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Minsky and Economic Policy: "Keynesianism" All Over Again?

by

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ABSTRACT

Recently, national newspapers all over the world have suggested that we should reread John Maynard Keynes, and that Hyman P. Minsky provides a valuable framework for understanding the world in which we live. While rereading Keynes and discovering Minsky are noble goals, one should also remember the mistakes that were made in the past. The mainstream interpretation and implementation of Keynes's ideas have been very different from what Keynes proposed, and they have been reduced to simple "fiscal activism." This led to the 1950s and 1960s "Keynesian" era, during which fine-tuning was supposed to be a straightforward way to fix economic problems. We know today that this is not the case: just playing around with taxes and government expenditures will not do. On the contrary, problems may worsen. If one wants to get serious about Keynes and Minsky, one should understand that the theoretical and policy implications are far-reaching. This paper compares and contrasts Minsky's views of the capitalist system to the tenets of the New Consensus, and argues that there never has been any true Keynesian revolution. This is illustrated by studying the Roosevelt and Kennedy/Johnson eras, as well as Keynes's reaction to the former and Minsky's critique of the latter. Overall, it is argued that the theoretical framework and policy prescriptions of Irving Fisher, not Keynes, have been much more consistent with past and current government policies.

JEL Classifications: E12, E2, E6, B22

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INTRODUCTION

Minsky's analysis led him to conclude that there are different forms of capitalism each with pros and cons. Laissez-faire capitalism, where the government represents an insignificant proportion of the economy, promotes individual initiatives and creativity (what one may call entrepreneurship) but also generates depressions, and unfair inequalities. On the contrary, big-government capitalism is more stable but also comes with its own problems like a lack of dynamism and inflationary tendencies. Following Keynes, Minsky stated that unfair distribution, economic instability and unemployment were structural problems of market mechanisms, and so he promoted a form of capitalism that significantly involves the government.

Many current economists would associate Minsky's view with the Neoclassical Synthesis of the 1950s and 1960s, a.k.a. "Keynesianism," when monetary and fiscal discretions were used to fine-tune the economy. In this case, most economists would brush away Minsky's proposal for the same reasons they rejected Keynesianism in the 1970s: lack of rationality (Lucas's critique), ignorance of credibility and reputation, and lack of consideration for lags and structural barriers to low unemployment.

However, Minsky was careful to note that there are different forms of big-government capitalisms and that not all forms of government activism are consistent with Keynes's policy agenda. The Bastard Keynesianism of the mid-20th century, to take Joan Robinson's colorful characterization, tends to generate inequalities, inflationary pressures and long-term unemployment by creating strong income disincentives to reenter the labor force and to hire, by not dealing properly with the chronic shortage of jobs and focusing mainly on retraining and fine-tuning, by limiting collective bargaining processes, and by limiting government involvement to unproductive activities. This form of big government capitalism also tends to promote moral hazard in the financial sector by putting most of the emphasis on sustaining investment while having a limited reactive regulatory and supervisory framework. On the contrary, Minsky put forward a form of big government that limits political discretion in daily socio-economic decisions, and that limits inflationary pressures as well as promotes work habits and individual initiatives.

The first part of the paper broadly reviews Minsky's theoretical framework and compares it to the New Consensus in order to understand his position regarding the role of the government. The second part of the paper presents some of the pros and cons of big-government capitalism and presents some of the solutions proposed by Minsky to deal with potential problems. The last part of the paper studies the "Keynesian" agenda of the Roosevelt and Kennedy/Johnson eras. Overall, the paper concludes that a big-government is needed but that it should not take the form of a fine tuner, nor of massive state control, but of a planner that complements, and interacts with, the private sector.

MINSKY AND MAINSTREAM: TWO VIEWS OF CAPITALISM

Real Exchange Economy vs. Monetary Production Economy

Today most economists assume that the study of barter provides a good proxy to understand all economic systems (tribal, command, and capitalist systems). In a barter theoretical system, economic agents have a given amount of resources and market exchange allows them to better their positions by obtaining the goods desired. Money may be added to the story but it does not change substantially, or at all, the conclusions drawn from pure barter. Money is just a means to smooth exchange and is not sought for itself; individuals care only about the material gains and losses from exchange before making a decision so that "prior to the introduction of informational asymmetries, […] financial structure is irrelevant" (Gertler 1988: 581). Once those gains and losses have been determined in a set of complete markets, all exchanges are executed instantaneously for all present and future contingencies, and nothing changes unless "shocks" affect the system. The future is known with certainty at least in the sense that all contingencies have been priced correctly and included in decisions. Moreover, if, as the result of a shock, someone decides to reverse a decision, this can be done easily and immediately.

Keynes called the previous system a real-exchange economy and argued that it does not apply to capitalism. Capitalism is a monetary-production economy. Commodities need to be produced before they can be exchanged, and production is undertaken with the expectations of selling output, needs to be financed, takes time to be implemented and completed, gathers groups with different economic interests, and involves irreversible decisions. All this is done in the context of a competitive environment that emulates monetary accumulation and imposes monetary return targets. Thus, capitalism has two salient features, it pushes individuals to anticipate an uncertain future in order to get an edge against competitors, and financial considerations are at the heart of the system. Consequently, "money plays a part of its own and affects motives and decisions" (Keynes 1933a [1973]: 408) and so influences the allocation, production and distribution processes (Veblen 1901: 214-215). Another consequence is that the system is highly dynamic and forever changing; stability is inconsistent with the principle of edging others through constant innovations.

All this is in sharp contrast with the barter system; money is not a patch that can be added at will to the theoretical framework, it must be at the heart of a theoretical framework that aims at understanding capitalism. In a capitalist economy, people focus on their liquidity and solvency and those financial concerns are inclusive of purchasing power concerns. Thus, more than the purchasing power of money, people care about the financial power of money, i.e. the capacity to meet financial commitments when they come due. The central importance of those financial attributes, however, is not based on the existence of asymmetries of information but on the nature of capitalist economies. Unfortunately, those financial aspects, which are at the core of Keynes's analysis, were pushed aside and made irrelevant by Bastard Keynesianism (Patinkin 1956; Modigliani and Miller 1958); "Keynesianism" was back to a Pigouvian world and the insights of Keynes and the late Fisher were ultimately lost.

Intrinsic Stability vs. Intrinsic Instability

In a real-exchange economy, under perfect competition, market forces help to stabilize economic activity, they do not generate economic instability by themselves. The latter is a rare event that is generated by external factors like government intervention and random shocks. Government intervention is thought to be intrinsically unstable for two reasons (Friedman and Schwartz 1963; Friedman 1968; Kydland and Prescott 1977; Barro and Gordon 1983). A first reason is the assumed incompetence of policymakers to deal with economic problems, as well as the lags involved in policymaking, which lead to economic mismanagement, instability, and suboptimal economic results. A second reason is political interests, which, even if policymakers are well-intentioned, lead to time inconsistency.

Minsky's research led him to conclude that capitalism is a highly dynamic system permeated by dialectical forces and circularities (feedback loops) specific to this system. He argued that "stability is destabilizing," i.e. prolonged economic growth generates financial fragility, and that relevant business cycles are mainly "due to financial attributes that are essential to capitalism" (Minsky 1986: 173). He noted that periods of financial instability are not rare events, but that since World War II their effects have been contained by massive government interventions (albeit with large side effects). He and others criticized Monetarists for being too restrictive in their definition of financial crises by reducing them to bank panics (Schwartz 1988, 1998), and for brushing aside events that would have been catastrophic (potentially of the same magnitude as the Great Depression) if the government had not intervened (Sinai 1976; Minsky 1986; Mishkin 1991).

The dialectical nature of capitalism means that both market forces and the government, as well as their interactions, may promote stability and instability. In terms of market forces, Minsky emphasized, among others, the dialectical nature of competition, innovations, and banks. Competition promotes economic growth and entrepreneurship, but it also promotes short-termism and conformism, even though this may entail a great deal of risks. Innovations create new markets but also alter the structure of the economy, behaviors, and incentives. Banks, at least in the "commitment" (or "partnership") banking model, promote stability by carefully selecting borrowers, but banks also promote instability because of the structure of their balance sheet and because of competitive pressures to meet targeted returns. In terms of government intervention, Minsky noted that a big government, through its buffer programs and regulations, promotes economic stability but also tends to generate inflationary pressures and to promote moral hazard. In addition, competition pushes the private sector to try to evade, through innovations, the barriers put on profit accumulation by regulation. Thus, if the government is too slow to respond to changes in the economy, its regulations may become obsolete and may promote instability.

This dialectical aspect of capitalism has been observed by many economists, practitioners and casual observers:

> In the 1960s, commercial bank clients frequently inquired how far they could prudently go in breaching traditional standards of liquidity and capitalization that were clearly obsolescent. My advice was always the same—to stick with the majority. Anyone out front risked drawing the lightning of the Federal Reserve or other regulatory retribution. Anyone who lagged behind would lose their market share. But those in the middle had safety in numbers; they could not all be punished, for fear of the repercussion of the economy as a whole. […] And if the problem grew too big for the Federal Reserve and the banking system were swamped, well then the world would be at an end anyhow and even the most cautious of banks would likely be dragged down with the rest. (Wojnilower 1977: 235-236)

Regarding the financial troubles involving the hedge fund Long-Term Capital Management (LTCM), Schinasi noted that:

> Although it is easy in retrospect to question why LTCM's counterparties did not demand more information, in a competitive environment, cost considerations must have weighed heavily. Clearly, LTCM's counterparties thought the cost of more information was too high, and walking away from deals was not seen as in their interest. (Schinasi 2006: 221)

However, even if the cost of information is low, it may not be in the interests of individuals to check the information:

> Above all, it is evident that the capacity of the financial community for ignoring evidence of accumulating trouble, even of wishing devoutly that it might go unmentioned, is as great as ever. (Galbraith 1961: xxi)

Recently, in the mortgage industry, lenders did not bother to verify the stated income of borrowers with the I.R.S. even though they had the means to do so quickly and at very low cost (Morgenson 2008). Overall, therefore, Minsky noted that there is nothing magical about market forces, and the same applies to government intervention; however, the government can help to stabilize the system.

Aside of proper regulation and supervision, stabilization comes through the cash-flow and balance-sheet impacts of governmental activities (including the central bank). In terms of cash flows, government expenditures and transfers provide some income to the private sector. In terms of balance sheet, a sovereign government injects default-free liquid assets in the private sector. Government deficits also indirectly help to sustain asset prices because the latter depend on the discounted value of expected future profits (which partly depend on current profits). Finally, the government also directly helps to sustain asset prices by acting as a lender of last resort whenever necessary. The Keynesian multiplier is a common way to present the direct and indirect income impacts, but Kalecki's equation of profit is maybe more insightful to show the direct impact of government spending and taxing on the private sector. The macroeconomic monetary gross profit of firms is equal to (Kalecki 1971):

$$\Pi = I - S_W + DEF + NX$$

With Π the gross profit after taxes, S_W the saving of wage earners, I the gross private domestic investment, *DEF* the government fiscal deficit, and *NX* net exports. Thus, through its fiscal policy, the government sector helps to contain the destabilizing effect of the positive feedback loop that is present in the previous equation. Indeed, the gross profit of the business sector is sustained by its investment expenditure, which in turn depends on the profit expectation of entrepreneurs. This "peculiar circularity of a capitalist economy" (Minsky 1986: 227) is part of the internal flaw of capitalism; however, entrepreneurs have usually no knowledge of this process, or do not take it into account, which has important implications for the dynamics of the Minskyan system (Tymoigne 2008).

Government: Temporary and Limited vs. Permanent and Broad

Because Minsky and the New Consensus have a diametrically opposed view of capitalism, it is not surprising that their view of the role of the government differs greatly. In the New Consensus, it is only if there are market imperfections, like price rigidities or asymmetric information, that the government has a role to play. The government should apply temporary, quick and targeted policies in order to compensate for those imperfections and to put the economy back on its "natural" path. Policy intervention, thus, may be good as long as the government does not try to push the economy above its natural path and the response is quick. The latter conditions are usually not verified; therefore, having policy institutions that are isolated from political influences, or constrained by rules, is important. Moreover, this short-term fine-tuning should be complemented by a long-term policy that aims at promoting competition so that market mechanisms can play fully.

On the contrary, Minsky viewed the government as a necessary complement to the profit-oriented sector (and more generally the individual sphere of the economy). Given that, according to Minsky's Financial Instability Hypothesis, market mechanisms tend to promote inflationary pressures and financial fragility as the economy tends toward full employment, a major role of the government is to promote stable full employment, that is, non-inflationary and financially sound full employment. This requires that the government intervenes continuously over the business cycle, rather than sporadically during downturns and upturns. Given the institutional context, specific financial developments always tend to generate stagflation and/or recession, and the point of policy is to prevent, or at least to constrain, their developments independently of short-term profitability and short-term welfare gains.[1]

In order for the government to be able to intervene continuously over the cycle, it should put in place structural *macroeconomic*[2] programs that directly manage the labor force, pricing mechanisms, investment projects, and constantly monitor financial developments. Because those programs would be permanent and structural, rather than discretionary and specific to one administration, they would be highly isolated from the political cycle and political deliberations. In addition, they would manage the goal directly, rather than indirectly through interest-rate manipulations, tax incentives or indirect spending.[3] All this eliminates problems of lags, credibility, and time inconsistency. However, this does not mean that the government should apply a rule blindly when implementing its policy; discretion is still possible within each program to make sure that it works best. For example, Social Security is a structural program but

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[1] Recently, innovative mortgage contracts and securities have been praised for allowing low-income households to become homeowners. However, given their structure, those financial innovations also led to the emergence of Ponzi home financing and frauds, and the welfare gains *predictably* were short-lived. Some of those financial innovations should probably not have been allowed to exist and low-income homeownership may not be sustainable without government programs.

[2] Micromanagement would be left to individual initiatives. The goal of the government is to control the overall direction of the system, not all prices and production processes (Minsky 1986: 293, 308).

[3] Discretion could still be used to smooth the business cycle if needed, but the structural programs would already do most of the job. Tax incentives and subsidies should be used for long-term purposes in order to stir the economy in the direction that the government would prefer.

government employees still have large discretion to determine if someone qualifies for benefits. As shown below, the same applies to the programs put forward by Minsky, in which human discretion is still possible within the set of rules and structures.

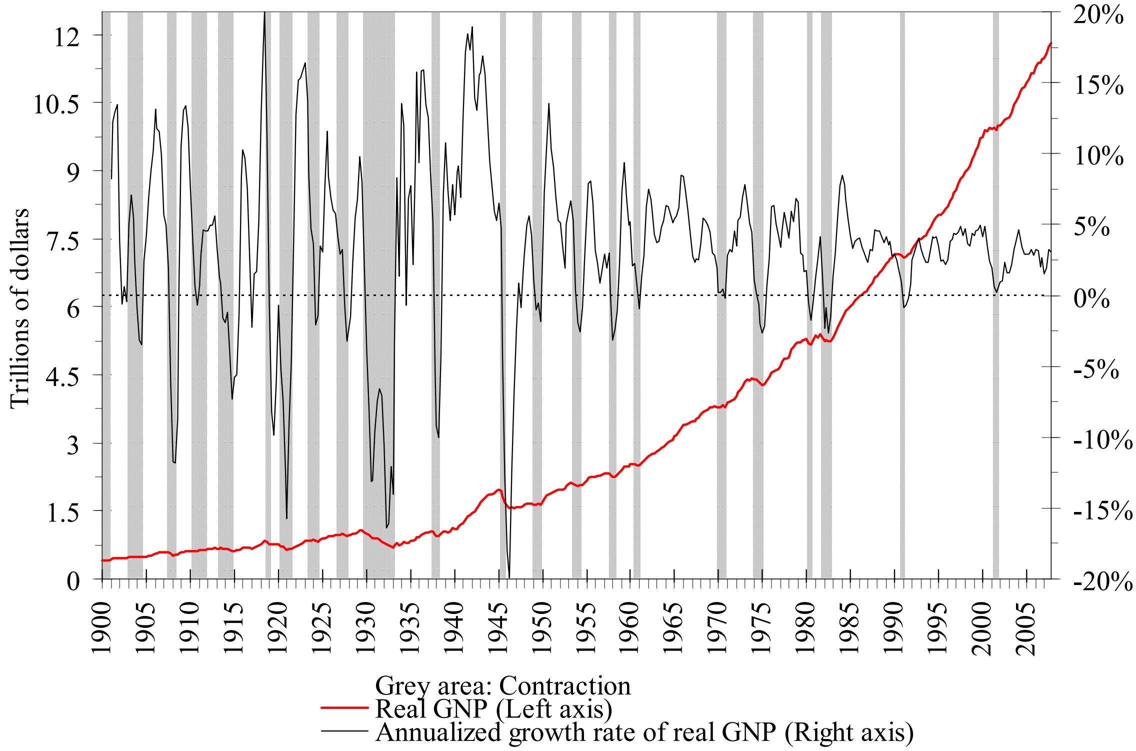
In the end therefore, for Minsky, individual economic freedom and big government are not incompatible. On the contrary, a big government is necessary to have an economy "where freedom to innovate and to finance is the rule" (Minsky 1993: 81). Entrepreneurs' creativity and imagination can thrive more fully and be more focused because of the higher stability of the system.

GOVERNMENT INTERVENTION IN MINSKY: STABILIZATION POLICY

From Small to Big Government

Without a doubt, a bigger government has helped to stabilize the growth process in the United States. As shown in Figure 1 and Table 1, the period between 1900 and 2007 can be divided into two parts with a dividing line set in 1946. The first period recorded more frequent, longer and deeper recessions. Upswings were also much more fast and short, making the overall business cycle erratic and unstable. The post-1946 era recorded smoother growth and grew at about the same rate as the first period, with a rate of growth of real GNP of 3.356% (against 3.364% for the first period).

Figure 1: U.S. Business Cycle, 1900:1-2007:4 (Base: 2000)



Sources: NBER, BEA, Gordon (1990). Calculation by the author.

Table 1: Characteristics of recessions before and after World War II

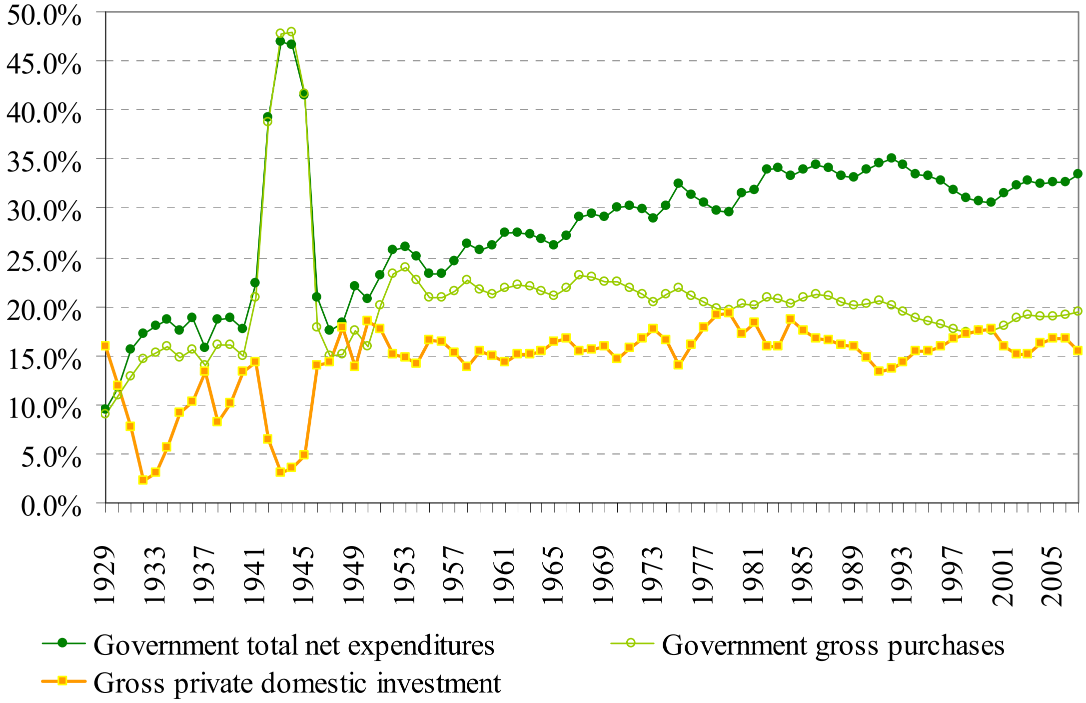
	Number of contractions	Average Frequency	Average Length	Average Decline in real GNP
1900-1946	12	3.9 years	18.1 months	-6.7%
1947-2007	10	6.1 years	10.4 months	-1.5%

Sources: NBER, BEA, Gordon (1990).
Note: The average decline in real GNP includes all quarters with a negative growth rate, even if there is no contraction at that time.

This much more stable economy is due to the much bigger size of the government. Figure 2 shows that the government has more than tripled in size from about 9% of GDP in 1929 to more than 30% of GDP in 2007. Figure 3 shows that most of the contribution to this growth has come from the federal government, which has grown from about 2% of GDP in 1929 to about 20% of GDP in 2007. The state and local governments have also contributed to the growth but in a more moderate way as shown in Figure 4. After the mid 1950s, this growth of the government sector has taken the form of increased Social

Security payments, welfare payments, interest payments and subsidies, while government consumption and investment have declined steadily especially for the federal government.

Figure 2: Size of the government sector

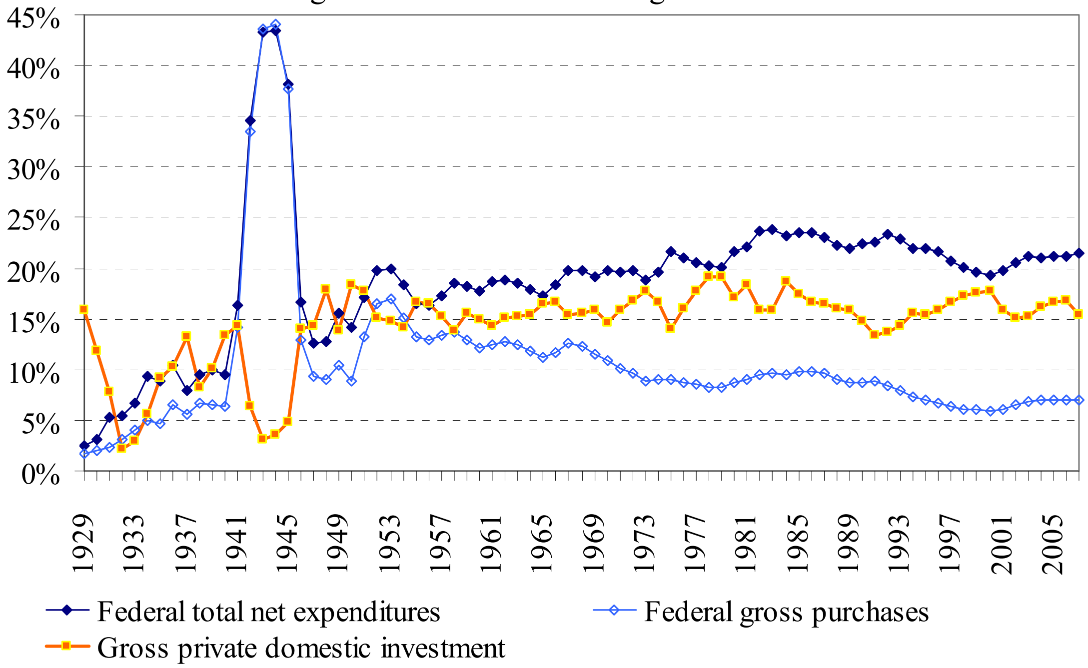


Source: BEA

Note: Government gross purchases refer to the gross investment and consumption of the government. Government total net expenditures include government gross purchases net of consumption of fixed capital, plus all net payments to the private sector and the rest of the world.[4]

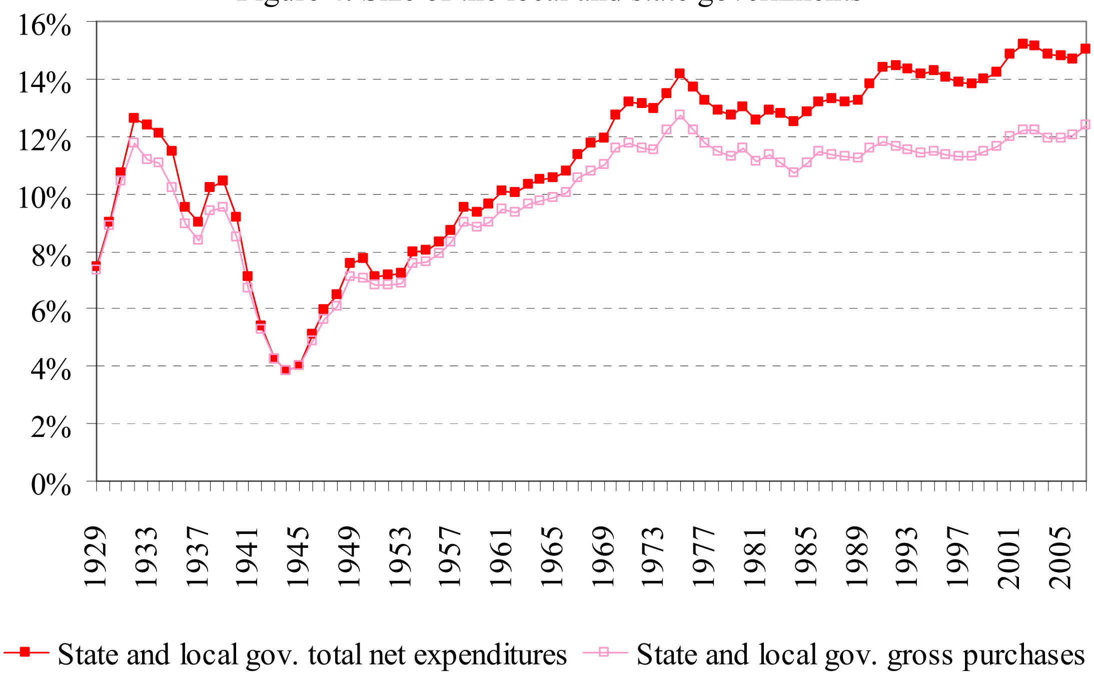
[4] To have a more accurate view of the capacity of government to inject funds in the domestic economy, one may want to exclude net payments to the rest of the world. In 2007, government total net expenditures represented 33.5% of GDP out of which 1.4 percentage points constituted net payments to the rest of the world.

Figure 3: Size of the federal government



Source: BEA

Figure 4: Size of the local and state governments

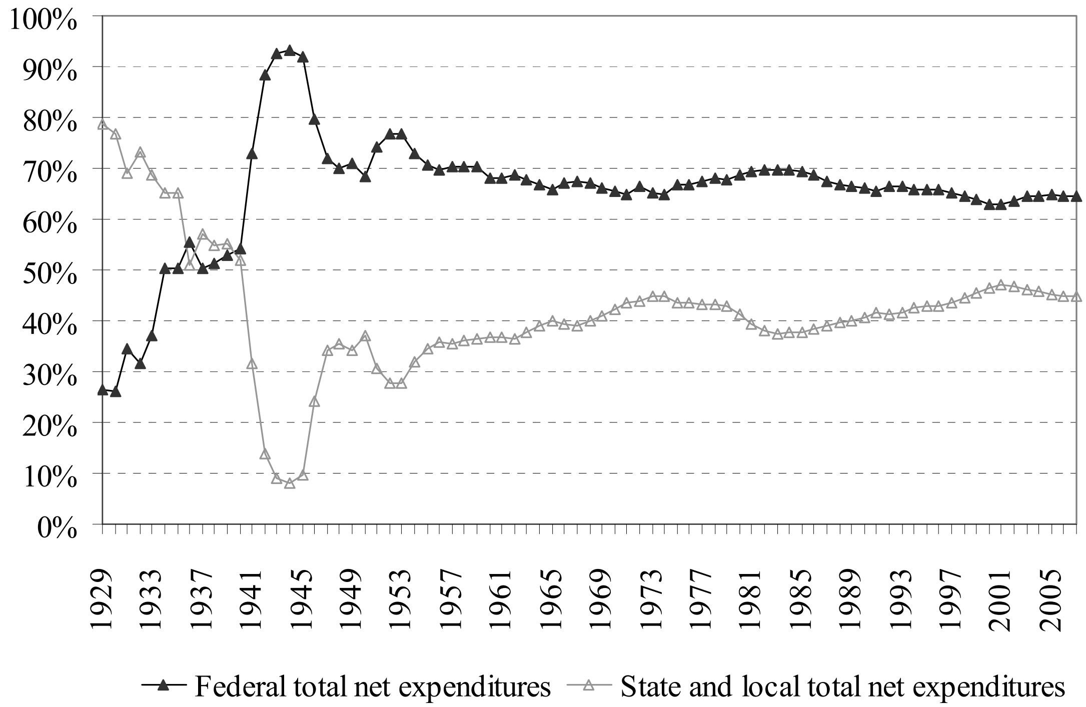


Source: BEA

This increased capacity of the government to stabilize the system is easy to understand if one refers to the Kalecki equation. Knowing that gross private domestic investment is the most erratic component of the equation, in order for the government to be able to stabilize aggregate monetary profit, its expenditures and taxes should be at least as big as investment. Of particular relevance is the federal government because of its monetary sovereignty and of the flexibility of its budgeting process. Figures 2 and 3 show that in the 1920s and 1930s the federal government was too small to be able to compensate for swings in investment. Leaving aside World War II, an adequate size was not reached until the early 1950s after which the federal government total expenditures always have been above 15% of GDP which is approximately the size of investment in the U.S. economy (post-1946 gross private domestic investment averaged 16% of GDP). Thus, for the U.S. economy, accounting for other fluctuations besides investment, a big government means a federal government that represents about 20% of GDP. Judged with this criterion, the size of the federal government was too big in the 1980s and early 1990s.

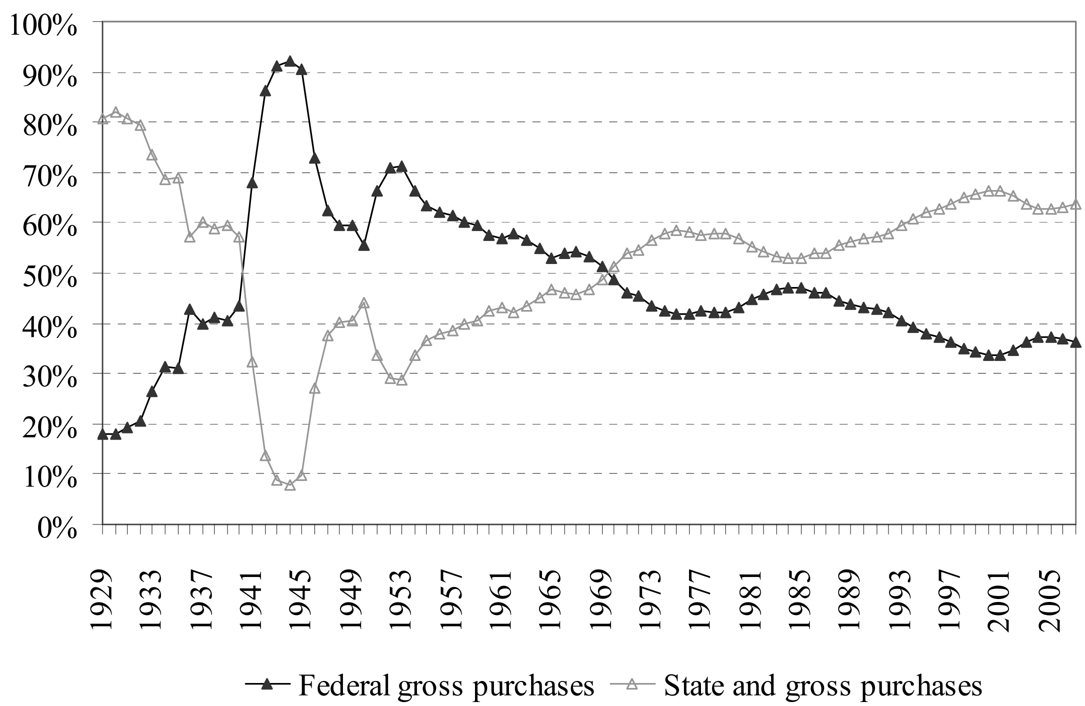
However, since the early 1980s some disturbing trends have appeared. As shown in Figures 3, 4, 5 and 6, not only has the size of federal government purchases been constantly declining, but there also has been a shift in responsibilities away from the federal government and toward state and local governments. This shift in the composition of government intervention is worrisome because state and local governments are not able to deal with macroeconomic issues, and because of the regressive nature of their tax structures. As shown below, one may also critique the composition of government spending. Minsky critiqued the ballooning role of transfer payments and the decline in regulation, which have respectively promoted inflationary tendencies and financial instability.

Figure 5: Size of the federal government relative to local and state governments



Source: BEA

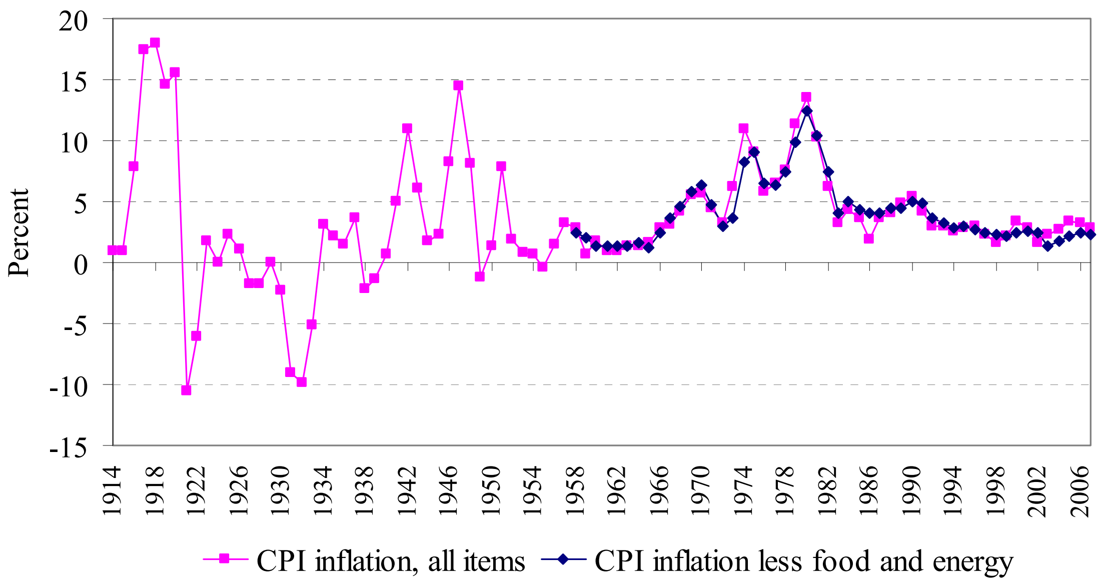
Figure 6: Size of the federal government relative to local and state government in the GDP



Source: BEA

If a big government is able to stabilize the system, a desirable property that a small government does not have, it also creates new problems. Indeed, by becoming too big it may generate inflationary tendencies, promote moral hazard, and dampen entrepreneurship. In terms of inflationary potential, Figure 7 shows that, after 1946, there is a clear inflationary bias.

Figure 7: Changes in the consumer price index from 1914 to 2007



Source: BLS

One may see the potential inflationary effect of big government by expressing in terms of relative growth the national income identity $PQ \equiv W + \Pi$ and the Kalecki equation of profit (Tymoigne 2008):

$$g_P \approx (g_w - g_{\mathrm{AP}_L})s_W + (g_Z - g_Q)s_Z + (g_{C_\Pi}s_{C_\Pi} - g_{S_H}s_{S_H} + g_I s_I + g_G s_G - g_T s_T + g_X s_X - g_J s_J) - g_Q s_{\Pi_{nD}} + (g_{T_\Pi} - g_Q)s_{T_\Pi}$$

With s_i the share of variable i in GDP and g_i the growth rate of variable i and, AP_L the average productivity of labor, w the average wage rate (including compensation and benefits), Π_{nD} the retained earnings of firms, S_H the saving level of households, and C_Π the consumption out of profit, I the level of gross investment, X exports, J imports, Z the non-wage incomes paid by firms (dividends, interests, rental income), and T_Π corporate income tax. This identity can be used to develop a theory of inflation by using, for example, the conflict-claim theory to explain g_w, the liquidity preference theory to explain g_Z, and the theory of effective demand to explain g_Q. g_{AP_L} can be assumed to behave differently depending on the structure of the labor market (very flexible in a sluggish labor market, close to constant in a free-market labor market). For the sake of argument, shares are given but could also be explained by using a monetary theory of distribution.

Thus, a big government, for which s_G, s_T and/or s_{T_Π} are big, can contribute to inflation by raising the wage of its employees too fast, by increasing spending too fast on goods and services, and by having a tax structure that contributes to a fast increase in corporate income taxes. Transfer payments may create additional inflationary pressures by growing disposable wage income and disposable net profit too fast. In addition, a big government in which political discretion in economic issues is high may prevent g_G and g_T to move up or down when they need to in order to prevent inflation or recession. Finally, if the government mainly focuses its spending defense and other unproductive expenditures, there is a greater chance that a big government will be inflationary (Han and Mulligan 2008).

In terms of potential moral hazard, by providing a safety net the government may achieve short-term stability at the expense of long-term instability. A first moral hazard is the tendency for businesses to take too many risks knowing that the government will rescue most of them in case of crisis. A second moral hazard is the potential decrease in labor force participation, especially if there are substantial income losses from going back into the work force and giving up transfer payments, which may affect production capacities of the country and so may compound the potential inflationary pressures over the long term.

In terms of entrepreneurship, a too tight control of the economy may remove the fun from entrepreneurship by limiting choices and constraining possibilities. As Keynes noted, investment activity is highly uncertain and risky, but uncertainty is also a factor that promotes investment by leaving some space for human creativity and imagination. Minsky was aware of this and noted that:

> Federal Reserve policy therefore needs to continuously "lean against" the use of speculative and Ponzi finance. But Ponzi finance is a usual way of debt-financing investment in process in a capitalist society. Consequently, capitalism without financial practices that lead to instability may be less innovative and expansionary; lessening the possibility of disaster might very well take part of the spark of creativity out of the capitalist system. (Minsky 1986: 328)

Overall, therefore, the government has to make sure to provide sound financing methods while also promoting a dynamic economy that can respond to the needs of society.

In order to contain those problems, specific policies should be created that limit political interests in their implementation and that promote price stability as well as check for potential moral hazards. Where politicians would have a way to influence long-term trends in government activity is by influencing the existing structural programs and creating new ones. Minsky had a view of a big government that tries to respect those conditions.

Minsky's Idea of a Big Government: The Economics of Control

In a controlled economy, to employ Abba Lerner's term, the government acts as a planner in order to prevent key elements of the economy from going out of hand by applying neither fascism nor socialism, but by following a "third course" which involves removing "certain substantial spheres of activity from the hands of private enterprise" (Robinson 1943 [1966]: 86).

> The policy problem is to devise institutional structures and measures that attenuate the thrust of inflation, unemployment, and slower improvements in the standard of life without increasing the likelihood of a deep depression. […] The current strategy seeks to achieve full employment by way of subsidizing demand. The instruments are financing conditions, fiscal inducements to invest, government contracts, transfer payments, and taxes. This policy strategy now leads to chronic inflation and periodic investment booms that culminate in financial crises and serious instability. The policy problem is to develop a strategy for full employment that does not lead to instability, inflation, and unemployment. (Minsky 1986: 295, 308)

Minsky was aware that, given the dynamic nature of capitalism, there is no definitive solution to the control of the economy, and that the government must respond continuously to and, even better, anticipate changes in the institutional structure. New regulations lead to regulatory arbitrages, and the creativity of economic agents generates new economic structures and so a need to change regulations.

A first element that should not be determined by market mechanisms is the level of employment. Minsky promoted the creation of an "employer of last resort" (ELR), i.e. broad government employment programs similar to those of the 1930s. The programs would be permanent, decentralized and would employ at a uniform wage anybody willing and able to work but unable to find a job in the private sector, and would take individuals as they are, where they are. Recently, this program has attracted growing attention and it has been applied in a limited way in Argentina (Tcherneva and Wray 2007; Wray 2007; Kaboub 2008). There are several benefits to this program. First, by fixing the base wage at which one is employed, the program would help to keep in check the growth of the average wage rate, which can be a source of inflation. In addition, this program tends to eliminate the inflationary tendency of the existing welfare and unemployment insurance programs that provide an income even though no current economic contribution to society is made.[5] By contrast, ELR workers would contribute to the growth of the economy (g_Q). Second, by acting as an income buffer for those who lost their job in the private sector, the program would act as an automatic stabilizer. This is a good way to eliminate lags and to limit political interests in fiscal activism because G and T would move automatically with the number of people employed in the ELR programs. Third, this program would also contribute to a more harmonious society by decreasing income inequalities (the ELR wage would be a living wage), and by lowering crimes and other negative consequences (most of them non-monetary) induced by unemployment.

A second element of the economy that should be controlled is the level and composition of investment. The government should socialize investment by fixing the reward received by entrepreneurs, and by allocating resources toward the most socially

[5] This does not mean that welfare and Social Security should be eliminated. Future contributors (children) and past contributors (retirees) to the economic welfare of developed societies deserve to be helped. However, an opportunity to work should be offered to those who are able and willing to contribute presently to the economic welfare of the society.

needed investment projects. This does not mean that all individual decisions would be removed because the government could just bring forward the areas that need investment and let the private companies propose solutions. The government (or special committees including government representatives) would select the most appropriate projects without necessarily undertaking their construction nor removing ownership from the private sector (Keynes 1936: 378ff.). The government could also leave frivolous investment projects (cell phones, etc.) to the private sector while housing, infrastructures and other social needs would be supervised by government.[6] Minsky's proposal for community development banks is part of this project. The goals of this policy are threefold. First, investment projects would be allocated to sectors that need them; this would help to homogenize society and so would contribute to its stability and well-being. Second, it would help to promote financial stability because the positive macroeconomic feedback loop between investment and profit would be mostly eliminated. Finally, given that the growth of investment may contribute to inflation, the socialization of investment would help to manage inflation.

A third element is the control of the growth of income through a generalized income policy. The ELR program and the socialization of investment already would help to control income growth by affecting the growth of wages and aggregate profit. Nevertheless, additional policies may be necessary that define general rules with respect to wage bargaining, as well as the payout ratios of firms. For example, Minsky proposed that the pay-out ratio of banks be controlled by a regulator so that the retained earnings of banks do not grow too fast because this is a major cause of instability and inflation (Minsky 1975b; Minsky 1977; Minsky 1986: 234-238, 321). This policy has two essential benefits; the first one is to help to dampen inflationary pressures. As shown earlier, wage payments, interest payments, retained earnings and other income payments may have an effect on inflation if they grow too fast. The second benefit is to promote

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[6] The recent bridge collapse in Minneapolis was a dreadful reminder that many major U.S. infrastructures are falling apart, mostly because their maintenance and expansion was not performed properly because of the lack of funding by state governments and private enterprises. The American Societies of Civil Engineers (2005) gave a *D* average to American infrastructures and recommended a major overhaul and expansion. A government employment program like the Public Works Administration (which was responsible for the construction of many of the existing major infrastructures) would be very helpful.

financial stability by limiting the demand that stockholders can put on rates of returns that firms and banks should generate.

A fourth element that should be controlled is the growth and distribution of assets of all financial institutions. The main way this should be done is by a cash-flow oriented regulation and supervision while also using a flexible capital requirement policy. One may note, however, that focusing mainly on equity is not a good strategy because it does not provide a direct measure of the capacity of a financial institution to withstand liquidity shocks. Actually, it is not even a good measure of solvency because of the multiple adjustments to capital equity that do not necessarily reflect the capacity to have a profitable business. Current cash flows, future expected cash flows, and current amount of liquid assets provide a much better view of what the potential needs and costs of refinancing or liquidation are.

One may note that all these programs are coherently related and are meant to be permanent. They are not a patchwork of temporary discretionary policies. These programs are also largely independent of the political climate, and influence both production capacities and purchasing power. Their implementation would be done by government employees who would have some discretion within the rules set up by the programs.[7] For example, an ELR worker may be fired if he or she does not perform, and, within the income policy, some sectors may be favored over others to encourage their development. Note also that the inflationary tendencies of a big government are constrained by controlling both public and private spending directly and indirectly. There is no doubt that all these programs will lead to changes in the behavior of individuals and that unpredicted and unintended adverse consequences will appear, but those have to be dealt with as we go in function of the changes in the structure of the economy. Again, there is no final solution to economic management in a society that is highly dynamic and that fosters individual decisions.

[7] These programs would be well funded and the government would try to attract the best and brightest individuals to manage them by paying a competitive wage. Too often, government programs are purposely underfunded in order to limit their effectiveness and push for their abandonment.

PAST BIG GOVERNMENT EXPERIENCES IN THE UNITED STATES

For most economists, "Keynesianism" is synonymous to any type of "fiscal activism." Keynes's approach is usually summed up in a 45-degree-line diagram that seems to guarantee that any type of government expenditures and tax measures brings full employment, now and forever, without any problems. However, Minsky noted that this is a gross simplification and he was highly critical of what happened in the 1960s:

> Just as there never really was a Keynesian revolution in economic theory, there also never really was one in policy. […] All that was assimilated from Keynes by the policy establishment and its clients was the analysis of an economy in deep depression and a policy tool of deficit financing. […] Keynesian economics, even in the mind of the economics profession, but particularly in the view of politicians and the public, became a series of simple-minded guidelines to monetary and fiscal policy. […] The institutional structure has not been adapted to reflect the knowledge that the collapse of aggregate demand and profits, such as occasionally occurred and often threatened to occur in pre-1933 small government capitalism, is never a clear and present danger in Big Government capitalism such as has ruled since World War II. (Minsky 1986: 291, 295)

In the last chapter of the *General Theory*, Keynes noted that the "outstanding faults of the economic society in which we live are its failure to provide for full employment and its arbitrary and inequitable distribution of wealth and incomes" (Keynes 1936: 372) which "may be considered dual aspects of a single basic trouble; for economists have long recognized a connection between unemployment and the maldistribution of purchasing power" (Keynes in Chew 1936). As a consequence, Keynes was for a direct participation of the government through *specific* fiscal *and* monetary measures, that included some form of planning *via* a cooperation between the private and public sector (socialization of investment), the maintenance of a low interest rate that rewards only risks and skills (euthanasia of rentiers), and a progressive tax policy that favors consumption. Let us look at past experiences and see how they conform to Keynes's view of government intervention.

The Roosevelt Era

When campaigning in 1932, Roosevelt ran on the popular idea that the federal government should balance its budget. He blamed Hoover for his fiscal "extravagance and […] rashly pledged to reduce government expenditure by 25 per cent" (Badger 1989: 111). However, given that society was on the brink of collapse, once elected, Roosevelt decided to increase government intervention and to deficit spend. These dramatic changes were not based on the *General Theory*, which was not available, or on the advice of Keynes who had not provided any.[8]

From the end of 1933, Keynes had applauded most of the New Deal policies and he continued to do so over time:

> I accept the view that durable investment must come increasingly under state direction. I sympathise with Mr. Wallace's agricultural policies. I believe that the SEC is doing splendid work. I regard the growth of collective bargaining as essential. I approve minimum wage and hours regulations. I was altogether on your side the other day, when you deprecated a policy of general wage reductions as useless in present circumstances. (Keynes 1938b [1982]: 438-439)

However, he was also very critical of the lack of engagement of the Roosevelt Administration in recovery efforts. Keynes wanted it to go much further and at a much faster pace by deficit spending massively through large-scale government expenditures in housing,[9] unemployment relief programs, aid to farmers, public utilities, railroads, and other public works (Keynes 1933d, 1934a, 1934b, 1938b). In addition to fiscal measures, he also pushed for a policy of cheap money that influences *directly* the whole yield curve:

> I put in the second place the maintenance of cheap and abundant credit, in particular the reduction of the long-term rate of interest. […] I see no reason why you should not reduce the rate of interest on your long-term government bonds to 2 ½ per cent or less, […] if only the Federal Reserve System would replace its

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[8] As Lee (1989) notes, the idea that government deficit can be good had been advanced long before Keynes.

[9] "The best aid to recovery because of the large and continuing scale of potential demand, […] the wide geographical distribution of this demand, and because the sources of its finance are largely independent of the stock exchange." (Keynes 1938b [1982]: 436)

present holdings of short-dated Treasury issues by purchasing long-dated issues in exchange. (Keynes 1933d [1982]: 297)

Further, in 1936 he was able to present the core policy agenda of the *General Theory* to the Roosevelt Administration:

> The main defects in our present society are its failure to provide full employment, and its inequitable distribution of wealth and incomes. […] In the conditions that now exist the "abstinence" of the rich impedes the growth of wealth, and action to remove great inequalities increases it. […] It appears that effective saving depends on the scale of investment, which varies inversely with the rate of interest. Thus, it is socially advantageous to reduce the rate of interest […] [so that it] would be possible to increase the stock of capital to a point at which the use of capital goods would cost little more than enough to cover wastage and obsolescence. This state of affairs, though it would leave scope for individual enterprise, would tend to eliminate the rentier, and to weaken the power of the capitalist to exploit the scarcity value of capital […] and the functionless investor would have no place in the economy. (Keynes in Chew 1936)

Thus, the recommendation of chapter 24, mostly considered as obscure radical sidetracks unimportant for the whole book, were pushed forward by Keynes.

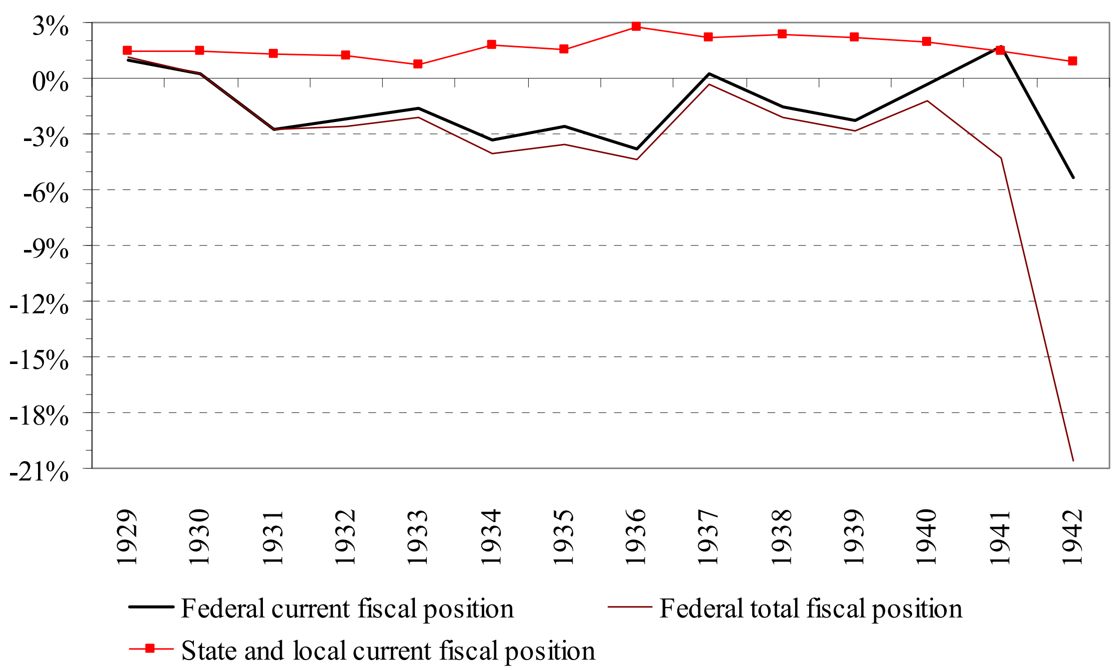
Overall, Keynes critiqued the Roosevelt Administration as "unprepared" (Keynes 1938a [1982]: 432) and "very slow to get moving" (Keynes 1934a [1982]: 308). He stated that the handling of some problems had been "really wicked" (Keynes 1938b [1982]: 436) and that "the attainment of the best results has been interfered with by certain fallacies of thought" (Keynes 1934d [1982]: 299). One of these fallacies[10] was the idea of "sound finance" that pushed Roosevelt to limit the funding of New Deal programs and, especially during election years, to try to generate a budget surplus (Lee 1989):

[10] Another one, promoted by Irving Fisher, was the idea that reflation was the best way to bring a recovery. Like Fisher, Keynes was for going off the gold standard and adopting a managed currency that gives the "liberty to make your exchange policy subservient to the needs of your domestic policy" (Keynes 1933c [1982]: 296; Keynes 1934e). However, contrary to quantity theoreticians, he thought that this was only a subsidiary policy. Output and employment should be stimulated directly through fiscal measures that affect spending and income, rather than indirectly by means of inflationary monetary measures (Keynes 1933d; Skidelsky 1994: 493).

> Most New Dealers believed that recovery would come from the revival of private investment. […] Similarly business advocates of spending in 1933 saw public spending as a 'quick fix' designed to 'start up' the economy, not a permanent crutch. Most supporters of government spending did not want to unbalance the budget. […] Roosevelt's Secretary of the Treasury, Henry Morgenthau Jr., argued that in order to revive the private investment necessary for full recovery, the federal budget must be balanced so that business would have the confidence to invest. (Badger 1989: 110-112)

As a consequence, as shown in Figure 8, the federal current budget deficit never accounted for more than 4% of GDP in the 1930s. This is minuscule if one considers the size of the problem and that the last minor recession of 2001 led to a deficit of about 3.5% of GDP. In addition, after 1936, the Roosevelt Administration aimed at reaching surpluses as fast as possible that led to a short but severe recession in 1937.

Figure 8. Fiscal positions relative to GDP



Source: BEA
Note: Over the period, the total budget of state and local governments was balanced.

Given the constraint of sound finance, as shown in Figure 3, federal government spending grew very slowly. In fact, most of the growth came under the Hoover Administration, and, from 1933 to 1941, federal government spending mostly stagnated. In addition, in order to reach a surplus, Roosevelt suggested cutting New Deal programs:

> He was embarrassed by Republican criticism of the budget deficits under the New Deal. He justified them by arguing that it was only extraordinary spending for humanitarian reasons that unbalanced the budget […]. He looked for ways to show that deficits were being scaled down so that he could promise a balanced budget for fiscal 1938. […] In 1936, an election year, he was even prepared to cut spending on the Civilian Conservation Corps […]. (Badger 1989: 111)

Rather than a sound economic program, Roosevelt and Congress saw the work programs as an emergency measure needed, if not for moral obligation, at least to avoid the destruction of capitalism altogether.[11]

By 1938, because of successful experimentations and through the influence of Hansen, Currie and Eccles[12], the idea that government deficit could be good to restore prosperity had gained some ground in the Administration and the business community but, at least for the latter, "only if it could be stripped of New Deal reformism" (Badger 1989: 116). However, Roosevelt remained skeptical of fiscal-led stimulus. As a proportion of GDP, government spending and the federal deficit were lower than in 1936 and the Administration went back to a surplus in 1941. This surplus allowed Roosevelt to keep a good public appearance, but it did not generate a recession because, due to national defense expenditures, the total fiscal position of the government was now a deficit representing 4.9% of GDP.

One has to wait until the entry of the U.S. into World War II to see a major government involvement in the economy and a commitment to let the budget deficits grow as much as needed. Between 1942 and 1945, the current deficit averaged 9.4% of

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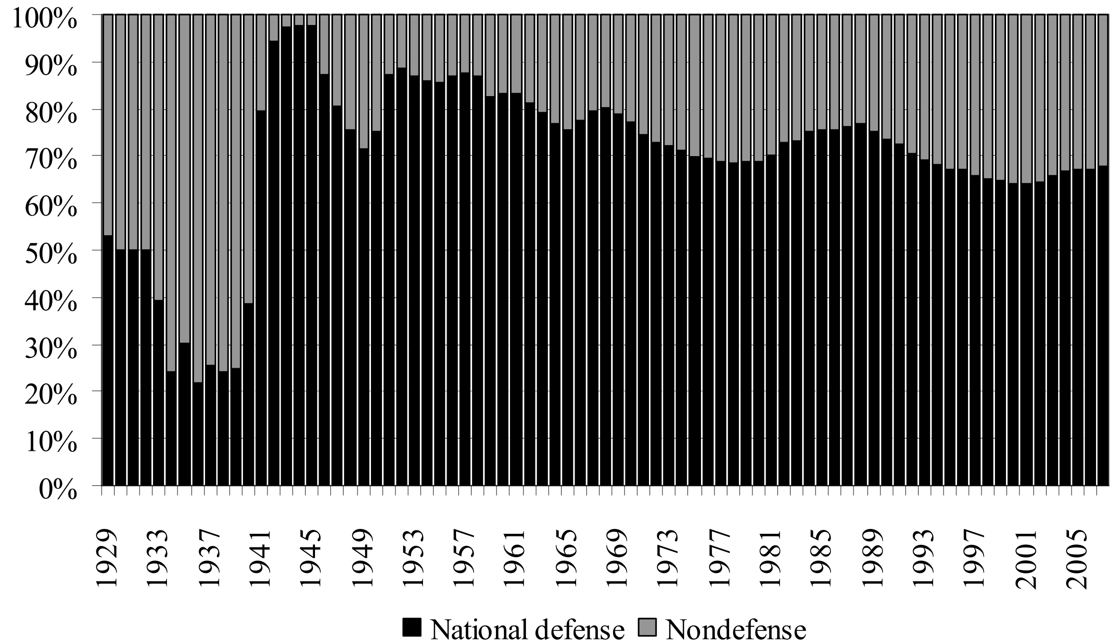
[11] This is illustrated by the name that the Administration gave to its first government work program. The Emergency Conservation Work Act of March 1933 created the Emergency Conservation Work Program (officially renamed the Civilian Conservation Corps in June 1937).

[12] However, this "Currie Keynesianism" (Barber 1996) was of the fine-tuner type that "shall exert such powers as it has toward promoting business stability and moderating fluctuations in production, employment and prices" (Eccles in Barber 1996: 94; Eccles 1937) and shall "fluctuate the total expenditure […] [and] income tax rates […] as a means to regularize the flow of total expenditures and to promote economic stability" (Hansen in Barber 1996: 160).

GDP and the total deficit averaged 22.1% of GDP, which had the unintended (and probably unexpected) consequence of strongly putting the U.S. economy back on its feet. Since that time, as shown in Figure 9, defense spending has been the main component of federal purchases.

Figure 9. Composition of Federal Spending



Source: BEA

However, Keynes lamented that this was not at all what he had in mind when he promoted government intervention and complained that:

> Alas, your letter confirms the prevailing opinion that money is only available for what is useless. (Keynes in Skidelsky 2000: 51)

Similarly, the monetary measures (management of the whole yield curve below 2 ½ percent) proposed by Keynes were only implemented because of the war and were abandoned in 1953.

By the middle of World War II, the National Resources Planning Board (NRPB), recognizing that the private sector cannot sustain full employment, took a giant step toward Keynes's position. It recognized that deficits far greater than in the 1930s would be necessary to maintain full employment, and that some private economic activities would have to be partly implemented by the government in order to make sure to "provide work for adults who are willing and able to work, if private industry is unable to do so" (NRPB in Barber 1996: 159). This was too radical for Congress who stopped funding the NRPB in 1943. Another shot at government planning was attempted by the Full Employment Bill of 1945 which proposed to put in place a structural "last resort […] program of federal spending and investment" (Bailey 1950: 13-14) in order to make sure that "all Americans able to work and seeking work have the right to useful, remunerative, regular, and full-time employment" (Section 2b of the Full Employment Bill of 1945 in Bailey [1950: 243]). However, the bill did not pass the House and it was replaced by the Employment Act of 1946. Often, the Act is thought to represent the final victory of Keynes's ideas and the establishment of a long period of Keynesianism that culminated in Nixon's famous tirade "we are all Keynesians now." However, the Act was substantially different from the 1945 bill (Santoni 1986) and Barber notes that:

> The legislative achievement represented by the Employment Act of 1946 has sometimes been treated as a triumph for a Keynesian point of view. It needs to be underscored that such a reading of that event is mistaken. […] Even […] the Council of Economic Advisers, owed less to their thinking than to the views presented by an economist hostile to Americanized Keynesianism. (Barber 1996: 169)

Rather than guaranteeing the right to employment, the 1946 Act transformed the U.S. government into a full-fledged fine-tuner in order to make employment consistent with business interests. This paved the way for incoherent, discretionary programs, time inconsistency problems, and credibility problems that ultimately led to the incapacity to manage both price stability and employment.

If one must associate an economist to the policies of the 1930s, Irving Fisher is a much more appropriate candidate. At the end of 1932, he sent his *Booms and Depressions* to Raymond Moley (an original member of the Brain Trust who played a key role in shaping the first New Deal) and asked to meet with him (Barber 1996: 22). In 1933 and 1934, "Fisher wrote to Roosevelt at least thirty-five times (receiving four replies) and visited him twice" (Allen 1993: 704) which is far more than Keynes. In addition, he had key allies in the Administration whom he personally recommended to the President (like George F. Warren), or who were sympathetic to the reflation approach (like the Secretary of Treasury Henry Morgenthau Jr.) (Barber 1996: 15).

In order to solve what he saw as a monetary problem, and based on the quantity theory of money and the money multiplier, Fisher advocated a plan that emphasized reflating and then stabilizing prices by controlling the money supply and the velocity of money in order to manage aggregate spending[13] (Fisher 1932: 121ff., 212ff.; Fisher 1935a). The control of the money supply would go through credit control (via large variations in nominal policy rates to affect real interest rates, enlarged open-market operations beyond real bills, manipulations of reserve requirements, and other means) and gold control (by forbidding gold coinage and by varying the bid and ask prices of gold at the Treasury desk). He also advocated temporary fiscal deficits during recessions (Fisher 1932: 104-105; Pavanelli 2004: 298) but was not very fond of public work programs and unemployment insurance. According to Fisher, the latter two were only "palliative" policies because unemployment was only a consequence of the depression and because work programs were slow to implement and only effective on a very large scale, which goes against the private profit system. Beyond *Booms and Depressions*, additional influence can be seen through the correspondence between Fisher and the Roosevelt Administration, sometimes at its request, in which he advised a bank holiday (2 days before Roosevelt declared it), going off the gold standard or at least devaluating the dollar by 50%, the continuation of employment programs and government spending as long as they have a monetary component like subsidies and loans to private businesses (Barber 1996: 84-85; Allen 1977).

The Roosevelt Administration followed Fisher on most of these points, by running temporary deficits, by buying large amounts of gold in 1933 and 1934, by going off the gold standard and by raising the trading price of gold at the Treasury desk in January 1934 (with the effect of devaluating the dollar relative to currencies still in the gold standard system), and by putting in place temporary working programs (Pavanelli

[13] In order to increase the velocity of money, Fisher proposed a "stamped dollar" plan (Fisher 1932: 226ff.) in which special dollar bills would be issued that would stay lawful only if their holders periodically apposed a postage stamp on the back of each bill. This would make hoarding costly and so would complement monetary growth in order to stimulate spending and so to reflate the economy.

2004). Over time, however, his influence diminished. Against Fisher's advice, Roosevelt did not raise the value of gold above $35 (Barber 1996: 81) and, later, Roosevelt did not go for his 100% money plan. In addition, Fisher vigorously opposed the New Deal measures to restrict supply and to institute economic planning.[14] In particular, "he considered the initiatives to regulate wages and production as totally misguided" (Pavanelli 2004: 298). In the end, only one of his secondary advices survived the trial period and this was the running of temporary fiscal deficits and temporary employment programs.

Thus, one does not have to look to Keynes for a justification of fiscal activism. However, Fisher's strategy is very different from Keynes's because for Fisher "the depression does not indicate a general breakdown of capitalism […]. It indicates almost solely a breakdown of our monetary system" (Fisher 1935b in Pavanelli 2004), whereas for Keynes the management of some aspects of economic life by the government is necessary to avoid "the destruction of existing economic forms in their entirety, and [to guarantee] the successful functioning of individual initiative" (Keynes 1936: 380).

In the end, therefore, the Roosevelt Administration followed many different advices. As Roosevelt stated, it was time for "bold and persistent experimentation" (Barber 1996: 19) and as Keynes noted:

> It must have been difficult for the President to know in what direction to turn for the best available advice. In practice he has shown himself extraordinarily accessible to anyone with new ideas to air whom he believed to be independent and disinterested. Naturally he had received a great deal of advice, some of it inconsistent with the rest and not all of it of equal quality. […] [H]e has been happy to provide the political skill and the power of authority to give some sort of a run to all kinds of *ideas*, ready to judge by results […] (Keynes 1934a [1982]: 306-307)

This experimental approach can be seen within the structure of the Roosevelt Administration with the division between the Structuralists and the Monetarists. However, both favored sound finance and relied on price policies to bring a recovery (either

[14] Keynes too did not approve of price fixing and output limitations in most industries because this was too complex and arbitrary (Keynes 1934c [1982]: 323).

through reflation or direct price manipulations) (Barber 1996: 80). Without the War, Roosevelt would have continued to muddle through, as any administration has since, because there was no conversion to the Keynesian principles of submitting fiscal and monetary policies to the achievement of stable full employment. Overall, the fiscal and monetary strategies of the Roosevelt Administration were much closer to what Fisher had in mind.

The Kennedy-Johnson Era

The Kennedy-Johnson era is thought to be the apex of "Keynesianism." Like the Roosevelt Administration, the Kennedy-Johnson administration focused on stimulating investment and economic growth but it put more emphasis on tax incentives. In order to cope with poverty, Johnson, following Kennedy's initial preparations, also put in place his famous War on Poverty. The idea that public employment programs could help in the fight was advanced but Johnson was convinced by the Council of Economic Advisers (CEA) that pro-growth and pro-market policies would more effective (Russel 2004). The idea that these policies allow everyone to benefit, reduce inequalities, and are a very effective means to reduce poverty has been a core assumption of the liberal program on poverty (Brady 2003).

All this again is far more consistent with Irving Fisher's idea of government intervention, and several authors have already criticized the Keynesian nature of this era (Kregel 1994; Wray 1994; Harvey 1999, 2000; Bell and Wray 2004; Russel 2004). Minsky, who by that time had become an accomplished economist, was very critical of the policy of the administration.

In terms of the overall strategy, Minsky noted that the strong emphasis on investment and tax incentives is misplaced:

> Certainly there is an unwarranted emphasis on investment as the source of all good things: employment, income, growth, price stability. But in truth, inept and inappropriate investment and investment financing deters full employment, consumption, economic growth, and price stability. (Minsky 1986: 326)

One can understand why if one follows Minsky's apparatus. The Kalecki equation of profit creates a destabilizing feedback loop in which current investment is implemented on the expectation that investment will be done in the future. This creates long-term explosive patterns *à la* Harrod and Domar by increasing future production capacities without increasing future demand. The *General Theory* mainly focused on short-term demand problems, but Keynes was aware of long-term problems and demonstrated the need to emphasize consumption[15] and government spending, and the importance of managing investment in order to manage the supply side of the system (Keynes 1936: 105-106; Minsky 1975a). Consequently, an economic plan that aims at long-term full employment and price stability cannot be based on continuously promoting private investment because of the financial vicissitudes of investment projects, and because of their impact on future production capacities. Minsky also noted that the emphasis on investment creates inflationary pressures and income inequality (Minsky 1973, 1981, 1986).

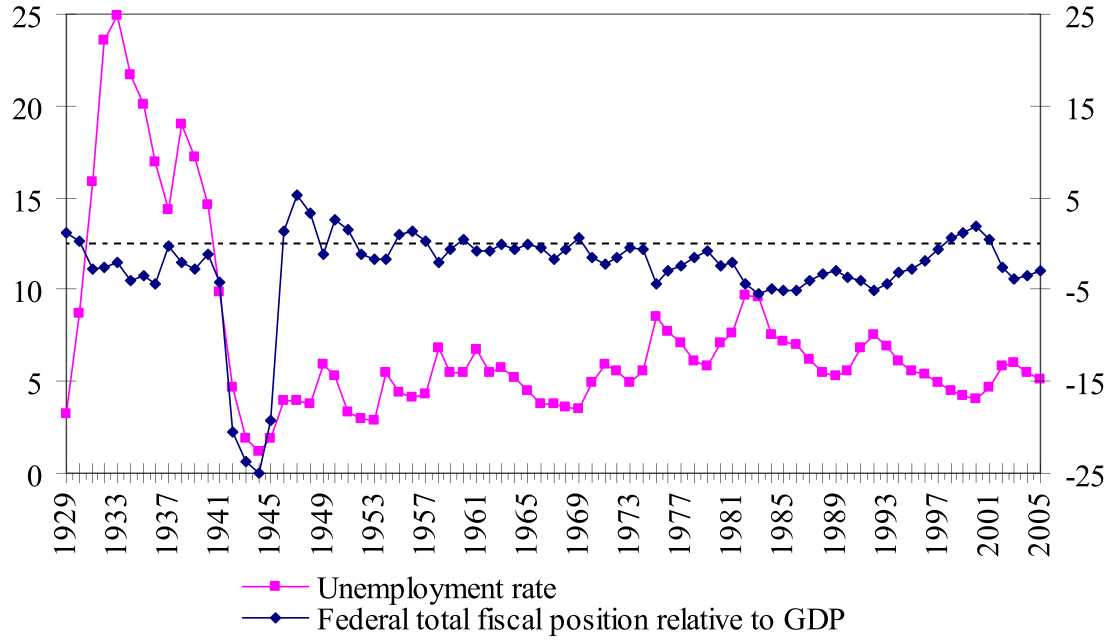
In terms of tax incentives, this method of stimulating employment is highly indirect. Decreasing taxes (or providing subsidies) does not promote employment if businesses do not expect that there is a profitable demand.[16] Similarly, not all government expenditures are equally effective in promoting employment, not to say full employment, and just deficit spending will not do. A shown in Figure 10, the deficits ran in the 1970s, 1980s and 2000s did not lead to unemployment rates below average. In fact, the correlation between the (current or total) fiscal position of the federal government and unemployment is about zero. The level of spending and taxing, if properly used, "only" helps to stabilize the economy. However, as Keynes said, there may be several slips between the cup and lip, and promoting smoother economic activity will not translate automatically into a large increase in employment because of labor saving (productivity increases) and labor limiting (price increases) behaviors in the private sector. If one focuses on full employment, even over long periods of economic growth, the private sector was never able to employ everybody willing to work, so stimulating the private sector through government spending and incentives will never allow everybody to

[15] Keynes was aware that consumption-based growth should be managed carefully because a marginal propensity to consume equal to or above one leads to instability (Keynes 1936: 117). Over the past 30 years, households in the U.S. (and all over the world) have been encouraged by financial institutions to do precisely that, which has resulted in large instability.

[16] Fisher himself was aware of the need to stimulate spending before business incentives (subsidies, etc.) can have any positive effects on economic activity (Fisher 1932: 142).

participate (Wray and Pigeon 2000; Harvey 2000). The only way to reach true full employment and shared prosperity is by orienting some government spending toward hiring the unemployed. The quality of government spending matters as much as the quantity of government spending (Tcherneva 2008).

Figure 10. Total fiscal position of the federal government and unemployment



Source: BEA

In terms of War on Poverty, strong economic growth maintained the unemployment rate at about 5% but the effects on poverty were limited. Again, the "Keynesian" administration chose a very indirect and market oriented way to solve a problem that cannot be eradicated by market mechanisms. The point was to train the low-skilled workers in order to make them competitive on the job market (Harvey 2000). But, as Minsky noted, if this strategy helps to homogenize the labor force and makes it more responsive to the needs of the business sector, it cannot deal with labor shortage. The implication is a redistribution of poverty not a diminution of poverty (Minsky 1965a, 1965b). Only providing enough jobs allows people to apply the skills they learned. Brady (2003) shows that the growth-market-productivity policy that has been applied in the second half of the twentieth century has had only limited success at reducing poverty in

Western societies, even more so over the long-run, and has not been effective at all in removing entrenched pockets of poverty.

Finally, Kennedy and Johnson were both heavily influenced by the Sound Finance approach and were reluctant to put in place structural programs that would decrease control over the level of federal spending and taxing:

> Keynesianism has been frequently misrepresented in this country, and this was the case in the Kennedy administration. Two general issues are involved in this misrepresentation. First, in the United States an incomplete kind of Keynesianism was practiced as understood and implemented by the [CEA] under Heller; thus, with no full commitment to planning and government deficit spending in place, the full impact of Keynesian measures has never been realized here. […] Second, Kennedy and his political advisers […] misunderstood and resisted the new economic practices. (Russel 2004: 145)

Kennedy and Johnson resisted government spending, tried to constrain it as much as possible, and refused any government employment program proposed by Structuralists at the Labor Department, and instead favored the fine-tuning of economic growth by tax incentives proposed by the CEA (under the influence of Tobin and Samuelson).

CONCLUSION

The debate between Structuralists (who think that market mechanisms are structurally flawed because they fail to provide full employment and economic stability) and the Fine-Tuners (who think that discretionary temporary measures help to maintain the economy on its non-inflationary employment path, and that it is the only relevant thing a government can do) is likely to persist. The debate focuses on, not only the goal to achieve, but also the fiscal *and* monetary macroeconomic strategies to reach the goal.

For Structuralists, in the spirit of Lerner's functional finance, the size of the federal fiscal position should be determined by the needs of the economy given the structural programs in place. When dealing with socio-economic issues, politicians should not try to reduce deficits or to use surpluses through discretionary choices. What they should do is to promote programs that aim at price stability, financial strength and full employment. This should be complemented by low permanent interest rates that reward only competence and risk.

Keynes was a Structuralist but Keynesianism has always been associated with the Fine-Tuners and has been reduced to any type of short-term fiscal activism to manage demand. This has allowed the economy to stabilize by producing smoother growth and shorter recessions. However, fine-tuning does not allow the economy to reach full employment, does not reduce unfair inequalities, leaves aside the importance of supply management, and tends to create financial instability and upward price instability. In addition, the U.S. government has limited its spending mostly to unproductive activities. Overall, fine-tuning is more consistent with Fisher's thought than with Keynes's, and, today, the former is still very influential, especially as a guide for modern monetary policy.

Like Keynes, Minsky was for a responsible big government, that is, a government that puts in place coherent structural programs that directly tackle socio-economic problems. Minsky was conscious, however, that big-government capitalism, while solving important problems, also creates new problems. Thus, rather than having a passive government that just reacts to economic problems through spending, taxing and manipulations of financial conditions, Minsky wanted a pro-active form of government that takes initiatives to direct the economy toward more stable and fair forms of capitalism. That would involve both monetary and fiscal measures and would influence both the supply side and demand side of the economic system. That is what Keynesianism is all about, systematic decentralized planning rather than discretionary incoherent fine-tuning.

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