



CONTRIBUTION OF JOHN MAYNARD KEYNES IN ECONOMICS

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ABSTRACT

The Man Who Transformed the Economic World

Keynes was a British economist and one of the most influential of the 20th century. Following the outbreak of World War One, Keynes joined the treasury, and in the wake of the Versailles peace treaty, he published 'The Economic Consequences of the peace' in which he criticized the exorbitant war reparation demand from a defeated Germany and prophetically predicted that it would foster a desire for revenge among Germans. This best-selling book made him world famous. During the inter-war years, Keynes amassed a considerable personal fortune from the financial markets and, as bursar of King's College, greatly improved the college's financial position. He became a prominent arts patron and board member of a number of companies. In 1926, he married Lydia Lopokova, a Russian ballerina. Keynes' best-known work, 'The General Theory of Employment, Interest and Money', was published in 1936, and became benchmark for future economic thought. It also secured his position as Britain's most influential economist, and with the advent of World War Two, he again worked for the treasury. In 1942, he was made a member of House of Lords. During the war years, Keynes played a decisive role in the negotiations that were to shape the post-war international economic order. In 1944, he led the British delegation to the Bretton Woods conference in the United States. At the conference he played a significant part in the planning of the World Bank and International Monetary Fund. He wrote 'The General Theory of Employment, Interest and Money' during the Second World War. He is known as the Father of Macro.

Keywords: Germany, Britain, Money, International.

INTRODUCTION

KEYNESIAN ECONOMICS

Keynesian Economics is an economic theory named after John Maynard Keynes (1883-1946), a British Economist. It was his simple explanation for the cause of the Great Depression for which he is most well-known. Keynes' economic theory was based on a circular flow of money. In Keynes' theory, one person's spending goes towards another's earnings, and when that person spends her earnings she is in effect, supporting another's earnings. The key to Keynes's contribution was realization that liquidity preference- the desire of individuals to hold liquid monetary assets. Keynes' solution to this poor economics state was to prime the pump. By prime the pump, Keynes argued that the government should step in to increase spending, either by increasing the money supply or by actually buying things on the market itself.



Keynesianism, or Keynesian economics, is a macroeconomic theory that focuses on total spending in the economy and its effects on output inflation. It was established by British economist John Maynard Keynes in his book, *The General theory of Employment, interest and Money*, in 1936. Keynesian economists believe that since private sector decisions sometimes lead to inefficient macroeconomic outcomes, or market failure, it requires an active policy response by government. Therefore, Keynesian economics supports a mixed economy guided mainly by the private sector but partly controlled by government. Keynes sought to establish a theory different from “classical economics”, which was based on the theories of such economists as David Ricardo, John Stuart Mill, and Arthur Cecil Pigou. Observing what he called classical economics’ failure during the 1930s, Keynes concluded that the classical theory of markets as self-regulating was wrong. Instead, he argued, recession and high unemployment are mainly the result of insufficient spending in the private sector. Therefore, to achieve full employment and sustained economic growth, the government needs to actively intervene to increase spending, if necessary through deficit financing.

II.CONTRIBUTION TOWARDS THE FIELD OF ECONOMICS

British economist John Maynard Keynes is one of the fathers of modern macroeconomic theory and widely considered to be one of the three most important economists of all time, along with Adam Smith and Karl Marx. His ideas shook up the dominant framework of classical economics and continue to influence both economic and fiscal policy for Western Governments many decades later.

III.THE GREAT DEPRESSION

From the beginning of the Depression in 1929 to the time the economy hit bottom in 1933, real GDP plunged nearly 30%. Real per capita disposable income sank nearly 40%. More than 12 million people were thrown out of work; the unemployment rate soared from 3% in 1929 to 25% in 1933. Some 85,000 businesses failed. Hundreds of thousands of families lost their homes.

In Britain, this had been plunged into a depression of its own; John Maynard Keynes had begun to develop a new framework of macroeconomic analysis, one that suggested that what for Ricardo were “temporary effects” could persist for a long time and at terrible cost. Keynes’ 1936 book, *The General Theory of Employment, Interest and Money*, was to transform the way many economists thought about macroeconomic problems. The experience of the great depression certainly seemed consistent with Keynes’s argument. A reduction in aggregate demand took the economy from above its potential output to below its potential output .period of high rates of unemployment. He advocated interventionist economic policy. Urged government to: o use financial and monetary measures to reduce the adverse effects of business cycles, economic recessions, and depression. Spend on public works like programs to promote employment.

The crux of Keynes’ views was that government interventionist policy was necessary in order to combat excessive boom and bust cycles in a nation’s economy. This marked a significant paradigm shift among economists at the time, many of whom argued for minimal governmental interface. Keynesian ideas began to gain favor during the great Depression when many of his proposals influenced the American and British



governments, particularly Roosevelt's New Deal policies. And while it took some time for Keynes' ideas to take hold, they eventually gained ground and became a dominant school of economic thought for the next 40-plus years.

IV.KEYNESIANS-THEORIES

Keynes argued that relying on markets to get to full employment was not a good idea. He believed that the economy could settle at any equilibrium and that there would not be automatic changes in markets to correct this situation. The main Keynesian theories used to justify this view were:

- The labour market
- The market for loanable funds (money market)
- The Multiplier
- Keynesian inflation Theory
- Theory of Income, Output & Employment

Keynes' seminal work, *General Theory of Employment, Interest, and money*, published in 1936, articulated what would later become known as the foundation for modern macroeconomics. It challenged the established consensus of the time, which was that an economy will naturally restore itself to full employment after a period of downturn. One of the key principles Keynes theorized was that saving and investment are determined independently of each other—saving rates being determined by a society's propensity to consume and investment by an expected rate of return relative to interest rates. He also believed that a nation's income is the aggregate of its consumption and investment. During a downturn, this could potentially create a never-ending spiral as businesses invest less, jobs are lost, consumers spend less, businesses have even less reason to invest, and so on. According to Keynes, that's where the government comes in. He argued it was the government's responsibility to step in and use the many tools at its disposal to stimulate investment and consumption. This meant that during hard times, governments must engage in deficit spending in order to stimulate activity. This would consequently lead to policies such as the reduction of long-term interest rates, public works projects, infrastructure spending, and the like..

Many people note Keynes' influence on Roosevelt's New Deal policies but this is somewhat disputed as to the degree of his actual influence on policies of that time. What is more widely acknowledged as significant is the acceptance of his theories near the end of the Depression and the adoption of Keynesian economics as de facto American policy going forward.

V.BRETTONWOODS , WORLDBANK AND IMF

The contributions of John Maynard Keynes did not end there. As World War II began to wind down, he played a significant role in the Bretton Woods Negotiation in 1944. Along with others, Keynes advocated for the establishment of a world central bank and an international currency regulation body. Keynes was instrumental in the formation process of the bodies, which would later take form as the World Bank and International Monetary fund.



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VI. RESURGENCE

Keynesian economics began to fall out of favor during the 1970s when recession, the oil crisis, and rapid inflation hit the U.S. Prominent economists such as Milton Friedman criticized tenets of Keynesian thought and advocate a move towards Monetarist principles, which were adopted in-kind.

While Keynesian economics never truly fell out of perception among policy makers, it would experience a renaissance of sorts near the onset of the financial crisis in 2008. The passage of stimulus packages and heavy government spending in the U.S., Europe, and China to combat the crisis marked its return to prominence.

VII. WAGE EXPECTATIONS AND LABOR ADJUSTMENT

Another novel idea proposed by Keynes was the idea of expectations from the viewpoints of the labor. Some commentators have shown that this might have been an indirect way in which Keynes claimed that peoples are irrational—something that has not yet been done before especially after the marginal revolution period. Keynes said that even though the decrease in nominal wages and increase in price levels should be treated the same, people resist a decrease in their nominal wages but is “sort” of fine when prices increase. This inconsistency means that wage rate doesn’t adjust accordingly to a shock as claimed by the Neo-Classical.

Critics of Keynes point out that his approach leads to inflation and ultimately to less long-term growth because government cannot know how resources should be distributed for most efficient use. Austrian economist Friedrich Hayek called Keynesian economic policies a “fundamentally collectivist approach” for its advocacy of centralized planning. Keynes’s idea that full employment could be achieved through inflation, which was thought to be proven by the so-called “Phillips curve”, was also discredited after the experience of stagflation during the 1970s—high unemployment accompanied by high inflation.

VIII. KEYNESIANS-BELIEFS

In essence Keynes argued that markets would not automatically lead to full-employment equilibrium, but in fact the economy could settle in equilibrium at any level of unemployment. Keynesian beliefs can be illustrated in terms of the circular flow of income. If there was disequilibrium between leakages and injections, then classical economists believed that prices would adjust to restore the equilibrium. Keynes, however, believed that the level of output (in other words National Income) would adjust



IX.IMPACT ON OUR CURRENT SOCIETY

Overall, Keynesian Economics does not greatly influence our current economic system. However, because of our economic crisis, a number of these theories are being pulled out to help create reform plans; such as, out bailout and stimulus packages. The military also uses Keynesian theory to support continued spending for national defense, claiming that otherwise we would fall into an economic recession

X.CRITICISMS OF KEYNESIAN ECONOMICS

Borrowing causes higher interest rates and crowding out. Keynesian economics advocated increasing a budget deficit in a recession. However, it is argued this causes crowding out. To borrow more, the interest rate on bonds rises. Also it means that the private sector have less to invest on private projects.

INFLATION: A problem of fiscal expansion is that it often comes too late when economy is recovering anyway and therefore, it causes inflation.

DIFFICULTY OF PREDICTING OUTPUT GAP: An assumption of Keynesian economics is that it is possible to know how much demand needs to be increased to deal with output gap.

ENCOURAGES BIG GOVERNMENT: In a recession governments increase spending, but, after recession government spending remains leading to high tax and spend regimes.

TIME LAGS: It takes a long time to change aggregate demand by the time AD increases it may be too late and it leads to inflation.

XI.CONCLUSION

Keynes's influence waned in the 1970s, partly as a result of problems that began to afflict the Anglo-American economies from the start of the decade and partly because of critiques from Milton Friedman and other economists who were pessimistic about the ability of governments to regulate the business cycle with fiscal policy. However, the advent of the global financial crisis of 2007-08 caused resurgence in Keynesian thought. In 1999, Time magazine included Keynes in their list of the 100 most important and influential people of the 20th Century, commenting that: "His radical idea that governments should spend money they don't have saved capitalism." He has been described by The Economist, Keynes was also a civil servant, a director of the Bank of England, a part of the Bloomsbury Group of intellectuals, a patron of the arts and an art collector, a director of the British Eugenics Society, an advisor to several charitable trusts, a successful private investor, a writer, a philosopher, and a farmer.

He died on 21 April 1946 at the age of 62 in United Kingdoms

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