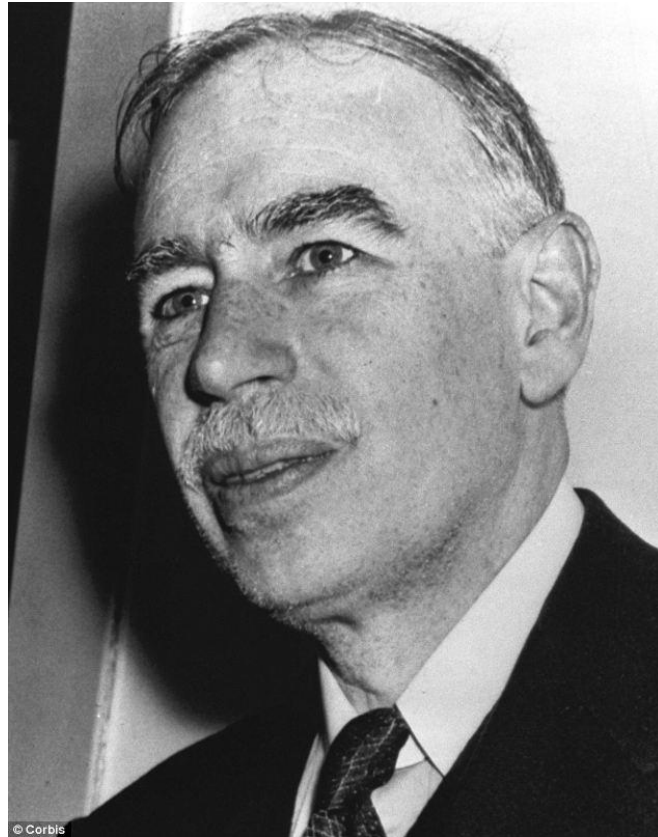




John Maynard Keynes
(1883-1946)

<http://www.youtube.com/watch?v=U1S9F3agsUA&feature=youtu.be>

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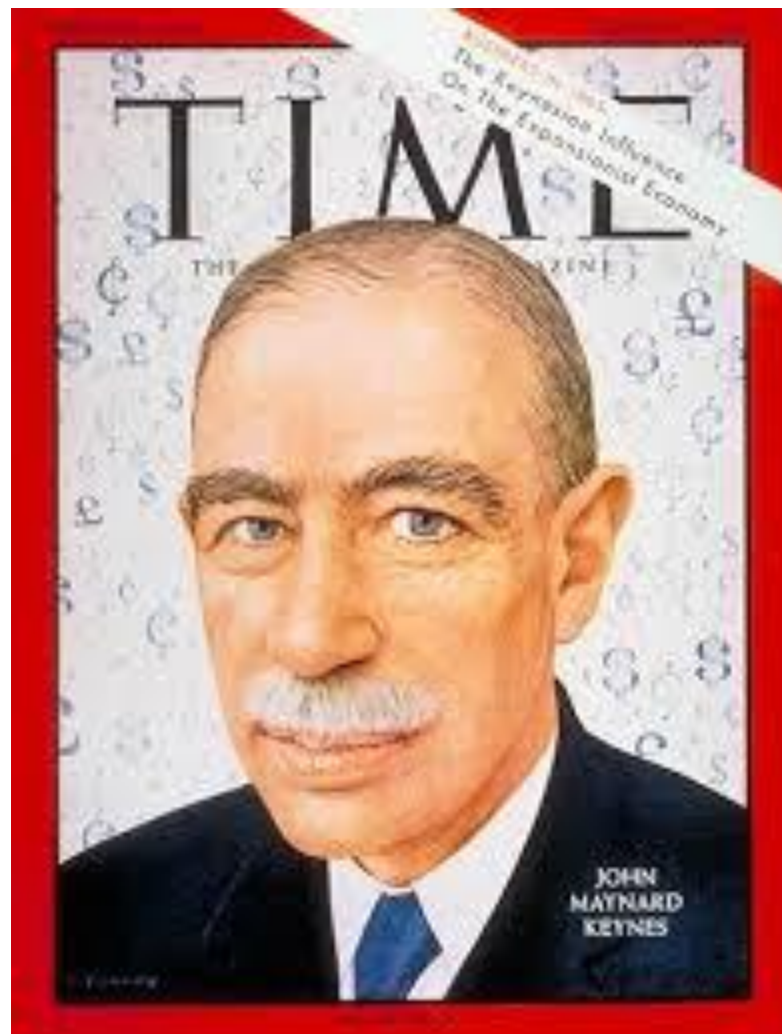


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His Contribution

- ◆ The father of macroeconomics
- ◆ Keynes was **the most famous** and perhaps **the most influential economic theorist of the 20th century**.
- ◆ His impact inside and outside the profession has been as great as **Ricardo, Mill** or even **Marshall**.
- ◆ ***The General Theory of Employment, Interest and Money*** (1936)
 - Income-expenditure modal
- ◆ Keynes was the first, after **the great depression of 1930**, to advise governments to **engage in discretionary spending and taxation** (budget deficits) to cure **depression and unemployment**.

His Contribution

Modern fiscal policy

The Gouvernement intervention by the help of the use of **government taxation** and **expenditure policy** to affect **prices**, **employment**, and **income**.

Keynes's Life and Works (1/6)

- Born in 1883
- His father **John Neville Keynes** was logician and specialist of economic methodology. His most important work, *The Scope and Method of Political Economy*, is published in 1890. He inherited to little John a great intellectual curiosity and a lifelong love for arts, especially theater.
- His mother **Florence Ada**, was scientific.
- Keynes was educated in Eton.
- Alternatively immersed in classical literature, in logic, in mathematics, dramatics etc.
- He studied in **King's College in Cambridge**.

My Cambridge Photos

- https://drive.google.com/drive/folders/1q9WHBq75iatAXqzFNsmnUH-yGjYrtw6X?usp=share_link

Keynes's Life and Works (2/6)

- 1905 **Marshall** wrote to his father that **he is good at economics**.
- Civil servant in Indian Office in 1906
- Bloomsbury group

The group had ten core members:^[10]

- ❖ [Clive Bell](#), art critic
- ❖ [Vanessa Bell](#), post-impressionist painter
- ❖ [E. M. Forster](#), fiction writer
- ❖ [Roger Fry](#), art critic and post-impressionist painter
- ❖ [Duncan Grant](#), post-impressionist painter
- ❖ [John Maynard Keynes](#), economist
- ❖ [Desmond MacCarthy](#), literary journalist
- ❖ [Lytton Strachey](#), biographer
- ❖ [Leonard Woolf](#), essayist and non-fiction writer
- ❖ [Virginia Woolf](#), fiction writer and essayist





BBC2 drama "Life in Squares"

- Virginia Woolf (1882-1941)
- an English writer, considered one of the most important modernist 20th-century authors and a pioneer in the use of stream of consciousness as a narrative device.
- His father, Leslie Stephan (1832-1904), an intellectual



Movie: The Hours

More in Virginia Woolf (in Turkish):

<https://blog.ofix.com/en-guzel-5-virginia-woolf-kitabi/>

Keynes's Life and Works (3/6)

- Keynes was trying to do a lot of things at the same time. These activities made his career brilliant.
- In 1911 Keynes became **coeditor** (with an other economist F. Y. Edgeworth) **of the Economic Journal**, the official organ of the Royal Economic Society (that still exists, they do conferences). He hold this position until 1945.
- In 1913 he published a work on **international finance** related to the **gold exchange standard**, *Indian Currency and Finance* (1913). And quickly becoming famous as a **monetary expert** and entered the **treasury department** in 1915. He stayed there until the war.

Keynes's Life and Works (4/6)

- He was assigned as a British treasury representative to the **conference of Versailles**.
- 1919 Keynes attacked the conditions of the treaty in a book that he wrote : ***The Economic Consequences of the Peace***. The book was an immense critical success, urging as it did moderation in the demands upon defeated Germany.
- In 1920's, Keynes taught at **King's College**. He was an **enthusiastic Lecturer** but he reduced his teaching load in order to engage in a multitude of other activities. For example having a fortune !!! (about half a million pounds in 1937) by **speculating in the foreign exchanges**.
- He passed the civil servant examination and was signed to a position in the **Indian office**.

Keynes's Life and Works (5/6)

- After a while, he devoted a large part of his time to a study of probability theory. He wrote ***Treatise on Probability*** (1921).
- He became the board of the famous liberal weekly **Nation**.
- He has the duties of bursar (financial analyst and manager) of King's College, for which he received, in the beginning, 100 pounds per year.
- 1923, Keynes published his ***Tract on Monetary Reform***. This book became polemical, it was against the gold standard.
- In 1925 Keynes married Lydia Lopokova, a prima ballerinas.





Keynes's Life and Works (6/6)

- The two-volume ***Treatise on Money*** appeared in late 1930. In this book, **saving** and **investment** were in the first roles influencing the level of incomes.
- In 1931 he wrote ***Essays in Persuasions*** and ***Essays in Biography*** (1933). He defends his thesis in *General Theory*.
- In 1930's Keynes get too involved with the financial burdens imposed by the impending war with Germany. The problems of reordering wartime resource priorities and the excess demand thereby created are dealt with in ***How to Pay for the War***, published in 1940.
- Between 1941 and 1946, Keynes negotiated wartime lend-lease financing, and in 1946, he was instrumental in arranging the Marshall loan to Britain.
- That same year Keynes was made a vice president of the **World Bank**, and plan to restore the **international monetary system** (which were made in **Bretton Woods**, New Hampshire). **IMF**
- In the summer of 1946, at the age of sixty-three, Keynes died of heart attack.



UNCOMMON, BOLDNESS ANSWERS THE GREAT ENIGMA: John Maynard Keynes in His Study in Cambridge. It was he who broke the dogma of "Friedrich" while that nation was still under international financial domination which made them poor. Today, at the age of 50, he has produced a book of 300,000 words and stands as the greatest economic revolution.

MR. KEYNES HAS A PLAN

To carry on a war successfully we must spend over \$100 billion a year. How are we to pay? How are we to avoid inflation? In this article King's College, Oxford, of "The New Economic and Social," writing of the man who has given an answer to these questions, describes the answer which he gives.

WHEN "The Economic Consequences of the War" by John Maynard Keynes was published in 1919 it caused a profound sensation. There was no longer doubt that the British Empire was in financial straits that could not be met by the war effort. The country was then at the height of its power, and the world was at the height of its power.

Today, from the point of view of common sense, it is only fair to say that in the years 1919-1920 the British Empire was in financial straits that could not be met by the war effort. It is only fair to say that in the years 1919-1920 the British Empire was in financial straits that could not be met by the war effort.

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Slavoj Žižek is a Slovenian, Marxist philosopher, cultural theorist and public intellectual.

IN THE LONG
run, WE
ARE ALL
dead.

John Maynard Keynes

So let's focus on the short run and longer runs... :)

General Theory

- The book took place in a milieu of depression. From the beginning of 1930, Keynes has been much concerned with the employment crisis that affected USA and England very badly.

Different interpretations:

- For **J. R. Hicks** (Nobel laureate in 1972): **Income-expenditure model** has been developed by him
 - For **Axel Leijonhufvud** (his book: *On Keynesian Economics and the Economics of Keynes*) Keynes' chief concern was a **presentation of a macroeconomic quantity adjustment model** rather than an analysis of unemployment equilibrium per se.
-
- He voiced this concern in several communiqués to President Roosevelt, including a famous open letter to him in the *New York Times*.

General Theory

- What has Keynes advised to Roosevelt?

Making vigorous use of fiscal policy (government tax and expenditure policy) to supplement the market mechanism of the private sector, which, in Keynes's view, was failing to get at the employment problem.

- Did Roosevelt listened him? Partially.

Keynes himself has raised questions concerning the adequacy of neoclassical monetary theory in his *Treatise on Money*. His colleagues were focusing upon the importance of expenditures in aggregate output determination.

Works

- ✓ *Indian Currency and Finance* (1913)
- ✓ *Treatise on Probability* (1921)
- ✓ *The General Theory of Employment, Interest and Money* (1936)

(many works are already mentioned in the biography part of this power point)

Keynes's Reaction to the Classics

- Who are classics?
- What does Keynes think about the Say's law?
- What does Keynes think the wage-rate adjustment mechanism? (money wage & real wage)
- Unemployment
- Aggregate demand
- The investment multiplier

Keynes' reaction to the Classics

- Who are classics **FOR KEYNES** ? (or classicals, both correct)

Answer:

Classical political economists + neoclassical economists
(From Smith, Ricardo to Marshall, Pigou etc.)

What does Keynes think about Say's law?

- The Critique Of Orthodoxy (reaction to neoclassical economics)

No unemployment, no bankrupt in the long run

Saving = investment at full employment?

Keynes says: No

- The exceptionality of labor market

Saving and Investment

- **The relation between S and I is not that simple. S and I are related to interest rate (i). But both of them are determined by a complex host of factors in addition the interest rate.** So there is no guarantee that the two would necessarily be equal at a level of economic activity that produces full employment.

- Keynes wanted to propose **and alternative to neoclassical economics**. He is bothered by “the idealized modal of classical macro theory”.
- *The General Theory* took aim at **Say’s law** in its **neoclassical version** and **especially at the thesis that unemployment is merely a result of real wages that are too high**.
- Keynes wants to fallcify that the **unemployment is merely a result of real wages that are too high**.

- So, employment is the result of what?
- What does Keynes think about the wage-rate adjustment mechanism? (money wage & real wage)
- Money illusion
- Solution: unemployment could be efficiently attacked only by manipulating **aggregate demand**

Consumption function

- $C=f(Y)$

C= Consumption

Y= aggregate income

- C is also related to other factors like **price, expectations, the utility of saving for future consumption versus present consumption, income expectations, institutions, mores and so on.**

The Simple Keynesian Model and Its Application

I. $Y = C + I + G$	The equality between Y , which represents income, and $C + I + G$, which represents total expenditures (or aggregate demand), is the (Keynesian) equilibrium condition.
II. $C = a + bY$	This simple linear equation shows the general form of the relationship between income and consumption. It describes consumer behavior. $a > 0$; $0 < b < 1$.
III. $Y = C + S$	In the absence of taxation, this equation is an identity which defines savings. That is, saving (S) is defined as that part of income not spent on consumption goods ($Y - C$). With taxation, we would write $Y = C + S + T$.

Now, consider some data (expressed in billions of dollars) that describe a particular economy:

i. $C = 100 + 0.8Y$	This is a specific consumption equation that describes the consumption behavior in some particular economy during some particular period of time.
ii. $I = 50$	This magnitude represents the current level of investment, which is based on the prevailing state of business confidence.
iii. $G = 60$; $T = 0$	These magnitudes represent the current levels of government spending and taxation. (Query: How is the government financing G if T is 0?)
iv. $Y_{fe} = 1300$	This is the full-employment level of income--the level of income that reflects an absence of (cyclical) unemployment and corresponds to a wage rate that clears the labor market.

Revolutionary ideas

- There could be an equilibrium level of income in an economy at less than full employment
- Expectations (depend upon capricious psychological factors, that has direct effect on income -consumption, saving etc-)

"Successful investing
is anticipating
the anticipations
of others."

John
Maynard
Keynes



General Theory

- Here we should talk about a concept: **investment multiplier** developed by Richard Kahn. Have discussed a lot in Cambridge. Keynes mentions it in the preface of *General Theory*.
- There was a pressure on Keynes and he wanted to propose an alternative to neoclassical economics. He started, in his theory, with **reacting to the Classics**. What are classics?

The role of investment

- Two sources of private expenditures were introduced: **consumption** and **investment**.
- **Investment demands** are determined by a host of factors besides the **interest rate**, including **expected future returns**.
- We are talking here **the marginal efficiency of capital** (which is actually INVESTMENT) which relates **the cost of investment capital** to **the expected returns** over the life of investment projects.

Unemployment

- Classical believes that **demand for labor** was equivalent to the **marginal productivity of labor** and **labor supply** was an increasing function of **money wage**.
- Keynes disagreed. ...was an increasing function of **real wage**.
- For classicals, only **voluntary** and **frictional unemployment** exist. Certain amounts of labor would voluntarily exempt themselves from labor force at certain wage (money matters).
- He said that workers could be involuntarily unemployed

https://www.youtube.com/watch?v=rDZr4mv2PZE&ab_channel=BeingCommerce

The role of money

- 1° Holding money for transaction purposes.
- 2° Holding money to speculate in the bond market (speculative demand for money)

Why he prefers fiscal policy and not monetary policy?

- Because of special forms of the speculative demand for money and the investment function, monetary policy was not predictable useful.
- He prefers fiscal policy.

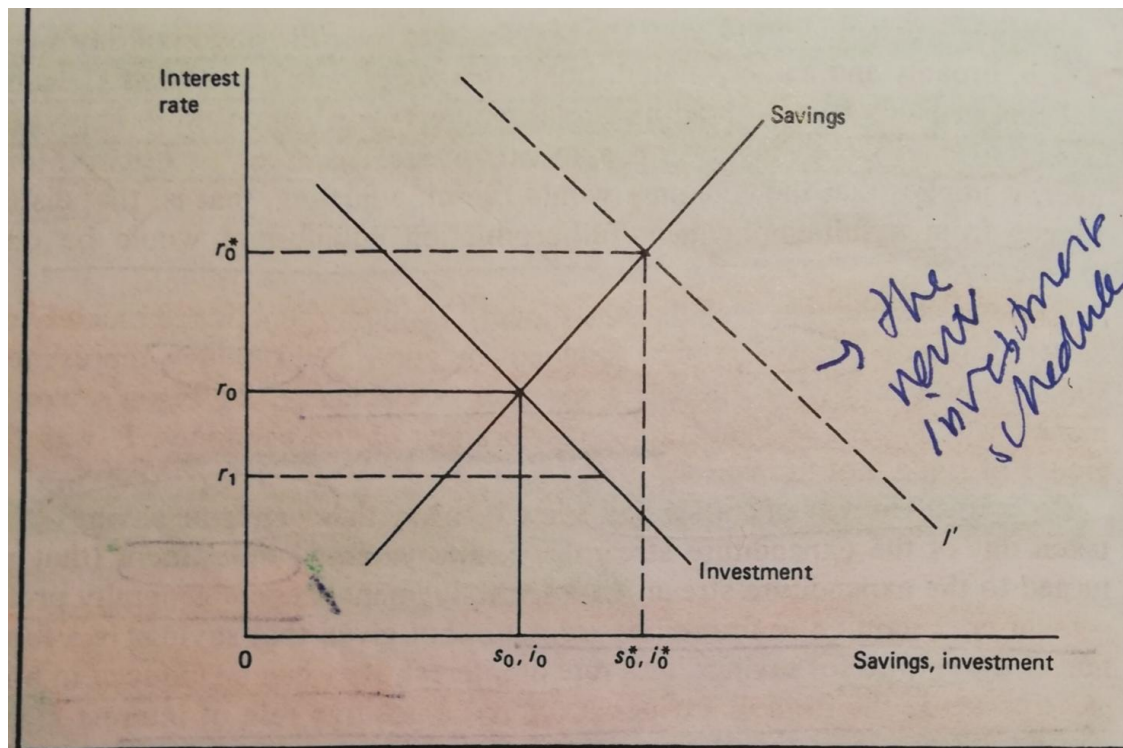


FIGURE 19-1

At interest rate r_0 , saving equals investment. If investment increases from I to I' , the new equilibrium rate of interest rises to r_0^* and the amount of saving and investment increases to s_0^* and i_0^* , respectively.

When the rate of interest rises, the society saves more. So consumption decreases.

FIGURE 19-2

The intersection of aggregate demand and aggregate supply schedules (point A) determines an equilibrium level of income, Y_0 . If income exceeds Y_0 , then aggregate supply will exceed aggregate demand.

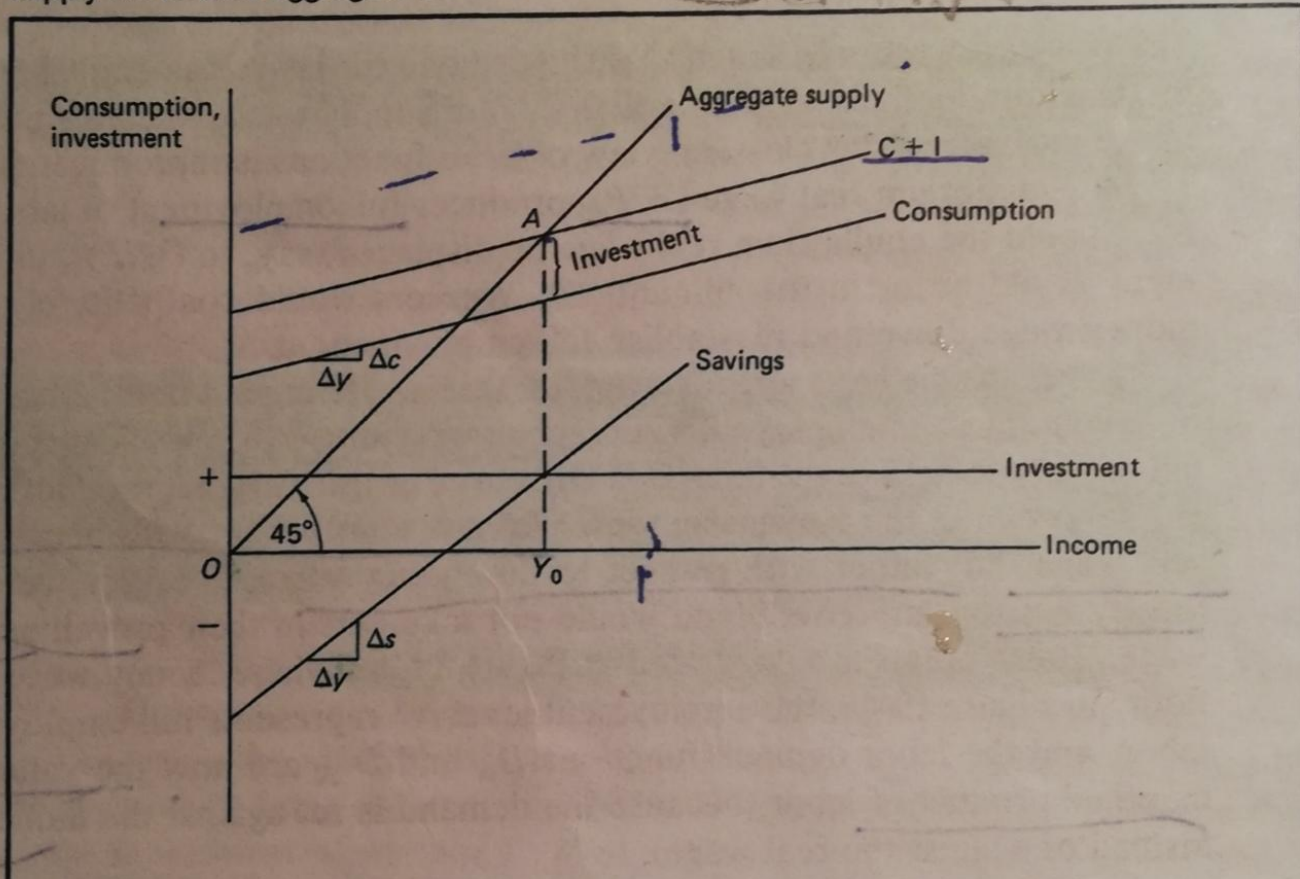
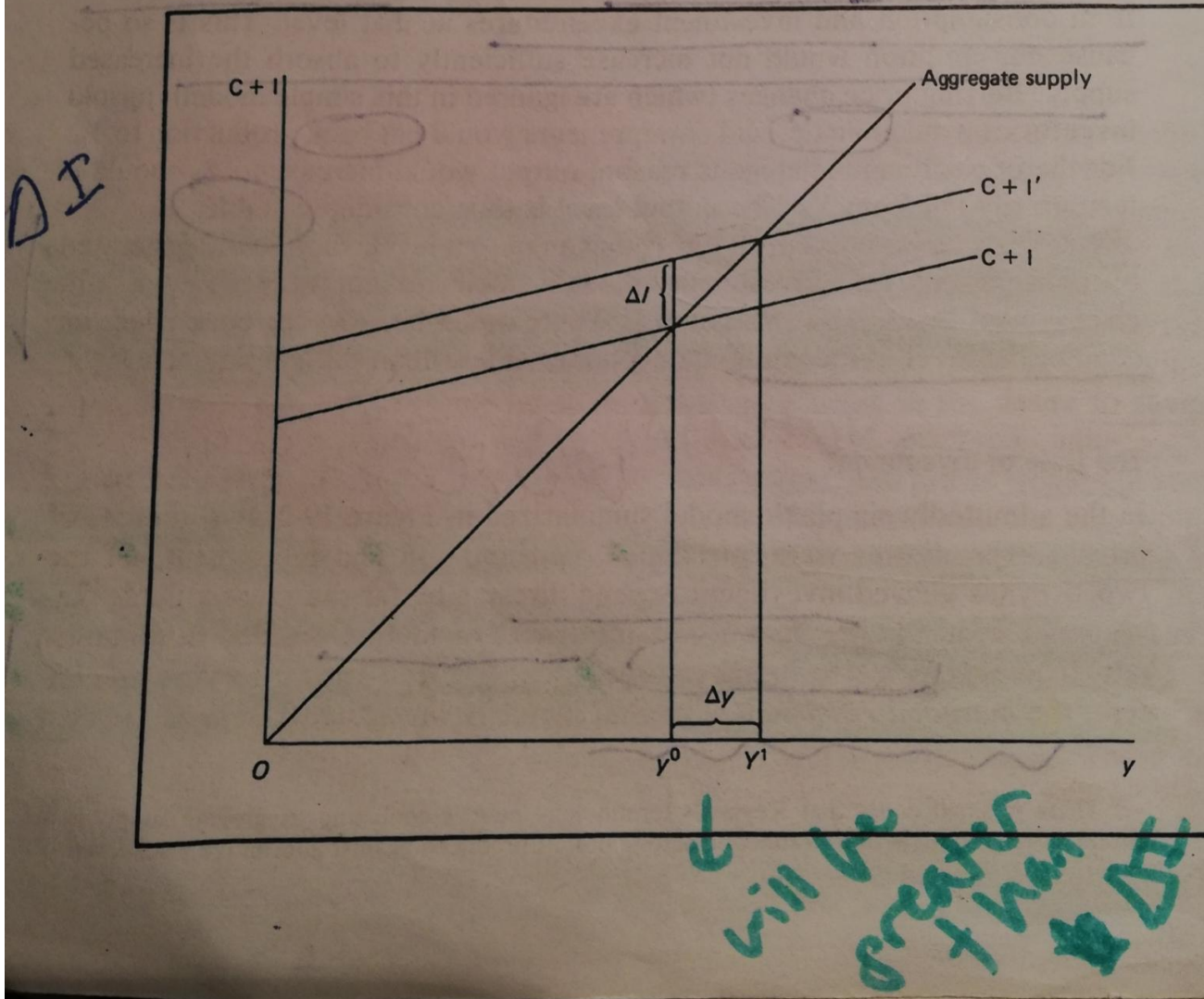
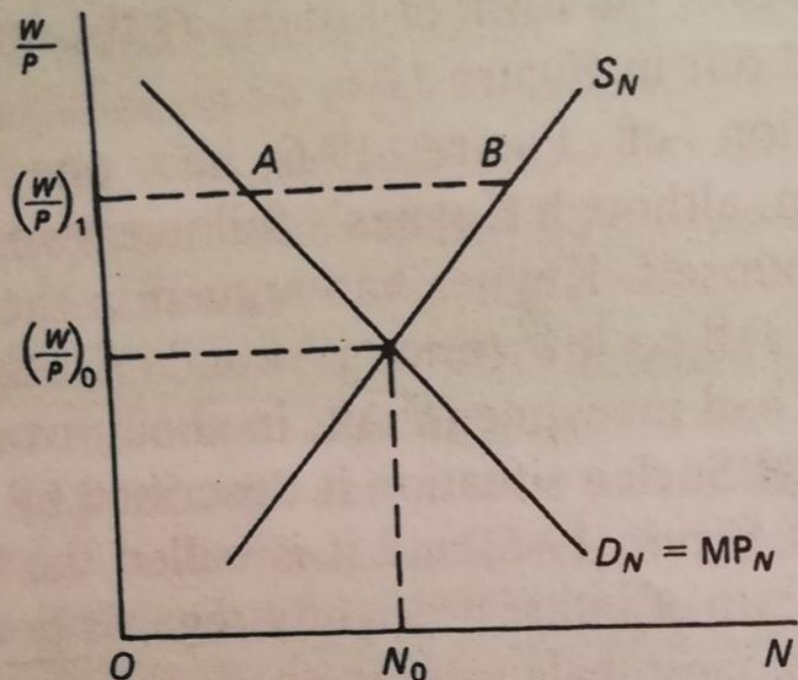


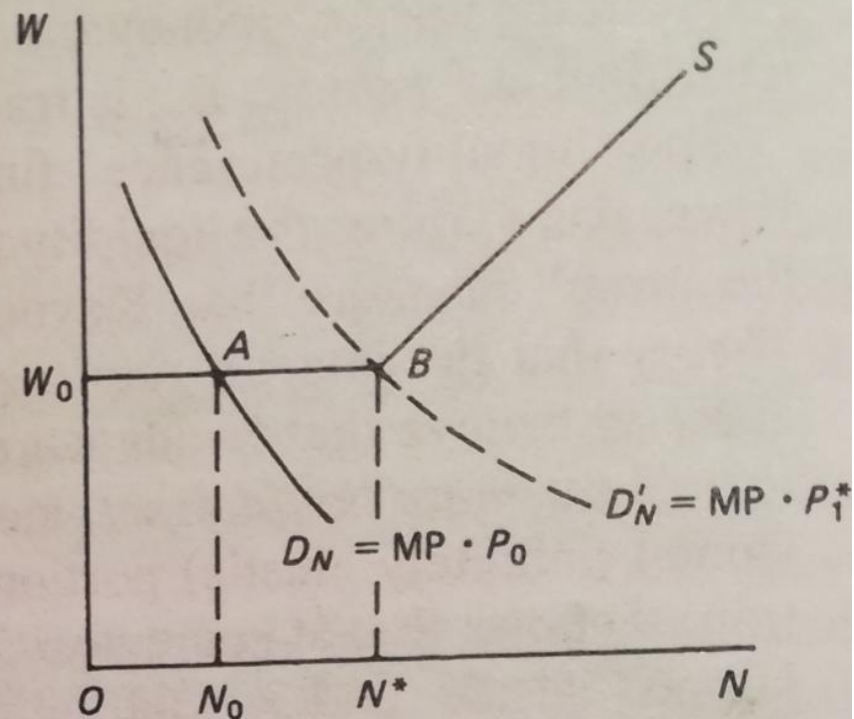
FIGURE 19-3

If investment increases from I to I' , the aggregate demand function will shift upward by ΔI . Income will also increase from Y^0 to Y^1 .





(a) Classical Labor Market



(b) Keynesian Labor Market

FIGURE 19-4

The classical labor market automatically adjusts itself to full employment whereas the Keynesian labor market does not automatically adjust.

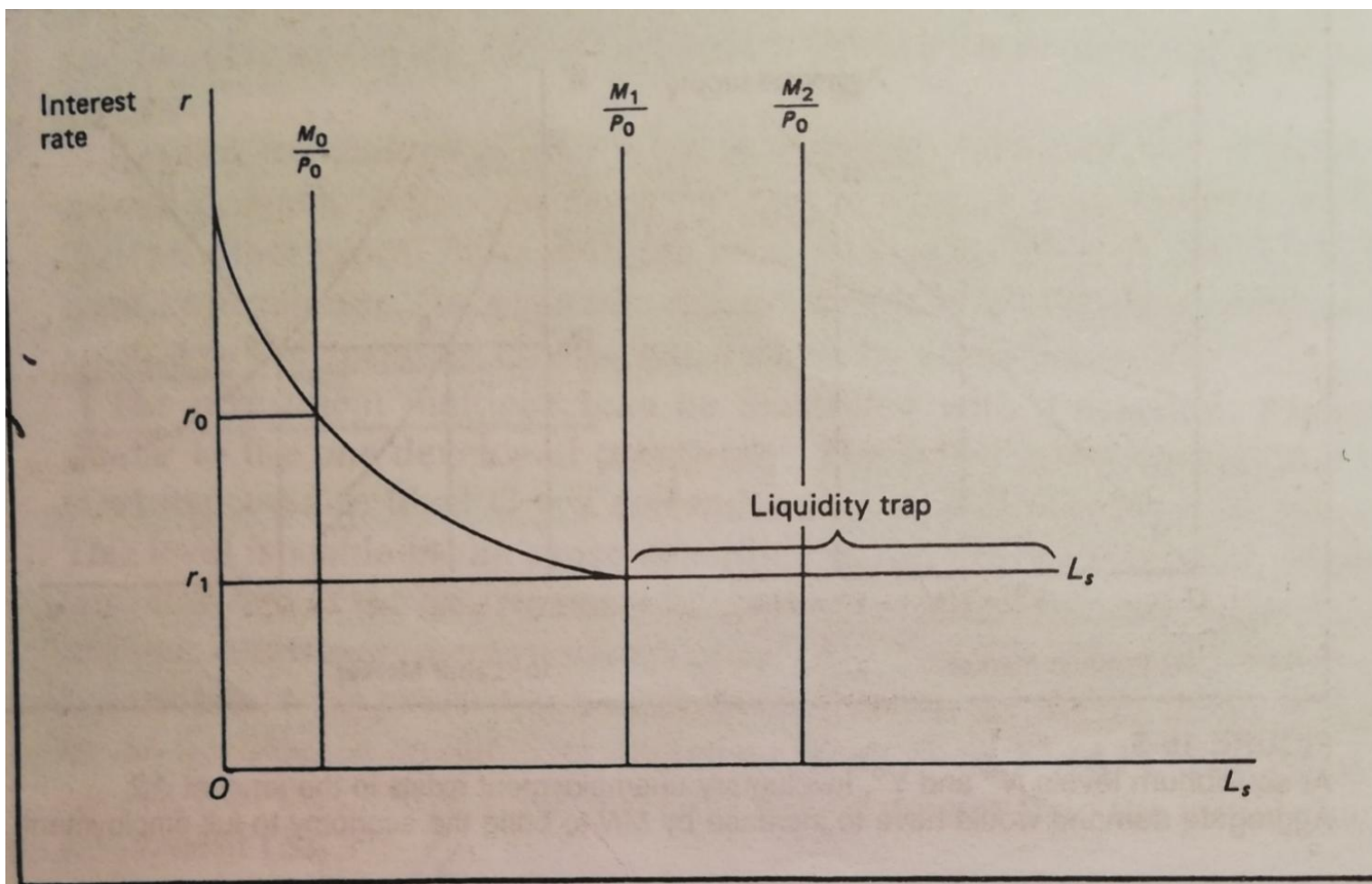
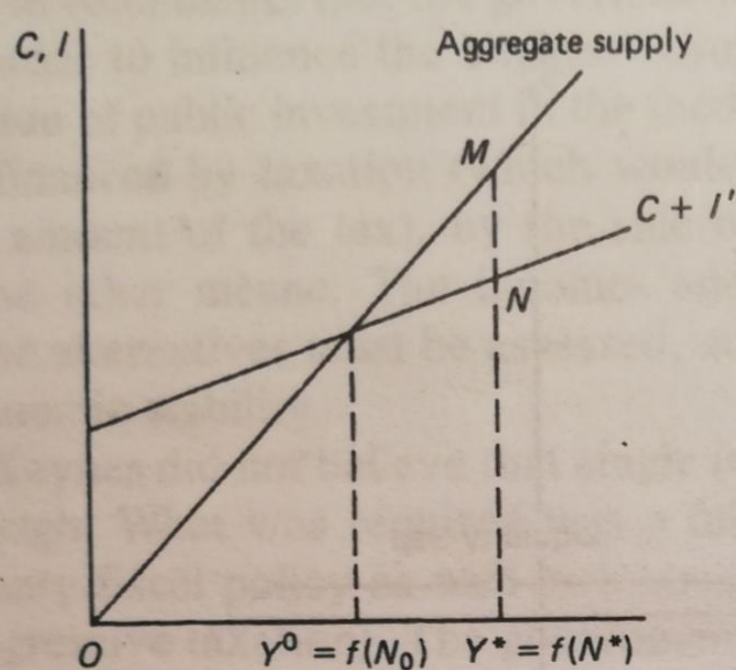
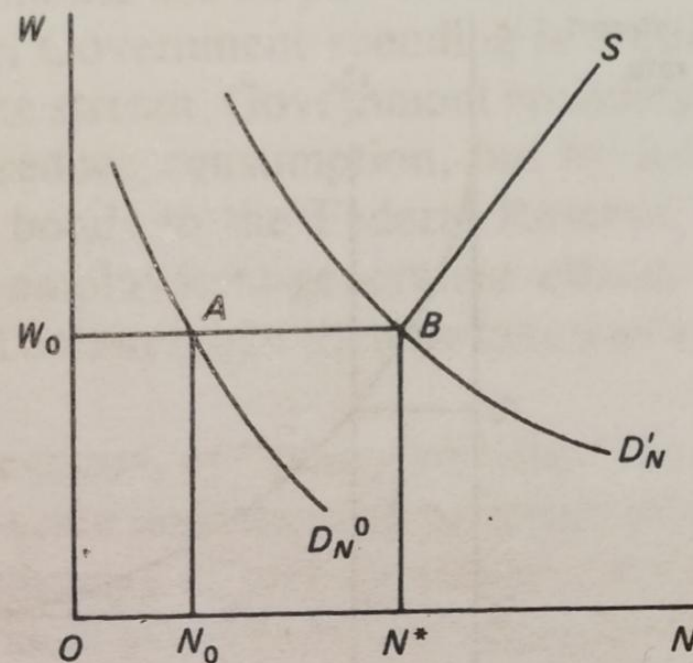


FIGURE 19-6

Increasing the nominal money stock from M_0 to M_1 will reduce the interest rate from r_0 to r_1 , but increasing the money stock further, to M_2 , will not have any effect on the interest rate.



(a) Product Market



(b) Labor Market

FIGURE 19-5

At equilibrium levels N^0 and Y^0 , involuntary unemployment exists in the amount AB . Aggregate demand would have to increase by MN to bring the economy to full employment.

KEYNESIAN ECONOMICS



In case of nothing
to do, break glass and then
sweep up broken glass.