

<http://economics.isdedu.de>

Syllabus Reference 2.6 (Part 1): Keynesian view of the 6 Supply side policies

- Cross reference: see webnote 305

1. Cutting tax rates does not work

Keynesians dismiss many of the above arguments as being far too simplistic. They argue that the disincentive effect of taxation is not borne out by any empirical evidence. The large cuts in marginal rates of income tax carried out in the UK in the 1980s, for instance, had no effect on incentives to work. The existence of generous state unemployment benefits does increase unemployment but Keynesians argue not to any great extent.

- ❖ See Laffer curve – webnote 331

2. Reduce Welfare ?

Keynesian argument is that genuine recipients will suffer. In the 1950s and 1960's U.K. unemployment rates were between 100,000 and 250,000 despite the existence of unemployment benefits- so it is most unlikely that the millions of people unemployed in the 1980s all preferred to be receiving unemployment benefit rather than working.

- ❖ Unemployment fraud
- ❖ genuine unemployed
- ❖ Need for retraining

3. Encourage Entrepreneurship ?

Keynesian view is that entrepreneurs are important in terms of economic growth small firms' account only for a small fraction of national output, employment and national investment.

- ❖ Use of subsidies to encourage more "start-ups"
- ❖ Training schemes
- ❖ Use welfare funds to subsidize jobs

4. Reducing workers rights

- Keynesian response is that reducing workers rights will lead not to extra employment but to greater profits and earnings for the owners of capital.
- Shareholders gain from the losses of workers. This is often a political question:
- **Jobs or profits?**
- **Role for 'collective bargaining'?**

5+6 Public sector is inefficient

As for public sector inefficiency it is of course easy to find examples of civil servants or of bureaucratic nonsense -such as the Millenium Dome in London. On the other hand, the private sector-with its expense accounts, company cars with every available gadget, and Christmas gifts of crates of whiskey can hardly be said to be always striving for efficiency. Neither the public sector nor the private sector is inherently inefficient. The level of efficiency depends to a great extent upon the quality of management of the organisation and in the public sector that ultimately means the Government itself

Conclusions:

1. Many Keynesians favour the use of the public sector to stimulate long term growth. Unlike monetarists, they view the private sector as often incapable of taking the correct policy decision for the well-being of the nation as a whole. In particular, they argue that the private sector may not undertake sufficient investment, that the investment that is taking place is not in the right industries, and that it is not in the right geographical regions. Pro Government role / markets inherently weak and do not reach equilibrium easily.
2. Keynesians favour direct government action to remedy these defects. Either firms can be given tax incentives or the state can give more grants. A more radical solution to the problem is for the state to invest on its own behalf, building up state-owned firms i.e. a policy of nationalization of industry although this approach is no longer common in DC's as most have established policies of privatization of state owned enterprises.
3. Monetarists argue that the state is incapable of managing investment wisely. Only the private sector can direct investment resources efficiently. If governments insist on pumping state aid into dying industries or industries in regions that are in decline economically, then yet more scarce resources are going to go down the public sector drain. Pro Market approach to management of the economy. Market allocation works well and less government interference in terms of resource allocation is advised.

You decide!

- Task 1: You decide whether the Keynesian or the Classical /Monetarist side wins the argument.
- Task 2: Summarize is the Keynesian response. Evaluate the Keynesian response.