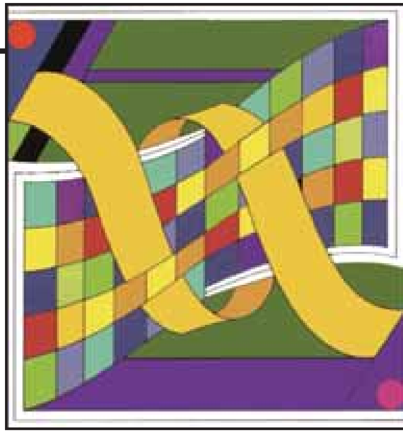

Keynes Was No Socialist

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A review of
Keynes: The Return of the Master,
by **Robert Skidelsky,** Public Affairs, 2009.

In a "Letter from America" in a recent issue of the *Newsletter* of the Royal Economic Society, British economist Angus Deaton complained how politicized the U.S. economic debate had become and how it was almost mandatory for Republicans to oppose a "fiscal stimulus." This was combined with the anathema often poured on the doctrines of the British economist John Maynard Keynes (1883–1946), who espoused stimulating spending as a cure for deep recessions. While in the United States he is often denounced as a "socialist," in the United Kingdom even Thatcherite Conservatives prefer to condemn the misapplication of his views.

Lord Keynes (as he later became) was famous for adjusting his theoretical framework to the facts of the situation. To ask what he would be saying now is a pretty futile exercise. It is not futile, however, to ask if there is anything in his doctrines that can offer hints on how to tackle the greatest threat to the international capitalist system since the Great Depression of the 1930s. Robert Skidelsky, author of a magisterial three-volume biography of the great man, is well qualified for this task. In his new book, *Keynes: The Return of the Master*, he attempts more than this. There is a chronology of the crisis up to May 2009; a critique of U.S. mainstream macroeconomics; a summarized easy-to-read version of his biography; a comparison of economic performance in the supposedly Keynesian Bretton Woods period of 1951–73 with the era of the so-called Washington Consensus from about 1980; some notes on Keynes's ethics and politics (which it would be a mistake for the most hardened Wall Street type to omit), and finally his own proposals for the future. And this is all given in 210 pages reasonably accessible to the interested non-specialist.

The chronological section is easily the best account I have read of the development of the credit crunch for those interested in the main macroeconomic story as distinct from the micro-financial nitty-gritty. I hope the next edition will contain a few blank pages for the reader to continue the narrative on his or her own. The section on the modern U.S. academy is bound to attract hostility. Skidelsky quotes a University of Rome professor of economics, Robert Waldmann, on the vogue for doctrines such as rational expectations and efficient financial markets characteristic of the New Classical school. Graduate students have to learn a huge amount of mathematics very fast, which is hardly possible unless doubts about the validity of the approach are set aside. This applies I suspect most of all to some of the business schools, where most students probably regard the MBA as a meal ticket and believe that they are merely learning a few technical tricks.

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Skidelsky regards the assumptions behind the New Classical School as "mad." At this point, I can hear the cautionary voice of Milton Friedman, who predates this school, saying "Go slowly." In Friedman's view, stylized assumptions are not to be criticized on their descriptive validity but on the fruitfulness of their analysis. After all, Isaac Newton's frictionless universe is also "mad" but retains its utility in defined situations. The charge against the New Classical theory is that its adherents were woe-

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fully taken by surprise by everything to do with the credit crunch. And while on the subject of Friedman, it is worth remarking that he never attempted to deny the logic of Keynes's General Theory, which Friedman often praised to the consternation of some of his followers. His point was that the Federal Reserve could have stopped a normal recession from developing into the calamity that it did through monetary policy, but through human error did not do so. This is too U.S.-centered a view, specific to a particular historical episode.

Adjusting to Circumstances

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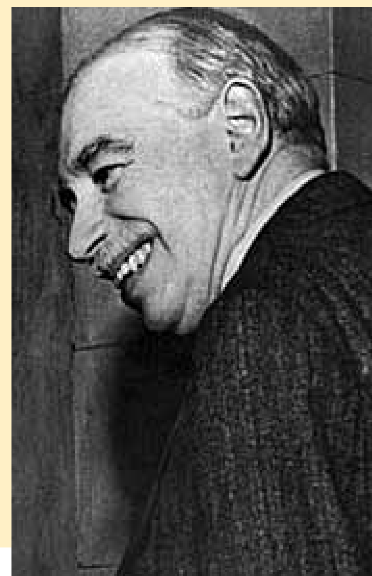
—S. Brittan



John Maynard Keynes

To the more practically minded, the key Skidelsky chapter will be the one comparing the post-World War II settlement with post-1992 period. The author has little difficulty in showing that the first period compares reasonably well with the second not only on growth and employment but also on sound money tests such as price and exchange rate stability. He does not, however, explain why the first period gave way to the second. The reasons were not ideological, but because the post-war compromise contained the seeds of its own destruction. For instance, "fixed but adjustable exchange rates" had to freeze into rigid rates or break down into generalized floating rates, as some critics pointed out at the time. Attempts to use trade unions to hold down money wages ran up against the *raison d'etre* of union existence. And Friedman was surely right to deride the idea of a long-term unemployment-inflation tradeoff depending on money illusion.

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If Skidelsky has a central point, it is the all-pervasiveness of uncertainty, as distinct from insurable risk, both in Keynes's writings and in reality. It is this which gives a body blow to most kinds of economic forecasts, including those purporting to be "Keynesian." Skidelsky's weakest chapter is the final one on international reform. Here he repeats Keynes's abortive 1944 proposals for a much more ambitious International Monetary Fund issuing its own currency, the bancor, and with the power to discipline chronic surplus countries like China and Japan. In fact, a more moderate plan for an "asset settlement system" was developed by an international committee under a Bank of England director Jeremy Morse, but was derailed by developments following the 1973 oil price crisis. I agree that the dollar is unlikely to stay forever as the main international currency, but exactly how this will come about is not now foreseeable.

Like some other writers, Skidelsky makes too much of Keynes's belief in balanced current national budgets. This was based partly on a quirk of UK procedure under which Parliament had given permission for certain capital items to be considered off-budget, or in UK parlance, "below the line." It was also based on exaggerated hope of the ability of redistributive taxation to raise the propensity to consume. There was, too, some wishful thinking about the ability of a fiscal stimulus to pay for itself through higher tax revenues, akin to that of some contemporary supply-siders, although on entirely differently grounds. If intended saving at full employment exceeds desired investment at high employment levels and monetary policy cannot bring them together, there is nothing for it but fiscal deficits for as long as it takes. The problem is that such a savings-investment gap is now most apparent at the international level with the emergence of Chinese, OPEC, and German surpluses. It is on this rather than exchange rates that international cooperation needs to focus. In the meantime, each country should use to the full the room for manoeuver given by floating rates. ◆