



100 YEARS
UNDERSTANDING
AND SHAPING
THE GLOBAL ECONOMY

Center of Applied Economic Research Münster
CAWM-Kolloquium | Münster, 26 June 2014

Towards a Coordinationist Paradigm for Macroeconomics - The Interplay of Money, Capital, and Interest

Prof. Dr. Stefan Kooths

Kiel Institute for the World Economy, Forecasting Center and Office Berlin
Business and Information Technology School (BiTS), Campus Berlin

The Kiel Institute for the World Economy (established 1914)



Outline

- **Market process-oriented microfoundations**
 - » What microfoundations?
 - » Why market process-oriented?
 - ⇒ **Contribution to methodological diversity (paradigmatic talk)**

- **Capital, interest, and money**
 - » Production: Capital-based and consumption-driven
 - » Interest: Pure Time Preference and Loanable Funds
 - » Money: The ultra-pervasive good
 - ⇒ **Role of time in macroeconomics (intertemporal links)**

- **Applications and research**
 - » Linking financial/monetary sphere and real economy
 - » Production possibilities, path-dependencies, and crises
 - » Global perspective and top-down-approach
 - ⇒ **Towards a coordinationist paradigm of macroeconomics**

Outline

- **Market process-oriented microfoundations**
 - » What microfoundations?
 - » Why market process-oriented?
 - ⇒ **Contribution to methodological diversity (paradigmatic talk)**
- **Capital, money, and interest**
 - » Production: Capital-based and consumption-driven
 - » Interest: Pure Time Preference and Loanable Funds
 - » Money: The ultra-pervasive good
 - ⇒ **Role of time in macroeconomics (intertemporal links)**
- **Applications and research**
 - » Linking financial/monetary sphere and real economy
 - » Production possibilities, path-dependencies, and crises
 - » Global perspective and top-down-approach
 - ⇒ **Towards a coordinationist paradigm of macroeconomics**

Microfoundations for macroeconomics

- One economic process
 - » Micro level: Economic mechanisms and individual decisions
 - » Macro level
 - Mismatches on micro level show up as „imbalances“
 - Universal drivers (permeating into all micro markets)

⇒ Macroeconomics: Evidence for systematic misallocation of resources?
- Universal (= pervasive) drivers
 - » Money (medium of exchange)
 - » Interest (price of time)
 - » Capital (means for intertemporal coordination)
 - » Labor (most universal production factor)
 - » Constitutional framework (regulations, policy)

⇒ **Systemic micro disruptions as macro symptoms**

Market process view (1/2)

- Disequilibrium approach
 - » Menger/Hayek vs. Walras/Marshall tradition
 - » homo agens (HA) vs. homo oeconomicus (HO)

- Role of entrepreneurs
 - » Uncertainty: speculation, search, and discovery (HA as explorer)
 - » Universal arbitrageurs: investment as intertemporal arbitrage

- Dynamics and time
 - » Permanent adjustment process rather than sequence of equilibria
 - » Market system as feedback mechanism (ex-ante and ex-post prices)
 - » Time cannot pass without modifying knowledge (Hoppe)

Market process view (2/2)

- Value theory
 - » Subjectivist perspective
 - » Reverse value imputation (from ends to means)

- Prices as knowledge surrogates
 - » Deficiency of monetary calculation:
Distorted price structures vs. price level movements
 - » Non-neutrality of money (Cantillon effects matter)

⇒ **Leaving the “evenly rotating economy” behind**

Outline

- **Market process-oriented microfoundations**
 - » What microfoundations?
 - » Why market process-oriented?
 - ⇒ **Contribution to methodological diversity (paradigmatic talk)**
- **Capital, money, and interest**
 - » Production: Capital-based and consumption-driven
 - » Interest: Pure Time Preference and Loanable Funds
 - » Money: The ultra-pervasive good
 - ⇒ **Role of time in macroeconomics (intertemporal links)**
- **Applications and research**
 - » Linking financial/monetary sphere and real economy
 - » Production possibilities, path-dependencies, and crises
 - » Global perspective and top-down-approach
 - ⇒ **Towards a coordinationist paradigm of macroeconomics**

“Final aggregate demand”: No demand and not all of it is final

Goods and services account

Source/Input (not: supply)

for period t

Use/Output (not: demand)

Intermediate consumption
(production structure)

Domestic value-added

Imports

Intermediate consumption
(production structure)

**Final consumption
(exclusive source of value)**

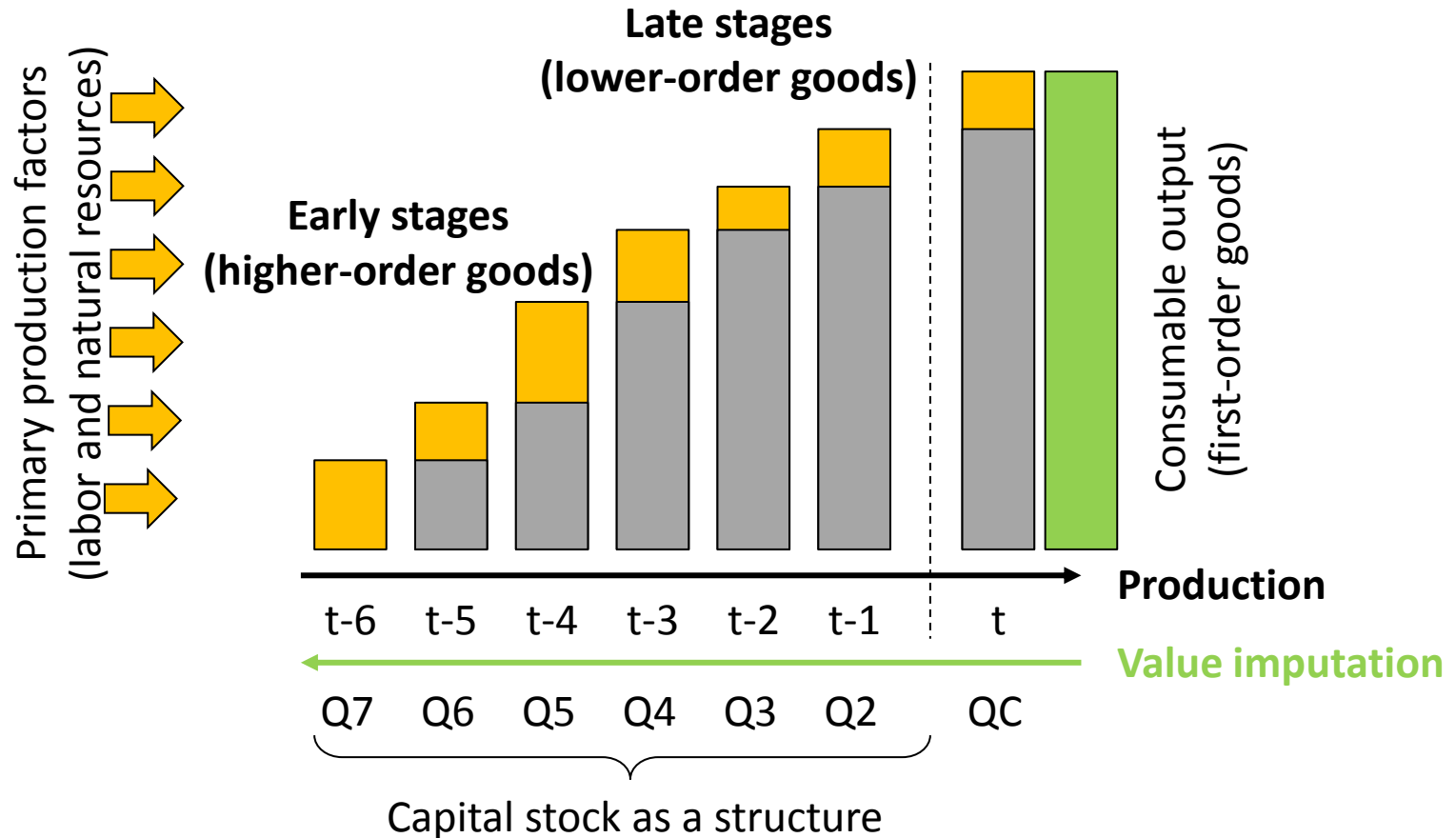
Domestic capital formation

Capital formation abroad

Exports

**„Final“ use of domestic production
(only with respect to period t)**

Production as a time consuming, multi-stage process



⇒ **Capital formation: intertemporal intermediate consumption**

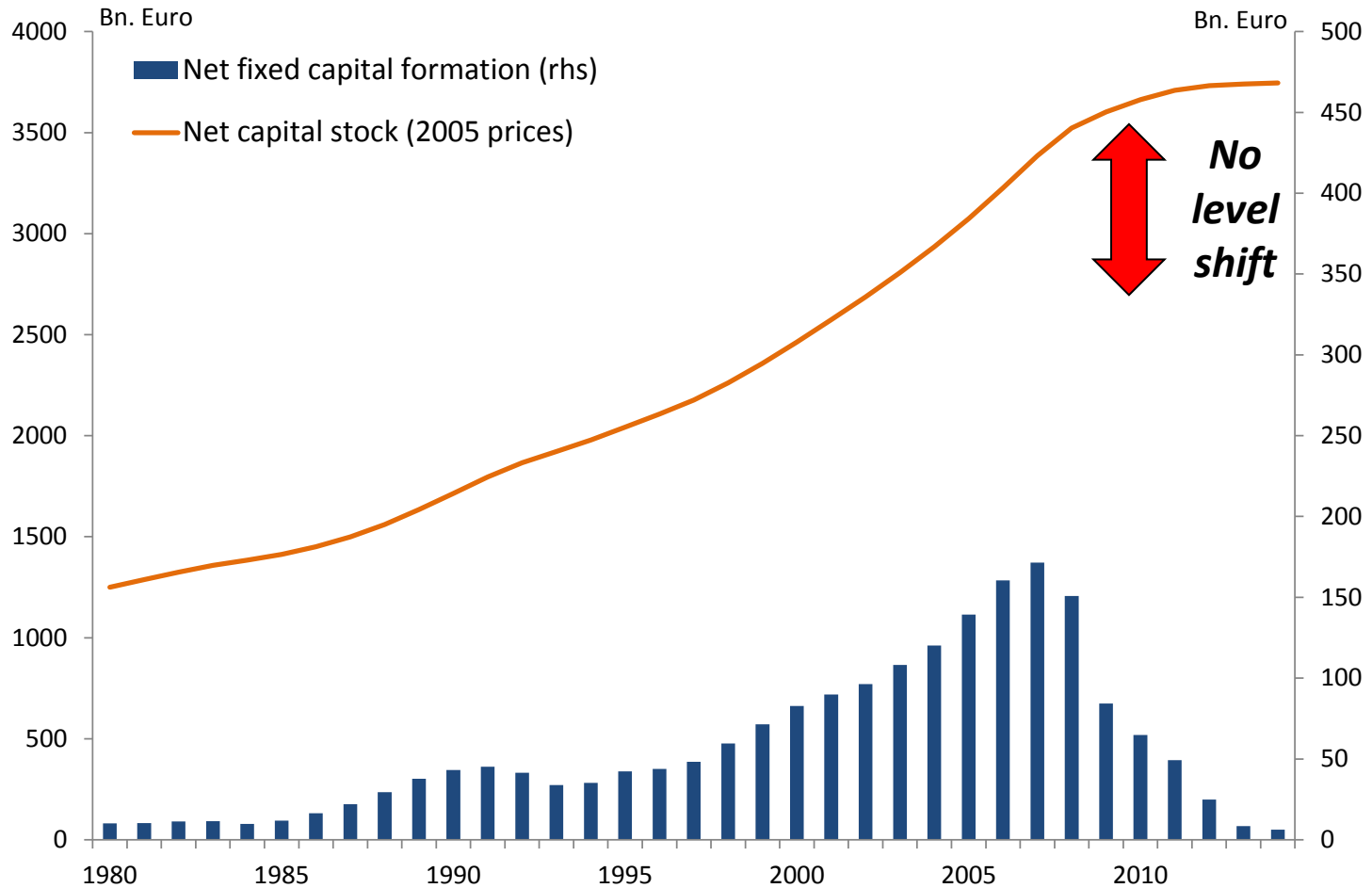
Capital

- Capital as intentionally produced productive means ...
 - » ... not a disembodied abstraction or homogenous aggregate
 - » ... nor a self-perpetuating (“Knightian”) fund

 - Structure of heterogeneous goods
 - » Limited convertibility and recombination losses
 - » Capital as a structural pattern (Lachmann)

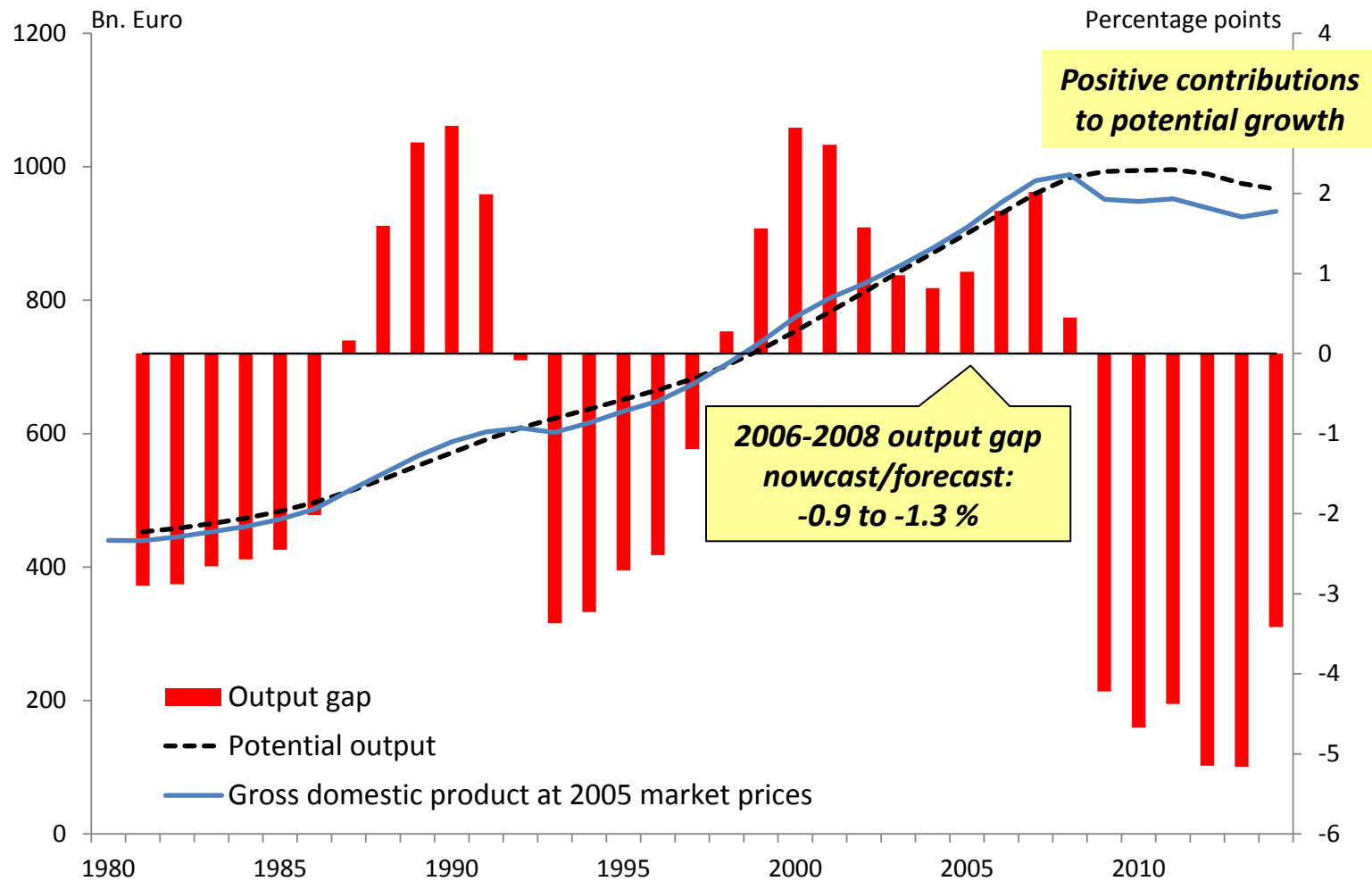
 - Value dimension:
 - » Ability to allow individuals to more readily realize their plans rather than physical characteristics or physical history
 - » “Unfinished entrepreneurial plans” (Kirzner): Capital goods to be assessed in light of their usefulness to those plans
- ⇒ **Missing link between micro and macro level (Skousen)**

Value of the Spanish capital stock?



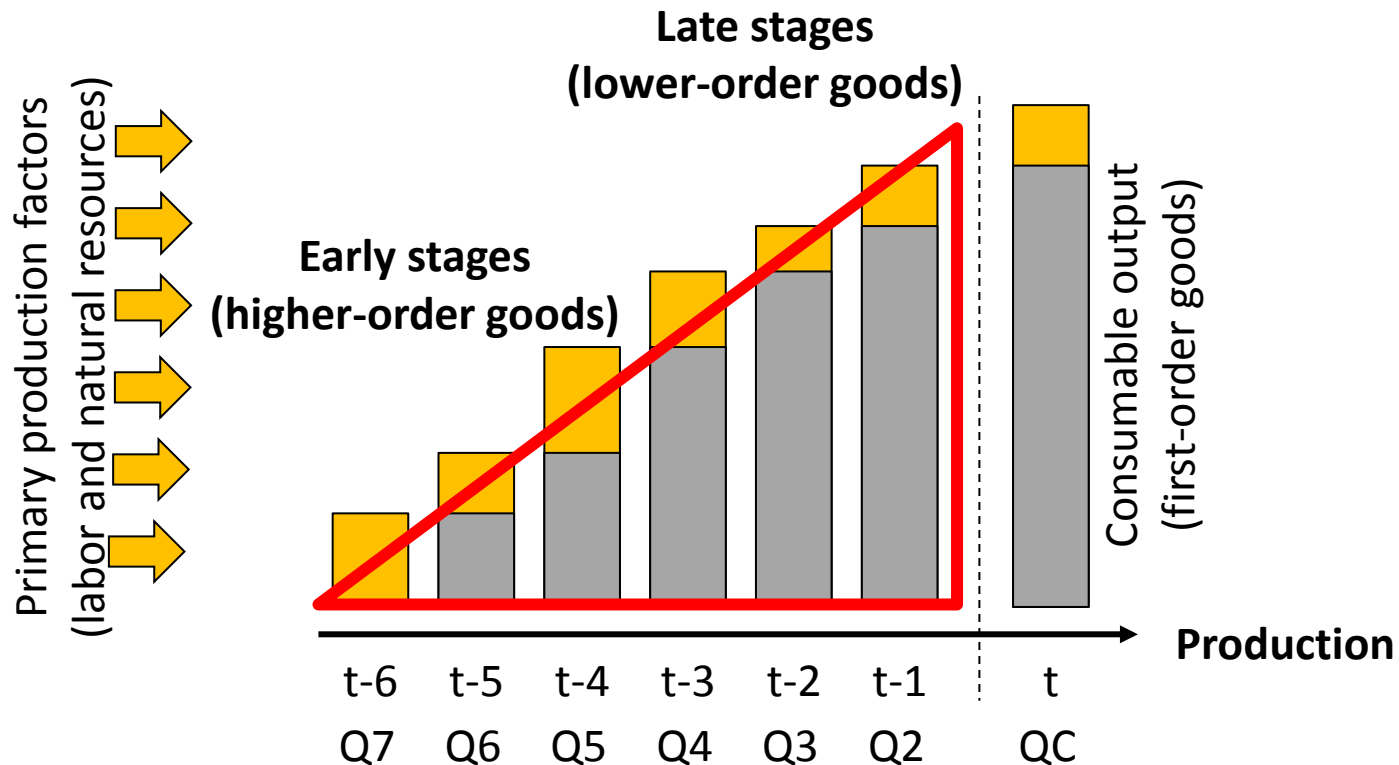
Source: AMECO Database.

Spain: Invisible “ghost estates”



Source: European Commission, AMECO and CIRCA databases.

Production: The Hayekian triangle

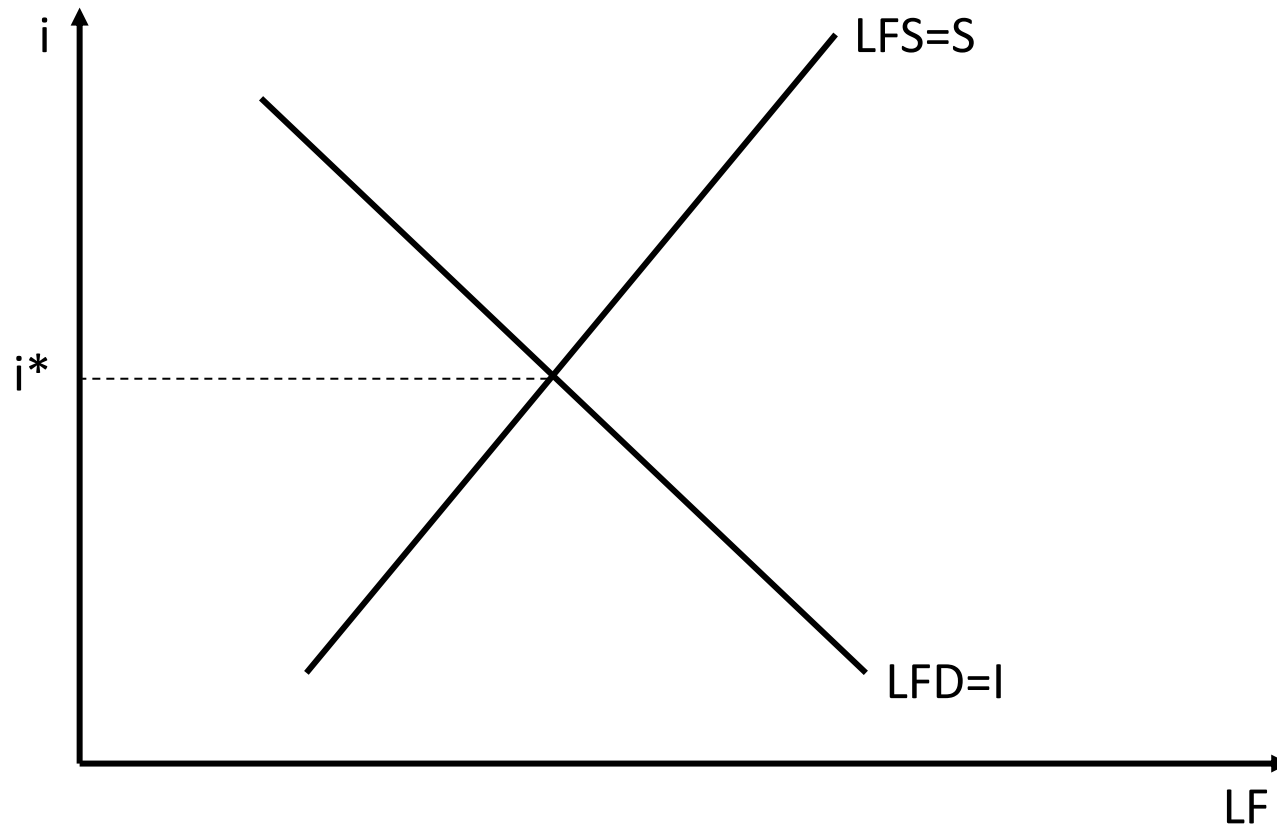


⇒ Number of production stages/shape of the Hayekian triangle?

Interest

- Interest as a value phenomenon
 - » Expression of time preference
 - » Price of future goods relative to present goods
 - » Discount rate interwoven in the entire price system
 - Capitalization theory (Fetter): Interest vs. price of capital
 - » Productivity of capital reflects in price of capital goods
 - » Valuation of reproducible capital pushed backward to primary factors
 - » Price of capital = present value of future income streams
 - Interest and “roundaboutness of production”
 - » Capital-intensity increases productivity of labor
 - » Choice of more roundabout production schemes depends on time preference
- ⇒ **Pure time preference = market rate of interest?**

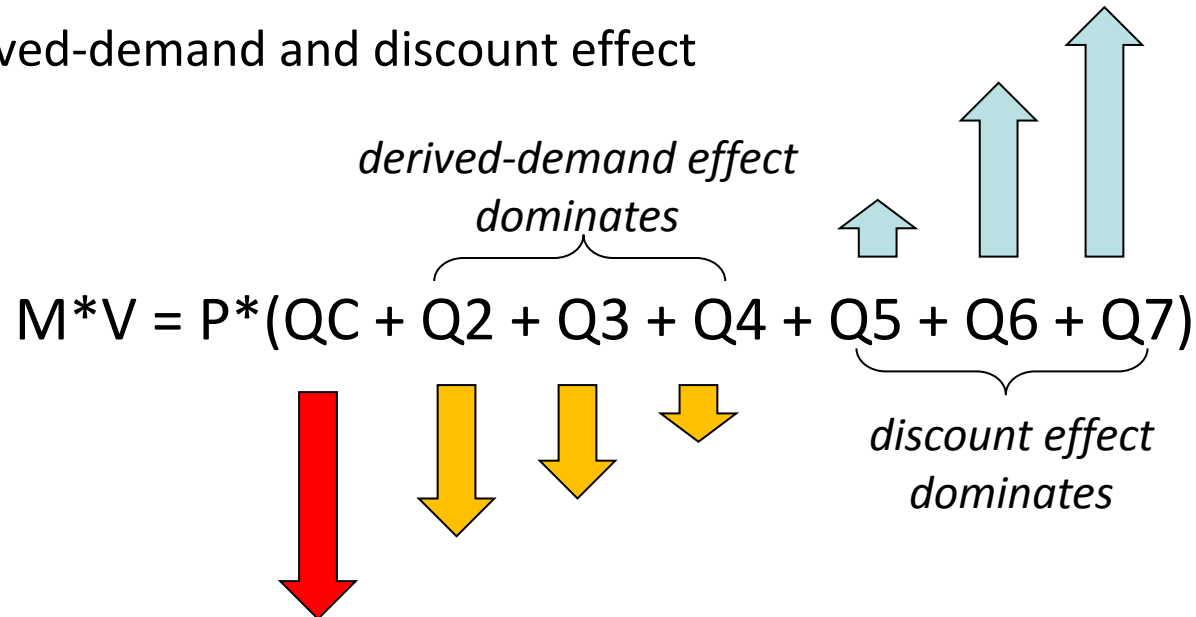
Interest rate and market for loanable funds



Coordinating saving and investment

■ Saving

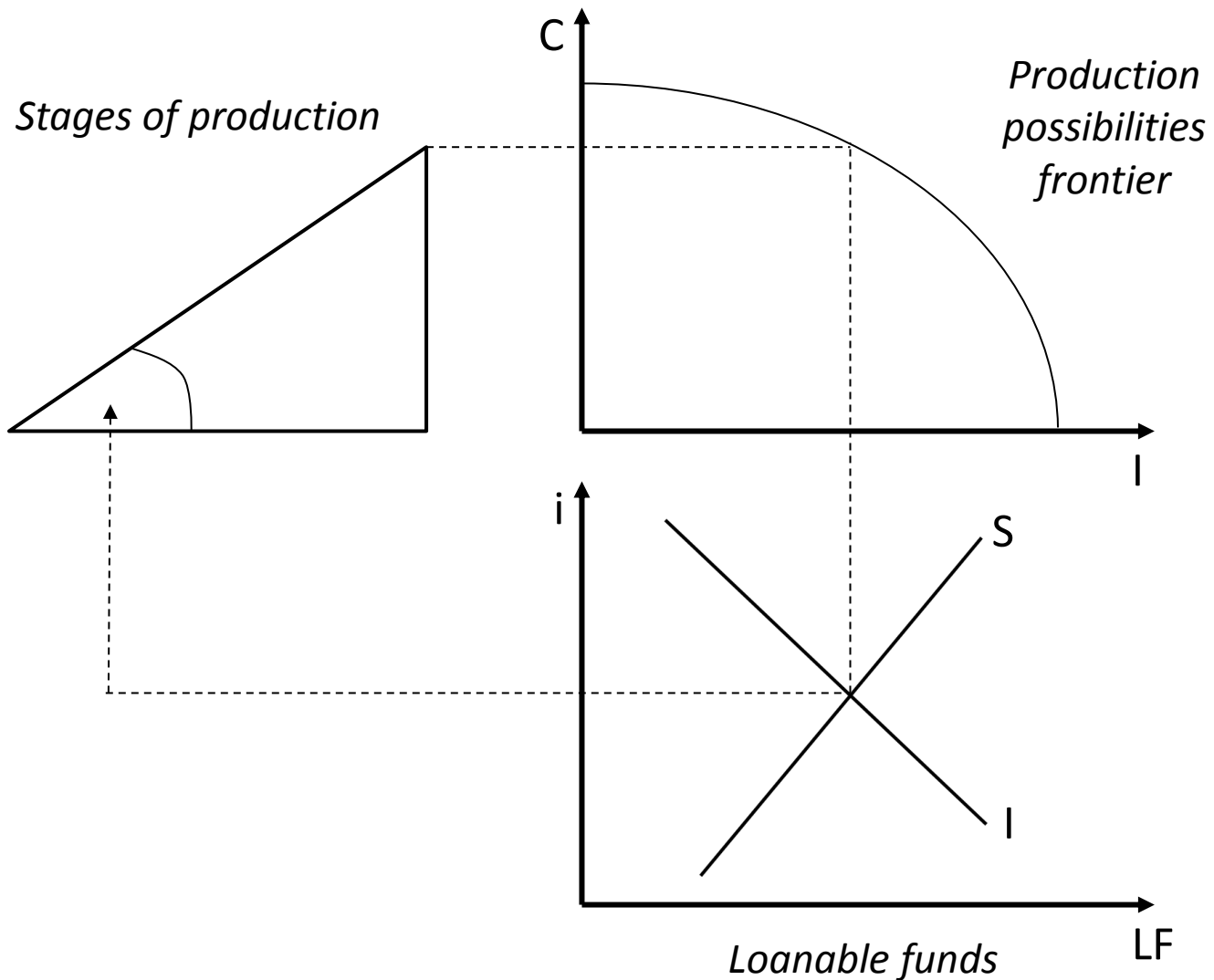
- » Saving up for something: Future demand, not a leakage
- » Derived-demand and discount effect



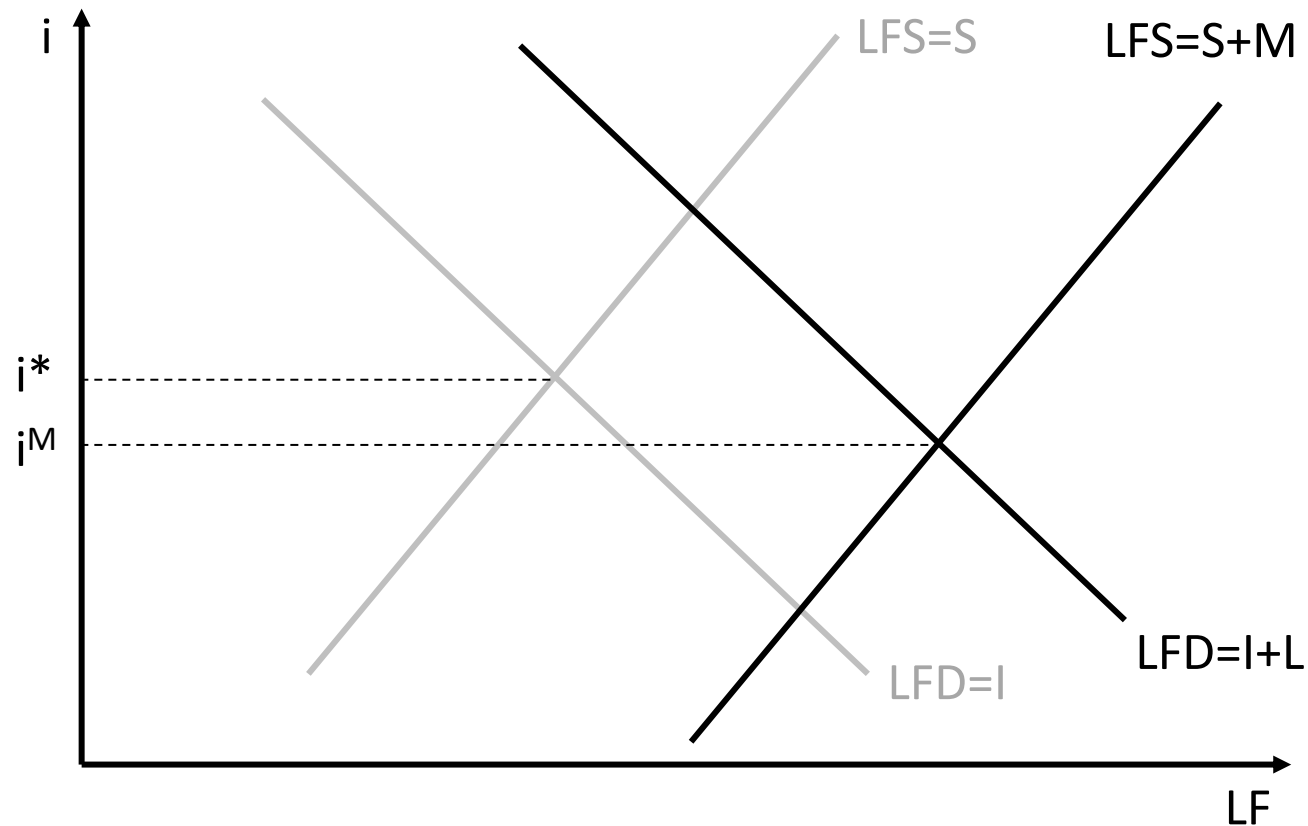
■ Investment: Stage pattern matters (not volume alone)

- ⇒ Entrepreneurial challenge: bringing capital structure in line with pure time preference (intertemporal arbitrage)

Capital-based macroeconomic framework (Garrison)



Interest rate and monetary policy



Monetary policy

- Multi-purpose weapon of “modern” economic policy
 - Generic target: Provision of a means of exchange
 - Other targets
 - » Government financing
 - » Debt-monetization
 - » Boosting employment
 - » Business-cycle stabilization
 - » Systemic financial stability
 - » ...
 - Monetary policy
 - » Today: Key price of capitalist system manipulated by central banks
 - » Back to simple money supply rules?
- What about Tinbergen?

Outline

- **Market process-oriented microfoundations**
 - » What microfoundations?
 - » Why market process-oriented?
 - ⇒ **Contribution to methodological diversity (paradigmatic talk)**
- **Capital, money, and interest**
 - » Production: Capital-based and consumption-driven
 - » Interest: Pure Time Preference and Loanable Funds
 - » Money: The ultra-pervasive good
 - ⇒ **Role of time in macroeconomics (intertemporal links)**
- **Applications and research**
 - » Linking financial/monetary sphere and real economy
 - » Production possibilities, path-dependencies, and crises
 - » Global perspective and top-down-approach
 - ⇒ **Towards a coordinationist paradigm of macroeconomics**

Macroeconomics and terminology

- Risks of macroeconomic misperceptions
 - » Aggregating/averaging the problems away (e.g. aggregate production function approach)
 - » Losing touch with microeconomic principles (e.g. key role of price mechanism)
 - » Over-interpreting national accounts concepts (e.g. identities tell nothing about causality or interdependency)
 - » Ignoring production structures (netting out intermediate consumption)

- Language (terminology) and reasoning (theory)
 - » Words can be misleading
 - » Wording matters

Applications (1/2)

- Potential production/output gap estimations
 - » Disaggregated approaches (marketable production possibilities)
 - » Market revaluations compared to national accounting data
- Capital stock distortions as flipside of financial crisis
 - » Repairing intertemporal discoordination problems
 - » New light on “austerity” debate
- Non-neutrality of money/monetary policy
 - » Monetary theory of the business cycle
(systematic investment failures due to excessive credit creation)
 - » “Capital gives money time to cause trouble” (Garrison)
 - » Scenario of globalizing monetary policy (multilateral swap agreements)

Applications (2/2)

- International macroeconomic imbalances
 - » Current account vs. financial account (capital vs. trade flows)
- Global macroeconomic imbalances: The savings glut debate
 - » Negative natural interest rates ahead?
 - » Need for more public debt to fill the global “investment gap”?
- Global business cycle and regional/national impact
 - » Top/down view:
Economic activity within countries derived from global dynamics
 - » National specialization and impact of capital restructuring

A coordinationist macroeconomic paradigm

- Key research and policy question:
Evidence for hampered market coordination processes?
 - » Coordination efficiency vs. macroeconomic management
 - » Important role of intertemporal coordination (capital and interest)
 - » Path-dependency of economic activity via capital allocation
- Beyond the demand-side vs. supply-side controversy
 - » Coordinationist macroeconomics is not a cheerleader for growth
 - » Intermediary step to linking macroeconomics and well-being
 - Overcoming the production-biased view
(production serves consumption, not vice versa)
 - Putting consumers/households back in the center
 - Value theory remains key pillar
(whether preferences are exogenous or endogenous)



Saving and growth

