

Table of Contents

Chapter 1. A Historical Introduction	1
1.1. The Keynesian revolution and the evolution of government's role	1
1.2. Keynesian orthodoxy	4
1.3. The political consequences of depression proofing	6
1.4. The economic consequences of depression proofing	9
1.5. Schools of thought	11
1.6. Ideology and politics	12
1.7. The market failure rationale for government intervention	14
1.8. Public choice	15
1.9. Conclusion	16
Chapter 2. Microeconomic Foundations	19
2.1. Introduction	19
2.2. Consumers	19
2.2.1. Special case: Lifecycle consumption	23
2.2.2. Special case: Keynesian consumption	24
2.3. Producers	25
2.4. General equilibrium	26
2.5. Pareto efficiency	28
2.6. Social welfare functions	31
2.7. Unemployment and inflation	36
2.8. The government budget and economic policy	37
2.9. Conclusion	39
Chapter 3. Social Choice	41
3.1. Introduction	41
3.2. The theoretical superiority of majority rule	43
3.3. The impossibility of asking for more	44
3.4. Median voter model	47

3.5. Two dimensional social choice	49
3.6. Probabilistic voting	52
3.7. Political information and party ideology	57
3.8. Conclusion	59
Chapter 4. Short-Run Macro Models	61
4.1. Introduction	61
4.2. Classical macro from micro foundations	61
4.3. Rationed equilibrium and rigid prices	66
4.4. Non-Walrasian equilibria	69
4.4.1. Type A: Excess supply of labor and goods	69
4.4.2. Type B: Excess supply of labor	72
4.4.3. Type C: Excess demand for labor	74
4.5. A Cobb-Douglas example	75
4.6. Conclusion	79
Chapter 5. The Phillips Curve and Expectations	81
5.1. Introduction	81
5.2. The natural rate hypothesis	82
5.3. Unemployment and output gaps	87
5.4. Expectations about inflation in the future	90
5.5. Econometric uncertainty	94
5.6. One model of supply: Producer uncertainty	97
5.7. Another model: Predetermined wages	99
5.8. New classical macroeconomics	100
5.9. Conclusion	102
Chapter 6. Fiscal and Monetary Policy	105
6.1. Introduction	105
6.2. Accounting peculiarities in the US budget	106
6.3. Built-in stabilizers	109
6.4. Balanced and unbalanced budgets	111
6.5. Doubts about fiscal policy effectiveness	113

6.6. The Federal Reserve and the President	114
6.7. Describing the money stock	116
6.8. Causality tests	119
6.9. Spurious regressions	122
6.10. Conclusion	124
Chapter 7. Keynesian Business Cycles	125
7.1. Introduction	125
7.2. Cycles in a Keynesian model	126
7.3. A linear econometric model	132
7.4. Linear versus nonlinear models	135
7.5. Regression results	137
7.6. Econometric cautions	142
7.7. Dynamic behavior	144
7.8. Conclusion	147
Chapter 8. Citizen Preferences	149
8.1. Introduction	149
8.2. Presidential popularity	151
8.3. Modeling popularity	153
8.4. Results	157
8.5. Conclusion	159
Chapter 9. Endogenous Stabilization and Macroeconomic Ideology	161
9.1. Introduction	161
9.2. Endogenous stabilization policy	162
9.3. Ideology	166
9.4. Perceptions and expected utility	168
9.5. Plausible parameter values	171
9.6. The zero-inflation rule and inflation volatility	172
9.7. Voters should prefer conservatives, under certain conditions	174
9.8. Uncertainty about candidate platforms	180

9.9. Conclusion	181
Appendix	182
Chapter 10. Political Business Cycles	185
10.1. Introduction	185
10.2. Election opportunism	185
10.3. Partisan macroeconomics	187
10.4. Backward looking expectations	189
10.5. Forward looking expectations	193
10.6. Observations	196
10.7. Regression tests	199
10.8. Growth rate targets	202
10.9. Conclusion	204
Appendix	205
Chapter 11. Government Debt, Deficit and Social Security	209
11.1. Public debt in the short and long-run	209
11.2. Overlapping generations and efficiency	211
11.3. Public debt	212
11.3.1. An analytic example	213
11.4. Pay-as-you-go social security	214
11.5. Overlapping generations and equity	216
11.6. Market imperfections in the credit market	219
11.7. The Ricardian equivalence theorem	221
11.8. Illusions, inertia and irrationalities	225
11.9. Economic growth and the bequest constraint	227
11.10. Social security	228
11.11. Conclusion	230
Appendix: More overlapping scenarios	231
Chapter 12. Conclusion	235
12.1. The Keynesian revolution	235

12.2. Foundations	235
12.3. Weak evidence of policy effectiveness	236
12.4. Rational expectations and the Phillips curve	237
12.5. An inherently unstable equilibrium	237
12.6. Stabilization and conservatism	238
12.7. Doubts about rational expectations	238
12.8. Long-run Keynesian outcomes	239
References	241
Subject Index	249