

## Tily's 'semantic pirouettes' and Lavoie's post-'Keynesianism': a comment on M.

### Lavoie "Rethinking monetary theory in the light of Keynes and the crisis"\*

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I am grateful to Marc Lavoie for reporting my position on Keynes and endogenous money.

Not only was the *General Theory* based on endogenous credit creation, but it was the foundation to the whole of Keynes's economics. As with other post-Keynesians, Lavoie rejects this position. He avoids my broader point that the failure to recognise endogenous credit creation is a symptom of a wider failure of interpretation of the *General Theory* and Keynes's economics more generally.

While post Keynesians reject IS-LM theory, 'Keynesian' policy has proven more difficult to dislodge. Yet Keynes's fundamental concern was not the resolution of economic crisis. His central insight was that defective monetary conditions – and above all a too high rate of interest ("meaning by the 'rate of interest' the complex of interest rates for all kinds of borrowing, long and short, safe and risky", Keynes, 1931, p. 272) – inhibited the sound operation of monetary economies. Over the course of his life he devised new institutional arrangements and process that would prevent dear money and allow cheap money to prevail on a permanent basis.

Lavoie revives aspects of Keynes's practical conclusions around debt management policy that have had little emphasis in the literature (drawing on Kregel, 2013; see also Tily, 2010, Chapter 6). But does so as part of an apparatus to resolve crisis, and to show Keynes anticipating quantitative easing. Though the Bank of England for one are alive to this point (Broadbent, 2014). In general he agrees with 'Keynesians' that in the *General Theory* Keynes made the switch to fiscal policy (p. 186), seeing monetary policy may be inadequate to resolve crisis. Indeed the substantial and concluding point of the paper is a call for fiscal policy at the zero bound à la Krugman (or Simon Wren-Lewis in the UK).

No matter how important the fiscal policy point, it was *not* the substance of the *General Theory*. The substance of the *General Theory* was the replacement of the classical theory of interest with the theories of liquidity preference and the marginal efficiency of capital (MEC). These explained how dear money resulted in low but unstable investment, and the means to and necessity of setting cheap money. The causality of the greatest importance was from interest to the economy, not the other way around. The impact of negative 'animal spirits' on the MEC also explained why fiscal policy was likely to be necessary in addition to monetary policy in a slump. But, on a fundamental level, the theory substantiated, in a logically rigorous way, his original and central insight about monetary conditions.

In doing so Keynes did not neglect credit, in this context the idea is ludicrous. With the *General Theory*, the emphasis switched to money as a store of value, and means of exchange considerations fell into the background (as he warned in the 'preface'). In the specific application of the theory of liquidity preference to debt management policy, money (as a store of value) is rightly understood as exogenous (e.g. gold or Treasury bills). But for the purposes

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of the theory of investment demand (and the wider repercussions on aggregate demand), money (as a means of exchange) and so credit is supplied endogenously at the rate of interest.

Lavoie's specific charge comes as follows:

"Tily and a few other post-Keynesian authors say that a distinction must be made between a constant variable and a given variable, but these semantic pirouettes cannot hide the fact that Keynes used to be a staunch defender of the Quantity of Money in his earlier works, and that this gets reflected many years later in the *General Theory*" (Lavoie, 2016, p. 179).

In Tily (2010) I borrowed the terminology 'given' from Victoria Chick and Sheila Dow (e.g. Chick, 1983, p. 184 and Dow, 1997) and it seems appropriate in the means-of-exchange context. Though Chick and Dow would have to speak for themselves. Maybe Keynes did defend the quantity theory, but as an accounting identity the relation is not so problematic. And of course with the *General Theory* he began to see the velocity of money as a measure of liquidity preference (Chapter 15).

In the case of fiscal policy itself, Keynes's theory permitted the expansion of government expenditure without upward pressure on the rate of interest. In the Second World War he devised 'Treasury deposit receipts' as an extension of the floating debt that obliged banks to create credit and lend it directly to the government (as *deposits*). Keynes saw that the expansionary effects of loan-financed expenditure on the whole economy would mean the policies were self-financing. With saving also a result of expansion, it is incidental to the determination of interest. Likewise the condition of the public finances, as in the War. In more normal conditions, with spare capacity, government expenditure (current or capital) would strengthen the economy (via the multiplier), increase tax revenues and reduce transfer expenditure. To endorse 'Keynesian' economics is also to endorse the conflation of a financial transaction – loan-financed expenditures – with an economic outcome – the deficit (strictly, public sector net borrowing) – and to underestimate the sophistication of Keynes's account of fiscal policy.

The emphasis on fiscal policy meant most post-Keynesians were little better prepared for the global financial crisis than the rest of the profession. Under Keynes's theory, private debt inflation is an inevitable consequence of excessive expansion when interest rates are dear: for a high rate of interest is harder to earn than a lower rate of interest (Tily, 2007, Chapter 7). The global financial crisis originates in a private debt crisis that was the eventual and inevitable result of the restoration of dear money from 1980. This restoration coincided with the decisive dismantling over the 1970s and into the 1980s of the institutions and processes that were owed above all to Keynes. That this reversal has led to a crisis of a comparable nature and severity to the one that motivated implementation should perhaps not be surprising. Equally, Keynes's practical conclusions may be no less relevant today than they were in the first half of the twentieth century. It is surely certain that the global monetary system is still seriously defective.

I seek to absolve myself of the charge of semantic pirouettes. My observation is that Lavoie's post-Keynesianism is more accurately post-'Keynesianism'. He bolsters 'Keynesian' economics and policy with a substantive theory of credit. As with Kaldor, Hicks and Moore, Lavoie distances Keynes from this account. I remain baffled why post-Keynesians spend so much energy trying to show Keynes as wrong, rather than address whether he had anything right to say that went beyond the 'Keynesian' interpretation. And I ask Lavoie for a view on my more substantive claims.

## References

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