This is the third in a series of articles dealing with the Keynesian influence on Economics. The first two, by Wallace Peterson and John Hotson, appeared in the Spring and Autumn, 1967, issues.

END OF THE ERA OF KEYNES?

(Translation of article by L. Albert Hahn, published in *Kyklos,*

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A famous Norwegian dramatist has said: a theory lasts for thirty years. If this is true, then the year 1966 would be not only the thirtieth year since the birth of Keynes' *General Theory of Employment, Interest and Money*[1] but also the year of its death. It could then be shown that what is generally understood by "Keynesianism" does not involve a change in the evolutionary trend of economic doctrines, especially of monetary theories. Doctrinally, "Keynesianism" would have to be regarded merely as a recent, one-way swing of the pendulum such as the world has often experienced before—this time in the direction of distinct overvaluation of the possibilities and effects of monetary manipulations and alterations.

Such a characterization can only appear as blasphemous to a generation brought up in quasi-religious veneration of Keynes' work. Two autobiographical remarks, however, might make the blasphemy appear in a somewhat more subdued light.

Professor Edgar Salin, to whom this volume of *Kyklos* is dedicated, refers in his *History of Economics*[2] to a "theory of credit inflation co-founded by him" (Hahn). Indeed—owing to my *Economic Theory of Bank Credit*[3]—I am, as it were, an orthodox Keynesian. It is well known, however, that orthodox believers view their religion more objectively than converts, who are inclined to overlook the questionable aspects of the newly discovered religion. In the United States it is precisely those who until the year 1936 reasoned in "classical" terms who, like Professor Alvin Hansen, in turn attached themselves with especial enthusiasm—and uncritically—to the novel theory.

It lies in human nature to assume that a development which one has experienced personally will repeat itself with others. In the first (1920) edition of my *Economic Theory of Bank Credit* I anticipated, as can be easily proved, the essential results of Keynes'

[1] New York, 1936.

[2] Published by A. Francke, Berne, 4th ed., 1951, pp. 169–70.

[3] Published by J. C. B. Mohr (Paul Siebeck), Tuebingen, 1st ed., 1920; 2nd ed., 1924; 3rd ed., 1930.

General Theory. In the third (1930) edition, however, I threw overboard exaggerations that were untenable in my judgment. I groped for a balance between overrating and underrating of monetary interventions. Since then I have combatted views which I regard as the sin of my youth.[4] I am convinced that if Keynes had not died prematurely he would in a later edition of the *General Theory* also have moved away from his earlier views.[5] He would have become an anti-Keynesian—in recent years at the latest.

Incidentally, the publication of the various versions of my *Economic Theory* was badly timed. The first edition, a typical soft money book, should not have been permitted to appear in 1920, during the big German inflation. But in 1930 it could have been useful in the battle against deflationism of the Bruening-Luther vintage. By the same token the third edition, in which inflationary measures were viewed much more skeptically, should not have appeared during a period of deflation but only later—say, in 1936—when the propensity to inflate already stood out clearly. I find comfort, however, in the fact that the timing of the *General Theory* was not propitious either. If it had been published in 1930 it would have helped those who sought to combat the "big deflation." In 1936 the enemy already stood to the left, on the side of inflation, and as a result the *General Theory* had rather a harmful effect. Nevertheless, during the last thirty years it has exerted a no less than overwhelming influence on economists of the growing-up generation. In what follows I will attempt to demonstrate that the pendulum is now about to swing back. The "era of Keynes" seems to approach its end.

The Characteristics of Economic Society

How does Keynes' theory differ from classical theory? Keynes himself gave the answer in his polemic against the classicists: The "characteristics [assumed by the classicists] happen not to be those of the economic society in which we actually live, with the result that its teaching is misleading and disastrous if we attempt to apply it to the facts of experience."[6] It follows that classical characteristics would be present only under exceptional and accidental circumstances, in Keynes' view, whereas his own assumptions would apply to "the general case" and "as a rule."[7]

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[4] A collection of my anti-Keynes articles may be found in *The Economics of Illusion*, Squier Publishing Co., Inc., New York, 1949; a German summary appeared in "Ordo, Jahrbuch fuer die Ordnung von Wirtschaft und Gesellschaft," 2nd volume, 1949, pp. 170 ff.

[5] As is well known, hints of such a veering away may be found in his article, published posthumously, "The Balance of Payments of the United States," *Economic Journal*, June, 1946, p. 186.

[6] *General Theory*, p. 3.

[7] *Ibid.*, p. 3 and p. 13.

Thus the difference between classical and Keynesian economics does not lie at all in a changed or amended logic. As I put it on an earlier occasion:

> The miracles the Keynesian system works can be attributed to the data taken as dependent and independent variables and as fixed, plus certain assumptions concerning the shape of important functions, especially the consumption, money supply, and investment functions. Change these assumptions to what non-Keynesians consider more realistic terms and the classical or neoclassical theory reappears like an old picture when the layers of paint laid on by successive generations are removed.[8]

The most important differences, however, between the Keynesian and the classical assumptions are the following:

First, according to Keynes, the demand for investment goods appears as low, constant, or at least so interest-inelastic that even at an interest-rate level near zero percent the supply of savings cannot be absorbed by it. In the classical system, the demand for investment goods is never constant but always interest-elastic and variable.

Second, Keynes regards wages as inflexible downward—and largely also upward—and treats them as a constant of the system. In the classical system they are variable.

Keynes' World

The preceding remarks imply the further characteristics of the Keynesian world which contrast it so sharply from the classical one. This Keynesian world is deflationary "in the general case." The demand for investment goods is declining because of dwindling investment opportunities. On the other hand, the supply of "capital" is growing because with increasing wealth the savings rate is growing in accordance with a "psychological law."[9] There arises the so-called "investment gap,"[10] leading necessarily to a lack of "effective demand," producing deflation. Even in the general case, however, the Keynesian world is one of underemployment. In a deflationary milieu wages would have to drop. But since, with downward rigidity of wages, their lowering is out of the question, the result is permanent underemployment.

Unemployment in this world is thus, as it were, of the frictional kind. It arises through failure of supply and demand to become equilibrated: on the capital market because demand is so rigidly limited that no new equilibrium can come about; on the labor market because of the rigidity of the offering price of labor.

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[8] *The Economics of Illusion*, p. 185.

[9] Keynes, *op. cit.*, p. 96.

[10] For a detailed refutation of the investment-gap theory I refer to my essay in *Schweizerische Zeitschrift für Volkswirtschaft und Statistik*, 1948, no. 4.

It follows, as already shown in my first critique of the *General Theory*,[11] that Keynes out of the "vice" of wages-rigid-downward made the virtue of an inflation theory of unemployment: since the offering price of labor does not fall, the demand must be inflated.

Friction type theories of unemployment, based on a lag of downward adjustment of wages during the downswing, are not new, of course. They are an essential ingredient of all monetary cycle theories of the Wicksellian type. But these theories are cycle theories, not theories attempting to explain extra-cyclical phenomena. Nevertheless—and despite repeated objections to this usage—Keynes called his theory general, although in reality it is of a very special kind. It is, as I put it on one occasion, a "business cycle theory gone wild."[12]

The Real World

Events took a different course than had been anticipated by Keynes in 1936. The factual assumptions of his *General Theory* proved to be invalid. The world was not deflationary. There arose no structural "investment gap," just as before 1936 there had been none. Seldom before, if ever, has the demand for investment goods been greater than it has been in the last thirty years. On the other hand, there has never in this period been a question of an oversupply of savings. The famous "psychological law," according to which the rich save more than the poor, is applicable—it should be remembered—only to the case of a redistribution of wealth within an economy. When on an average all people become wealthier, the savings rate remains rather constant, as has been shown. In historical reality, there can be found no more of a counterpart for the oversaving theory than for the underinvestment theory, which is not a novel theory either. In the course of economic history it emerges whenever, in the eyes of impatient observers, cyclical depressions seem to be of infinite duration. Thus Professor Adolf Weber, who died a few years ago, branded as a bad joke the assumption of an excessive capital supply.[13] In retrospect, it appears that the Keynesian deflation jitters are weakly founded, indeed. In terms of doctrinal history, there is a certain irony in the fact that around the year 1936 there began a period of seemingly secular inflation. He who rereads the *General Theory* today believes therefore that he is confronted with a purely fictitious world, rather than the real world. Rarely has somebody been so subject to "faulty vision" as was Keynes in 1936.

[11] "The new business cycle theory of Keynes," *Neue Zuercher Zeitung* (trade section), November 19 and 20, 1936.

[12] "Eine wildgewordene Konjunkturtheorie" (original). Cp. "Wirtschaftswissenschaft des gesunden Menschenverstandes," publ. by Fritz Knapp, Frankfurt/M., 1st ed. 1954, 2nd ed. 1955, p. 221 and p. 251.

[13] *Der Wirtschaftsspiegel*, Wiesbaden, October 1, 1947, p. 365.

The fear of chronic unemployment, which permeates the *General Theory*, has also proved to be unfounded—outside the United States. It is true that in the United States until 1964—i.e., during almost the entire period in question—unemployment rarely fell below 5 percent.[14] But certainly it was not a result of deflationary policies: a glance at the evolution of the money supply[15] and the price series[16] shows that the milieu was not deflationary but pronouncedly inflationary. Consequently, existing unemployment was not caused by a lack of "effective demand," as is assumed by the adherents of the "New Economics." There was thus no reason to train cyclical canons on structural sparrows*—and thereby to endanger both the internal and external value of money.

A recognition that the Keynesian world does not exhibit the characteristics of the economy in which we actually live is gradually, but firmly, gaining ground. The huge "stagnation literature" which mushroomed in the United States during and after the war has long been gathering dust. The front line of the enemies of saving—those who fear the deflationary effect of saving—has become quiet. On the other hand, the deflation theory of unemployment has held fast for a relatively long time. In the most widely used textbook in the United States, only in the last few editions was the level of wages mentioned at all as a determinant of the employment level. This is not surprising in view of the fact that a "wage theory of unemployment" is damaging to strong vested interests, political and economic. Only recently—much too late and in the main unsuccessfully—have measures been taken which aim at keeping wage increases in check. Guidelines, income policy, and other expedients attempt now to solve a problem which cannot be mastered without a substantial weakening of the power of labor unions.

A Goal-Oriented and Illusionary Theory

Perhaps an injustice is done to Keynes by examining his theory, *qua* theory, too closely. Indeed, one sometimes gains the impression that it may not have been meant too seriously. It is known that at the end of his life Keynes went so far as to ridicule the Keynesians. To non-Keynesians, his *General Theory* has always appeared to be one which is purely goal-oriented. Keynes wanted to unburden the conscience of those who were anxious to combat unemployment

[14] Cp. *Historical Federal Reserve Chartbook*, p. 78. (Translator's note: This page reference seems to be in error.)

[15] *Ibid.*, p. 11.

[16] *Ibid.*, pp. 98–99.

*Translator's note: The passage in question reads, "Es bestand demnach keine Veranlassung, mit konjunkturellen Kanonen auf strukturelle Spatzen zu schiessen . . ." p. 275.

by methods which until then had been largely tabooed as pure monetary manipulation and as an all too primitive "easy way out" of all difficulties.

In this he succeeded—one may say, only too well. The *General Theory*, or what was eventually read out of it by the Keynesians, for one thing served to rationalize an irresponsibly long continued easy money policy, a policy of lasting budget deficits, and of almost unintermittently rising public debt. For another, it served the policy interests of labor unions, not only by acknowledging as a fact of life the downward inflexibility of wages, but also by legitimizing every wage increase, as capable of increasing effective demand. An increase in wages was said to imply an increase in demand, thus not aggravating but alleviating unemployment.

Things developed as they had to. Not as an exclusive result of Keynes' theory, but helped a great deal by it, the value of money declined in the United States and eventually—via the export of inflation—it also declined in all countries, notably including the German Federal Republic, tied to the dollar by fixed exchange rates. It has turned out to be an illusion to assume that economic maladjustments can be eliminated through inflation without endangering the value of money. Keynes' theory has therefore been dubbed an "economics of illusion."

His economic teachings are illusional, though, in yet another and particular sense: in their therapeutic recommendations they presuppose that the populace continue to be blinded by Irving Fisher's so-called "money illusion," and this even in those cases where inflation is programmed at the outset as a means to augment employment. As a matter of fact, however, there are bound to occur, with little delay, compensating reactions on the part of the disillusioned populace.

Compensating Reactions by Moneyholders and Creditors

First place among the means recommended by Keynes in order to stimulate investment demand—and thus "effective demand"—is occupied by an "easy money policy." The same as any reduction of the rate of interest below the "natural rate" in the Wicksellian sense, it can be brought about only by an inflation of the money supply. For this reason an "easy money policy" causes price rises "in the general case." As was prophesied by the antagonists of such a policy, the purchasing power of the dollar, as expressed in consumer goods prices, has shrunk a great deal. It is customary now to talk about a "45-cent dollar."

The inflationary increase of the supply of funds obviously can add to the willingness to invest only if the noninflationary supply of funds remains the same. Such will be the case, however, only if savers, still blinded by "money illusion," ignore the reverse side

of the "unnaturally" cheap supply of funds, namely, upward pressure on prices. For short spans of time, and for some time after a recession, this condition will be met. But in the longer run, and especially after an easy money policy—and thus inflation—have become official policy, reaction of the savers will in all likelihood become compensating. They will insist on an interest premium to compensate for the loss in the value of money.

The extent to which rising interest rates during the last decade should be attributed to such compensating reactions of savers cannot, of course, be indicated statistically. According to inquiries among them, however, savers are quite conscious of the progressive erosion of the value of money. Their interest-demands discount future losses of the value of money. Thus one talks of net interest as the nominal rate of interest, minus the estimated future loss of the purchasing power of money. There are other phenomena that confirm the collapse of "money illusion" among fund-supplying groups: the advance of institutional sources of supply as contrasted with the supply by individual savers, and the utterly characteristic so-called negative spread between share yields and bond yields. Whereas in earlier times the yield of shares of stock, because of inherent industrial risks, moved notably above the yield of bonds, bond yields now—on account of the money risk—are notably higher than yields on stocks. Moreover, there is a suspicious stirring of inclination to insert loss-of-purchasing-power clauses not only in employment contracts but also in long-term money loan contracts. Thus what the classicists predicted would happen as a result of an artificially low interest rate has actually occurred. Creditors adjust their interest-demands to the dwindling value of money, with the result that the stimulating effect of an easy-money policy is being weakened or offset—unless a cumulatively growing, inflationary money supply continues to keep interest rates at an unnaturally low level.

The policy of easy money obviously rests upon an attempt to exploit the savers' "money illusion." As in the case of any other such deceptive maneuvers, it is self-defeating in the long run.

Compensating Reactions vis-a-vis Deficit Spending

If it should happen that a lowering to near zero of the interest rate does not stimulate the propensity to invest, Keynes, as is well known, recommends government intervention: ". . . the State which is in a position to calculate the marginal efficiency of capital-goods on long views and on the basis of the general social advantage . . . (has to take) an ever greater responsibility for directly organizing investment,"[17] and this, apparently, can be effected only by way of a budget deficit.

[17] Keynes, *op. cit.*, p. 164.

The suggestion that the government should step in whenever private investors—fearing losses—get out, rests on the idea that the government can create the requisite means out of thin air, so to speak, i.e., that nobody has to back up the repayment of loan issues and of interest payments thereon. In reality, each and every government debt is a debt of the individual members of society. Deficit spending can add to total investment spending only so long as each individual believes that somebody else will foot the bill. As soon as this illusion collapses—and this may happen only after a considerable lapse of time—it will be recognized that by dint of increasing taxation, government expenditures will reduce the income of the factors of production. The latter will correspondingly raise the supply prices of their services, which can have only a negative influence on the propensity to invest. How large in practice this influence may be can be seen from certain movements of the stock exchange. When it is anticipated, e.g., that, as a result of growing expenditures for war and a consequently rising level of taxation, net profits of corporations will be reduced, share prices will drop and the launching of new firms will be handicapped. A reaction in the private sector will offset the expansion of the public sector as soon as it becomes a matter of paying the bill.

Compensating Reactions of Labor

The point of departure of Keynes' employment theory is entirely classical. Unemployment arises to the extent that wages exceed the profits expected to result from the use of marginal workers. The conclusions which Keynes draws, however, are anything but classical: wages are not to be lowered but "effective demand" is to be increased by expansion of the money supply. This "effective demand spends itself partly in affecting output and partly in affecting price."[18] Thus additional workers can be suddenly employed usefully in spite of lower productivity. The reason is that "the decreasing return from applying more labor to a given capital equipment has been offset by the acquiescence of labor in a diminishing real wage."[19] And the workers accept the reduction in real wages caused by the rise in prices because "the supply of labor is not a function of real wages,"[20] for "it is not their [the workers'] practice to withdraw their labor whenever there is a rise in the price of wage goods."[21]

It follows that the Keynesian recipe obviously works only when workers succumb to "money illusion," and if in wage bargaining,

[18] *Ibid.*, p. 285, and in slightly changed phrasing, p. 296.
[19] *Ibid.*, p. 289, and in slightly changed phrasing, p. 284.
[20] *Ibid.*, p. 8.
[21] *Ibid.*, p. 9.

as maintained by Keynes,[22] it were a question of nominal rather than real wages. At a time, however, when just about everybody—and certainly every union leader—seems to carry with him a chart showing changes in the purchasing power of money, such an assumption is, of course, entirely unrealistic. Incidentally, it was already unrealistic in 1936.

Of course, Keynes recognizes that workers cannot be fooled for the duration. For "a point comes at which there is no surplus of labor available at the then existing real wage."[23] From this point on "the crude quantity theory of money" will operate again. "Output does not alter and prices rise in exact proportion to [the quantity of money]."[24]

The unpleasant truth is, however, that wages begin to rise not only at the attainment of full employment; they are long before that being autonomously forced up by the labor unions. During the last thirty years, wages in the United States, especially the legally fixed minimum wages, have risen although the unemployed were still counted by the millions. They even kept rising in periods of outright recession. Consistently, wages rose more than did prices, in most cases also if productivity increases are taken into account, so that one could rightfully speak of "cost push inflation" and "wage price spiral." At any rate, there was never any question of a lowering of real wages in the Keynesian sense, nor was there a question, at least before 1961, of a substantial reduction of unemployment.

It may be noted in passing that the stimulating effect on output of an increase in "effective demand" was not at all unknown to the much slandered classicists. But, in this context, they were careful to guard against "generalizations" and exaggerations. Read, for example, what David Hume[25] had to say on this point.

A Deceptive Interlude

Unemployment in the United States began to decline only with the inauguration of President Kennedy, when, influenced by his extremely expansionist advisers, money and credit policies were swept into a current of inflation.[26] A glance at the money supply[27] curves clearly reveals the change. One perceives how the (total) money supply curve, and especially the "currency in circulation"[28]

[22] *Ibid.*, p. 8.
[23] *Ibid.*, p. 289.
[24] *Ibid.*
[25] Cp. "A Select Collection of Scarce and Valuable Tracts and Other Publications on Paper Currency and Banking," edited by J. R. McCulloch, 1862.
[26] *Federal Reserve Chartbook*, 1966, p. 53.
[27] *Ibid.*, p. 10.
[28] *Ibid.*, p. 10.

curve (which between the end of the war and 1960 ran rather flat), after Kennedy's inauguration changed direction and moved up steeply. The same is true for the curve showing demand deposits, or checkbook money, and even more so for that of total deposits, including time deposits,[29] which in the correct view have to be considered as part of the money supply.

The referred-to recent evolution of unemployment, however, has certainly not been the result of the Keynesian therapy of lowering real wages. It is true that prices of consumer goods rose, especially those in the construction sector. The index of the cost of living—much better suited than the wholesale price index for a comparison of total money supply and total output, i.e., for any analysis in terms of the quantity theory—rose by about 10 percent, incidentally only a weak reflection of the "dearness" which every regular visitor to the country will note even in the absence of any knowledge of the statistical series. But wages rose more strongly still—by some 22 percent.[30] Hence real wages rose—they did not fall. To what, then, may the improvement in the employment situation be attributed?

It is obvious that the profitability of employing labor may be enhanced for two reasons: one, because of a lag of money wages behind prices à la Keynes, and second, because of their lag behind increases in the productivity of labor. According to a generally held view, this latter happened during the last five years: while nominal wages rose 22 percent, but real wages only 12 percent, the productivity of labor rose by about 15 percent for the period as a whole. Consequently, one is tempted to modify the Keynesian statement that it is not "the workers practice . . . to withdraw their labor whenever there is a rise in the price of wage goods," by saying that it is not "the workers practice . . . to withdraw their labor whenever there is a rise of productivity."

Times of rapidly rising productivity, when real wages are capable of rising (i.e., money wages increase much more than the value of money decreases), apparently create a favorable atmosphere for a certain "moderation" in wage demands. Although full compensation for the loss in the value of money is being demanded, there is no demand for full participation in the productivity increase.

The Pendulum Swings Back

It is well known that the honeymoon period of "moderation" ended during the year 1966. The so-called "guidelines," coupling wage increases with productivity improvements, were exceeded everywhere, in some cases considerably so. The whole "guidelines" policy has collapsed—not for lack of responsibility of the so-called

[29] *Ibid.*, p. 7.
[30] *Ibid.*, p. 55.

"social partners," but because after the attainment of full employment the labor market situation was altered in favor of employees who believe they have the power to claim for themselves the entire productivity gain, or even more than this. However, wholesale prices finally have started to move upward. By the way, they had remained stable only because, in full harmony with classical foreign trade theory, stability had been "imported" from the world market.[31] At any rate, the stated objective of the government since the beginning of 1966 has no longer been stimulation of demand but its dampening.

What is more, the whole atmosphere has changed. The hitherto prevailing notion of "prosperity-through-spending" appears to have been thoroughly discredited, what with two illusions essential to the applicability of the Keynesian recipes having been conclusively shown up as such: the illusion that an easy money policy adopted for reasons of promoting high employment and economic growth can be maintained without any regard to its repercussions on the value of money; and the illusion that the factors of production do not react to changes in the value of money in a compensating fashion. The Keynesian fear of deflation has vanished. The so-called "classical" worries, maintaining currency stability and preserving the credit of the government, have become prominent again. Budgetary deficits no longer appear as desirable but as harmful "in the general case;" wage increases are no longer viewed one-sidedly as supporting "effective demand," but also as a "propping up" of costs.

Evidently the times are thus past in which all maladjustments, particularly every excessive wage increase, could be made bearable by an all-forgiving inflation tending to make people forget everything. An epoch has begun when the economy has to cope with and master its problems in "real" terms, i.e., without the possibilities of a monetary escape hatch. But this can only mean that the stability-restoring crisis, or at least pause, which inescapably occurs at the end of long periods of inflation, is due. Italy and France have already gone through a period of stabilizing adjustment; the German Federal Republic is in the midst of it. In England, Wilson is using classical means, so far with uncertain success, in an attempt to stabilize prices and wages. In the United States the spirit is at long last beginning to be willing, but the political flesh is weak. The government, however, should become clear on this point: in view of the now widespread inflation-consciousness of the public,

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[31] See also my essay "Nationale und internationale Aspekte der amerikanischen Waehrungspolitik," publ. by J. C. B. Mohr (Paul Siebeck), Tuebingen. 1966, p. 12.

the only alternative to stabilization is a galloping inflation—not, as previously, a merely creeping inflation.[32]

One may, of course, dispose of the depicted change in the atmosphere surrounding monetary theory and policy with the assertion that it represents essentially a cyclical phenomenon only, i.e., the reaction to an overly long-endured boom. There are many indications, though, that more is in question: specifically, the earlier mentioned swinging back of the pendulum from a pronounced overrating of the possibilities and effects of monetary manipulations to a more normal estimation of their potential—hopefully, not again to their underrating.

The End of a Theory

Keynes' theory is goal-oriented. It was its purpose to make inflation intellectually respectable as a means of combatting what appeared to be deflation unemployment. The attainment of this objective, however, has become both unnecessary and impossible: unnecessary because, unless all appearances are false, apart from cyclical recessions, the battle of the foreseeable future will be one against inflation, not one against deflation; and impossible because, after the definitive collapse of "money illusion," it will be possible to fight unemployment through monetary expansion only quite temporarily and never without the gravest consequences for the value of money. *But with the passing of the goal of a goal-oriented theory, the theory itself will have to die, too.*

If, then, the year 1966 has become the year of death for the thirty-year-old *General Theory,* it must necessarily also have become the year of birth, or rebirth, of a classical view of things. Imperceptibly but surely, the quantity theorists will be reinstated in their rightful place for "the general case" and "on the longer run," as will be, for the "cyclical case," the traditional monetary cycle theories; thus, on the one hand, Ricardo, John Stuart Mill, and above all David Hume, and, on the other, Wicksell and his students. They will be studied increasingly more often, but the Keynesian literature, swollen to proportions beyond grasp, will be studied less often. At least, such should be the case.

This is not to imply that economists will not continue to use Keynesian categories in talking and writing, nor that they will abandon his much-praised "conceptual apparatus." The external forms of a particular religion have always survived the faith going with it. Faith in the Keynesian world is shaken, though. Therefore, the scientific mode of expression will slowly change, too. The pride in using finely elaborated functions, mathematical equations, and

[32] A detailed evaluation of the cyclical situation in the U.S. may be found in the before-mentioned essay.

graphs to say something which can also be expressed simply and verbally will decline with the insight that such pride only leads to unrealistic premises.[33]

OBITUARY

In a year of death an obituary may well be appropriate. I will not repeat here what since the publication of the *General Theory* has been written pro and con this theory—the con also including my own writings. But since at the end of a life, including the life of a theory, one sees many things more clearly than during his lifetime, I may perhaps be permitted the following summary note.

There is no doubt that Keynes has influenced the thinking of the young—from my vantage point—generation as much as the classicists influenced mine. But was Keynes' influence a blessing? I doubt it.

As far as the alleged progress in economic thinking is concerned, I would like to endorse the judgment of Hayek who at the end of a remarkable article, "Personal Recollections of Keynes and the 'Keynesian Revolution'," [34] remarks as follows: "I venture to predict that once this problem of method is settled, the 'Keynesian Revolution' will appear as an episode during which erroneous conceptions of the appropriate scientific method led to the temporary obliteration of many important insights which we had already achieved and which we shall then painfully have to regain." As an example of an "insight which we shall painfully have to regain" I would like to refer merely to the alleged multiplying effect of government spending which plays such a prominent role with Keynes and his disciples. According to the multiplier theory, government spending will increase spending and employment in the private sector by a multiple. Under quite special monetary and real elasticity conditions this may have elements of truth.[35] "In the general case," however, more government spending means less private investment spending. The public sector displaces the private sector, as a generation blinded by multiplier theory now—much too late—cannot fail to recognize, to its sorrow. For these and many other reasons I cannot help but repeat that what is being celebrated as the "Keynesian Revolution" appears to me to be the "Keynesian Confusion"—and this not least because of the disastrous medley of business cycle theory and general theory.[36]

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[33] This danger was already recognized by Keynes; cp. his *General Theory*, pp. 297–98.

[34] Cp. *The Oriental Economist*, January, 1966.

[35] By the way, the multiplier is at best an "additioner." Cp. *Wirtschaftswissenschaft des gesunden Menschenverstandes*, pp. 134 ff. and 160 ff.

[36] *The Economics of Illusion*, p. 6.

With respect to the applicability of Keynesian theory to the solution of the practical problems of our time, the late Professor Slichter as early as 1947 remarked that "modern employment theory sheds little light on the practical problems of today."[37] It not only has done no good, but has led to what I should like to call the "Keynesian Demoralization," because the atmosphere created by Keynes is at least partly responsible for it.

Under the influence of Keynesian theory, the politicians are demoralized because they have become used to satisfying, from the apparently inexhaustible inflationary supply of funds, every want in a welfare state.

Demoralized are the labor unions of the entire world to whom, in an inflationary milieu, could be granted every wage demand. It will be very difficult, indeed, to make them see again the self-evident truth that the income of the masses cannot exceed the amount that the masses produce. As a matter of fact, this income must be somewhat less, for the factor capital, too, needs to be remunerated for its productivity-increasing services.

Also demoralized became a whole generation of entrepreneurs in industry and banking for whom doing business was made too easy by an "easy money policy." This generation so far has never experienced a crisis or a prolonged recession. It might suddenly be confronted with "real" manager problems.

Finally, I also view as demoralized all national and international organizations which are involved in the latest "modern craze," programming, forecasting, and forcing growth at any price—the growth fanatics. From between their trees of intricate calculations and formulas they are unable to see any longer the forest of sane common sense, which suggests that growth is a function of labor and of saving rather than of targets and of pious wishes.

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[37] Sumner H. Slichter, *Review of Economics and Statistics*, 1947, p. 140.

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