MACROECONOMIA DO DESENVOLVIMENTO. UMA PERSPECTIVA KEYNESIANA
JOSÉ LUÍS DA COSTA OREIRO

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DEVELOPMENT MACROECONOMICS: A KEYNESIAN PERSPECTIVE

INTRODUCTION

In Brazil, Professor José Luís Oreiro is considered one of the most talented and productive Keynesian economists of his generation. Prof. Oreiro was hired by the Department of Economics at the Federal University of Paraná in 2003, when I came into touch with some of the theories organized in this book.

This book written by Oreiro presents the debate around development macroeconomics from a Keynesian perspective, which is a new and particularly important topic for those who wish to understand a little more about macroeconomics, growth, and economic development.

The main contribution of the book *Macroeconomia do Desenvolvimento. Uma Perspectiva Keynesiana* is to demonstrate that, for Keynesian theory, macroeconomic

policies traditionally more related to business cycles, have effects on long run growth and development. Short run policies affect the long run, because aggregate demand is considered the engine of long-run growth (Keynes, 1982).

The book organizes the theoretical debate into three parts. In the first part, the author presents some stylized facts related to differences in the levels and growth rates of per capita income in capitalist economies. In the second one, attention turns to the traditional Keynesian-inspired growth models, which underlie its interpretation and the possible ways to overcome the low growth rate of economies in the process of industrialization. The last part is intended to explain development macroeconomics, with a special emphasis on the Brazilian economy, in which the author presents the post-Keynesian response, "new developmentalist", of macroeconomic policy formulation to the problem of uneven development.

PART I - UNEVEN DEVELOPMENT

In this part of the book, the author presents some stylized facts through an inspection of countries' per capita income data. Uneven development stems from the existence of these different levels and growth rates of technical progress between countries, which generate significant and persistent differences between the growth rates of per capita income (Oreiro, p. 18). Indeed, Oreiro identified the phenomenon of uneven development and demonstrated that the dominant neoclassical theory was incapable of explaining it satisfactorily.

Neoclassical growth models, in their "exogenous growth" version (Solow, 1956), can only explain a small fraction of the differences in per capita income levels between countries, but they are not capable of explaining the differences in their growth rates, given that these differences are only temporary in such type of models and, in the long run, economies will grow at the same rate due to the public good nature of technology in such models (Oreiro, 2016, p. 6). The "endogenous growth" version (Romer, 1990), on the other hand, is uncapable of explaining why some countries converge in their per capita income levels, that is, why there are some convergence clubs among nations.

In the neoclassical perspective, factors on the supply side of the economy determine the long-run growth trend, which is independent of aggregate demand, which is only responsible for fluctuations/economic cycles. The problem is that empirical evidence demonstrates the opposite,

that is, temporary shocks (in demand or supply sides) permanently affect real output. In other words, the cyclical component associated with changes in aggregate demand in the short run affect the long-run trend. This phenomenon is known in the literature as "path dependence".

The implications of the thesis presented by the author that the phenomenon of uneven development results from technological asymmetries and asymmetries in the productive structure are several, but the main one is that we will have two types of economies. On the one hand, there are the economies specialized in the production and export of primary products (commodities) and, on the other, the more diversified economies, which can produce and export manufactured goods with higher value-added and a higher technological intensity. In this sense, the author states that models of growth driven by demand, mainly, by exports, may be able to explain the differences observed in the growth rates of per capita income across countries.

PART II - KEYNESIAN-INSPIRED GROWTH MODELS

In the second part of the book, the author presents the growth models with limited supply of labour (Harrod, 1939; Domar, 1946; Kaldor, 1955-1956; 1957; 1966; Pasinetti, 1974), which represent the hard core of the post-Keynesian growth theory.

These canonical models gave rise to the theory of growth and income distribution, so that they can explain the determinants of economic growth in mature economies with limited supplies of labour, defined as those that have completed their industrialization process, as all the workforce available in the traditional sector has already been transferred to the modern industrial sector.

In this approach, the supply of labour is not unlimited. In the short and medium run, the labour force can be expanded, but in the long run the natural rate of growth will grow. As technical progress is largely incorporated into new machinery and equipment, the pace of productivity growth will be induced by the growth rate of the capital stock (Kaldor, 1957). However, the maximum growth rate will be determined by the sum of the labour force growth rate and the labour productivity growth rate.

In the case of mature economies, uneven development results from divergences in the natural growth rates between countries. These, in turn, are the result of the interaction between the technological gap and the ability of countries to absorb technological spillovers from countries operating at the technological frontier. Thus,

the "laggard" countries will be able to make the so-called catching-up. These countries will tend to present a higher profit share. Thus, the growth models presented establish a positive relationship between the natural rate of growth and the share of profits (and capital) in national income (wealth) for these economies. This relationship between growth and income (and wealth) distribution defines the existence of a growth-led profit regime.

In addition, the author also presents an important theoretical contribution to the canonical post-Keynesian literature by demonstrating that the existence of different levels of technological gap between countries will cause them to exhibit different values for the natural rate of growth of real output and, given the growth of population, for the growth rate of gross domestic product and per capita income. Thus, for this class of models with limited supply of labour, the divergence between per capita income growth rates results from technological asymmetries between countries (Oreiro, 2016, p. 67).

In the case of economies in the process of industrialization, the growth rate of output is not restricted by the availability of labour, but by the balance of payments. In this context, the differences in the growth rates of labour productivity and per cap-

ita income result from asymmetries in the productive structure or level of productive specialization of the countries. These are dual economies which can be classified into two large groups, namely: Diversified economies and primary-export economies. Evidently, the rate of growth of output consistent with the equilibrium of the balance of payments is higher for diversified economies.

At this point, Thirlwall's Law is recovered by the author to explain the balance of payments equilibrium growth rate (y_{Bt}), in which we have:

$$y_{Bt} = \frac{\in .(z_t)}{\pi}$$

Where $\in$ is the income elasticity of demand for exports; π is the income elasticity of demand for imports; and z_t is the growth of world income.

However, Oreiro goes on to explain which factors determine the ratio of income elasticity of exports and imports, demonstrating that these are endogenous and depend on the degree of productive specialization, the technological content of exported goods and the share of the manufacturing industry in gross domestic product. Indeed, in a seminal way, the literature of balance of payments constraint growth is linked with structural change models.

The author goes further in the theoretical debate by presenting the

Kaleckian models, in which the use of productive capacity is below the maximum, normal or satisfactory level in the long run. In these models, the engine of long run growth is attributed to the autonomous share of investment that stems from technological progress. Depending on the specification of the investment function, however, the relationship between the share of profits in income and the degree of utilization of productive capacity can be either negative, thus characterizing a wage-led demand regime, or positive, thus defining a profit-led demand regime. The canonical Kaleckian model is compatible with the existence of persistent differences in the level of the technological gap between countries, but by treating the source of long run growth as exogenous to the system, it is not able to explain the existence of divergences of per-capita income growth rates.

PART III - DEVELOPMENT MACROECONOMICS

In the last part, the author returns to the central issue explored in the book, which is the definition of an ideal macroeconomic policy regime capable of helping developing economies to improve their pace of economic growth and reach the level of per capita income of developed countries.

As explained in the book, production factors are not a limit for economic growth, but autonomous demand. Indeed, the growth rate of exports is the exogenous variable *par excellence* since the other components of demand put pressure on the balance of payments. In the case of open economies that do not have an international reserve currency, exports are the engine of long run economic growth, as investment and technical progress adjust to expected growth in demand. Thus, for Keynesian theory, economic growth must be led by exports.

In this sense, differences in per capita income levels between countries reflect differences in export dynamism, which is related to the degree of productive specialization and the technological content of exports. The first factor critically depends on the real exchange rate, since a rate that is more appreciated than the industrial equilibrium exchange rate can initiate or intensify the process of deindustrialization, reducing the income elasticities ratio of exports and imports. The second one depends on the technology gap, which strongly affects the income elasticity of exports.

Policy makers must ensure that there is no mismatch between the industrial equilibrium exchange rate and the current account equilibrium exchange rate, what would make

the latter more appreciated than the former, a phenomenon known as Dutch disease. If the real exchange rate appreciates, a perverse structural change in the economy begins, with deindustrialization and reprimarization of exports, reducing the ratio of income elasticities, as defined by Thirlwall's law (Thirlwall, 1979). Thus, the restriction to long run growth has its origin in the long-run trend of exchange rate overvaluation due to Dutch-disease and inflows of financial investments.

Another contribution of the book, rarely found in textbooks, is the application of theory to the reality of an economy. The debate around the macroeconomic policy regimes in Brazil is presented in a didactic way, from the macroeconomic tripod to the new macroeconomic matrix of the Dilma Rousseff government, always highlighting the mistakes and successes of each regime so that the reader can follow the reasoning proposal, which shows the feasibility of the export-led growth model.

The macroeconomic tripod adopted in the Brazilian economy, prevailing from 1999 to 2005, consisted of inflation targeting, primary surplus target for central government and relatively free floating of the exchange rate, where the main objective was the stability of the inflation rate. However, economic growth in the period

was not pleasing, as a result of high interest rates and a reduction in the investment rate.

Aware of this, the Brazilian government, in 2006, made macroeconomic tripod more flexible by reducing the target for surplus, eliminating declining inflation targets and accumulating international reserves. At the time, the exchange rate began to be managed through international reserves and the government implemented the minimum wage readjustment policy. In this context, the detachment of monetary, fiscal, wage and exchange rate policies become evident, which made the goals of accelerating growth, controlling inflation and maintaining the exchange rate inconsistent with one another. The maintenance of high interest rates contributed to the appreciation of the real exchange rate, which favoured controlling inflation in the period, but compromised the trade balance and the current account.

In 2008, with the deepening of the international financial crisis, the Brazilian economy implemented an inward-looking model of development, with tax reductions, increased public spending, expansion of bank credit and an increase in the minimum wage. The Brazilian government was betting that these policies would stimulate private investment, allowing a simultaneous increase in productive

capacity and labour productivity. The idea was to enable a high growth of the output and wages, with controlled inflation. However, according to the author: "This regime generated a trade-off between external competitiveness and inflation stability. Thus, this regime can be characterized as "inconsistent developmentalism" (Oreiro, 2016, p. 198).

In late 2011 and early 2012, the country had the opportunity to resolve the dilemma. At that moment, the Brazilian economy implemented the so-called "new macroeconomic matrix", which began a cycle of reduction in the basic interest rate and the gradual devaluation of the exchange rate. However, the new matrix was not successful for two reasons: 1) the devaluation was not strong enough to eliminate the overvaluation of the real exchange rate accumulated in the past; and 2) the real interest rate remained at high levels (Oreiro, 2016, pp. 199-200).

From the above, the analysis presented in the book demonstrated that the economic policy regimes prevailing in Brazil were not compatible with the export-led growth regime, which compromised the growth potential of the Brazilian economy in most part of the period under consideration. Thus, President Dilma Rousseff's second term begins with a stagnation process, a strong fiscal imbalance, and major challenges for the conduct of economic policy.

Based on this reasoning, the author presents a post-Keynesian proposal for an ideal macroeconomic policy regime, which can be summarized as follows:

- With regard to fiscal policy, its role must be to reconcile the maintenance of the Debt/Gross Domestic Product ratio at a low level with the stabilization of the level of economic activity.
- The wage policy must be compatible with the stability of the functional distribution of income in the long run. Indeed, the real wage growth rate should not be regulated by the labour productivity growth rate over time.
- The export-led growth regime critically depends on the ability of exchange rate policy to generate a competitive real exchange rate in the medium and long run. To this end, it must prevent the inflow of foreign capital that appreciates the real exchange rate, given that it compromises the competitiveness of exports, which would give rise to (or deepen) a process of deindustrialization.
- The role of monetary policy will be to keep the inflation rate at low and stable levels, as well as to smooth fluctuations in the growth

rate around the long run growth target, maintaining a relatively low real interest rate in the international comparison.

In my opinion, this book can be an important reference for the disciplines of macroeconomics, growth and economic development, for its pioneering role in organizing the debate around the post-Keynesian literature on economic growth, as well as for the various contributions and applications presented, which show the paths already taken by economists and the debates that must be faced in the coming years, in particular, for the Brazilian economy to reach the ideal economic policy regime and overcome economic stagnation. The main bottlenecks would be to advance in the monetary stabilization process, which is still unfinished, in order to ensure stable inflation, exchange rates and interest rates compatible with those of developed countries, with the aim of expanding investments in strategic sectors and recovering the share of industry in the gross domestic product for a sustainable export-led growth. ◄

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