

Truger, Achim

Book Review

Book review: Davidson, Paul (2011): Post Keynesian Macroeconomic Theory: A Foundation for Successful Economic Policies for the Twenty-First Century, 2nd Edition, Cheltenham, UK (360 pages, paperback, Edward Elgar, ISBN 978-1-84980-980-1)

European Journal of Economics and Economic Policies: Intervention (EJEEP)

Provided in Cooperation with:

Edward Elgar Publishing

Suggested Citation: Truger, Achim (2013) : Book review: Davidson, Paul (2011): Post Keynesian Macroeconomic Theory: A Foundation for Successful Economic Policies for the Twenty-First Century, 2nd Edition, Cheltenham, UK (360 pages, paperback, Edward Elgar, ISBN 978-1-84980-980-1), European Journal of Economics and Economic Policies: Intervention (EJEEP), ISSN 2052-7772, Edward Elgar Publishing, Cheltenham, Vol. 10, Iss. 3, pp. 385-388, <https://doi.org/10.4337/ejeep.2013.03.11>

This Version is available at:

<https://hdl.handle.net/10419/277285>

Standard-Nutzungsbedingungen:

Die Dokumente auf EconStor dürfen zu eigenen wissenschaftlichen Zwecken und zum Privatgebrauch gespeichert und kopiert werden.

Sie dürfen die Dokumente nicht für öffentliche oder kommerzielle Zwecke vervielfältigen, öffentlich ausstellen, öffentlich zugänglich machen, vertreiben oder anderweitig nutzen.

Sofern die Verfasser die Dokumente unter Open-Content-Lizenzen (insbesondere CC-Lizenzen) zur Verfügung gestellt haben sollten, gelten abweichend von diesen Nutzungsbedingungen die in der dort genannten Lizenz gewährten Nutzungsrechte.

Terms of use:

Documents in EconStor may be saved and copied for your personal and scholarly purposes.

You are not to copy documents for public or commercial purposes, to exhibit the documents publicly, to make them publicly available on the internet, or to distribute or otherwise use the documents in public.

If the documents have been made available under an Open Content Licence (especially Creative Commons Licences), you may exercise further usage rights as specified in the indicated licence.



<https://creativecommons.org/licenses/by/4.0/>

Book review

Davidson, Paul (2011): *Post Keynesian Macroeconomic Theory: A Foundation for Successful Economic Policies for the Twenty-First Century*, 2nd Edition, Cheltenham, UK (360 pages, paperback, Edward Elgar, ISBN 978-1-84980-980-1)

Achim Truger

Department of Business and Economics, Berlin School of Economics and Law, Germany

The publishing of a second edition of a macroeconomic textbook 17 years after the first edition is not an event that usually receives great attention – even if the subtitle promises that a ‘foundation for successful economic policies for the twenty-first century’ will be delivered. The second edition of Paul Davidson’s textbook, *Post Keynesian Macroeconomic Theory*, however, should be an exception to the rule for at least three reasons.

First, it is one of the few textbooks of post-Keynesian macroeconomic theory which provides a real alternative to the (macro-)economic mainstream and which is therefore highly relevant to critical students and others who are interested in economic theory and policy.

Second, the author is one of the most distinguished and prominent post-Keynesian economists in the world and one of the – if not the very – exponent of post-Keynesianism in the US. Paul Davidson is professor emeritus for political economy at the University of Tennessee in Knoxville, Tennessee, co-founder and editor of the *Journal of Post Keynesian Economics* and senior fellow at the Schwartz Center for Economic Policy Analysis at the New School University in New York. In his long academic career, he has published extensively on fundamental theoretical questions – above all, the interpretation of John Maynard Keynes’s works and the pivotal role of fundamental uncertainty therein – as well as on economic policy matters. Regarding economic policy, he has always stressed the fundamental role of reforming the global monetary system. Over the last few years, Davidson has been very active publishing a Keynes biography (Davidson 2007) and a very topical monograph about economic policy after the crisis (Davidson 2009).

Third, as the second edition is published after the Great Recession, the reader may expect insights about the most recent global financial and economic crisis, or may expect answers to the question of whether the crisis has changed or confirmed the author’s previous views. It does not come as a big surprise that Paul Davidson – like many other post-Keynesians – sees his theoretical and economic policy views confirmed by the recent crisis.

What is more surprising, however, is the fact that readers have to figure out for themselves both the differences between the second and the first edition and whether and where new developments have been included in the textbook: there is no preface or afterword or a new introduction that would provide even the slightest hint as to these matters. This is a bit annoying, and quite strange, because, in fact, Paul Davidson has taken notice of many new developments and has incorporated them into the new

edition: a new chapter 9 on 'Financial markets, fast exits and great depressions and recessions' has been added. There, the deregulation of financial markets, the problem of shadow banking and the resulting stability risks of overindebted private households in the US are being addressed. Davidson quotes – with quite a bit of satisfaction – his own evaluation from the year 2004 where he correctly assessed the monstrous risks and the gigantic crisis potentially lingering within the US financial system. In addition to the new chapter, the whole book has been substantially updated and new literature has been processed.

Throughout the book, Davidson proves to be a truly exceptional interpreter of Keynes. He really succeeds in working out Keynes's key messages and above all the key features that make Keynes's ideas different from those of mainstream macroeconomics. Reading the second chapter about 'The essential difference between the general theory and the classical system' will prove to be a revelation on its own for students or practitioners of economics who have been educated within the mainstream. Davidson demonstrates both vividly and convincingly why Keynes thought of his theory as the general theory that comprises the classical theory as a special case, and why the traditional claim in the mainstream textbooks that downgrades Keynes's theory to be a special case within a neoclassical system is inappropriate. In the chapters that follow, Davidson develops an axiomatic foundation of Keynes's approach which serves two purposes. First of all, it helps to acquire a deeper understanding of the approach. Second, in this way, Keynes's approach can be better distinguished from the mainstream which uses an axiomatic approach as well.

According to Davidson, the mainstream can be characterised by three axioms, all of which were explicitly refuted by Keynes: the neutrality of money, the substitution axiom according to which anything can be substituted by something else, and the ergodicity axiom according to which the future could in principle be predicted on the basis of past experience and current data. In contrast, Davidson presents five essential characteristics that make up reality in Keynes's view (p. 17):

1. The non-neutrality of money both in the short and the long run.
2. Non-ergodicity – that is, the conviction that the future cannot be predicted even in a probabilistic way and therefore fundamental uncertainty is a fact that all economic agents have to cope with.
3. Money is a general means for the settlement of payments resulting from contractual obligations.
4. The special elasticity properties of money – that is, a production elasticity of zero and a zero elasticity of substitution with regard to producible goods.
5. Unemployment is the normal case in a capitalist monetary economy and full employment is an improbable special case: economic agents rationally hold money (liquidity), in order to make sure that they can meet their contractual obligations in the face of fundamental uncertainty.

As money is not a producible good and cannot be replaced by a producible good, the holding of liquidity automatically leads to a loss in output and employment; unemployment, therefore, is the normal case.

In the chapters that follow this discussion in chapter 2, the fundamental insights are deepened and applied step by step. After an extensive discussion of consumption and investment demand (in chapters 3 and 4), chapter 5 develops the multiplier analysis of government expenditure. Chapters 6 to 8 deepen monetary analysis. After the new chapter 9 mentioned above, Davidson proceeds to the topics of inflation, Keynes's

supply and demand analysis, and the supply of and demand for labour (in chapters 10–12). The ensuing chapters focus on the international perspective, and culminate in chapter 17, where proposals for a new global monetary system are presented.

Throughout the book, Davidson writes in a very comprehensible manner – his style and rhetoric are simply outstanding. The often complex material is presented in an easily accessible way yet without oversimplifying. In addition, economic policy relevance remains a key issue.

Davidson keeps on attacking the economic mainstream throughout the book. These attacks culminate in the final chapter, 18, on ‘Truth and labelling in economic textbooks’. Here, he once again focuses his attacks on the old Keynesian mainstream in the form of the neoclassical synthesis and against New Keynesianism, neither of which, according to Davidson, have a right to be termed as Keynesian in any way. It is almost impossible to show the differences between true Keynesianism in Keynes’s sense and its ridiculous caricature in the mainstream in a more coherent and convincing way than Davidson does in this chapter.

Throughout the book, Davidson goes as far as to personally attack important mainstream people and sometimes openly ridicules them. For example at the end of chapter 1, Alan Greenspan is mocked for having to publicly admit at a hearing in Congress that he simply had not foreseen and understood certain things related to the financial and economic crisis. Therefore, Davidson hopes that reading his own textbook may foster Greenspan’s future understanding of the crisis and the necessary measures to fight it. This passage may strike many readers as funny; however, it already gives a hint as to the one major weakness of the textbook: Paul Davidson’s sense of mission seems so large that he sometimes tends to see his views of Keynes and post-Keynesianism as the only true and legitimate ones, while at the same time downgrading or ignoring the important contributions by other post-Keynesian authors and schools. Readers looking even for a mention, let alone discussion, of the Kaleckian tradition, the neo-Ricardian school, Modern Money Theory or other recent developments in post-Keynesian thought will be disappointed. It is astonishing to note which prominent names have not even made their way into the index: Philip Arestis, Amit Bhaduri, Alfred Eichner, Wynne Godley, Geoffrey Harcourt, John King, Jan Kregel, Marc Lavoie, Hyman Mynski, Basil Moore, Malcolm Sawyer, Randall Wray – to enumerate just a few important ones.

The sheer number of authors not mentioned rules out oversight as an explanation. In fact, the exclusion of certain views and persons from ‘his’ post-Keynesianism has more than once been used by Davidson in the past. Davidson’s project of developing a coherent axiomatic foundation for Keynes’s key message and using it as a demarcation line against the mainstream is very understandable and in principle even attractive. However, in detail he sometimes seems to exaggerate. This certainly was the case in the legendary episode when Davidson (1982: 252) created considerable confusion within the scientific community by claiming that the term ‘Post-Keynesianism’ is always to be written without and never with a hyphen. And it was the case with his comprehensive review of John E. King’s (2003) *History of Post Keynesian Economics since 1936* in the *Journal of Post Keynesian Economics* in which he explicitly excluded the Kaleckian and Sraffian schools from post-Keynesianism, because they allegedly had not sufficiently renounced the classical axioms of ergodicity and neutrality of money (Davidson 2003: 263). Such an exclusion and downgrading of important parts of heterodox economics can only serve to further weaken post-Keynesian economics in its intellectual discourse with mainstream economics. It will therefore probably achieve the exact opposite of Davidson’s goal.

Summing up, Paul Davidson has written an absolutely brilliant macroeconomic textbook of the highest theoretical and economic policy relevance. Those who would like to know more about contemporary post-Keynesianism in all its important facets should, however, also consult some of the other outstanding (text)books, for example by Lavoie (1992 und 2006), King (2003), Harcourt (2009) and Hein/Stockhammer (2011).

REFERENCES

- Davidson, P. (1982): *International Money and the Real World*, London: Macmillan.
- Davidson, P. (2003): Setting the record straight on *A History of Post Keynesian Economics*, in: *Journal of Post Keynesian Economics*, 26(2), 245–272.
- Davidson, P. (2007): *John Maynard Keynes*, Great Thinkers in Economics Series, New York: Palgrave Macmillan.
- Davidson, P. (2009): *The Keynes Solution: The Path to Global Economic Prosperity*, New York: Palgrave Macmillan.
- Harcourt, G.C. (2009): *The Structure of Post-Keynesian Economics: The Core Contributions of the Pioneers*, Cambridge, UK: Cambridge University Press.
- Hein, E., Stockhammer, E. (eds) (2011): *A Modern Guide to Keynesian Macroeconomics and Economic Policies*, Cheltenham, UK: Edward Elgar.
- King, J.E. (2003): *A History of Post Keynesian Economics since 1936*, Cheltenham, UK: Edward Elgar.
- Lavoie, M. (1992): *Foundations of Post-Keynesian Economic Analysis*, Cheltenham, UK: Edward Elgar.
- Lavoie, M. (2006): *Introduction to Post-Keynesian Economics*, Basingstoke, UK: Palgrave Macmillan.