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When the 2008 financial crisis struck, both US policy makers and central bankers were quick to resume distinctively Keynesian policies to stop the recession and help the unemployed.

Maybe President Obama's (2009) stimulus plan was not big enough, but it was certainly far bigger than anything of the sort attempted in the Euro Area. Since 2010 the US economy always performed better than that of the Eurozone.

As the public debt crisis (2010-2012) started magnifying the effects of the previous private debt crisis, European politicians, dominated by the modern "German Ideology", chose to tangle up their countries (and the whole Area) with ever more complicated "medium term objectives", "preventive and corrective arms", "fiscal compacts" and the like, whilst the European Central Bank was prevented by its own self-inflicted rules from acting as a lender of last resort.

Only Mr Draghi's (July 2012) announcement to do "whatever it takes to save the Euro", prevented a Euro-collapse. Now - on the verge of the third recession in less than 7 years, and with the sword of Damocles of the German Constitutional Court pending on the ECB's capability of doing "whatever it takes" - Europe needs Keynes more than ever before.

Keynes was already famous among economists and policy-makers in 1930, when he published his monumental *Treatise on Money*. His critique of the economic policy implemented by the Treasury in the face of the 1930 slump made him well known beyond economic and political circles.

Many economists of the time saw the slump and the following decade-long Great Depression as "not simple evils, but something which has to be done" (to quote Joseph Schumpeter, 1934); that is something inevitable or even necessary to clean up capitalist economies, in which much garbage (inefficiencies, distortions, etc.) accumulates in times of normal growth.

The 'destructions' of the crisis are always 'creative' – part of the economy's adjustment to change – and therefore cannot and should not be avoided or lessened through economic policy, even if were it effective, which in the eyes of those economists it was not and it is not in the eyes of many European economists today.

Keynes thought along different lines. As early as in 1930 he wrote:

"This is a nightmare, which will pass away with the

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LEONHARD DOBUSCH
THE TRANSATLANTIC FREE TRADE NEGOTIATION: THE ZOMBIE AGREEMENT

The dispute over the planned TTIP transatlantic free trade agreement between the European Union and the United States goes far beyond the treaty itself, the reason being the tradition in which TTIP is grounded.

EMMA BONINO
EUROPE SHOULD NOT FORGET THE MEDITERRANEAN

Conflicts and tensions in Libya, Syria, Egypt, Iraq and Palestine worry us for many reasons. Security, oil supply, migration are just some among the rising concerns. The role of the European Union in the Mediterranean is too weak and gives little assurances on the future of these challenges.

MARK THATCHER
VIVIEN SCHMIDT
WHY ARE NEOLIBERAL IDEAS SO RESILIENT?

How do we explain the resilience of neoliberal economic ideas? We propose five lines of analysis to explain such resilience: the flexibility of neoliberalism's core principles; the gaps between neoliberal rhetoric and reality; the strength of neoliberal discourse in debates; the power of interests in the strategic use of ideas; and the force of institutions in the embedding of neoliberal ideas.

morning. For the resources of Nature and men's devices are just as fertile and productive as they were. The rate of our progress towards solving the material problems of life is not less rapid … But today we have involved ourselves in a colossal muddle, having blundered in the control of a delicate machine, the working of which we do not understand. The result is that our possibilities of wealth may run waste for a time – perhaps for a long time." ("The great slump of 1930", in *Essays in Persuasion*).

According to Keynes, economic crises were not the inevitable and incurable outcome of capitalism malfunctioning, nor happy episodes of creative destruction. At first Keynes thought that the crisis was a 'magneto trouble'. And magneto troubles can be rather easily fixed: charge or change the magneto!

Between 1930 and 1935 Maynard (slightly) changed his mind. He became convinced that the long lasting depression was not just a magneto problem and he started to think about finance-dominated capitalism as an eminently fragile machine, which is not doomed as Marxists would maintain, but which certainly needs continuous and expert handling.

In 1932 Keynes started revising his theoretical approach up to what was called the 'Keynesian revolution'. However Maynard's fundamental philosophy hadn't changed. He described his analysis in *The General Theory of Employment Interest and Money* (1936) as "moderately conservative in its implications". Once again, he wanted to fix capitalism, not replace it with a permanently government-run economy.

He was advocating simple, satisfying solutions (if more sensible ones were not implementable), as it is apparent from this famous quote from the *General Theory*:

"If the Treasury were to fill old bottles with bank-notes, bury them at suitable depth in disused coal-mines, which are then filled up to the surface with town rubbish, and leave it to private enterprise on well-tried principles of laissez faire to dig the notes up again (the right to do so being obtained, of course, by tendering for leases of the note-bearing territory), there need be no more unemployment and, with the help of the repercussions, the real income of the community, and its capital wealth also, would probably become a good deal greater than actually is. It would, indeed, be more sensible to build houses and the like; but if there are political and practical difficulties in the way of this, the above would be better than nothing." (*The General Theory*, ch. XXIV)

In the Post-War era, Western economies (except for Germany, where Keynesian ideas were never accepted either in academic or in political circles) were run along roughly Keynesian guidelines all through the 1950s and 1960s, i.e. those decades that have become known as the 'golden age of capitalism': unprecedented high growth rates; unprecedented low unemployment rates; unprecedented (and unequalled) equality in income and wealth distribution; unprecedentedly muted business fluctuations; steady and low inflation.

International trade flourished; fixed exchange rates were easily maintained within the Bretton Woods agreements (negotiated by Keynes himself, by the way). The dark side of capitalism was tamed, that is banks and finance were tightly and effectively regulated so as to provide sufficient credit to the economies and to avoid booms and busts.

In my view two things went wrong in those golden days and help to explain the subsequent crisis of Keynesian economics (and policies) and the return of the free market ideology which dominated from the early 1970s to the outbreak of the financial and economic crisis of 2007-2013.

1) Keynesian policies were often embodied in welfare state provisions and entitlements, which are permanent in nature, i.e. very difficult to fine tune according to anti-cyclical needs, as Keynesian policies always should be. That is, it became difficult to stop pressing the aggregate demand (public budget) throttle and start pressing the brakes when needed. In turns, this created an inflationary bias, which was just ready to deliver high inflation were some kind of inflationary shock to hit the world economy.

2) The inflationary shock finally came in the form of repeated shocks in the price of oil (1973-74 and 1979-80).

Keynesian economists and policy-makers were not able to deal properly with these inflationary shocks and with the rigidities caused by the debt-financed welfare state, whilst the counter-revolutionary monetarists, led by Milton Friedman (Nobel Prize for 1976) and later by Robert Lucas (Nobel Prize for 1995), had an easy and appealing recipe: government retreat, deregulation of all markets (including the financial market), possible dismantling of the welfare state and letting the invisible hand do its work. Fertile political ground was found in President Reagan's US and in Mrs Thatcher's Britain and of course (at the macroeconomic level) in Germany, even though Mr Schmidt was a Social-Democrat and Mr Kohl a Christian-Democrat, both somehow concerned with the welfare state.

As early as 1980, in a paper entitled *The death of Keynesian economics*, Robert Lucas (the counter-revolution leader) went so far as to claim that:

"People even take offence if referred to as Keynesians. At research seminars people don't take Keynesian theorising seriously any more; the audience starts to whisper and giggle to one another."

Eventually, the anti-Keynesian counter-revolution went far beyond Friedman's relatively moderate theoretical and political positions.

In particular the pessimistic Keynesian view of financial markets as a *casino* was replaced by the so-called efficient market hypothesis, according to which financial markets always get asset prices right, given the available information.

According to such a theory, bubbles are out of the question (if asset prices are always right, there cannot be anything wrong in continuously high and rising prices) and there is no need to regulate markets or to fine tune monetary policy in order to prevent the bubbles that cannot be there in the first place! This was the economics (and finance) of Doctor Pangloss. As Paul Krugman (Nobel Prize for 2008) aptly summarises:

"In other words, finance economists believed that we should put the capital development of the nation in the hands of what Keynes had called a *casino*".

And such a casino was allowed to grow to a hundred times its original size, making a very few people incredibly rich. Free market ideology supported the idea of the trickle-down society. Coincidentally, the distribution of income and wealth in 2008, was back to what it was in 1929. Nothing relevant according to

Robert Lucas, who in 2004 declared that:

"Of the tendencies that are harmful to sound economics, the most seductive, and in my opinion the most poisonous, is to focus on questions of income distribution."

Unfortunately, the then prevailing idealised view of financial markets and of the economy didn't allow the forecast of the upcoming financial disaster of 2007-2008, nor did it allow the casting of the instruments to prevent the subsequent collapse of 'real' markets or to cure it.

In 2003 Robert Lucas had triumphantly (however myopically) declared that "the central problem of depression-prevention has been solved".

In 2009 his Chicago followers were still thinking that the Obama administration's stimulus plans were based on discredited (Keynesian) 'fairy tales'.

To be fair, New Keynesian economists (including, I have to sadly admit, myself) – who had tried to re-cast Keynesian views in contemporary academically respectable models – were not much better than their Panglossian colleagues at forecasting the crisis.

However the New Keynesians had kept sufficient memories of Keynes to rapidly understand that the 'black swan' was once again inshore and that it was urgent to revert to Paleo-Keynesian fiscal policies, given that monetary policy had hit the so called zero-lower-bound where it becomes ineffective at stimulating the economy. (Once again, this is something that Maynard Keynes had explained very well in his General *Theory*, under the name of 'liquidity trap'.)

As the crisis became wider and deeper, many other Keynesian views were vindicated. One for all: fiscal policy, during recessions, has exactly the effects predicted by Keynes, with the traditional multiplier and all that ... That is, austerity, or fiscal consolidation, implemented in the middle of a depression has contractionary effects. This is something to be expected – the layman may say.

However, a number of (alas Italian) economists, educated in the US in the 1990s and early 2000s made the world believe that fiscal consolidation may be expansionary (i.e. may have 'non-Keynesian' effects). They were very effective in convincing European politicians (especially of the German breed). However the non-Keynesian effects were far more convincingly proved to be non-existent, whilst the Keynesian ones are stronger than predicted by means of standard New-Keynesian models.

Krugman says that "we are seeing, within the Keynesian camp, a distinct if polite rise of neopaleo-Keynesianism". In other words, Maynard is back. Unfortunately, Maynard was even too right in writing (*The General Theory*, ch. XXIV) that practical men are "usually the slaves of some defunct economist. Madmen in authority, who hear voices in the air, are distilling their frenzy from some academic scribbler of a few years back."

Most practical men, especially in the Eurozone, are still distilling their frenzy from Panglossian scribblers of the 1970s and 1980s, as if the war to be fought were the same as that of thirty or forty years ago (high inflation caused by supply side shocks).

Instead the war is similar to that of eighty years ago (high unemployment caused by negative aggregate demand shocks due to a financial meltdown), the very same war that Maynard taught us how to fight.

Forty years of oblivion of the demand side of the economy messed up what acting on the supply side can achieve (higher, more efficient, sustainable growth) and what only the demand side can do (pulling the economy out of a recession).

Very serious people apparently have problems with understanding that the global recession (and the second dip experienced by most Euro Area countries) was not due to the supply side: nature or technology or labour having become less productive, the labour market having become more rigid, firms exercising more monopoly power, etc. It was due to a dramatic drop in aggregate demand caused by the burst of a world-wide financial bubble based on leverage (i.e. excessive private debt).

The need for private deleveraging and the credit crunch have caused a demand contraction, to which an early (and unsuccessful) attempt at public deleveraging has been added, causing the second dip. Many Panglossian economic and political ideologues are apparently unable to grasp what infants would get with little effort: "It's the demand, baby."

Simultaneous austerity policies in all ailing Euro Area countries, complemented with the recommendation of supply side 'reforms', has been the wrong medicine, already dispensed in 2011 by wrong-headed European politicians, obsessed by high public debt and little concerned with high unemployment.

Millions suffered and still suffer for that. It was not fate: it could have been avoided, by acting quickly and cooperatively the way Keynes suggested eighty years ago.

Further readings:

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