

How Progressive is Post-Keynesian Economics?

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Introduction

As did many of my predecessors, I need to say that I am honoured to be associated with the name of John Kenneth Galbraith. I recently checked my library at home and realized that in various bookshelves I had more than 15 different books written by Galbraith, including the volume containing the six books translated into French compiled by Gilles Dostaler, in 2007. I also possessed a half-dozen books written by others on the economic theories and life of Galbraith, including the recent and impressive study of Galbraith's major works written by Alexandre Chirat (2022), which I was asked to comment in an online seminar a couple of years ago. Obviously, I was an avid reader of Galbraith's works and an admirer of his.

Two months ago, I was advised that I had been proposed to deliver a lecture in the context of the John Kenneth Galbraith Prize. Not being as productive as I used to be, I had no new and unpublished paper in inventory, and I did not want to bore listeners by rehearsing the results of my past research or my past works, at least not directly as you will find out later. So, I decided to take the risk to come up with an entirely new topic, one that I had not given much thought in the past, but one that would seem to be appropriate within the auspices of the organization to which we belong, the Progressive Economics Forum. So here is the chosen topic: *How progressive is post-Keynesian economics?* It is risky business because one has to try to find something smart to say within a short time period, and also because today the term "progressive" can be understood in quite different ways by different people, in contrast probably to the time, say, when the Progressive Economics Forum was created more than 25 years ago.

The first thing to do is to define terms. What is post-Keynesian economics? This in itself is already controversial. This lecture is being held at the Université du Québec à Montréal (UQAM), so it may be appropriate to mention the definition of post-Keynesian economics that has been provided recently by Till Düppe, a professor in methodology and history of economics in the department of economics at the UQAM, who was hired

to replace our friend Gilles Dostaler who had unfortunately passed away two years earlier. Düppe (2025, p. 4) believes that post-Keynesian economics is “a psychological phenomenon rather than a set of ideas”. He defines the identity of post-Keynesian economics in the following, sometimes detrimental, terms:

... its reactionary character resulting in a simultaneous vicinity and distance to neoclassical Keynesianism, its attachment and loyalty to ideas, the insistence of the truthfulness of assumptions instead of analytical convenience, and the emphasis on controversy, as well as its tendency towards factionalism (Düppe 2025, p. 26).

So post-Keynesianism would have a reactionary character, whatever that means. Certainly, it can be granted to Düppe that there are sometimes strong similitudes in the economic policies advocated by post-Keynesians and Liberal Keynesians, such as Paul Krugman or Joseph Stiglitz, as I previously argued in a book review of these two authors (Lavoie 2013). It is also true that post-Keynesians, like several other heterodox schools of thought, prefer to start their analysis on the basis of realistic assumptions that describe the actual world instead of elegant but arcane abstractions that would apply to an irrelevant non-existing economy. There is also some evidence that, in the past, some post-Keynesian authors took as Gospel the writings of well-known authors, such as John Maynard Keynes or Piero Sraffa, and more lately Hyman Minsky. But obviously, Düppe has not read any of the post-Keynesian literature over the last two or three decades, for otherwise he would be hard-pressed to say that post-Keynesian economics is just a psychological phenomenon and not a set of ideas.

Definitions

Post-Keynesian economics

Before fully leaving aside Düppe and his psychoanalysis, let us move on to a more joyful topic. As some of you know, one of the biggest and unrelentless controversy is how to spell post-Keynesian economics. With or without a hyphen? With or without capital letters? Some German and French authors even write postkeynesian as one single word, with no hyphen and without any space between post and Keynesian. Personally, I prefer to use post-Keynesian with a small p and a dash, as was first suggested in 1969 by Alfred Eichner, the American author of *The Megacorp and the Oligopoly*, a 1976 book very much in line with the arguments of J.K. Galbraith about big corporations and its technostructure. The term was agreed to by Joan Robinson in the correspondence that she had with Eichner in the early 1970s, and her student Jan Kregel was the first author to put the term in print in a book, in 1973. This was followed by the 1975 article by Eichner and Kregel in the *Journal of Economics Literature*, which defined what they called “post-Keynesian economics: a new paradigm”.

Initially, in the 1950s and 1960s, post-Keynesian economics was mainly associated with the models of growth and distribution coming out of the University of Cambridge, designed by Robinson, Kaldor and Pasinetti. Initially they were referred to as the neo-Keynesian model, but the name was eventually dismissed as it created confusion with American Keynesianism à la Samuelson-Solow-Tobin, which carried the same name. Other names that survived for a while were the Anglo-Italian theory, the Cambridge theory or the Cantabrigdian theory. When Paul Davidson and Sidney Weintraub created the *Journal of Post Keynesian Economics* in 1978, under the chairmanship of John Kenneth Galbraith, Post Keynesian without a dash was proposed, in an effort to make the journal more general than a strict obedience to the Cambridge version, which was thought to be overly left wing or too close to Marxism, especially because of its neo-Ricardian branch or what today we call Sraffian economics. Davidson and Weintraub wished to attract Liberal Keynesians towards their fold, a bit as does the *Review of Keynesian Economics* today.

As recalled by the late Frederic Lee (2000; 2009), a post-Keynesian group was first organized in December 1971, in New Orleans, on the occasion of Robinson's speech at the annual meeting of the American Economic Association, invited by its chair John Kenneth Galbraith. Some economists who are usually considered as neo-Marxist economists or post-Keynesian Marxists, also attended the dinner meeting: Donald Harris, John Gurley, Howard Sherman and Howard Wachtel. Steve Marglin was supposed to be there, but there was some miscommunication. Tom Asimakopulos, from McGill University, also attended. The second reunion occurred again at the AEA annual meeting, in Toronto in December 1972, with presentations by Eichner, Harris and Hyman Minsky. The session was sponsored by the Union for Radical Political Economics (URPE), which had been created just a few years earlier, in 1968.

Thus, from the very beginning, we see that there were some links between post-Keynesianism and left-wing economists. The journal of URPE, the *Review of Radical Political Economics*, from the start announced that it was open to any submissions within "the broad definition of radical political economics". The editors later pointed out that this included "Marxian, institutionalist, post-Keynesian and feminist" economics. This is certainly true. For instance, I have myself published three articles in the *Review of Radical Political Economics*, one of which had been rejected by the *Cambridge Journal of Economics* and the *Post Keynesian Journal of Economics*! I also attended an URPE summer school in 1986, almost 40 years ago, in Cape Cod, where I remember meeting at the time two young economists who became famous post-Keynesians, Robert Blecker and Marty Wolfson, sharing the same dormitory. All this to say that there were and there are tight links between left-wing or neo-Marxist economists and post-Keynesian economists. Thus, the question of how progressive is post-Keynesian economics is not an absurd one.

Immediately, another issue of definition arises: whose works should we associate with the concept of progressive economists? At first hand, one would think that Marxist, neo-Marxist or Marxian economists, whatever term we prefer, ought to be the measuring rod of a progressive view. But things can be confusing. Some authors, I think here of the Dutch economist, Ludo Cuyvers (2022), consider some economists to be *post-Keynesian neo-Marxists*. He has in mind Kalecki, Steindl, Sraffa, Joan Robinson, which many of us would put in the post-Keynesian camp; but he also has in mind Paul Baran and Paul Sweezy, and I guess the whole body of authors associated with the *Monthly Review*, certainly a Marxist journal. As an aside, it may be mentioned that there are many similarities between their book *Monopoly Capitalism* and Galbraith's book on the American corporate economy, so much so that for a while I wondered whether Galbraith was closer to the post-Keynesian or the Marxist camp?

I have yet to define post-Keynesianism, but for time constraints I will say no more about it, except to refer you to my 720-page book that came out in 2022, in case you really care about its definition (Lavoie 2022).¹

Progressive

So now, I move on to define the word "progressive". The word can be understood in two ways. The meaning that comes immediately to mind, at least I suppose for the members of this organization, can be related to the definition of the mandate of the PEF, the Progressive Economics Forum: "The **Forum's** general purpose is to promote progressive approaches to economic analysis, policy-making, and activism in Canada". A similar definition of sort can also be found on the website of URPE, which also emphasizes activism. A second meaning can however also be given to the question of whether post-Keynesian economics is progressive, in the sense given to it by methodologists or philosophers of science: is post-Keynesianism a progressive or a regressive research programme in the sense of Imre Lakatos? In other words, is there progression, stagnation or degeneration, to borrow the title of the book of Glass and Johnson (1988). I will deal in turn with these two meanings of the term progressive, concluding, at least in some sense, that post-Keynesian economics sometimes can be said to be more progressive than neo-Marxist or Marxian economics, and that the post-Keynesian paradigm shows some progression.

Now, before I start discussing these two aspects of the question at the heart of the lecture, how progressive is post-Keynesian economics, there still is an issue that needs to be cleared up. I am old, my career is behind me, not ahead of me, so I will risk a few personal remarks that might shock some listeners, those who think that the woke

¹ Louis-Philippe Rochon (2024), a former undergraduate of mine in the 1980s, has recently written his assessment of the history of post-Keynesian economics. Lavoie and Seccareccia (2025) discuss post-Keynesian economics in Canada.

movement is the best thing that ever happened since Hitler and the Nazis were defeated in 1945. So, this is a trigger warning of sort.

Today, it is not so clear anymore what the Left stands for. Sometimes, one feels that we are living in the world described in the George Orwell's novel, *1984*, where words take a new meaning, sometimes the complete opposite of what was previously understood. Feminist movements once meant the improvement of the economic and social conditions of all women. Besides thinking that the inclusive writing of the French language, which makes the reading of a text nearly incomprehensible, will improve the economic condition of ordinary women, neo-feminists today argue that women should be free or even encouraged to wear the hijab or the jilbab, despite the fact that it is a sign of the submission of women to a view of patriarchy that intends to demonstrate that they are not easy preys or prostitutes. The same neo-feminists approve of males who feel to be females being allowed to compete in athletic venues that used to be reserved to girls and women, even thus this might hurt female athletes who could lose their spots on high school, university, provincial or national teams.² Progressive activists encourage teenagers to take puberty blockers and then cross-hormones, at the risk of becoming sterile and unable to ever achieve orgasms. They even advise teenagers with psychological problems, who wonder whether their soul was born in the right body, to mutilate their breasts.

The Left is said to be against all forms of racism. Today we hear from some leftist activists or even judges, as happened in December 2021 at the Ontario Superior Court, that black and so-called other racialized candidates for teaching positions should be exempted from taking exams in mathematics because they have acquired an incapacity to perform in that subject.³ Some activists also argue that being on time should not be imposed to students, because being punctual is not an innate attribute of people of African descent. In a recent past these claims would have been taken as statements of racism; today they are associated with being awoken to the disasters of white colonialism. Leftists argue that there ought to be positive discrimination in favour of blacks and some other coloured candidates, even though this might imply the creation of restrictive quotas against good candidates of Asian descent, because otherwise there would be too many of them in scientific programmes. I have myself published a dozen studies on the issue of discrimination, mainly in ice hockey but also in baseball. What annoys me most about current studies about diversity, equity and inclusion, is that no consideration is being given to cohort effects: for instance, one cannot expect the percentage of black full professors in universities to reflect the percentage of black

² By contrast, social justice activists despise those who obtain scholarships or jobs by wrongly claiming to be Indigenous or Métis – the pretendians. You can self-identify as a woman, even without a vagina, but you cannot feel to be Indigenous, even if you have a non-status Indigenous background.

³ See: *Ontario Teacher Candidates' Council v. The Queen*, 2021 ONSC 7386. The Court of Appeal overturned the ruling one year later, based on more detailed evidence

students today: setting aside foreign recruits, it should reflect instead the percentage of black students many years ago.

Neo-left activists accuse their old-left comrades, such as Bob Rowthorn (2018), of being neo-fascists when the latter wish to discuss restrictions on immigration, arguing that unrestricted immigration has no positive fiscal benefits and might put stress on infrastructures, the education and health systems, and is likely to hurt mostly low-pay workers. At the annual meeting of the European Association of Evolutionary Political Economy (EAEPE) in the fall of 2016, I listened to my socialist colleagues, comfy in their universities and central Parisian apartments, piss on the British who had voted in favour of Brexit, while an old left-wing British economist had to explain that traditional supporters of the Labour Party in low-income areas had voted for Brexit out of frustration with the deterioration of their way of life. In other words, it is not quite clear what is progressive or what is not progressive today.

Well, I am not the only one on the left to be greatly puzzled as to where progressive ideas are driving us. Thomas Weisskopf (2014, p. 443), in his 2014 URPE David M. Gordon Memorial Lecture, has also pointed out diplomatically that significant progress on social issues has favoured beneficiaries that are relatively well off, while the reduction of sexism and the advances in LGBT rights “have benefitted well-to-do minorities probably more than the less well-off”, a claim that seems ever more valid ten years after it was made by Weisskopf.⁴

In a sense, there is nothing new with confused progressives. Where the Camp of the Good stands has often not been very clear. In the 1970s I was an undergraduate in Canada and then a graduate student in France, so what I am to say has been influenced by this stay in France and many not apply so well to Canada. Nearly all the greatest leftist intellectuals gave their full support to Lenin, Trotsky and then Stalin and Communist USSR, despite the dozens of millions of dead opponents that roamed concentration camps in Siberia. Aleksandr Solzhenitsyn, with his *Gulag Archipelago*, for a long time was described as a fake by progressives. The same French leftist intellectuals, including Jean-Paul Sartre and Simone de Beauvoir, as well as Deleuze, Derrida and Foucault, the last three having been the inspiration for the current woke movement based on *French Theory*, signed a petition in 1977 expressing an implicit support for pedophilia. A few years before that, progressive students were rooting for the Vietcong and the liberation of Saigon: within a year 65,000 South Vietnamese had been assassinated and within a

⁴ As an anecdote of the above, when my then common-law spouse went for a job interview as an assistant to the Vice-Rector Academic at the University of Ottawa, she was asked whether there was a conflict since the man she lived with was a teacher in the Economics department, a rather politically-incorrect and unwarranted question, especially coming from a feminist scholar. No such questions were asked when my spouse was previously or later interviewed by male deans. My spouse did not get the job, whereas the lady feminist later became the first woman to be President of a large Ontario university, an exemplar that progress in gender equality may have benefitted mainly well-to-do educated persons.

few years there were three million Boat people. My first wife, a French woman brought up in a communist family, thought that the take-over of Phnom Pen in 1975 by the Red Khmers was a victory for democracy; she tenaciously held that the accusations against the Red Khmers of mass genocide of the Cambodian population – no less than two million killed individuals out of eight million – were just another instance of American propaganda. Left-wing intellectuals also rejoiced when the shah of Iran was forced to flee in 1979 and when the Ayatollah Khomeini took over, quickly imposing his theocracy with the creation of the Islamic Revolutionary Guards, only realizing later that the Guards were imprisoning all opponents, including thousands of communists. Today, students, intellectuals and artists are demonstrating in favour of Hamas, the liberation of Gaza and the destruction of Israel, claiming that they are on the right side of History, despite using the same slogans and rhetoric that were propagated 60 or 70 years before by USSR and East-European communist leaders to nazify jews and Israel. None of these students ever gave a thought about the eight million people who died in Congo since the 1990s, despite issues of colonialism there being particularly obvious. Finding where the camp of the Good sits can be a complicated business.

Post-Keynesians are not free of confused ideology. Joan Robinson was an admirer of North Korea and wrote that this country would soon achieve the standards of living of the UK. She also gave her full support to Mao Zedong, being rather lenient about the consequences of his Great Leap Forward and of the Cultural Revolution led by the Red Guards, which left dozens of millions of dead or purged Chinese, both intellectuals and peasants. Is there still left any meaning of the word progressive?

On theories: Wage-led or profit-led economies?

Being done with this long aside, let me come back to issues of economic theory. I will essentially deal with two issues, fiscal policy and wage-led growth, although the two themes can be somewhat related. I shall also make a few technical remarks, current issues *oblige*, regarding post-Keynesian views on tariffs.

I start with the issue of wages, real wages and the wage share. There is no doubt that, today, progressives are quite adamant to ask for increases in the minimum wage. But this was not always so. Robert Pollin and his Political Economy Research Institute at UMass have successfully lobbied for increases in the minimum wage or in the living wage in various US cities. Here in Quebec, Québec Solidaire and the IRIS, a left-wing think tank, have also advocated the implementation of minimum wages at levels that were never thought possible before, but that seem more and more adequate today. However, I remember listening to a radio programme many years ago, where Françoise David, a former co-leader of Québec Solidaire, argued that it would not be a good idea to raise the minimum wage. I am sure she has changed her mind a long time ago.

However, at the time, in that interview, she argued that raising the minimum wage would lead to an increase in the level of unemployment as firms would not afford the rise in their costs and would be forced to lay out their workers. This obviously is the standard mainstream or neoclassical argument, which has been debunked by several empirical studies, starting with Card and Krueger already 30 years ago, and more convincingly by several meta-regression analyses, for instance Doucouliagos and Stanley (2009). But why was Mrs David favourably influenced by this mainstream point of view? Françoise David has often been involved with popular organizations, part of the social economy, where these organizations lack financial resources and are constantly on tight budgets. These organizations do not or hardly sell services or goods, and as a consequence their revenues are constrained and depend mainly on government subsidies. Within this context, where their workers are either volunteers or paid the minimum wage, a rise in the minimum wage means that less workers can be paid by the organization. So this explains that.

But this is all anecdotal, as a way to put you in appetite for evidence from scholarly work among heterodox economics regarding the impact of wages, real wages or the wage share on economic activity, productivity and employment, or more precisely on the growth rate of these three variables. What is at stake is the kind of economic policies that should be advocated, for instance to get out of a crisis, at least when setting aside issues related to equity. Peter Skott (2017: 357) once wondered whether left-wing economists would “advocate an increase in inequality if it could be established that a rise in inequality tends to raise the rate of economic growth”. Well, perhaps Skott would not, but other progressive economists in the past have advocated real-wage restrictions on the basis of their empirical and theoretical results.

A key issue, which is at the heart of a protracted debate, is whether the economy is wage-led or profit-led. It is generally understood that an economy is wage-led when an increase in the wage share will lead to an increase in economic activity: in the rate of capacity utilization, the growth rate of capital accumulation, or the rate of employment. When the increase in the wage share leads to a fall in economic activity, we say that the economy is profit-led. In very rough terms, although there are a number of exceptions, one can say that heterodox economists closer to post-Keynesian economics have put forth models that show that economies are generally wage-led, and they have found through their empirical studies that this is the case; on the other side, heterodox economists with some background in Marxist or Marxian economics, and more recently those who rely on the Marxist Goodwin model, have put forth models that show that economies are generally profit-led, and their empirical work has also provided support for their belief. As I said, there are exceptions, for instance Howard Sherman, who has been involved with URPE and less so with post-Keynesians, seems to be more on the wage-led camp.

On the matter of whether post-Keynesian economics is progressive or not, one would have thought that progressive heterodox economists (the neo-Marxists) would be favourable to economics policies that promote a rise in the wage share, and that they would be tempted to torture theoretical models or empirical data in such a way that they would demonstrate that policies favourable to wages have a positive impact on the economy. But this is not what has been observed over the years, as I recall in a long article that goes over the history of this wage-led versus profit-led controversy (Lavoie 2017). If one accepts this characterization of the issue, one would need to conclude that post-Keynesians are more progressive than neo-Marxists. What I say next on this controversy is inspired by this 2017 paper.

There are two causal issues at stake. One, as already said, is whether an increase in the wage share will cause an increase in economic activity, however defined. This concerns the shape of effective demand. The other, is whether an increase in economic activity will cause a change in the wage share or the profit share. This is what has been called the distributive curve. Putting these two causal effects together, the Marxist story of the business cycle, as conventionally told, is that an increase in the profit share will cause an increase in economic activity, so the economy is profit-led; but then this increase in economic activity feeds back into a rise in wages and the wage share, the so-called profit squeeze, which Marxists attribute to an employment effect, tied to the rise in the bargaining power of workers. This story corresponds to a cyclical model, the 1967 predator-prey model of Richard Goodwin. It was first put forward empirically by Boddy and Crotty (1975). The model was at the heart of the Social Structure of Accumulation (SSA) school, led by a group of authors in the 1980s that included Sam Bowles, David Gordon and Tom Weisskopf, and indirectly Robert Boyer from the French Regulation School; it was endorsed by Stephen Marglin; and it was picked up by Lance Taylor and many of his former students at the New School, who are now referred to as neo-Goodwinians. These former students of Lance Taylor have now added a dose of complexity to the story in recent years, in particular the positive impact of a higher wage share on the growth rate of labour productivity, which is called the Marx-Webb effect.

The argument of SSA was that the American economy in the late 1970s and 1980s, in contrast to what had happened during the Great Depression, was suffering from a supply-side crisis, that is, a profit-squeeze crisis brought about by an overly-long economic expansion, with high-employment conditions, which had overly strengthened the power of the labour force and lowered the cost of job loss to workers, giving rise to an increase in the share of wages. The fall in the profit share and profit rate, according to the SSA school, had thus brought about a fall in the rate of investment and hence a secular slowdown in economic activity. As a consequence, in their view, while a redistribution of income towards labor during the Great Depression could stimulate demand and end the crisis, no such solution was possible in the early 1980s.

For Weisskopf *et al.* (1985: 261), “no such happy coincidence of short-term material interests and longer-term radical objectives is associated with the type of supply-side crisis which results when the capitalist class is too weak. The most obvious exit from the crisis is that pointed to by the right: strengthen the capitalist class, restore profits and rekindle the capitalist accumulation process”. Indeed, during my stay at the 1986 URPE summer school, I heard Weisskopf being adamantly against any wage-led policy.

A similar conclusion was reached by Stephen Marglin in his famous *Cambridge Journal of Economics* article. Marglin (1984a: 142) claimed the following: “A Left program, I would suggest, must respect the logic of the economic situation. Productivity does place limits on wages, and not just physical limits. As long as profitability remains the mainspring of investment, there are economic limits that constrain the wage share. Under capitalism, profits are indeed the geese that lay the golden eggs....A Left program must therefore accept limitations on real wages”. Presumably, Marglin, at least in those years, believed that the neo-Marxian model was the appropriate one to understand capitalism, because in his book he wrote that “the neo-Keynesian analysis leads to policies designed to stimulate investment demand or to reduce capitalists’ propensity to save; the neo-Marxian model leads ... to policies that will stimulate saving, or to policies that will reduce the subsistence wage” (Marglin 1984b: 101).⁵ In a nutshell, this conclusion can be obtained by relying on the Cambridge version of the warranted rate of growth, where the rate of accumulation $g = s_p r = s_p m u_n / v$, where m is the share of profits and s_p is the propensity to save out of profits. An increase in any of these two variables will be associated with a higher rate of accumulation.

Lance Taylor (2004: 305) has more recently issued the same warning: “Wage increases as advocated by people on the Left cannot restore aggregate demand if it is in fact profit-led”. Observing business cycles, and being inspired by Goodwin cycles, he argues that, when looking at the wage share and the rate of utilization, the US economy shows “negatively inclined counterclockwise spirals” (2004: 287), and hence clockwise spirals when looking at profit shares and utilization rate. This in his view (Taylor 2004: 291) is explained by the fact effective demand is profit-led (there is a negative impact of the wage share on the rate of utilization), while the distributive curve is positive (higher rates of utilization lead to higher wage shares, signaling a profit squeeze). The empirical work supporting this assessment is presented in more detail in the oft-quoted paper that he wrote with his former Brazilian student Barbosa-Filho (Barbosa-Filho and Taylor 2006). Taylor (2004: 236) has explicitly recognized the strong relationship between his

⁵ I must note that when I met Marglin in Paris, in 2017 I think, he expressed surprise at me calling him a neo-Marxist. It is true that his latest work is devoted to a dynamic interpretation of the claims of Keynes in the *General Theory* (Marglin 2021). It is the theoretical article of Bhaduri and Marglin (1990) that has generated a flurry of empirical studies on whether the economy is wage led or profit led.

neo-Goodwinian model and the arguments made in the past by Boddy and Crotty and the SSA school.

As noted dismally by an occasional co-author of mine and a former post-doctoral fellow at the University of Ottawa, Brett Fiebiger (2018: 173), “a pro-cyclical profit share is commonly interpreted as providing evidence of a ‘profit-led’ demand regime and that, in turn, as supporting the Marxian conclusion that higher output growth requires abstinence by workers (via lower real wages). The flipside to the ‘profit squeeze’ theory is that a ‘wage squeeze’ is good for growth”.

It would be unfair not to point out that Bowles, Gordon and Weisskopf in other publications argued the opposite of what I just mentioned. After having said (Bowles et al. 1984: 4) that the reigning conventional wisdom, even among the left political spectrum is the “trickle-down distributive strategy for economic recovery”, which “sacrifices wages and living standards to boost profits and investment”, so that “raising business profitability is the way to stimulate investment and growth, and that to do this workers will have to accept a period of austerity”, they contended that the US economy is in a regime of wage-led productivity growth, that is, “high wages contribute to productivity because they constitute an important source of motivation” and because they force “employers to modernize or go out of business” (1984: 8), so that rising wages could lead to more investment.

A variation of this Bowles et al. argument is now at the heart of the most recent versions of the neo-Goodwinian models put forth by former students of Lance Taylor. It is claimed that accumulation is profit-led in the short or medium run, through an aggregate demand effect, but that it is wage-led in the long run, because of the supply-side productivity effect which I mentioned earlier, that is, higher real wages will induce investment in technical progress and hence an increase in productivity growth. This is what I called the Marx-Webb effect, also sometimes called classical-induced factor-biased technical change. As a result, somehow, in the long run, the economy comes back to its potential or natural rate of growth determined by the growth in the labour force and the growth in labour productivity. Neo-Goodwinians, which we might call neo-Marxist post-Keynesians, such as Codrina Rada, Rudiger von Arnim, David Kiefer, Daniele Tavani and a few other former students of Lance Taylor, argue that there is good empirical evidence supporting this extended version of the Goodwin model. The economy is profit-led in the short run, and wage-led in the long run, but because of supply-side effects, not because a higher wage share has a positive impact on consumption and aggregate demand. There might be more investment, but this investment is not designed to increase production capacity; it is designed to bring in more mechanization and faster labour productivity growth.

The neo-Goodwinian model however does not take into account another supply-side effect, the Kaldor-Verdoorn effect, which says that faster growth of aggregate demand will lead to faster productivity growth. If this effect is relatively strong, then an increase in the wage share in a profit-led economy would lead to a fall in the growth rate of aggregate demand and hence to a fall in productivity growth. The neo-Goodwinian results would not hold, a critique made by Mark Setterfield (2023).

Another critique, this time related to demand-side effects, is that the profit-led demand regime may be an *artefact*, associated with a case of reversed causation, an argument that I have made on numerous occasions, including once in front of Lance Taylor, who sternly admitted it could be right. This critique is related to the fact that most models assume away the presence of overhead labour, which is at least partially fixed in the short run – a case of labour hoarding. This implies that an increase in economic activity automatically leads to a concomitant increase in labour productivity, a decrease in unit cost, and hence an increase in the profit share, even though markups or profit margins are constant, as first argued theoretically by Robert Rowthorn (1981) and empirically by Howard Sherman (Sherman 1979, Sherman and Evans 1984, ch. 10), ironically both more neo-Marxists than post-Keynesians. A further irony is that Weisskopf (1979) himself shows that changes in the profit rate arise mostly from changes in the rate of utilization. Thus, in the short run upswing, we observe a contemporaneous increase in economic activity and in the profit share, as more recently empirically shown by Michael Cauvel (2023). A case in point is what happened at the beginning of the Covid, when economic activity fell dramatically because of the lockdown. In Canada, the labour share moved up from 56% to 64%. It did so, at least in part, because of the presence of overhead labour. Neo-Goodwinians, based on their story, would have had to argue instead that the observed increase in the wage share in 2020 caused a dramatic fall in economic activity.

Finally, a last word on this profit-led wage-led issue. Bowles and Boyer pointed out, already in 1995, that economic activity could be wage-led while employment could be profit-led. This possibility has also been pointed out by post-Keynesians in the Kaleckian tradition, I am thinking here of Servaas Storm and Ro Naastepad (2012). If the Kaldor-Verdoorn effect is strong, an economy with fast increases in aggregate demand may be accompanied by rising unemployment rates because of high labour-saving innovations, or inversely, slowly-growing economies may be accompanied by low unemployment rates, because of slow productivity growth.

On theories: Fiscal policy

When it comes to fiscal policy, what is progressive and what isn't is perhaps not so clear. Certainly, most heterodox economists would agree that a progressive income tax is better than an income tax with constant rates, or that tax loopholes that favor the rich and that favour tax avoidance ought to be closed. Also, there might be some agreement that

subsidies to the corporate sector ought to be eliminated. But besides this, what else? Left-wing activists would usually argue that tax rates on corporate income ought to be increased, but then there is some empirical evidence and some economic theories that show that the incidence of the corporate tax can be shifted to consumers. But then, if this is so, why are corporate leaders so much opposed to increases in the corporate tax rate? A lot could also be said about the incidence of various government expenditures.

Here I shall focus on the macroeconomic side, on the issue of fiscal deficits. As is well-known, Keynes, who opposed the Treasury View, which was akin to what Abba Lerner called “sound finance”, had a hard time in the 1930s to convince politicians and in particular those of the Labour Party. Abba Lerner, who was not particularly left-wing as far as I could figure out, advocated instead “functional finance”. The latter doctrine says that a public deficit in itself is neither good nor bad: what matters is to procure sufficient stimulus to counter-balance the loss of aggregate demand coming from the private sector.

This view of functional finance has been mostly endorsed and advocated over the last 25 years by neo-chartalists, that is, the advocates of Modern Monetary Theory, or MMT. MMT is a variant of post-Keynesian economics, a variant which I have associated with one of the five strands of post-Keynesian economics, the Institutionalist strand. The MMT view is that the fiscal objective of a sovereign state ought to be full employment, whatever fiscal deficit this entails. A sovereign state is a state, for instance the Canadian federal government, which has a central bank, which has its own domestic currency, which collects taxes in this domestic currency, and which issues debt denominated in the domestic currency. If this is the case, then the country cannot default, whatever the size of the deficit. MMT adds that the country must run a flexible exchange rate, but in my opinion external constraints are nearly similar whether the country is on a flexible or a fixed exchange rate regime.

Before MMT, other post-Keynesian economists have been making similar arguments, such as my friend and colleague Mario Seccareccia, although probably with less success. While our mainstream colleagues were all getting in the bandwagon of sound finance in the 1990s, several post-Keynesian economists were fully endorsing functional finance, reiterating that counter-cyclical fiscal policy is a highly effective tool. This was done at the time, among many others, by none other than the son of John Kenneth Galbraith, James Galbraith (1995), and also by William Vickrey (1997), the 1996 Nobel prize recipient, who turned into a post-Keynesian economist in the early 1990s. Besides Philip Arestis and Malcolm Sawyer who kept writing about fiscal policy, one can also mention the name of Steve Fazzari (1994-95: 233), a former colleague of Hyman Minsky, who was also quite adamant about the effectiveness of fiscal policy, arguing as follows: “Conventional claims about the impotence of Keynesian fiscal policy are largely

unfounded.... Our current state of knowledge provides no reason to reject Keynesian demand management principles as the appropriate response to an economy operating with substantial idle resources. Furthermore... effective Keynesian fiscal policy may raise potential output, as well as addressing problems of underutilized resources”.

MMT authors sometimes go so far to say that there is no need to issue bonds to finance deficits, it could all be financed by issuing money. This may explain why MMT gets sometimes supported by right-wing organizations, such as the former Tea Party in the USA, who are opposed to taxation. Left-wing economists then get annoyed at MMT authors, saying that the latter, by denying the role of taxation, leave aside the efforts of society to modify the secondary income distribution, by using taxation to improve the fairness of income distribution.

Leaving this aside, it must be said that, at least until recently, since the Justin Trudeau years and the Covid pandemic, the New Democratic Party, the NDP, has been rather hostile to government deficits. The same can be said about the Alternative Budget regularly presented by the Canadian Centre for Policy Alternatives, the CCPA. While the Alternative Budget has always proposed a vast array of progressive measures, for a long time its estimates were based on a balanced budget. This Alternative Budget, based on the doctrine of “sound finance”, has irritated in particular my colleague Mario Seccareccia. If I may recall a personal anecdote tied to the NDP, back in September 2008, Jack Layton, then leader of the federal NDP, happened to be in front of me at the security gate of the Ottawa airport, and I told him that to pre-empt the huge recession that I could see coming, he should ask the Parliament to go for a stimulus program and argue in favour of a large federal deficit. Layton responded that provincial NDP governments had run eight balanced or surplus budgets in a row, and told me that if I held such crank ideas I ought to start my own political party. I did not have to do such a thing because just two months later the NDP, along with the Liberals and the Bloc, all demanded the implementation of a fiscal stimulus package, which the Conservatives stubbornly refused to design until January 2009, when the IMF recommended such a policy.

The NDP, as did others, then adopted what Mario Seccareccia has called the “new fiscalism”. Counter-cyclical fiscal policy should only be used when things are really bad, in particular when monetary policy seems to be running out of ammunition, for instance when the monetary authorities reach the zero-interest lower bound, otherwise, governments should achieve balanced budgets or surpluses. *New fiscalism* explains why, one year after the 2009 global expansion in government expenditure designed to fight the Great Recession, international organizations such as the IMF or the G-20 exhorted national governments to *consolidate* their budgets and implement austerity measures. New fiscalism has certainly been back into action since the Covid episode, although there

is some evidence that federal parties didn't seem to be much concerned with balanced budgets during the recent April election.

If I may recall another personal anecdote, in August 2015, I wrote a new blog for the Broadbent Institute precisely about fiscal deficits. This was a couple of months before the October 2015 election when Thomas Mulcair was the leader of the NDP and when Justin Trudeau was eventually elected for the first time. The intent of the blog was to analyse the implications of the Federal Balanced Budget Act (<http://laws-lois.justice.gc.ca/eng/acts/F-5.8/page-1.html>), which was included in the omnibus Bill C-59 and which passed third reading in June 2015. The Act had been suggested two years earlier in the Speech for the Throne, when the Canadian Conservative government announced that it would introduce a balanced-budget legislation. Neither the proposal nor the Act attracted much interest, although in 2014 the Parliamentary Budget Office (PBO) did produce a substantial document analyzing the benefits and costs of such a proposal. I did publish a blog in French in 2014 for the Broadbent Institute, where I criticized the few presumed advantages that had been identified by the PBO.

The Act of 2015 did not force the federal government to adopt a balanced budget – it had some of the flexibility advocated by the PBO. But it included measures designed to discourage the federal government from taking expansionary fiscal measures preemptively before a recession is declared. Furthermore, its purpose was to induce the federal government to minimize budget deficits during recessions and thereafter to quickly achieve a balanced budget or budget surpluses. In addition, the Federal Balanced Budget Act contained clauses that were akin to some sort of wage control policies since the overall payroll for civil servants were to be frozen when the federal government ran a budget deficit while the economy was not in a recession or when the economy had just got out of a recession.

The purpose of my blog was to show that the 2015 Federal Balanced Budget Act would have detrimental consequences on the macroeconomic stability of the Canadian economy whenever the economy would run into a recession or stagnate. The blog, also based on some arguments of MMT, argued that deficits by a federal government, were not of the same nature as deficits by provincial governments. My conclusion was that the Federal Balanced Budget Act should be repealed as soon as the Conservative government would be voted out of power. Well, the people running the Broadbent Institute thought that the blog ought not to be published, because they feared that it might hurt the chances of the NDP to win the October 2015 election. I reluctantly accepted their decision, as I understood the contradiction between my arguments and those implicitly put forward by the NDP. The rest of it is history. During the election campaign, Harper and the Conservatives promised more tax reductions and a balanced budget. Trudeau and the Liberals said they would create an extra tax bracket for the rich, and they intended to

increase government expenditure and the public deficit to counter the economic slowdown. Mulcair and the NDP claimed that they would not increase tax rates on personal income, and they vowed to keep their first federal budget in balance. The Liberals got an absolute majority and the NDP went from more than 100 MPs to just 44 MPs – a result that seems good by today's standards, but which was a huge deception at the time. The text of my 2015 unpublished blog is to be found in an appendix.

Free trade and tariffs

The conjuncture, meaning the obsessions of Donald Trump, has brought about the issue of free trade and tariffs. The 1988 free trade agreement between Canada and the US was sold to us at the time of the Mulroney government on the basis that the agreement would protect Canada against US moves towards isolation and protectionism.⁶ Progressives mostly objected to the free trade agreement. Indeed, in November 1987, Mario Seccareccia with the late Paul Phillipps (of the University of Manitoba) and the late Mel Watkins (of the University of Toronto) wrote down a petition against the Canada-US free trade agreement, a petition which was signed by about 75 Canadian economists. As I vaguely remember, the main argument against free trade was that it would give more bargaining power to corporations, who could more easily threaten their employees with the possibility of outsourcing production to the other country if the trade unions did not cooperate enough. Ironically, given Donald Trump's mockeries about Prime Minister Justin Trudeau being the Governor of Canada, Wikipedia says that some opponents to the free trade agreement argued that "Canada would become the 51st state of the US if the agreement was implemented".

Opponents to free trade are in a queer situation today, as we realize the chaos that the sudden imposition of tariffs can create to the domestic and world economies. Is it still possible to be against tariffs or import quotas today? As I recall in my synthesis of post-Keynesian economics (Lavoie 2022: 552-559), post-Keynesians have a favourable view of capital controls, tariffs and quotas. One of the major reasons is that post-Keynesians reject the analysis of international trade based on comparative advantage, as do some Marxists authors such as Anwar Shaikh. The imposition of tariffs and quotas is justified on the basis of increasing returns and, in dynamic terms, on the empirical evidence of the Kaldor-Verdoorn effect, in other words it is justified on the basis of the infant-industry argument. The development economist in the Cambridge tradition, Ha-Joon Chang (2002), in his book *Kicking Away the Ladder*, has been in the forefront of this argument. But post-Keynesians have been adding another argument in favour of tariffs,

⁶ If I may add a personal note, I should also say that the chief negotiator for Canada, Simon Reisman, had been my father's boss when he was part of the Canadian team at the GATT Dillon and Kennedy rounds in Geneva in the 1960s.

at least under certain circumstances, when the international constraints overly slow down economic activity. In the 1970s and 1980s, it used to be claimed by Wynne Godley and several of his associates at the former Cambridge Economic Policy Group that tariffs allow governments to pursue more expansionary fiscal policies, which in time will allow greater international trade and eventually the removal of these tariffs. Of course, one could argue that the United States certainly do not fulfill these conditions currently.

What is the effect of tariffs on the economy? It all depends on whether the tariff is on a final product or on intermediate goods and raw materials. In the case of a tariff on raw materials and intermediate goods, the tariff will lead to an increase in the prices of domestic finished products, since this is an increase in cost faced by all firms. The increase will be fully transferred in the case of raw materials, as the price of raw materials is often determined in international markets; in the case of intermediate goods, the increase may be mitigated because the exporter of the intermediate good may decide to absorb part of the tariff. Similarly, in the case of final goods, domestic producers in highly industrialized countries are unlikely to raise their prices because they are based on the normal unit cost of the price leader, who is likely to be a domestic firm; foreign producers will thus be forced to take a financial loss or lose market shares. By contrast, in semi-industrialized countries, price leaders are likely to be foreign firms, and hence the pass-through of the tariff increase is likely to be very high.

The Progressivity of the post-Keynesian research programme

As pointed out earlier, there is a second way in which the word “progressive” can be used, and this in relation to whether a given paradigm, research tradition or school of thought can be said to be making progress. The concept of whether a research programme can be said to be progressive or degenerative can be mostly attributed to the philosopher of science Imre Lakatos. While this kind of question was very much debated in economics in the 1980s and early 1990s, the topic and perhaps the method suggested by Lakatos, and discussed and criticized both by economists and philosophers, for instance by Larry Laudan and Paul Feyerabend, seem to attract less interest today, perhaps because the criteria suggested by Lakatos to define a progressive research programme seem so difficult to apply to actual science, and to economics in particular.

As a consequence, I will mostly use my own criteria to assess whether the post-Keynesian research programme can be said to be progressive. One obvious criterion, an obvious sign of a degenerating research programme, is when the number of its participants are dwindling. There can be many reasons for this, it can be because its members are abandoning the research tradition, or it may be because the institutional circumstances are such that it is highly difficult for the research programme to reproduce

itself. In the case of post-Keynesian economics in Canada, unless you consider that there are a lot of closet post-Keynesians advising the Liberal Party of Canada on the issue of public deficits, the number of post-Keynesians in academia is going down, because of institutional difficulties, rather than abandons, as I have recently reported with Mario Seccareccia in a paper devoted to post-Keynesianism in Canada (Lavoie and Seccareccia 2025). However, in countries such as Brazil and Italy, this is not the case, there is a relatively large and growing number of young scholars that have joined the post-Keynesian tradition. In other countries, such as France, the flow of new members is low but steady. Thus, from this naïve point of view, there is no evidence that the post-Keynesian research programme is degenerating. To some extent, the survival of post-Keynesianism can be attributed to the incredible impact that MMT has had on social media, as several students discovered post-Keynesian economics by reading blogs written by MMT scholars. Through MMT, post-Keynesian ideas have reached an audience that goes beyond strict academia.

There are other signs, just as relevant and probably more relevant, that show that the post-Keynesian school of thought is progressive in the Lakatosian sense. One such positive sign, coming back to the remarks of Düppe noted in my introduction, is the fact that most research activity among post-Keynesians has been diverted away from examining the strictures of the Gospel. The power of the “self-appointed Guardians of the Temple”, as my former colleague Jacques Henry (1993: 19) used to call them, has been greatly diminished. Henry, whose untimely death occurred in 1989 when he was only 55 years-old, very rightly pointed out as early as 1982, that post-Keynesian economics would be unlikely to progress as long as “the preferred point of departure of most investigations continues to be: what did Maynard (or Karl, or Piero) really mean?, what did Maynard (or Karl, or Piero) really think he was saying? Those questions are extremely interesting from the point of view of the history of economic thought. However, they become less pertinent if the objective of the post-Keynesian research programme is to arrive at the formulation of a theory better able to explain the world in which we really live today” (Henry 1993: 2-3). It took some time for the diversion to occur, but today post-Keynesianism is fully versed into modelling, empirical work and economic policy. This is a major sign of progress to me.

Not too far from the Lakatosian methodology to consider whether a research programme is progressive or not, is the consideration of whether or not a research programme is able to explain novel facts. Such a novel fact, at a time when mainstream economists were claiming that business cycles were a thing of the past, was the 2008 financial crisis, also called the Great Recession. In a paper that was part of a symposium directed by Jim Stanford for the *Studies in Political Economy*, I tried to convince readers that the post-Keynesian theory of financial fragility put forth by Hyman Minsky, the financial instability hypothesis, was highly relevant to explain and comprehend, and even

predict, the 2008 financial crash (Lavoie 2016). In the same paper I pointed out that the post-Keynesian theory of endogenous money and banking was a perfect fit to understand what occurred during the crisis, pointing out in addition that many central bankers had implicitly or explicitly adopted this post-Keynesian monetary theory to make sense of their actions during the financial crisis.

In the same spirit, post-Keynesian economics now has some influence in geographical economics and in international political economy, in particular when it comes to comparative political economy, as the adoption of the demand-led models of post-Keynesian economics provide an alternative to the supply-side approach that was dominant until recently, through the varieties of capitalism approach. Some political scientists, namely Lucio Baccaro and Jonas Pontusson, have first adopted and incorporated the post-Keynesian growth models into their analysis of comparative political economy. Now, post-Keynesians themselves, such as Eckhard Hein and Engelbert Stockhamme among others, have ventured into the field of comparative political economy, adding to it growth drivers as well as monetary and financial stability issues.

To some extent, the integration of post-Keynesian economics into comparative political economy is due to the simplicity and flexibility of the Kaleckian model of growth and distribution, based on the principle of effective demand. This model, which appeared in the early 1980s, has been a workhorse of post-Keynesian economics. But it has also been a highly useful tool to compare various possible closures illustrating different viewpoints, such as the Sraffian viewpoint or different varieties of neo-Marxian economics. Thus, the model has spread beyond strict post-Keynesian circles. The initial simple model has been improved and has benefitted from various extensions or complications that have allowed to examine several new issues, for instance those associated with the works of Piketty on the origins and the impact of wealth distribution, in addition to income distribution. The Kaleckian model of growth and distribution also turned out to be highly useful to discuss issues related to gender for instance, by studying the macroeconomic consequences of income inequality between men and women.

Another workhorse of post-Keynesian economics since the mid-2000s has been the so-called stock-flow consistent approach, the SFC approach. It even shows up implicitly in the 2025 Alternative Budget. Its main purpose is to make sure that there are no black holes in the modelling. Another major feature is that it allows the full integration of the real and financial sides of the economy, something which has not always been so easy to accomplish, so much so that this search for a full integration had been considered to be the Holy Grail of macroeconomics. The SFC approach has also helped to bring back into its fold those economists who were attracted by the realistic aspects of post-Keynesian economics but who at the same time were annoyed by its lack of formalization,

or by the lack of formalization of some of its components, compared to neoclassical economics.

The SFC approach, along with many of the assumptions entertained by post-Keynesian economics, has also been adopted by several researchers working in the field of ecological economics. It may even have become the dominant approach in ecological macroeconomics when developing models for a post-growth economy. Whereas in the past post-Keynesians paid little attention to environmental and ecological issues, this is not the case anymore, so much so that post-Keynesian conferences are now replete with papers dealing with the ecological crisis. Thus, over the last decade, there has been a double movement, with an acceleration in the study of ecological issues by post-Keynesian economists or closely-related allies, and a similar acceleration in the incorporation by ecological economists of post-Keynesian theories and tools. This may be due to the fact that the stock-flow consistent approach to macroeconomic modelling can be easily integrated into a system dynamics framework, as done by Peter Victor at York University for instance (Jackson and Victor 2020). Post-Keynesian economics is thus a theory which is able, and which others find useful, to deal and confront new problems, which I see as another sign of its progressivity.

Conclusion

Just a few more words to conclude and summarize. According to Weisskopf (2014: 439), for radicals it is important to understand “the deep roots – as opposed to surface appearances – of economic phenomena”. Tony Lawson, the famous methodologist from the University of Cambridge, somewhat also influenced by Marxist political economy, believes the same, arguing that a researcher must go beyond surface phenomena and find the true structures and causal mechanisms. But how far does that get us? What ultimately is the difference or was the difference between post-Keynesian economists and radical economists or neo-Marxian economists? Weisskopf (2014: 438-9), again in his URPE David Gordon Memorial Lecture, recalls that most radicals “expected that revolutionary change was actually possible...., called for a new socialist economy...., envisaged a revolutionary transformation of American capitalism into a distinctively new form of socialism”. Some believed “in the inevitable tendency of the rate of profit to fall, leading ultimately and inevitably to a collapse of capitalism”. I would argue that this was not the vision of the vast majority of post-Keynesian economists. Post-Keynesians from the beginning perceived capitalism as a system that was hard to surpass, in particular because of its dynamism and its ability to innovate, so that the main task of economists according to this perception is to find the means to tame capitalism and its severe defects and instabilities. Perhaps, as was also pointed out by Weisskopf (2014), the challenges of

ecological contradictions rather than social contradictions will help to reconcile the post-Keynesian and neo-Marxian views about the future of capitalism?

As a last word, I remember sitting in the auditorium of the National Arts Center in Ottawa, listening to a lecture by John Kenneth Galbraith, about 45 years ago, in 1980 or 1981. Ronald Reagan had recently been elected president of the United States. Galbraith said there was no reason to be discouraged by this election; he argued that ideology necessarily fades when faced with actual facts, even if it takes time. I must say that this is the only statement that I remember from Galbraith's lecture, but I think that it is still relevant today.

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Appendix

Do we need a Federal Balanced Budget Act?

Marc Lavoie

In October 2013, in the Speech for the Throne, the Canadian government announced that it would introduce a balanced-budget legislation. At the time this vague proposal attracted little interest from anyone, although a year later the Parliamentary Budget Office (PBO) did produce a substantial document analyzing the benefits and costs of such a proposal (http://www.pbo-dpb.gc.ca/files/files/BalBudLeg_EN.pdf). Broadly speaking, the PBO seemed to see more disadvantages than advantages in such a balanced-budget legislation, arguing that in all likelihood it would reduce the ability of the federal government to pursue proper counter-cyclical fiscal policy, and fearing as well that that the federal government might be tempted to shovel its deficits towards provincial government or else engage in the kind of creative accounting that was pursued by the Greek government in the 2000s. The PBO concluded that if a balanced-budget legislation were to be introduced it would need to be a flexible one. As a follow up to this, I wrote a blog in French criticizing the few presumed advantages that had been identified by the PBO (http://www.institutbroadbent.ca/94751/une_loi_sur_lequilibre_budgetaire_une_tres_mauvaise_idee).

The Federal Balanced Budget Act (<http://laws-lois.justice.gc.ca/eng/acts/F-5.8/page-1.html>), which was included in the omnibus Bill C-59 and which passed third reading in June 2015, does not seem to have attracted much attention either. The Act does not force the federal government to adopt a balanced budget – it has some of the flexibility advocated by the PBO. But it includes measures that should discourage the federal government from taking expansionary fiscal measures pre-emptively before a recession is declared. Furthermore, it will

induce the federal government to attempt to minimize budget deficits during recessions and to quickly achieve a balanced budget or budget surpluses. My understanding of this law is the following:

If there is a budget deficit or if one is projected while the country is not in a recession (or in an extraordinary situation), the operating budgets to fund annual wage increases are to be frozen and the salaries of ministers and deputy ministers are to be diminished by 5 percent until the budget is back to balance.

If there is a budget deficit or if one is projected while the country is in a recession (or in an extraordinary situation), the operating budgets to fund annual wage increases and the salaries of ministers and deputy ministers are to be frozen as soon as the country is out of recession, until the budget is back to balance.

To provide some intuition of what this entails, recall that the last recession went from October 2008 to May 2009. The Act considers that 'a recession ends in the fiscal year in which the second consecutive quarter of positive growth in real gross domestic product in Canada is recorded'. This implies that the recession would have 'officially' ended in March 2010. A freeze on the government operating budgets to fund annual wage increases would thus have been in place starting in April 2010 until the federal budget is back in balance, that is, until at least now! Furthermore, since the Act defines a recession in the standard way, that is, 'a period of at least two consecutive quarters of negative growth in real domestic product', the cabinet would have been encouraged to stand still until the recession had been officially declared, sometime after April 2009, and hence the stimulus program would not have been announced as early as January 2009.

Thus, roughly speaking, what the Act means is that: budget deficits can occur when a country experiences a recession, a war, or some large catastrophic event; when out of recession, *consolidation* should occur as fast as possible (the country should come back as soon as possible to a balanced budget); in other time periods, the government should run budget surpluses or balanced budgets. This view of fiscal policy is what my colleague Mario Seccareccia (<http://www.tandfonline.com/doi/abs/10.2753/IJP0891-1916410204#.Vd9seE2FOUk>) has called *new fiscalism*: counter-cyclical fiscal policy should only be used when things are really bad, in particular when monetary policy seems to be running out of ammunition, otherwise, governments should achieve balanced budgets or surpluses. *New fiscalism* explains why, one year after the 2009 global expansion in government expenditure designed to fight the Great Recession, international organizations such as the IMF or the G-20 exhorted national governments to *consolidate* their budgets and implement austerity measures.

The Act has two obvious consequences. First, the Act is a wage control policy. With the Federal Balanced Budget Act, consolidation occurs to a large extent by freezing the wages of civil servants or the overall government wage bill! So now in Canada we have two incomes policies, which, more truly, should be said to be *wage* control policies. First, we have the new Federal

Balanced Budget Act, which directly targets the wages of federal employees. Second, we also have the inflation-targeting policies of the Bank of Canada, which, in agreement with the federal Department of Finance, indirectly target the *wage increases of all employees*. Labour unions and employers know that the Bank of Canada can always use the stick by means of what is an incomes policy of fear, because the central bank can always slow down the economy through appropriately large doses of high interest rates and greater unemployment. The effect of both incomes policies is to reduce the wage share in national income, which has a negative effect on domestic demand

(http://www.ilo.org/wcmsp5/groups/public/@dgreports/@dcomm/@publ/documents/generic/document/wcms_234602.pdf).

The second obvious consequence of the Act is that it weakens the federal role in economic stabilization. The Act will weaken the desire of the federal government to pursue strong counter-cyclical measures in case of a recession. The Act will also weaken the desire of the federal government to pursue strong counter-cyclical measures when the Canadian economy has zero or low growth, while not being technically in a recession. And as pointed out earlier, the Act is likely to induce the federal government to shovel its deficit towards the provinces and thus provincial governments will encounter larger swings in their budget balances.

This is bad news, because it has long been a tenet of public finance that the federal government is the institution best placed to pursue counter-cyclical fiscal policies. For instance, Richard A. Musgrave, the best known author of textbooks in public finance, has long pointed out that 'responsibility for stabilization policy has to be at the national (central) level. Lower levels of government cannot successfully carry on stabilization policy on their own'. Musgrave added that 'stabilizing fiscal policy requires periodic budgetary deficits or surpluses with corresponding borrowing and debt repayment. These pose a more serious problem for provincial governments, which have less ready access to the capital markets and no control over supporting monetary policy' [R.A. Musgrave, P.B. Musgrave and R.M. Bird, *Public Finance in Theory and Practice*, First Canadian Edition, McGraw-Hill Ryerson, 1987, pp. 487, 479].

While the Bank of Canada Act (<http://laws-lois.justice.gc.ca/PDF/B-2.pdf>) allows the Bank 'to buy and sell securities issued or guaranteed by Canada or any province', and while the Act allows the Bank to make loans to the federal government or to provincial governments, in practice the Bank only buys securities issued by the federal government. Indeed the Bank currently buys 15 to 20 per cent of any new security issue of the federal government on the primary market. Thus if any level of government should encounter budget deficits, it should be the federal government because it benefits from a purchaser of last resort – the Bank of Canada – which has unlimited capacities to purchase bonds or bills issued by the Canadian government. If investors were to lose confidence in the debt issued by the federal government – something that still needs to happen in the US and in Japan despite their enormous debt – the Bank of Canada, just like the Fed, the Bank of Japan, the Bank of England or the Reserve Bank of Australia, has the power to control the prices of securities issued by the federal government. These countries are thus immunized from the kind of problems that plagued some of the

countries of the Eurozone (the GIIPS), as the European Central Bank declined to perform its duty of purchaser of last resort before 2012.

As implied earlier when discussing the *new fiscalism*, since the early 1990s until 2008, mainstream economists had relegated fiscal stabilization to the dustbin. It was believed that monetary policy was good enough to counter slowdowns or recessions, that fiscal policy was unable to stabilize the economy, and hence that fiscal policy should content itself to balance budgets, run more efficient programs, and possibly reduce tax rates. This view, *sound finance*, modified somewhat by the *new fiscalism* view, is endorsed by the Federal Balanced Budget Act, which argues that 'a sound fiscal position is crucial to economic growth and job creation over the longer term', and thus that the federal government should 'achieve annual balanced budgets and reduce debt, other than when a recession or extraordinary situation occurs'. It is said that such a sound fiscal policy will 'instill confidence in consumers and investors'.

This is the confidence fairy that Paul Krugman has criticized so often in his blogs (http://krugman.blogs.nytimes.com/2011/09/13/the-death-of-the-confidence-fairy/?_r=0). The confidence fairy is the belief that despite a fall in aggregate demand, due to a contractionary fiscal policy that intends to bring back the budget in balance, falling sales will still induce firms to produce or invest more. Pundits like to give the Canadian federal budget of 1995 as a counter-example: but they forget to mention that the federal government did shovel its deficit to the provinces, that the Bank of Canada brought interest rates down after having produced our first home-grown recession in 1990-1992, that the exchange rate fell to almost 60 American cents, and that the Clinton boom in the US pulled up our exports.

Apart from the mainstream, there have always been economists who have held a different vision of what sound finance stands for. Michal Kalecki (*Selected Essays in the Dynamics of the Capitalist Economy*, Cambridge University Press, 1971, p. 139), like Keynes, argued that with capitalism 'the level of employment depends on the so-called state of confidence', but he further contended that this gives 'to the capitalists a powerful indirect control over Government policy: everything which may shake the state of confidence must be carefully avoided because it would cause an economic crisis. The social function of the doctrine of "sound finance" is to make the level of employment dependent on the "state of confidence".' This alternative view is thus that sound finance, like free trade agreements, is just another trick in the hands of powerful vested interests to gain more traction in society.

The alternative to *sound finance* is *functional finance*, as proposed by Abba Lerner in 1943 (http://www.jstor.org/stable/40981939?seq=1#page_scan_tab_contents), which says that a government deficit or surplus, in and of itself, is neither good nor bad. While the proponents of *new fiscalism* came to recognize the ability of fiscal policy to achieve economic stabilization when the monetary authorities reached the zero-interest lower bound in 2008, the proponents of *functional finance* never doubted that counter-cyclical fiscal policy was an appropriate tool. While their mainstream colleagues were all getting in the bandwagon of sound finance in the 1990s, several heterodox economists were fully endorsing functional finance, reiterating that

counter-cyclical fiscal policy is a highly effective tool. This was done at the time, among many others, by James Galbraith (http://www.jstor.org/stable/4538439?seq=1#page_scan_tab_contents), the son of John Kenneth Galbraith, and by William Vickrey (http://www.jstor.org/stable/4538552?seq=1#page_scan_tab_contents), the 1996 Nobel prize recipient. More recently, neo-chartalist authors have been quite active in promoting functional finance and the renewed interest in fiscal policy, both in academia and in the blogosphere (<http://neweconomicperspectives.org/>).

Despite functional finance being out of fashion in the 1990s, Steve Fazzari (http://www.jstor.org/stable/4538438?seq=1#page_scan_tab_contents), a former colleague of the late Hyman Minsky, was also been quite adamant about the effectiveness of fiscal policy arguing as follows: ‘Conventional claims about the impotence of Keynesian fiscal policy are largely unfounded.... Our current state of knowledge provides no reason to reject Keynesian demand management principles as the appropriate response to an economy operating with substantial idle resources. Furthermore... effective Keynesian fiscal policy may raise potential output, as well as addressing problems of underutilized resources’. This is now recognized to be true by a number of mainstream economists, such as Larry Summers (<http://larrysummers.com/wp-content/uploads/2014/06/NABE-speech-Lawrence-H.-Summers1.pdf>), the former Secretary of the US Treasury, or economists at the IMF.

Besides these arguments in favour of a fiscal policy unhindered by sound finance considerations, there are a couple of further arguments against a Federal Balanced Budget Act. First, investors and pension funds are always on the look for super-safe assets. If the federal government keeps running balanced budgets or budget surpluses, the financial system will run out of a sufficient amount of safe assets and will engage in the kind of dicey operations that led to the subprime financial crisis. Second, as much as it may seem bizarre, in a growing economy, balanced public budgets are conducive to more financial instability. This can be shown by looking at flow-of-funds identities, which were used by many of those who predicted the global financial crisis, but which are ignored by advocates of sound finance. If households wish to accumulate net financial assets such as RRSPs or pension funds, (in a closed economy) this can only be done either because the corporate sector is accumulating net financial debt or because the government is running budget deficits. For a given desire of households to accumulate net financial balances, balanced public budgets imply a larger accumulation of corporate liabilities. If corporations are accumulating cash reserves, as they have in most years of the recent past, balanced public budgets imply *less additions to household financial assets or more additions to household financial liabilities* – hence less financial stability.

Thus, to conclude, the federal government is not a province, and is not subject to the same budgetary constraint. If there is a level of government that can afford to pursue substantial counter-cyclical policies and run large deficits, it is the federal government, as it can always benefit from the support of the Bank of Canada and thus runs no risk of default as long as its debt is denominated in Canadian dollars. No law should hinder the federal government from

running budget deficits to achieve the full employment of Canadian citizens. Thus the Federal Balanced Budget Act should be repealed as soon as the Conservative government is voted out of power.