **Spain:** University of the Basque Country, Bilbao,
- **Germany:** Berlin School of Economics and Law and the HTW University of Applied Sciences Berlin
- **Erasmus Mundus Master Programme** on *Economic Policies in the Age of Globalisation* (EPOG1), *Economic Policies or the Global Transition* (EPoG+), and International Master course *Economic Policies in the Age of Globalisation* (EPOG2): Universities in Paris, University Torino, University Rome 3, the Berlin School of Economics and Law, University of Economics and Business Vienna, University of Witwatersrand as major partners, several international associated partners. <https://www.epog.eu/> and <https://epog.univ-paris13.fr/>