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Introduction to Post-Keynesian Economics

Elisabeth Springler

1. Foundations and roots
2. View into endogenous money and financial stability
3. Economic Policy issues: European Integration and the impact of emerging markets

[#Business News](#)

October 19, 2017 / 1:12 AM / 20 days ago

China's central bank warns of 'Minsky moment' as economy powers ahead

[Kevin Yao](#), [Elias Glenn](#)

BEIJING (Reuters) - China's central bank chief on Thursday issued a stark warning about asset bubbles in the world's second-largest economy, which looks set to clock its first acceleration in annual growth since 2010, driven by public spending and record bank lending.

Speaking on the sidelines of the closely-watched, twice-a-decade Communist Party Congress, People's Bank of China Governor Zhou Xiaochuan spoke of the risks of a "Minsky moment" in the economy, referring to a sudden collapse in asset prices after long periods of growth, sparked by debt or currency pressures.

Zhou's comments refer to a theory on prices derived by American economist Hyman Minsky and follow official data that showed China's economic growth slowed in the third quarter from a year earlier, as expected, but remained on track to post the first full-year pickup in seven years.



1. FOUNDATIONS AND ROOTS

1. Foundations and roots

Keynesianism vs. Post-Keynesianism

Three views after Keynes:

- Neoclassical synthesis
- Neokeynesian approach
- Post-Keynesian approach.

PK:

- Joan Robinson 1971, New Orleans, American Economic Association, first named „Post Keynesianism“
- Weintraub, Davidson (*Money and the Real World*, 1972)
- Macroeconomic analysis;
- Counterpart to monetarism and neoclassical synthesis; in the beginning mainly driven by counteracting mainstream analysis which led to heterogeneous views and lacks in concrete policy advice.
- Interdisciplinary approach: Institutionalism; Critical political economy

1. Foundations and roots

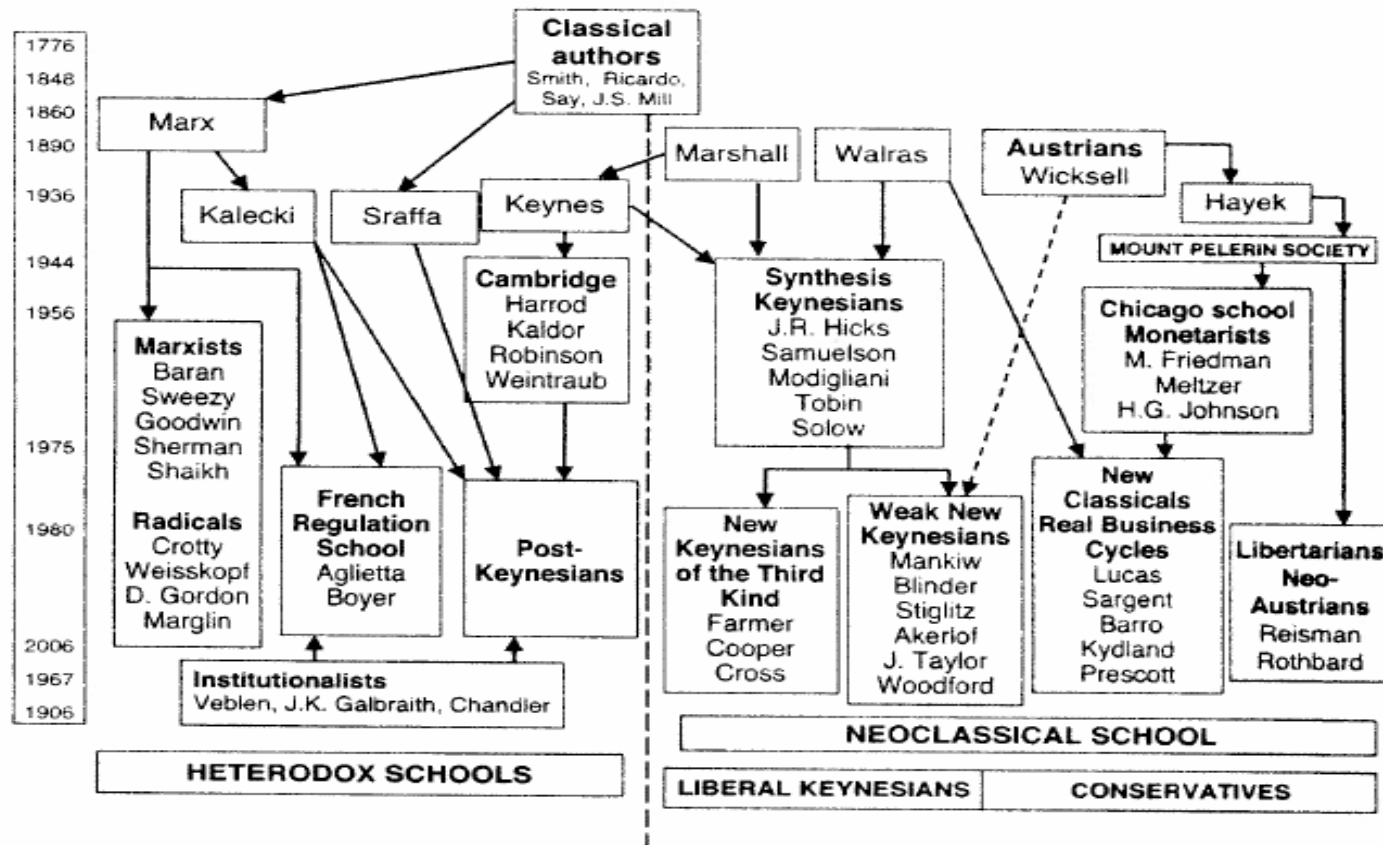


Figure 1.1: Schools of thought in macroeconomics

Lavoie, M. 2009, S.3

1. Foundations and roots

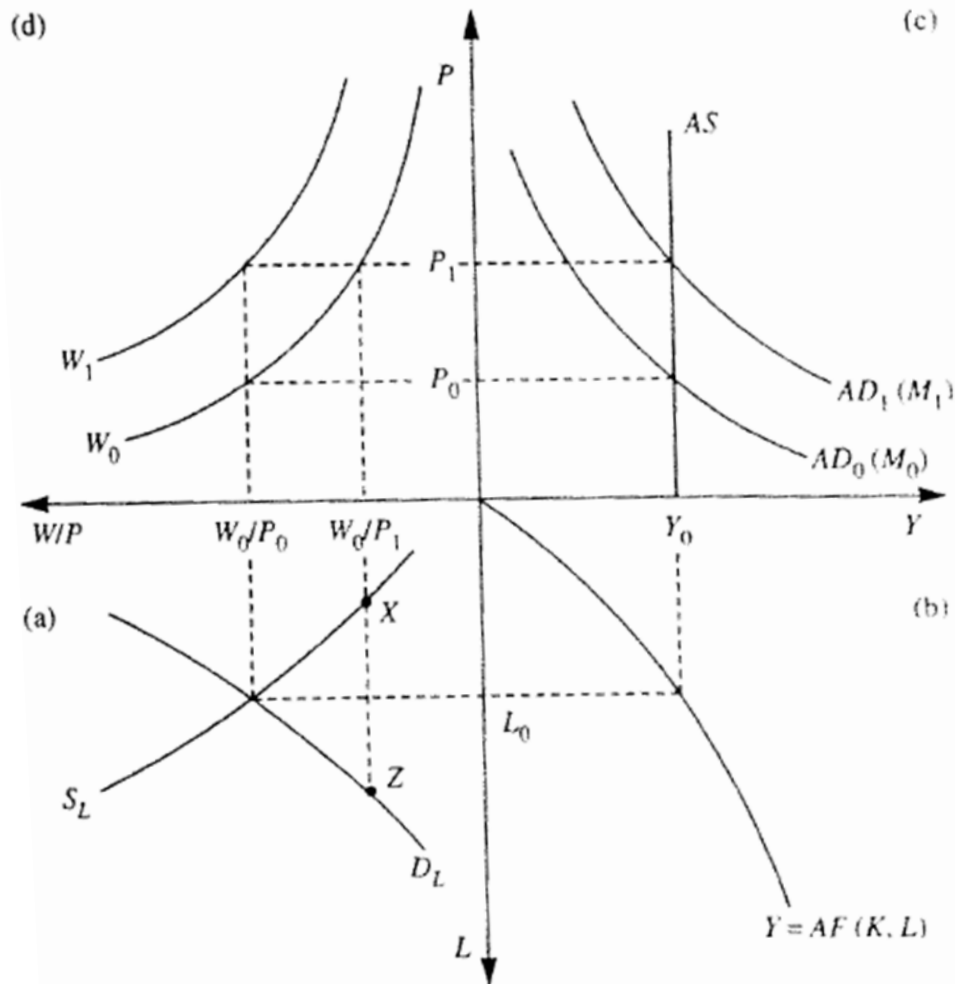
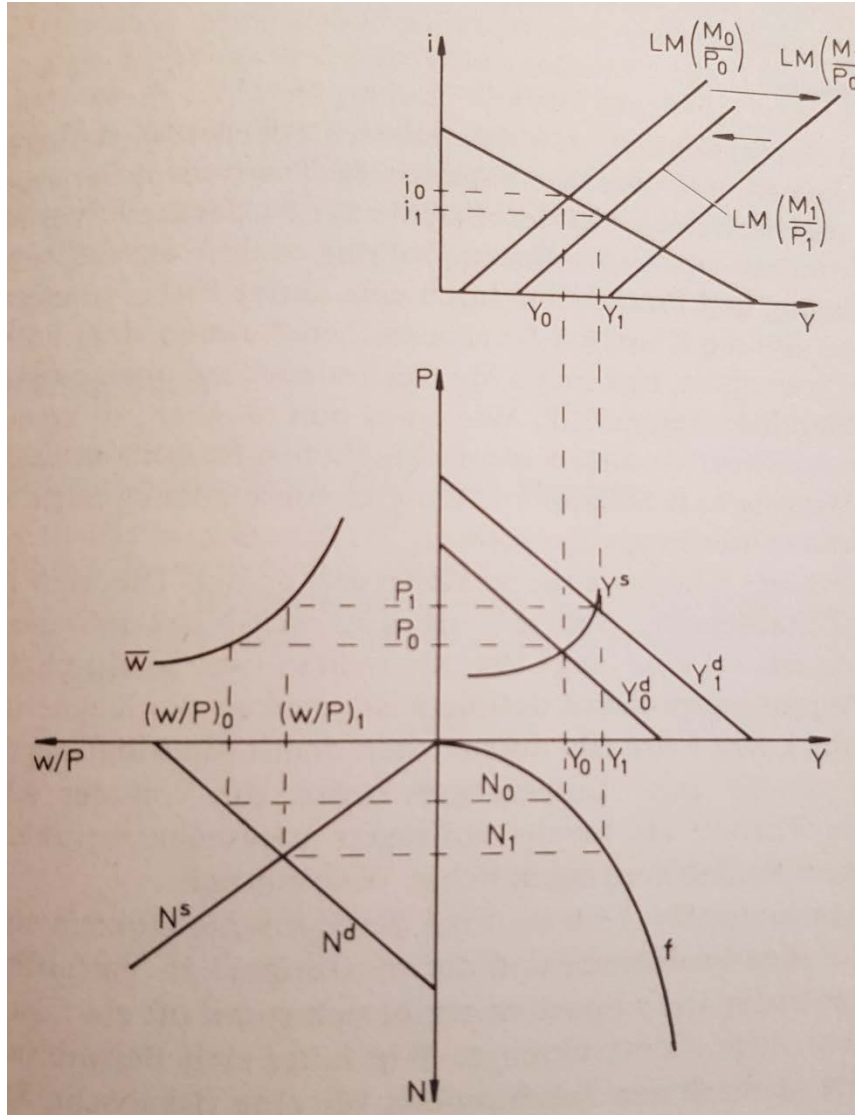


Figure 2.4 The determination of the price level in the classical model

1. Foundations and roots



How to deal with Keynes in a mainstream textbook?

1. Foundations and roots – wrapping it up

Main concepts:

- Effective demand and involuntary unemployment
- Interrelation between monetary and real sector – effects of monetary policy.
- $I = S$ does not work
- Dynamics and economic development:
 - Comparative analysis important: stabilization policy; restrictive monetary and fiscal policy is counter productive („wage earners“)
 - functional income distribution
 - Institutional setting has to be taken into account (historical developments)
 - Capitalism leads to unequal development
 - Focus on real world – quantitative and qualitative analysis.



2. VIEW INTO ENDOGENOUS MONEY AND FINANCIAL STABILITY

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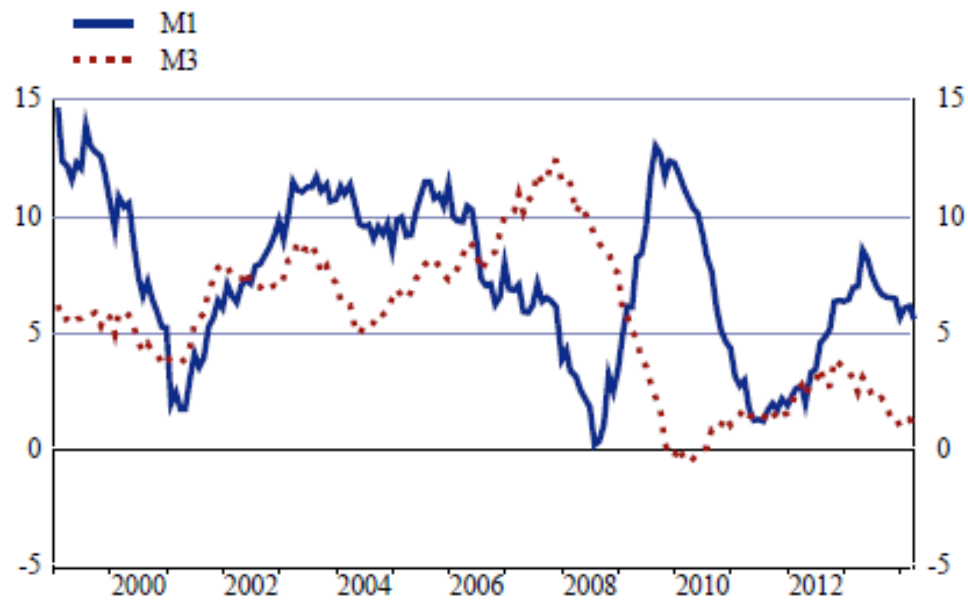
2. Money and financial stability

- **Three steps:**
 - A. monetary theory
 - B. monetary policy
 - C. financial stability

2. A. Monetary theory

- **Neoclassical logic:**
 - Exogenous money:
 - Money supply is determined by the central bank;
 - Monetary intervention via money supply
 - Stable and determined money demand
 - Assumptions: *homo oeconomicus*; trust in banks
- **Unsolved questions:**
 - Which actors have and impact on money supply ?
 - *finanzialisation* and gap between real and financial investments
 - Expectations: Impact on demand for money and credit.

CI Monetary aggregates ¹⁾ (annual growth rates; seasonally adjusted)



ECB Monthly Bulletin May 2014

2. A. Monetary theory

Alternative approach: endogenous money :

- **Starting with the missing links in exogenous money:**
 - Meaning of debt for investment
 - Power of commercial banks
- **Basics:**
 - Demand-driven credit demand causes money supply
 - Central bank does neither have full control over money supply not full control over effects of monetary policy: banks have strong impact
 - *Money is not neutral* (Davidson)
 - *I owe you* (Wray): modern monetary theory



2.B. monetary policy

- **Mainstream logic:**
 - Mainly driven by money supply guidance, newer approaches interest rate guidance
 - Endogeneity of money based on money multiplier of commercial banks
 - Transmission mechanism
 - C.B is in control of money market interest rates – interbank market not included
 - Optimum interest rate determined by *Taylor rule* and influence of *NAIRU*

2.C. Financial Stability

How questions of financial stability/instability enter the stage:

- **Stages of banking** (Chick / Dow)
- **Minsky:** Financial instability hypothesis:
 - Hedge, Speculative, Ponzi
 - Minsky moment
 - *supercycle* – increasing instability over longer time periods: institutional setting important (see among others Th.Palley)
 - Policy recommendations:
 - Big government
 - Wage policy
 - Strengthen regulatory setting of the financial sector
- **How to tackle the institutional setting?**
 - Bank based vs. Market based national financial systems

2. C. Financial Stability

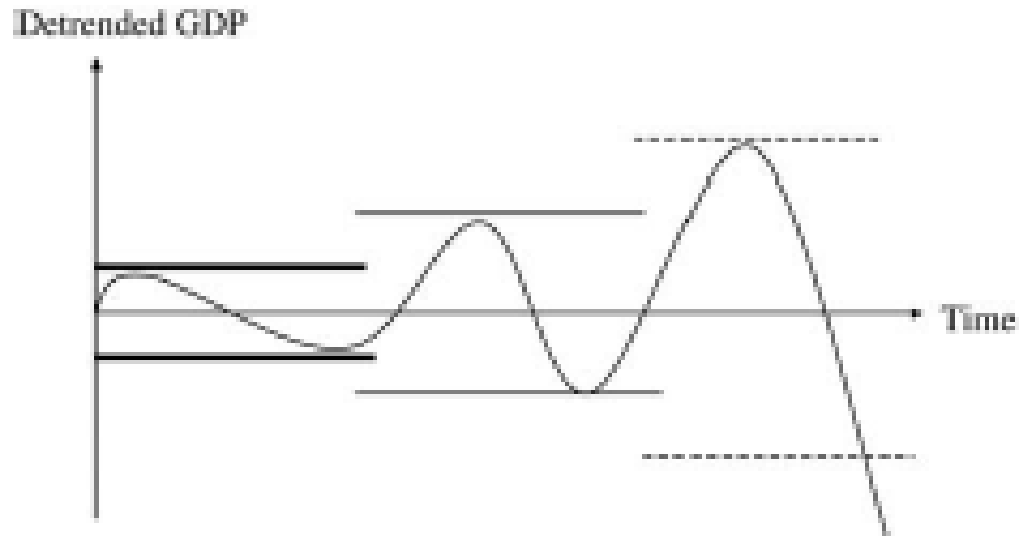


FIGURE 4. A symmetric Minsky super-cycle.

2. C. Financial Stability

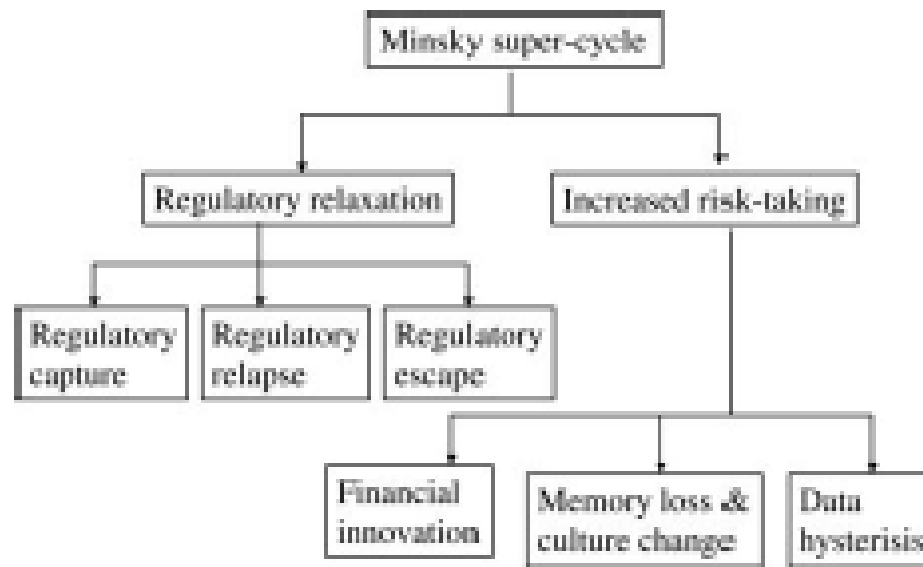


FIGURE 6. Details of the Minsky super-cycle.

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2.C. Financial Stability

- Financial market regulation: *preventive* vs *protective*

	Bank based	Market based
Flow of funds	banks	stock exchange
Control /Ownership	concentrated	split
Relation debtor / creditor	close	loose
Time horizon	long term	short term
Regulatory mode	protective	preventive

2. Financial Stability

Classification of Economies into national Financial Systems

- *Quantitative approach*

World bank:

- Bank vs capitalization
- Bank credit versus trading
- Trading versus overhead costs

⇒ Structure index

⇒ Sample dependent

2. C. Financial Stability - Quantitative Approach

Table 1: Classification of national financial systems according to financial funds flow

	EU25	Central EU&EE	South EU &EE	North EU & EE	EE
Austria	b	m			
Belgium	b	b			
Cyprus	b		b		
Czech Republic	b	b	b	b	m
Denmark	b			b	
Finland	m			m	
France	b	b			
Germany	b	b			
Greece	b		b		
Hungary	b	b	b	b	b
Ireland	m	m			
Italy	b		b		
Latvia	b	b	b	b	m
Lithuania	b	b	b	b	b
Luxembourg	b	m			
Netherlands	m	m			
Poland	b	b	b	b	b
Portugal	b		m		
Slovak Republic	b	b	m	m	m
Slovenia	b	b	m	b	m
Spain	m		m	m	
Sweden	m				
United Kingdom	m	m			

Source: Springer, 2005.

2. C. Financial Stability - Quantitative approach

Table 12.4 Structure index of the new member states

	EU25	EU south	EU central	EU north	EE
Czech Rep.	B	b	b	b	M
Hungary	B	b	b	b	B
Latvia	B	b	b	b	M
Lithuania	B	b	b	b	B
Poland	B	b	b	b	B
Slovak Rep.	b	m	b	m	M
Slovenia	b	m	b	b	M

Source: For data, see Annex 2.

2. C. Financial Stability - Qualitative approach

Table 12.5 Deposit insurance systems

Countries	type	Date enacted/ revised	Administration	Membership	Permanent fund	Source of funding
	explicit = 1 implicit = 0		official = 1 joint = 2 private = 3	compulsory = 1 voluntary = 0	funded = 1 unfunded = 0	0 = Private funding 1 = Joint funding 2 = Public funding
Czech Republic	1	1994	1	1	1	1
Estonia	1	1998	2	1	1	1
Hungary	1	1993	2	1	1	1
Latvia	1	1998	1	1	1	1
Lithuania	1	1996	1	1	1	1
Poland	1	1995	1	1	1	1
Slovakia	1	1996	2	1	1	1
Slovenia	0	—	—	—	—	—

Source: Demirgüç-Kunt and Sobaci (2000)

2. C. Financial Stability – Qualitative Approach

Table 12.6 Banking supervision

Country	Minimum capital-asset ratio	Actual risk-adjusted capital ratio	Risk-weight in line with Basel guidelines	Discipline – direct interventions
Czech Republic	8%	10.60%	Yes	Yes
Estonia	10%	16%	Yes	Yes
Hungary	8%	16.70%	Yes	Yes*
Latvia	10%	16%	Yes	Yes*
Lithuania	—	—	—	only provisions to cover actual losses
Poland	8%**	14.20%	Yes	
Slovakia	8%	Yes	Yes	None
Slovenia	8%	14.50%	Yes	Yes

Note: * direct interventions have not been undertaken in the last 5 years; ** first year 15%, second year 12%.

Data source: Database Banking Supervision, World Bank.

2. C. Financial Systems

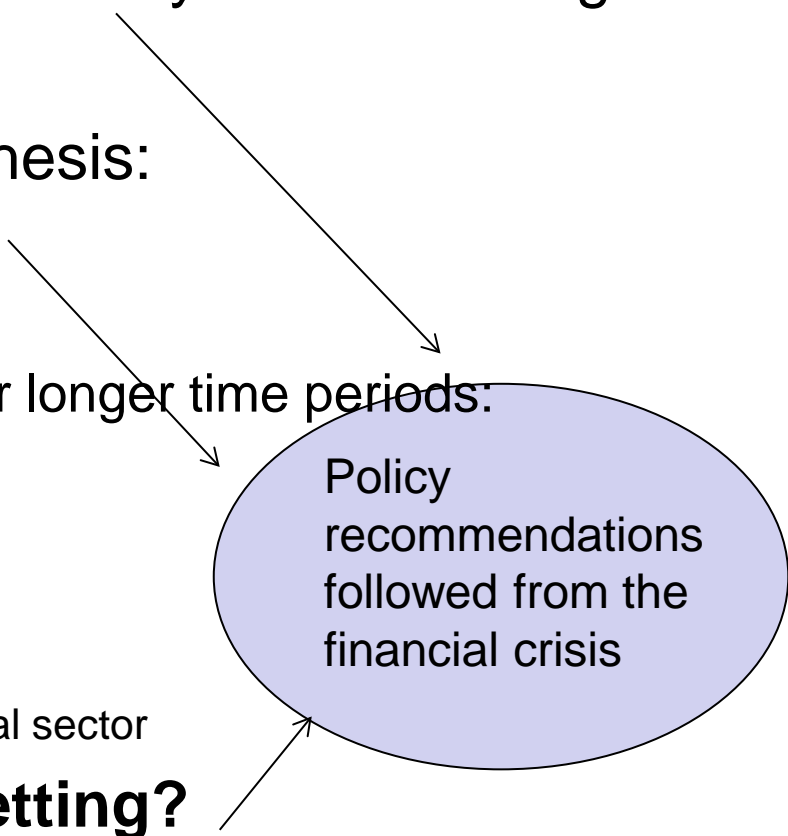
Findings from the classification of economies into national financial systems:

- institutional setting matters
- New Member States of the EU seem to comply to supranational regulations and do not have a historic development of national regulations => misfits increase potential for instability.

2.C. Financial Stability

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Policy
recommendations
followed from the
financial crisis

2.C. Financial stability

Based on the effects of the economic crisis the following policy recommendation came up:

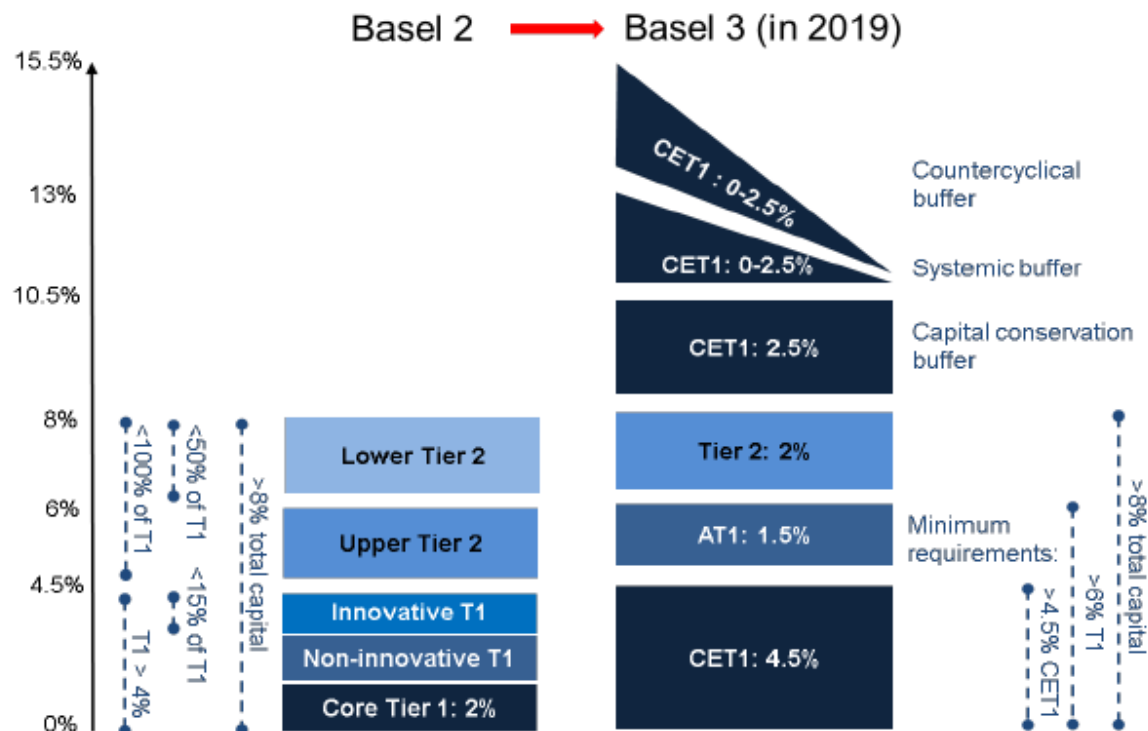
- Changes in investment banking
- Financial transaction tax
- Banking regulation reform:
 - Basel II to Basel III (requested: *Asset based reserve requirements* – Palley)
 - Banking supervision: *marcoprudential* regulation

2.C. Financial Stability

What has been done ?

No shifts towards asset based reserve requirements
but capital puffer regime !

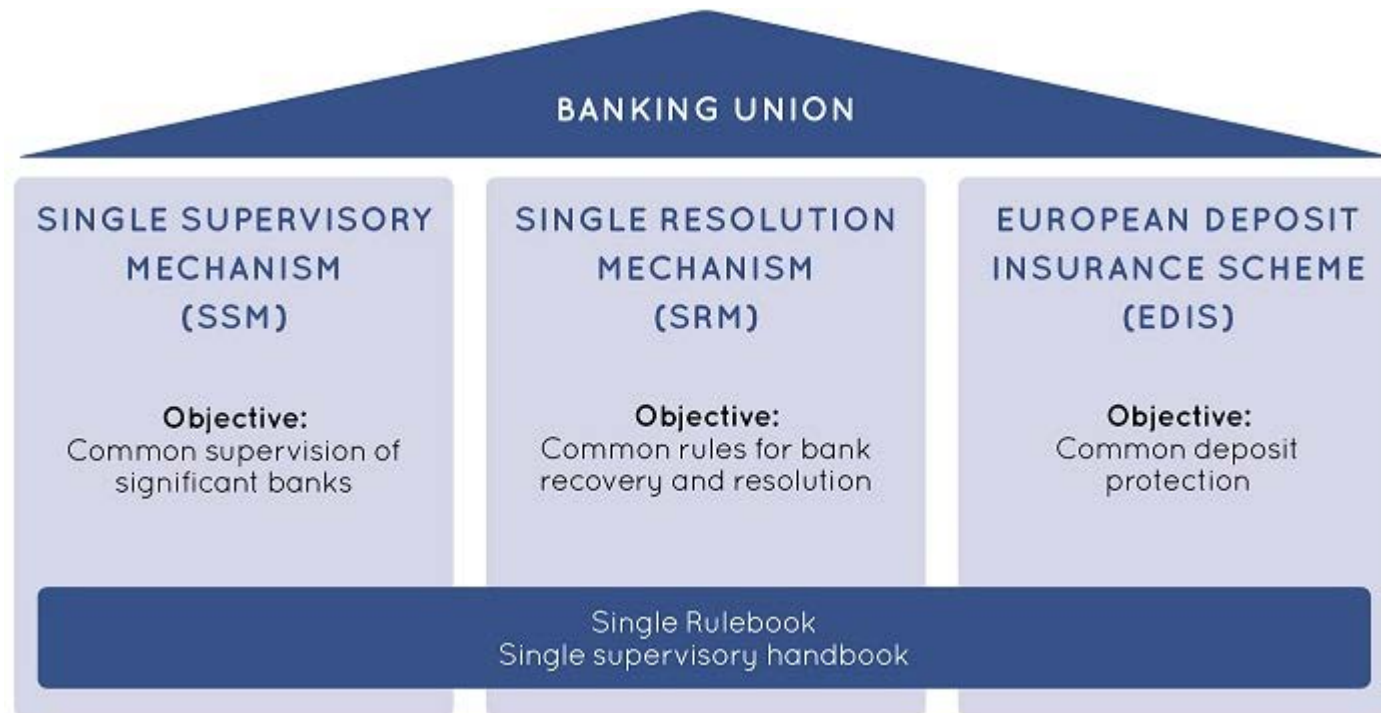
Figure 3. Basel II versus Basel III requirements from 2019



Source: Citi Research

2.C. Financial stability

What has been done ?



Example Austria: Effects of macroprudential regulation

List of identified institutions	Applicable systemic risk buffer			
	1.1.2016	1.1.2017	1.1.2018	1.1.2019
	% of risk weighted assets			
Erste Group Bank	0.25%	0.50%	1.00%	2.00%
Raiffeisen Zentralbank	0.25%	0.50%	1.00%	2.00%
Raiffeisen Bank International	0.25%	0.50%	1.00%	2.00%
UniCredit Bank Austria	0.25%	0.50%	1.00%	2.00%
Raiffeisenlandesbank Oberösterreich	0.25%	0.50%	1.00%	1.00%
Raiffeisen-Holding Niederösterreich-Wien	0.25%	0.50%	1.00%	1.00%
BAWAG P.S.K.	0.25%	0.50%	1.00%	1.00%
Sberbank	0.25%	0.50%	1.00%	1.00%
HYPO NOE Gruppe Bank	1.00%	1.00%	1.00%	1.00%
Vorarlberger Landes- und Hypothekenbank	1.00%	1.00%	1.00%	1.00%
Hypo Tirol Bank	1.00%	1.00%	1.00%	1.00%
Oberösterreichische Landesbank	1.00%	1.00%	1.00%	1.00%

Note: When both the systemic risk buffer (SRB) and the buffer for other systemically important institutions (O-SII buffer) might be applicable, the higher of the two shall apply.

Source: FMSG website

3. ECONOMIC POLICY ISSUES: EUROPEAN INTEGRATION AND DEVELOPMENT OF EMERGING MARKETS

3. Economic Policy: European Integration

Currently a missing link:

- 2 approaches:
 - Economic findings: free markets, welfare enhancing; common regulation rules
 - Political sciences: institutional setting, functionality of different findings
- ⇒ Liberal idea – no crisis possible
- ⇒ no success story – shortfalls documented very well
- ⇒ necessary to search for a coherent alternative view

3. Economic Policy: European Integration

	Postkeynesianism
General focus	Focus on specific economic mechanisms and causal relations and macroeconomic aggregates
Ultimate goal	Establish full employment and welfare state
Source of policy change	Benevolent politicians establish adequate institutions and implement the correct PK economic policy

3. Economic Policy: European Integration: - Possibility for heterodox approaches

	Postkeynesianism
Explaining crisis	Low economic growth due to economic policies which do not promote effective demand adequately
Spatial considerations	Nation states and regional analysis with their specific institutional structure; view on unequal developments
Focus on EU crisis	What are the problems in economic policy? How could the structure / setting be changed to improve the situation?
Dealing with the crisis	The institutional setting of the EU/Euro zone has to be improved: The implementation of proper structural setting is imperative.

3. European Integration:

Scenarios according to a PK point of view

[Niechoj (2015) and Jäger/Springler (2015) discussion]

- Scenario 1: Total meltdown into the unknown
 - Debts are high
 - Rescuing financial sector
 - Adoption of Keynesian policies; Stronger focus on competition and the new European economic governance
- Scenario 2: Social democratic (green) Europe
 - PK with high level of abstraction;
 - Keynesian institutions of EU level – coordinated fiscal policy; wage led growth; Regulation on financial sector; Progressive integration – Fordist national welfare states
 - Follows PK Idea

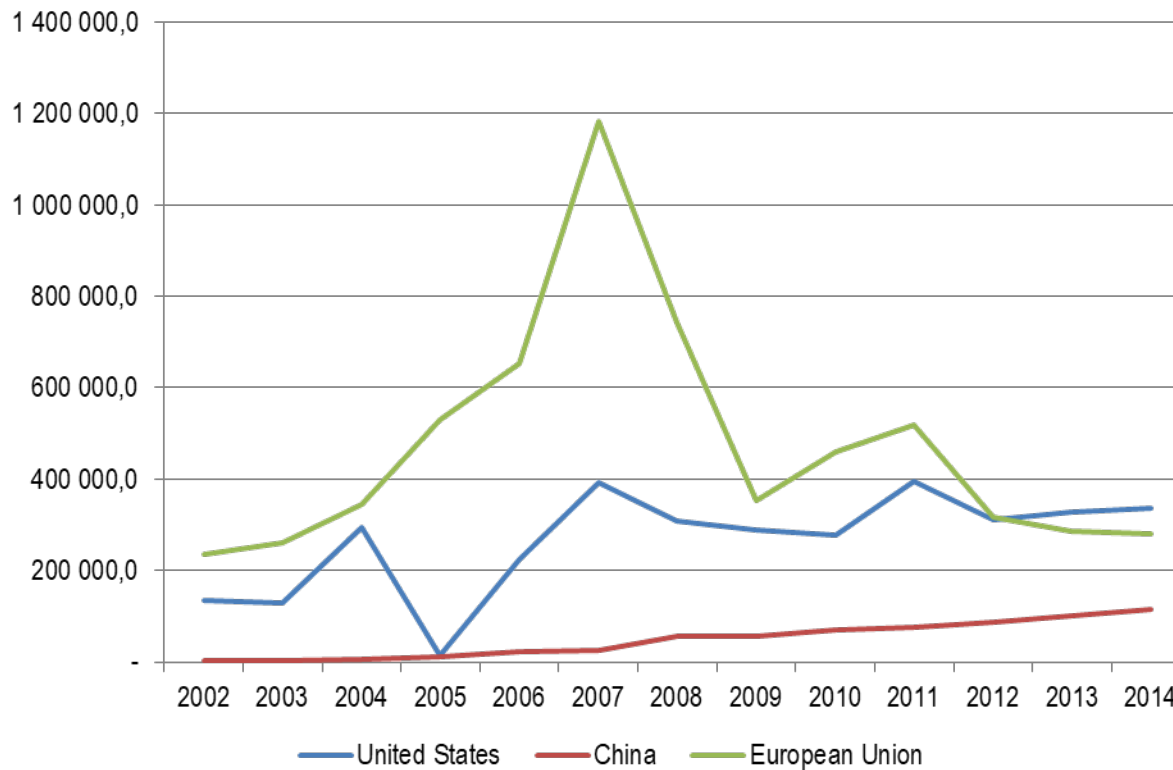
3. Scenarios for European Integration

- Scenario 3: Radical reformism to overcome capitalism
 - Erosion of neoliberal hegemony
 - Alternatives to reduce exploitation, not only regulation on financial markets but also more radically views to more equal income distribution;
 - PK capitalism needs to be reorganized
 - Not very likely
- Scenario 4: Authoritarian neoliberalism and muddling through
 - Strong anti-Keynesian Bias
 - Powerful export oriented capitalists and well organized transnational fractions have pushed for a deepening of neoliberalism - transnational companies profit from wage differentials and different productivities...
 - Deepen polarization

3. Economic Policy: Development of emerging markets

- New developments: FDI outflows from emerging markets – especially China into Europe.
- Mainstream economics: FDI flows always positive
- No distinction in ownership structures; power relations for *megacorps* are not taken into consideration
- Heterodox (PK) view to strongly integrate views from political science:
 - Starting points: SMN / NMN

3. Development of emerging markets

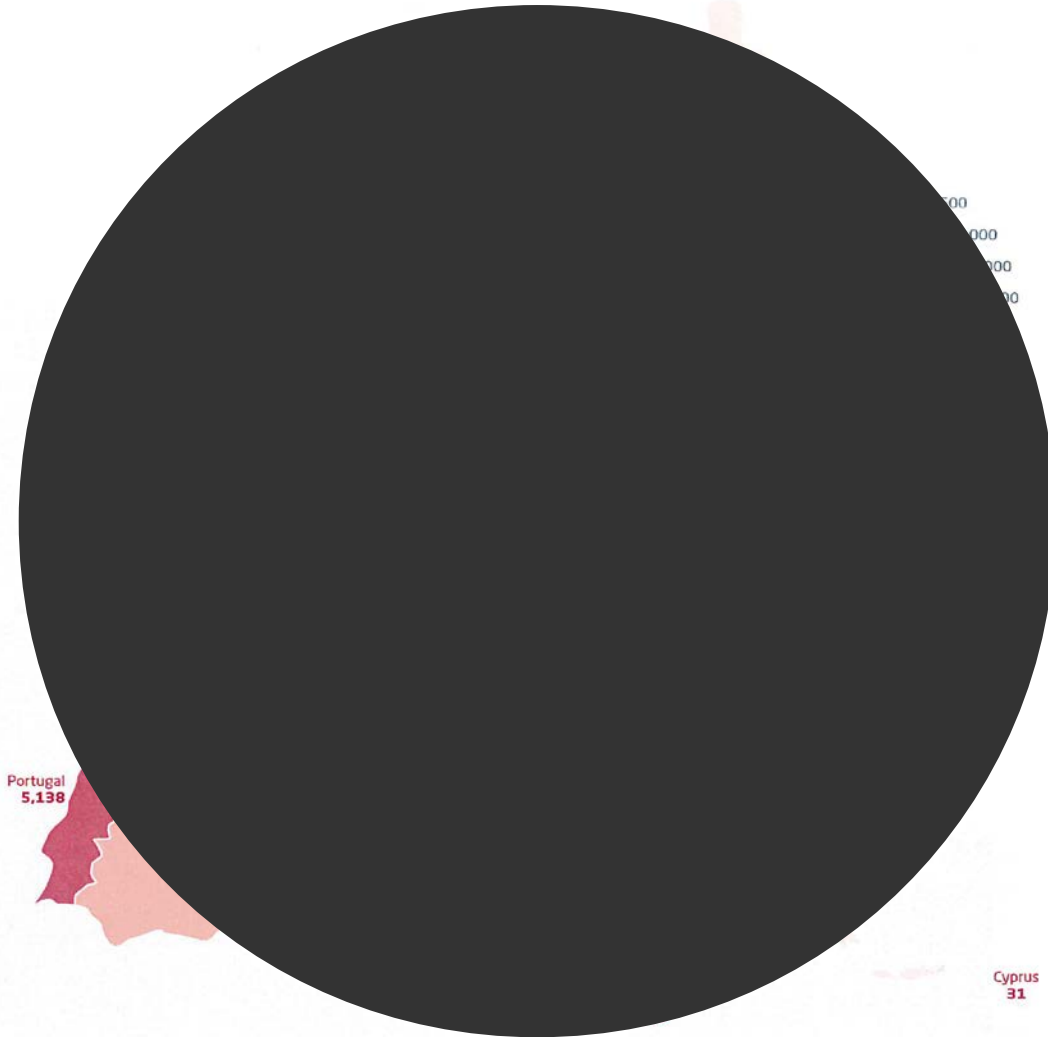


FDI outflows, 2002-2014 / WRI

3. Development of emerging markets

Investment sources are necessary in Europe, therefore FDI inflows are widely seen as possibility to overcome economic slump after financial crisis.

- ⇒ New role of Europe?
- ⇒ Is it now for economists to focus more strongly on more differentiated view on FDI ?
- ⇒ Labor conditions ?



3. Development of emerging markets

Mainstream Analysis:

application of OLI for FDI and location theory does not allow the implementation of power relations and institutional settings.

Alternative view :

Differences between NMN and SMN

- Based on Nölke (2013): differences in 5 institutional features between NMN and SMN
 - **Investment finance**: strong direct or indirect finance of the state even when company is listed at the stock exchange – therefore less depending on shareholders
 - **Corporate governance**: ownership structures and e.g. pension fund support
 - **Selective implementation of social rights** – division between formal and informal labor relations
 - **Education and Training** – qualifications are more general and not directed towards employability mode of firms
 - **Innovation transfer**: acquisition of innovative technologies
- Overall strong support by the respective nation-state !

Conclusions

- PK foundations and roots offer a concise alternative to mainstream economies
- Monetary theory and policy is applicable to current situation in Europe
- Financial distress is not tackled sufficiently by mainstream economics and can be explained by PK and is followed by policy advice. This is only implemented partly.
- Broader economic policy approach: European Integration – different scenarios can be distinguished. Keynesian approach applicable
- Openness to interdisciplinary approaches allow for the integration of political sciences views – institutional settings and power relations in MNE are explained in this discipline => might be starting point for shift in analysis of FDI (as Europe is affected in a new role currently)

Thanks !



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