Keynesian Humility or Neoliberal Arrogance?

The essence of the capitalist engine is uncertainty which translates into success for some, economic disappearance for others and more or less violent crises. It is therefore absolutely unthinkable to adhere to theories of perfect markets where information is efficient. The myth of self-regulation, which had once marginalized the state, was destroyed by the crisis which began in 2007 and has just been buried by European setbacks. Instability is the very heart of the world of finance: we suffer the brunt of it since 2007 and had been successively warned by Marx, Keynes and Minsky. Let us therefore return to reality and integrate uncertainty within our economic decision-making process and financial investment. Let us once again become modest and realistic and reduce our claims. Since the immense work and accomplishment of Keynes can be summed up in a single word – doubt –, as the monetarists and neoliberals are likened to their certainties which stick to them like glue. That it is healthy to have doubts! Doubt is the key underlying idea on which Keynes based all his theories. Doubt also leads to managing its risks or accepting measured losses, as it restrains the disproportionate bait of gain. The key doubt to all the most essential questions, and it is a survival instinct as a lesson in modesty, in both economic life and from the point of view of morality and intellectual honesty. Let us therefore learn again to respect and fear uncertainty which is an integral part of our daily lives. It is only having started arrogantly from his doubts that man multiplied acts with serious consequences.

Experts in economic science must therefore profoundly question their certainties again in light of today’s collapse since they are woefully misguided. One thing is for certain: it is essential, in these almost unprecedented turbulent times to return simplicity to economics, since the resolution to the crisis lies in basic, even elementary, remedies. Just as, in the reverse, it is the sophistication of financial instruments and neo-conservative fallacious reasoning which deliberately made the situation worse. Macro-economic considerations (employment, income and production, the role of the state) must therefore take precedence over micro-economic data where actors are decked out with the “rational” qualifier and where the market is likely to calmly balance supply and
demand by using key straightforward mathematical models. During periods of financial and economic crises and in the face of such imbalances, microeconomics — which cannot stabilize activity — must cede to the forces of macroeconomics. What, of the rest, must even be admitted by a monetarist of the caliber of Friedrich Hayek (1899-1992) and Nobel Economics Laureate in 1974), who himself recognized in 1966 “the domination of macroeconomics and the temporary decline of microeconomics”. During periods of financial and economic crises and in the face of such imbalances, microeconomics — which cannot stabilize activity — must cede to the forces of macroeconomics. What, of the rest, must even be admitted by a monetarist of the caliber of Friedrich Hayek (1899-1992) and Nobel Economics Laureate in 1974), who himself recognized in 1966 “the domination of macroeconomics and the temporary decline of microeconomics”. Or by Friedman in person who, in a letter to Time Magazine in February 1966, resignedly asserted: “In one sense we are all Keynesians now; in another, nobody any longer is a Keynesian…”, meaning by that that, if Keynesian theories face a wall when they should integrate microeconomic factors, they are systematically called to the rescue in times of crisis. It is within this same optic that Friedman was to declare in 1997 about the Japanese crisis: “The Bank of Japan can buy government bonds on the open market, paying for them with either currency or deposits at the Bank of Japan, what economists call high-powered money. There is no limit to the extent to which the Bank of Japan can increase the money supply if it wishes to do so. Higher monetary growth will have the same effect as always. After a year or so, the economy will expand more rapidly; output will grow, and after another delay, inflation will increase moderately. A return to the conditions of the late 1980s would rejuvenate Japan and help shore up the rest of Asia”. Today, Friedman’s prescriptions for remedying Europe’s woes would be identical, if he were still alive… Still, Keynesian theories and their enthusiasts were sent to their laboratories in favor of the good times of the previous decades for not being able to integrate the dogma of the perfect market and for doubting the rationality of economic agents. In doing so, the “neo-cons” strived to make the state obsolete. However, salvation could only be assured today by the intervention of this same state. While it had been ironically asked not to inhibit self-correcting market forces, it is finally realized that only its action can rebalance the macroeconomic indices during recession.

Since it is macroeconomics which teaches us the fundamental operation of debt in rebooting economic activity. In other words, it is macroeconomics itself which shows that the effects of public spending, investment by the state and tax reductions are more dramatic episodes where consumption and producing are on the decline. It is also during times of crisis that the increase in public spending is the least harmful effect on
deficits. Despite virulent criticisms from orthodox economists who ridicule Keynesian principles while accusing them of favoring lax behaviors, even irresponsible, it is now evident that the solution to the crisis will be by intervention on the part of the state, a precondition to restoring investment. Keynesianism is not about spending, recklessness or some kind of encouragement of “grasshopper” behavior. In this regard, the neoclassical safeguards vis-à-vis the worsening of public deficits are outdated to totally silence the automatic – mechanical – reductions in these deficits upon the return of growth and confidence. Restoring healthy and robust growth must be the number one priority knowing that creditors themselves – who never required that austerity be implemented – are certainly aware that drastic reductions in public spending will notoriously diminish their chances of being repaid. How do you deny the proof that a nation’s wealth is the immediate result of what is produced by its citizens?

Moreover, contrary to microeconomic certainties and claims, the activity of the players in our economy are not guided by rationality or by a wise person and a generous quest for balance, but simply by intuition, instinct and greed, when it is not by a sense of panic… All this being said, confidence – which is very far from finding its source or its explanation in rationality – is naturally the cornerstone of this building: its presence allows for progress as well as growth, whereas its absence leaves the door open to all contractions. As they are the psychological and behavioral factors which condition particularly economic activity, only the soothing, regulating and stabilizing action of the state is likely to restore balance – and equity – during turbulent times. It is from this angle, les idyllic but oh so much more prosaic and realistic, that the economy and investment must be analyzed which, far from responding to noble aspirations, are the manifestations of our most intimate, yet sometimes most vile, instincts, appetites, anxieties and obsessions. Therefore, “Homo economicus” falls from its pedestal: it is its greediness and lack of scruples which are self-destructive. Debt itself is like a type of hot potato that everyone tries to pass around in a “game of musical chairs before the music stops” says Keynes. But, how do we explain the “irrational exuberance” of markets (the famous expression of Alan Greenspan, Chairman of the U.S. Federal Reserve from 1987 to 2006) or how do we understand, in contrast, stock market crashes? The return of the state will prevail when we admit that our control over the economy is at a minimum imperfect and limited by our own intellectual and mental abilities. Since, to borrow again from Keynes, economy “is one of these pretty, polite techniques which tries to deal with the present by abstracting from the fact that we know very little about the future”. Keynes, who never stopped reminding us that it was impossible to predict the future or even our future behavior, wished “economists could
manage to get themselves thought of as humble, competent people on a level with dentists”, adding “that would be splendid”…

Only typical Keynesian measures will save us now. Only government stimulus conducive to encouraging investment and job creation can actually save the economy, in the absence of private initiative and as part of an anemic demand. And only the determined action of central banks in the sense of compressing financing costs motivates companies to invest in the real economy, as long as the banking intermediation system plays its role. The objective is the famous “euthanasia of annuities” that promotes the channeling of savings into investment and therefore into employment. As many emergency measures recommended even by the high priests of monetarism, Milton Friedman and Anna Schwarz. And even greedily applied in 2001 by the then President of the Federal Reserve, Alan Greenspan, and of course by his successor Ben Bernanke – yet a faithful follower of Friedman – from the intensification of the crisis in fall 2008. Taking advantage of its multiple quantitative rate cuts, did he not cause hatred and harsh criticism from the neo-liberals, who prefer clearly high unemployment to inflationary threats that challenge their wealth? The Republican candidate in the last U.S. presidential election, Mitt Romney, did not he hastened to demand the head of Bernanke? Besides, staying with the Republicans and with the right-wing people persuaded that tax cuts are a neo-conservative find… and who seem to ignore that it is Keynes who had first suggested reducing individual and corporate taxes as a way of boosting a faltering economy. While the great exponent of the Austrian School, Friedrich Hayek, was strictly against tax cuts so long as the state does not also reduce its lifestyle. Yet, is it not precisely the opposite course that was chosen by the most worthy descendant of the “neo-con” movement – that President George W. Bush – who, when he became president, adhered to tax cuts (especially for the more affluent), accompanied by an unprecedented surge in spending U.S. federal spending? Indeed, Keynes departed from the principle that large tax reductions should target the middle class, who would thus be encouraged to spend more, since it spends almost all its income, whereas the wealthy have a tendency to save. In the same vein, it is government that must take over when the private sector is no longer able to stimulate the economy. And why would it not be the “spender” of last resort in the exact same way as it is the lender of last resort? Indeed, aren’t the U.S. Democrats, like the U.S. Republicans, unanimous in demanding that the government cut its spending drastically in order to avoid falling off the fiscal cliff? Isn’t the very choice of this expression not likely to incur anxiety among a population – not necessarily aware of the technical debate – who is led to believe that the cataclysm is imminent? And that the only answer is sacrifice – more and more sacrifices – while the financial elite feasts and
the 1% become wealthier… The fact is that integrating the proposals discussed above – healthy state intervention against a backdrop of a devastated economy, maintaining low interest rates, tax cuts – are void and have no effect if the state decides to drastically reduce its lifestyle. Keynes taught us already: debts must be repaid only when the economy recovers. Otherwise: growth will be stifled in an environment where activity is very fragile. Tax increases, debt repayment and reduction in public spending can only be achieved without risk in a healthy economy. Knowing that, contrary to myth – or horror story – we the happy orthodox economists and “neo-cons” politicians, it is perfectly possible to arrive at a healthy economy despite, and in the presence of, a large public debt. Thus the true fiscal cliff would put into place today in the U.S. austerity measures comparable to the rigorously imposed dementia in Europe. It is not possible – or honest – to be guided in half measure by Keynes whose teachings are clearly cohesive.