

Introduction to Post-Keynesian Economics. By Marc Lavoie. Palgrave Macmillan, Basingstoke, UK and New York, USA, 2006. 168pp., \$85.00. ISBN: 0-230-00780-5.

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Marc Lavoie is one of the most well-known and prolific Post Keynesian economists. His *Foundations of Post-Keynesian Economic Analysis* [Lavoie 1992] is the most advanced and well-written textbook on the economics of Keynes, Kalecki, and their modern followers. The little book under review is an easy-to-read and updated synthesis of the most important topics discussed in the *Foundations*. It is balanced and extremely well done, a must-read for anyone interested in knowing what Post Keynesian economics is all about.

The book consists of five main chapters, to which are added an insightful introduction about the origin of the book, and some brief conclusions to highlight the modern relevance of “pro state intervention” Post Keynesian economics *vis-à-vis* “pro free market” mainstream economics. All chapters are enriched by clear pictures, and very useful boxes presenting ancillary material. These boxes enhance the accessibility of the book, clarify difficult concepts, and provide additional information about key issues discussed in the text.

The first chapter mainly deals with definitional issues. What are the characteristics of heterodox economics? Who are the so-called Post Keynesians? How do they differ from other heterodox schools? The chapter ends with a controversial issue. As Post Keynesian economics is made up of several strands, shall we exclude some approaches (e.g., the Sraffian strand) or emphasize others (e.g., the New Keynesian approach)? To his credit, Lavoie remains consistent. He is a fervent eclectic Post Keynesian scholar, particularly appreciative of the work of Kalecki and his modern followers. This means that under the label of Post Keynesian economics, this book discusses themes that are of interest to a variety of Post Keynesian economists, including Fundamentalists like Paul Davidson, and Sraffians like Edward Nell.

The second and the third chapters deal with the microeconomic and macroeconomic components of Post Keynesian theory. Microeconomics is still an underdeveloped area in Post Keynesian theory; yet, in the last decades, great strides have been made. Starting with consumer choice theory, Post Keynesians have replaced the principle of decreasing marginal utility, and the marginalism concept more generally, with the principles of separability and subordination of needs. According to the former, consumers divide needs and related expenditures into many categories, only loosely tied one to another, where the latter principle maintains that needs and related expenditures are organized in a hierarchical order. This means that the notion of gross substitution no longer holds, and hence goods cannot be treated in an identical fashion. Similarly, in the Post Keynesian theory of the firm, the perfectly competitive environment has been replaced with oligopolistic markets, where issues of power and growth become prominent. These issues are discussed in terms of the finance frontier and the expansion frontier. The former combines each growth rate pursued by firms with the minimum profit required to finance it. The latter relates each growth rate with the maximum attainable profit rate. The intersection between the two frontiers represents the



maximum growth rate of the firm, under the constraints of its competitive and financial environment.

Post Keynesian macroeconomic theory is grounded on the principle of effective demand, namely the idea that aggregate demand plays a key role in determining the level of output and employment in a country. This principle is nowadays coupled with the endogenous money hypothesis, according to which the supply of money is determined by the demand for loans and the liquidity preference of savers, rather than being controlled arbitrarily by the central bank. Interestingly, the endogenous money hypothesis is also behind modern macroeconomic theory, the so-called “new consensus macroeconomics (NCM).” NCM has rejected the quantity theory of money, but has retained its major policy implication, namely the principle of neutrality of money and monetary policy, which is antithetic to the principle of effective demand [Fontana 2007]. Lavoie is masterful in explaining the main features of money in Post Keynesian theory *vis-à-vis* old and modern mainstream theory [see Table 3.1, p. 56], together with their different policy implications. The analysis of the macroeconomic component of Post Keynesian theory ends with a review of a new methodology for studying the evolution of modern economics. Stock-Flow models are based on a balance-sheet matrix that deals with (tangible and financial) stocks, and a transaction-flow matrix describing a vertically integrated production economy. Lavoie has great hope for the stock-flow methodology, and indeed is now a leading scholar in the field [see Godley and Lavoie 2006]. In this book, he uses the stock-flow methodology to verify the endogenous money hypothesis and its policy implications.

The last two main chapters are concerned with short and long period issues, respectively. As in the previous chapters, the principle of effective demand retains a dominant role. Chapter Four concerns the impact of effective demand on the labor market. Building on the famous profit equation of Kalecki, Lavoie explains in a simple and concise manner the Kaleckian labor market model, before using it to debunk some well-established claims, including the view that an increase in the minimum wage or average real wage necessarily leads to an increase in unemployment. Similarly, the Kaleckian model is used to interpret the modern debate on work-sharing programs, and the effects of technical progress on employment levels. I have personally found this chapter quite pleasant to read, especially for its beautifully balanced combination of theoretical material and real-world issues.

Chapter Five is of a more technical nature. It concerns old and new growth models. It starts with a discussion of the Cambridge model before introducing the new Kaleckian growth models. These models, as well as their modern extensions and criticisms, are discussed extensively. In this context, Lavoie reviews highly debated issues in Post Keynesian theory, including the endogeneity of the natural growth rate, and the Verdoorn Law.

In conclusion, this little book provides a concise and comprehensive introduction to Post Keynesian economics. It is particularly valuable because it recognizes the need to move beyond criticisms of mainstream theory and policy, and presents an alternative economic theory and policy. It makes a very pleasant reading, which is not common for works on the “dismal science.” In short, for anyone interested in learning about Post Keynesian economics, this book is a must.

References

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Strategies of Commitment and Other Essays. By Thomas C. Schelling. Harvard University Press, Cambridge, MA, 2006. 341pp., \$39.95. ISBN: 0-674-01929-6.

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This collection of papers by Thomas Schelling follows by a year his selection as winner of the Nobel Prize. Its range is similar to his 1983 collection *Choice and Consequence*, but most papers were written since 1983. Five of the 18 essays were first published in the 1980s, nine were published in the 1990s, and three were published since 2000. Four focus on ecological issues, four on national defense and warfare, four on the issue of “self-command,” three on methodological issues, and two on the valuation of human life. An early essay, dating from 1971 and one of the best in the volume, focuses on the dynamics of residential segregation.

A collection of Schelling’s works covering so many years and so many subjects makes more apparent than ever the qualities that unite his writings. His economy and clarity of presentation, and his ability to offer memorable examples, are hard to equal. Economists have a deserved reputation for writing too abstractly, with good examples an occasional event at best. In contrast, for Schelling, colorful examples are practically non-stop and support the view that more attention to examples would go a long way toward lessening the divide between economists and the rest of the world.

Nowhere is his power with words clearer than in the essay “Prices as Regulatory Instruments.” Over a space of 40 pages appears a streamlined account of the role of the price mechanism in correcting for spillovers. No graph is to be found or equation confronted, and yet one is left with a nuanced sense of spillovers. I found myself second-guessing the extent of my own reliance on graphical demonstrations of these ideas. I also felt convinced that no better introduction to correction for spillovers at the intermediate undergraduate level or above can be found.

Three other essays stand out as particularly powerful. “What do Economists Know” (first published in 1995) presents the most compelling defense of mathematical identities that I’ve seen; Schelling’s main point here is that what is necessarily true is too often equated with what is obviously true. “Social Mechanisms and Social Dynamics” (first published in 1998) more clearly specifies what distinguishes social mechanisms from theories and laws. This is one of only two essays that relies on some mathematics (mainly relegated to an appendix), and Schelling’s reader-friendly way of fitting the mathematics into the discussion would