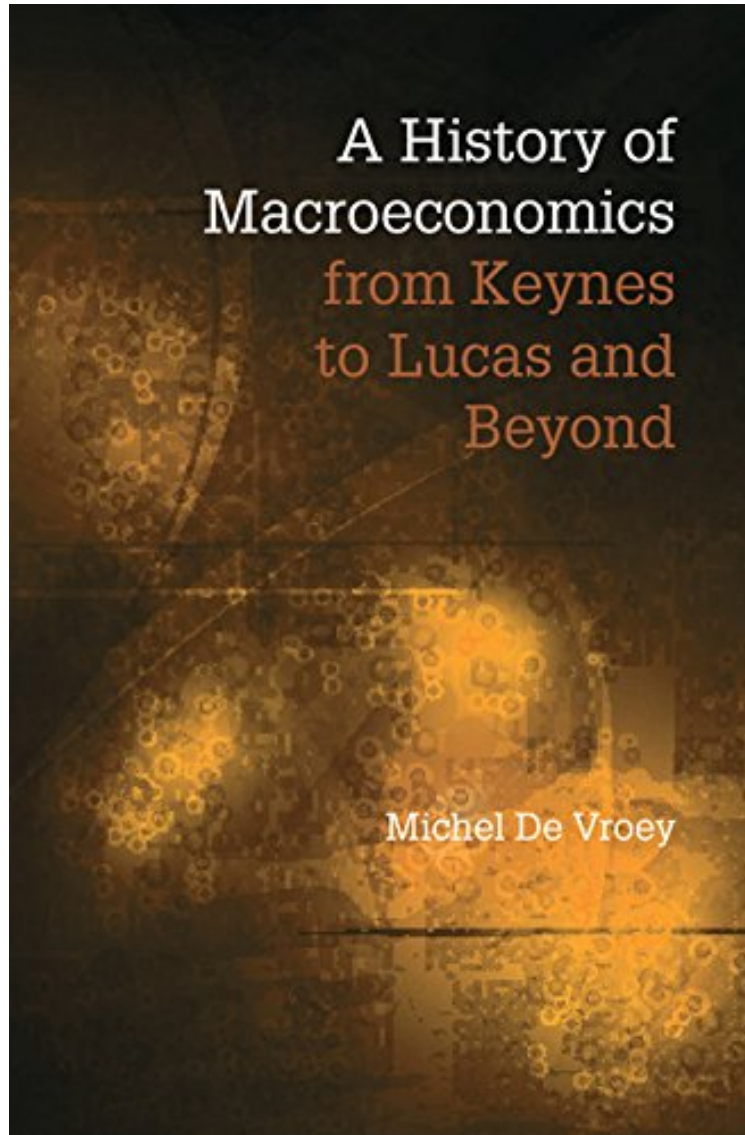


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A History of Macroeconomics from Keynes to Lucas and Beyond

Michel De Vroey

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Michel De Vroey : A History of Macroeconomics from Keynes to Lucas and Beyond before purchasing it in order to gage whether or not it would be worth my time, and all praised A History of Macroeconomics from Keynes to Lucas and Beyond:

9 of 9 people found the following review helpful. A History of Business Cycle Theory By P. Johnson It's all about business cycle theory, with a little bit of inflation. NO significant growth theory, except as it plays into business cycles. No Acemoglu, no Paul Romer, no endogenous growth theory. Banks, banking, finance - no. It's not a history of "Macroeconomics." It's a history of mainstream business cycle theory. If you're interested in the history of the great

disputes: Keynes, ISLM, Friedman, Phelps, Leijonhufvud, Walrasian/Non-Walrasian/ Lucas, New Keynesians, RBC etc. etc.. then you will like this book. De Vroey has done a magnificent job as an historian of this aspect of macroeconomics. 0 of 1 people found the following review helpful. Instead of a dull history of macroeconomics By Roger Instead of a dull history of macroeconomics, this gives the flavor of academic fights, give and take, keep the best, discard dead ends. It shows that Macroeconomics still had a very long way to go. I would say the "Novel prize for economics" was created long before economics can be called a science. 5 of 7 people found the following review helpful. Magisterial account By Philip George Most macroeconomists tend to be specialists in one or the other of its contending schools. It is therefore a delight to read a sweeping account of the entire period since Keynes revolutionised the subject in 1936 with his General Theory. Apart from taking readers into areas with which they may be relatively unfamiliar, this book makes them think anew even about economists with whom they are familiar. Nevertheless, I have a bone to pick with de Vroey's treatment of Keynes. In the concluding critique he says: "The question to address is what explains that Keynes could introduce an involuntary unemployment (rationing) result in a model that was a mere extension of [the] Marshallian without resorting to the wage floor assumption. The answer to this question is that he actually resorted to this assumption." It seems to me that this is a complete misunderstanding of Keynes. A good place to begin is the fish market with which de Vroey illustrates the Marshallian model. At the start, the demand and supply of fish are in equilibrium. Then sellers of fish find themselves confronted with a market in which demand has fallen. In the short run they respond by cutting prices; this clears the market. In the longer run the suppliers of fish attempt to cut input costs and thus go down the supply curve. Some resources (including labour) that are employed in the fish industry may also seek to be employed in other industries. So in the longer run the equilibrium price is likely to fall somewhere in between the original price and the short-run market-clearing price. The Keynesian model bears no resemblance to this. In it, sellers of fish find that cutting prices does not clear the market. And excess resources from the fishing industry cannot find a use in other industries. Both these follow from the fact that in the Keynesian model the fall in demand is not particular to the fish industry but extends across the economy. It is a fall in aggregate demand. Given the fall in aggregate demand, involuntary unemployment follows as a matter of course without any additional assumptions. It also follows, as we shall now show, that wage flexibility does not reduce involuntary unemployment. Consider a firm that manufactures 100 widgets for a total revenue of \$100. It employs 10 workers at a wage cost of \$50, with all other costs including profit amounting to \$50. The firm finds itself in a recession as a result of which demand for its product falls to 90 widgets. To manufacture this it requires only 9 workers, so one is sacked. Its wage bill falls to \$45 and other costs to \$45. The involuntary unemployment is thus explained. But why does the capitalist not cut the wage rate? The reason is that although this would cut the cost of its product, it would not help to sell a higher number of widgets because it is the aggregate demand in the economy that has fallen. A cut in the wage rate would increase profitability but would not lead to the capitalist employing any additional workers. He has no interest in cutting rates because it does not help him sell additional widgets. All this is not to say that Keynes did not commit huge errors. He did. But what de Vroey considers his errors are actually the most revolutionary part of Keynes and where he differed from the economists before him. The Great Recession has brought Keynes's mistakes into sharp focus. Perhaps the most important is his view that investment is sharply responsive to a fall in interest rates. The US, Europe and Japan have all cut interest rates to near-zero, even negative, levels and investment has not responded. Another is his equation of consumption, $C = C_0 + bY$, where C_0 is the consumption at zero income levels, b is the marginal propensity to consume and Y is the income. It appears at first glance that b can be greater than 1 only when consumption is greater than income. Actually, there is another possibility, and this is that consumers respond to a fall in their income by increasing their saving by an even greater amount. This turns the so-called Keynesian multiplier into a negative number, and explains why large fiscal deficits have not brought economies rapidly back on track. Keynes confused the average propensity to consume with the marginal propensity to consume. The APC is close to and less than 1. The MPC is greater than 1. But why is that during a recession, even a fall in prices is unable to clear markets? Why is that consumers respond to falling prices, which amounts to an increase in their income, not by raising consumption but by increasing their saving? The reason is that in the housing market crash which preceded the recession they lost a huge proportion of their net worth, and are desperately saving whatever they can to recoup their loss. This is of course why the worst and most prolonged recessions in history have all followed massive asset market crashes. I have explored the subject at some length in my book "Macroeconomics Redefined" (<http://www..com/dp/B00ZX9O5XQ>)

This book retraces the history of macroeconomics from Keynes's General Theory to the present. Central to it is the contrast between a Keynesian era and a Lucasian - or dynamic stochastic general equilibrium (DSGE) - era, each ruled by distinct methodological standards. In the Keynesian era, the book studies the following theories: Keynesian macroeconomics, monetarism, disequilibrium macroeconomics (Patinkin, Leijonhufvud and Clower), non-Walrasian equilibrium models, and first-generation new Keynesian models. Three stages are identified in the DSGE era: new classical macroeconomics (Lucas), RBC modelling, and second-generation new Keynesian modeling. The book also examines a few selected works aimed at presenting alternatives to Lucasian macroeconomics. While not eschewing

analytical content, Michel De Vroey focuses on substantive assessments, and the models studied are presented in a pedagogical and vivid yet critical way.

"Michel De Vroey does not simply record what he finds. He has a vision of the kind of macroeconomics he would like to see, perhaps one he developed gradually over the years he has worked on this book. What makes this book enjoyable is that he has high hopes for economics, he flatters us that we are important, and he praises the progress we have achieved. In the end he has the integrity not to hide his disappointments, his conviction that while there is no turning back, there is still a long way to go." Robert E. Lucas, Jr, John Dewey Distinguished Service Professor in Economics, University of Chicago "No branch of economics has witnessed as many revolutions and counter-revolutions as macroeconomics, starting from Keynes' General Theory eighty years ago. Michel De Vroey's book provides a thorough but highly readable account of the main developments in the field over that period. It conveys a sense of the excitement generated by the advent of every new paradigm, as well as of the growing tension between the requirements of theoretical purity and those of empirical and policy relevance that macroeconomists keep facing these days." Jordi Galiacutè, Research Centre for International Economics (CREI), Universitat Pompeu Fabra and Barcelona Graduate School of Economics "Macroeconomics research has largely proceeded through 'revolutions'. One wishes for a more linear and evolutionary process, one where most new contributions would naturally fit and the common core become steadily stronger. But the immense complexity of modern economies, the difficult methodological choices, may be such that 'revolutions' will keep happening, with their share of destruction, confusion, and eventual reconstruction. Understanding the nature of these revolutions is essential to understanding where we are today, and Michel De Vroey's book does a masterful job of doing just that. A thoroughly illuminating and enjoyable read." Olivier J. Blanchard, Robert M. Solow Professor of Economics, Massachusetts Institute of Technology "Macroeconomics is a complex evolving system of thinking. Michel De Vroey's latest book dives into that evolving complexity and, by distinguishing between Marshallian and Walrasian macroeconomics, helps make the history of macroeconomics a bit more understandable. It's sad that more economists don't make that distinction." David Colander, Distinguished College Professor, Middlebury College "De Vroey's book reads like a travelogue recounting his life journey as a macroeconomist, and his considered response to key texts he encountered along the way. Always thoughtful and penetrating, he stimulates this reader to reflect anew on how we got to where we are today, and what might lie ahead." Perry Mehrling, perrymehrling.com About the Author Michel De Vroey is a Professor Emeritus at the University of Louvain and visiting professor at the Université de Saint Louis, Brussels. He has published several books, including *Involuntary Unemployment: The Elusive Quest for a Theory* (2007) and *Keynes, Lucas: D'une macroéconomie ... l'autre* (2009). He has also published extensively in scholarly journals.