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The Political Economy of Keynesian Theory

Hyman P. Minsky Ph.D.

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Hyman P Minsky
Economics Department
Washington University
St Louis Mo 63130

<u>...political economy, a science which is a credit to thought because it finds laws for a mass of accidents</u>. G.W.F. Hegel

Some twenty years ago several economists came to the conclusion that what both academic and policy circles called Keynesian economics had litle in common with the economics of the General Theory. This awakening occurred even as the policy effectiveness of the approach to macroeconomic policy that had been hammered out largely in the Hansen-Williams Fiscal Policy seminar at the Littauer School was seemingly successful. The well nigh golden age of economic performance that began in 1946 ended about 1966, although at that time to most practitioners the credit crunch and growth recession of 1966-67 seemed to be an error in fine tuning rather than the first sign of a sea change in the performance regime. In my eyes the credit crunch was the bit of evidence that coalesced the view that the liquidity prefernce function was misspecified when it was put into a form that could be viewed as a demand function for money.

Monetarism and post Keynesian alternatives to the orthodox Hicks-Hansen interpretations of Keynes surfaced at different times, monetarism came first. I believe one of the first presentations of the Friedman -

Schwartz interpretation of money's influence was in Friedman's testimony to hearings on Employment Growth and Price Levels. Senator Paul Douglas, a serious economist who may very well have coined the term monetarism, chaired a major congressional research effort. Otto Eckstein was the research director for this effort.

Monetarism had its run and has largely failed, both as theory and a framework for policy. Perhaps it is time to take another look at the discontents of 1966 that gave rise to post Keynesian economics and see if these views are worthy of another run.

One of the main contentions of the Post-keynesian economics is that successful functioning of a capitalist economy requires a visible hand. A word of reminising may be in order. I came to Harvard from Chicago in 1942 and was in the fiscal policy seminar during 1942-43 until I went off to the Army. At Chicago Henry Simons' public policy pamphlet A Positive Program For Laissez Faire, the theme of which was that markets need prior and continuing systems of intervention if they are not to generate private power or "monopolies" and that the market way of organizing economic activity is likely to give rise to a distribution of income that was incompatable with the distribution of income. Thus I viewed that a structure of industry policy needed to accompany the fiscal policy measures..the implicit view was that the effectiveness of fiscal policy actions depended upon the structure of industry and the organization of nlabor markets.

Questions about dynamic stability and structural change, the schumpeterian ideas extended to institutional change

Use the quotation from Henry Simons re old forms in new quises as a rationalization for visible hand..In fact the entire positive program view calls for visible intervention

The validity of the floors and ceilings approach. In a system that is capable of generating not nice movements through time and which can generate impossible values by its own dynamics the actual time path of the system can best be interpreted as the combined result of the internal dynamics and the new initial conditions established by the interventions. The interpretations of lender of last resort interventions and the interventions by local clearing house associations in crises periods as preventing market dynamics from having a free hand and setting up new intial condtions. This view as validating the importance of institutions. use the Gray and Gray point about the stability efficiency of an economy. How does institutional change affect the allocational and the stability efficency of the economy?

Get off of it They want you to talk about monetary and banking theory. The endogeniety of money. The material of central banking and monetary policy

You must get to the virtues of big government as a device for stabilizing profits. That downside profit instability is the root cause of major depressions etc.