Contents

Definitions of Variables 1

Part One. Fundamentals

Chapter I. Some Methodological Considerations 5

§1 Economic Theories 5
§2 Economic Models 6
§3 Methods 7
§4 Equilibrium and Disequilibrium. Stability 7
§5 Statics, Comparative Statics, and Dynamics 9
§6 Ex Post versus Ex Ante Analysis 10
§7 Partial versus Total Analysis. The Ceteris Paribus Clause 10
§8 Microeconomics versus Macroeconomics 11

Chapter II. A Historical Survey 13

§9 The Predecessors 13
§10 The Classical Economists 14
§11 The Neoclassical Economists 15
§12 From KEYNES to the Present 17
Further Reading 18

Chapter III. National Income Accounting 19

§13 The Economy as a Circular Flow 19
§14 The Circular Flow-Model of FRANÇOIS QUESNAY 20
§15 The System of Income Accounts 21
§16 Notions of Income in the System of Income Accounts 24

Part Two. Macroeconomics

§17 Introduction to Part Two 31

Chapter IV. The Classical Theory 33

§18 The Classical Vision. Plan of the Chapter 33
§19 Production Functions 35

§20 The Firms . . . 38
§21 The Households . . . 45
§22 The Labor Market . . . 48
§23 The Capital Market . . . 50
§24 The Commodity Market . . . 51
§25 The Quantity Theory of Money . . . 53
§26 Say's Law . . . 58
§27 The Classical Model . . . 59
§28 Digression: Walras' Model . . . 62
§29 Conclusion . . . 66
Further Reading . . . 67

Chapter V. The Keynesian Theory . . . 69

§30 The Crisis . . . 69
§31 The "General Theory" and Its Interpreters . . . 70
§32 The Effective Demand . . . 72
§33 Consumption Demand . . . 73
§34 Investment Demand . . . 78
§35 The Income-Expenditure Model . . . 80
§36 The Simple Multiplier . . . 83
§37 The Markets for Money and Bonds. The LM Curve . . . 85
§38 The Capital Market. The IS Curve . . . 92
§39 The IS/LM Model . . . 94
§40 The Complete Keynesian Model . . . 97
§41 First Scenario: The Investment Trap . . . 101
§42 Second Scenario: The Liquidity Trap . . . 105
§43 An Under-employment Equilibrium with a Flexible Real Wage? . . . 108
§44 Third Scenario: Sticky Wages . . . 109
§45 Conclusion . . . 112
Further Reading . . . 113

Chapter VI. Political Implications: A Comparison . . . 115

§46 The Role of Government. Goals and Means of Economic Policy . . . 115
§47 Fiscal Policy . . . 117
§48 Fiscal Policy in the Classical Case . . . 118
§49 Fiscal Policy in the Complete Keynesian Case . . . 121
§50 Fiscal Policy with an Investment or Liquidity Trap . . . 126
§51 Fiscal Policy with Sticky Wages . . . 129
§52 The Concept of Counter-cyclical Fiscal Policy . . . 130
§53 Monetary Policy . . . 133
§54 Monetary Policy in the Classical Case . . . 134
§55 Monetary Policy in the Complete Keynesian Case . . . 134
§56 Monetary Policy with an Investment or Liquidity Trap . . . 135
§57 Monetary Policy with Sticky Wages . . . 137
§58 Conclusion . . . 138
Further Reading . . . 138

Part Three. New Macroeconomics

§ 59 Introduction to Part Three 141

Chapter VII. The Real-Balance Effect 143

§ 60 A Criticism of Classical Monetary Theory 143
§ 61 A Criticism of Keynesian Monetary Thoery 148
§ 62 Conclusion 151
Further Reading 152

Chapter VIII. The Theory of Portfolio Selection 153

§ 63 Microeconomic Foundations 153
§ 64 Macroeconomic Applications 161
§ 65 Conclusion 168
Further Reading 170

Chapter IX. Monetarism 171

§ 66 The Theoretical Foundations, or: Monetarism versus Keynesianism . 172
§ 67 The Empirical Investigations, or: Monetarism versus Fiscalism . . . 180
§ 68 The Political Inferences, or: Monetarism versus Activism 183
§ 69 Conclusion 184
Further Reading 185

Chapter X. New Classical Economics 187

§ 70 Expectations and Rational Expectations 188
§ 71 The Phillips-Curve. Stagflation 191
§ 72 The New Classical Vision 196
§ 73 The New Classical Model 197
§ 74 Political Inferences 200
§ 75 Conclusion 205
Further Reading 208

Chapter XI. Neokeynesian Theory 209

§ 76 The Evolution of Neokeynesian Economics 209
§ 77 The Dual Decision Hypothesis 212
§ 78 The Logic of the Fix Price-Method 218
§ 79 A Reconsideration of the Consumption Function 225
§ 80 The Neokeynesian Model 229
§ 81 Political Inferences 240
§ 82 Walras' Law with Quantity Constraints 245
§ 83 Conclusion 247
Further Reading 249

Mathematical Appendix

Introduction 253

1. Calculus of Functions of a Single Variable 255
1.1 Functions of a Single Variable 255
1.2 Derivatives 255
1.3 Taylor's Theorem 258
1.4 Differentials 260
1.5 Concavity and Convexity 161
1.6 Maxima and Minima 263
* 1.7 Profit Maximization 265

2. Linear Algebra 267
2.1 Vectors 267
2.2 Matrices and Determinants 268
2.3 Simultaneous Linear Equations 271
2.4 Characteristic Value Problems 273
2.5 Quadratic Forms 274

3. Calculus of Functions of Several Variables 277
3.1 Functions of Several Variables 277
3.2 Partial Derivatives. Gradients 277
3.3 Chain Rule 279
3.4 Taylor's Theorem 281
3.5 Partial and Total Differentials 282
3.6 Concavity and Convexity 283
3.7 Maxima and Minima 284
3.8 Maxima and Minima under Constraints 286
* 3.9 Profit Maximization 288

4. Implicit Functions 291
4.1 Explicit and Implicit Functions 291
4.2 Implicit Differentiation with Two Variables 292
4.3 Implicit Function Theorem 293
* 4.4 The Slope of Equilibrium Loci 294
* 4.5 Properties of Demand Functions 298
* 4.6 Fiscal Policy in the Keynesian Model 300

5. Ordinary Differential Equations 303
5.1 Function Equations and Functional Equations 303
5.2 Solution of a Linear Differential Equation 304
* 5.3 Stability of a Market 305
5.4 Solution of Simultaneous Differential Equations 307

* 5.5 Stability of the IS/LM Model 312
* 5.6 Stability of the Neokeynesian Model 313
Further Reading 315

Bibliography 317

Author Index 323

Subject Index 325