The Relevance of Keynes's *General Theory* after 80 years

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This year marks two important anniversaries in macroeconomics: the 80th anniversary of the publication of Keynes's *The General Theory of Employment, Interest and Money*, and the 70th anniversary of Keynes's premature death, at the age of 63. To mark these anniversaries, the first issue of the fourth year of the *Review of Keynesian Economics* is dedicated to Keynes.

The issue contains a symposium of papers titled "The Relevance of Keynes's General Theory after 80 years" and some previously unpublished archive material on Keynes. The unpublished material is notes from a 1936 University of Chicago course taught by Frank Knight in which the *General Theory* was discussed, and a memorandum written by Lauchlin Currie, who is considered the first and most combative Keynesian in the Roosevelt administration during the early phases of the New Deal.

The 80th anniversary of the *General Theory* takes place at a time when the global economy is struggling with economic stagnation that set in after the financial crisis of 2008. In some regards, these conditions have parallels with the 1930s when the Great Depression followed the financial crisis of 1929. However, this time economic depression was avoided by timely economic policy interventions that either bore the direct hallmarks of conventional Keynesian thinking or were inspired by Keynesian thinking about the economy's limited self-stabilizing capacity.

Given Keynes's early death, it is impossible to know how his views would have continued to evolve, or what he would have had to say about the immediate post-crisis fiscal stimulus or about the subsequent turn to austerity in many places, including in the United Kingdom. What we do know is that, over the last eight decades, the ideas in Keynes's *General Theory* have been a persistent source of intellectual ferment and macroeconomics has oscillated between proving and disproving the essence of his views. That makes the *General Theory* one of the greatest books written in economics.

The Neoclassical Synthesis developed by John R. Hicks, Franco Modigliani, Paul Samuelson, and Robert Solow dominated much of the teaching and research in macroeconomics until the rise of Milton Friedman's Monetarism in the 1970s.[2] Friedman's Monetarism was then followed by New Classical Macroeconomics (NCM) that added rational expectations to the pre-Keynesian Classical macroeconomic model. NCM, in turn, provoked a counter-response that has become labelled New Keynesian economics and which emphasizes nominal rigidities.

In sharp contrast to these mainstream evolutions, Post-Keynesians have persistently emphasized fundamental uncertainty as the fulcrum of Keynes's thinking. Others within this school have emphasized the instability elements of chapter 19 of *The General Theory*, in particular the effects of deflation on debt, as

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[2] The latter is a patron of this journal.

being central for Keynes' message. Furthermore, Post-Keynesians believe New Keynesian economics has deviated significantly from the teachings of Keynes, even though his work remains an inspirational influence for them and there are often close policy perspectives between the two schools.[3]

In addition to these two well-known interpretations of Keynes, there are many other interpretations that often preclude classification and are hard to pin down as part of a particular school of thought.[4] However, all emphasize the notion that left to its own, the economy will not quickly reach equilibrium with full employment, and that government intervention is required both to stabilize the economy and to promote full employment.

The *General Theory* sought to explore the real world where unemployment is involuntary and where aggregate demand plays a crucial role in determining the level of economic activity, ideas that Keynes thought were "extremely simple and should be obvious" (1936, p. viii). It challenged the dominant classical economic doctrine which Keynes sought to escape.

Over the last eight decades, the disputes over Keynes's ideas suggest that there is nothing 'obvious' about his theory, and the struggle to escape classical economics continues. The acceptance of Keynes's ideas seems to fluctuate with conditions. Most recently, the global financial crisis of 2008, and the policy successes that helped avoid a second Great Depression, have shown anew the relevance of those ideas. Yet, despite this vindication, it has not been enough to assuage the critics, as evidenced by the quick reversion to anti-Keynesian austerity policies.

For this symposium, dedicated to Keynes's *magnus opus*, we invited four distinguished, yet varied, authors to comment on Keynes and Keynesian economics. The questions discussed range from domestic to international policy issues, from the theoretical to the policy oriented based on historically specific conditions, and to the more profound question of what determines progress in science. In our view, the lack of consensus in macroeconomics, eighty years after its seminal book was published, is a strong reason for the acceptance of a pluralist approach to the discipline.

In his contribution, Robert Skidelsky explores how Keynesian ideas made their way into British public policy. He argues that the breakdown of pre-World War I macroeconomic conditions led to a "blocked" system, where the adjustment mechanisms presupposed by neoclassical economics were jammed and that Keynesian economics offered an escape from this system. He then explains the Keynesian response to the new problems in monetary and fiscal policy: the gold standard impeding credit control, and the tenacity of the balanced budget rule, respectively. Finally, he outlines how Keynes's ideas, including their policy

[3] In many respects modern macroeconomics owes more to Knut Wicksell and Irving Fisher, and even the Keynes of the *Treatise on Money* than to the one of the *General Theory*.

[4] A few that come to mind are Robert Clower, Wynne Godley, Axel Leijonhufvud, Hyman Minsky and G. L. S. Shackle. In that group one could also add the, mostly French, non-Walrasian Disequilibrium School of Pascal Bénassy and Edmond Malinvaud.

implications, took hold after the Great Depression via the events at the Macmillan Committee.

Simon Wren-Lewis suggests that to understand the standing of the *General Theory* today, and why so many policy makers felt they had to go back to it to understand the Great Recession, we need to understand the New Classical Counter Revolution (NCCR) and why it was so successful. This revolution can be seen as having two strands. The first, which attempted to replace Keynesian policy, failed. The second, who was to change the way academic macroeconomics was done, was successful. Before the NCCR, macroeconomics was an intensely empirical discipline: something made possible by the developments in statistics and econometrics inspired by the *General Theory*. After the NCCR, with its emphasis on microfoundations, macroeconomics became much more deductive.

As a result, most academic macroeconomists today see the foundation of their discipline as not coming from the *General Theory*, but as coming from conventional microeconomic theory – arguably the 'classical theory' that Keynes was so keen to cast aside. Students are also taught that pre-NCCR methods of analysing the economy are fatally flawed, and that simulating DSGE models is the only proper way of doing policy analysis. Wren-Lewis argues that this is simply wrong. The problem with the NCCR was not the emergence of microfoundations modeling, which is a progressive research programme, but that it discouraged the methods of analysis that had flourished after the *General Theory*. Wren-Lewis argues that had there been more academic interest in these alternative forms of analysis, the discipline would have been better prepared ahead of the financial crisis.

The next article, by Peter Temin and David Vines, argues that Keynes was interested primarily in the world economy. In saying this, the authors do not seek to diminish the innovative advances Keynes made in the *General Theory*, but instead want to expand the perceived scope of Keynesian economics. They analyse Keynes's contributions at three points during his career— the writing of *The Economic Consequences of the Peace* just after World War One, Keynes's testimony before the Macmillan Committee at the outset of the Great Depression, and his negotiating position at Bretton Woods during and after World War II. The authors then show how an international Keynesian analysis clarifies the economic problems of Europe today.

Lastly, the paper by Nicolas Rowe argues that Keynes missed the importance of the distinction between saving in the form of money ("hoarding") and saving in all other forms ("thrift"). Rowe argues that it is excessive hoarding, not excessive thrift, that causes recessions and the failure of Say's Law. The same failure to distinguish hoarding from thrift continues from the *General Theory* into the ISLM model and into New Keynesian macroeconomics. On this score, Rowe argues that economists should follow Silvio Gesell rather than John Maynard Keynes. The rate of interest in New Keynesian models should be interpreted as a negative Gesellian tax (i.e. a subsidy) on holding money issued by the central bank.

Keynes intended the *General Theory* for an audience of economists, but the ideas contained in the book had the loftier goal of saving capitalism from itself. Eight decades after its publication, it is our belief that the ideas in Keynes's *General Theory of Employment, Interest and Money* remain fundamental, both for understanding how capitalism functions and for designing economic policies that ensure capitalism delivers shared prosperity.