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Employment and Income Distribution from a Classical–Keynesian Viewpoint

Some Tools to Ground a Normative Analysis

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Abstract. *Two unambiguous phenomena have characterized the environment in which the global crisis has spread: a thirty–year increase in the profit share and a significant increase in the 'degree of financiarisation'. Dominant economic theory does not seem suitably equipped to provide solid benchmarks for orientating a normative analysis on these aspects. This paper will analyze the two mentioned phenomena in light of an alternative paradigm, based on Classical and Keynesian lines, with the purpose of not only highlighting the two specific issues but also outlining a normative framework based on the Classical–Keynesian approach to political economy.*

Employment and Income Distribution from a Classical–Keynesian Viewpoint

Some Tools to Ground a Normative Analysis[1]

Enrico Bellino[2]

1. Introduction

Industrial and post–industrial economic systems are characterized by two unambiguous phenomena which are at the center of discussions on the current crisis: the increase of the profit share over the past thirty years and the increased degree of 'financiarisation' of economic systems. Mainstream economics seems ill equipped to face these issues satisfactorily, in particular from a normative stance. For example, questions like 'what levels of profits are needed by the system?' or, 'is there a desirable degree of financiarisation for economic systems?' do not seem to find useful answers in the Paretian approach.

This paper sets out to provide the basic elements needed to develop an alternative normative framework based on the Classical–Keynesian approach. The theoretical reference framework is the Classical one as reproposed and reformulated quite recently by Sraffa (1960), and later developed and generalized by Garegnani (1983), (1984) and Pasinetti (1981), (2007). Part of the arguments presented are intrinsically connected with output levels and their evolution through time. The Keynesian principle of effective demand seems quite compatible with the methodology of Classical analysis. For this reason,

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the Pasinetti's framework of structural change represents an excellent tool for presenting my arguments. This paper suggests a way to derive some normative propositions concerning income distribution (and related issues) with the purpose of suggesting a line of research along which all strands of the modern Classical approach can agree with and, hopefully, to which they can contribute with further results.

2. Welfare Paretian analysis and income distribution

Neoclassical analysis has developed in parallel both a positive and a normative level of economic analysis based on the same individualistic approach. This methodological basis has proved to have several strengths in both levels of analysis, essentially because it is based on the ultimate consequences of economic activities: satisfying the final wants of the individuals. Nevertheless, this methodological approach has at times conditioned the kind of results that could be obtained: as the description of any situation is reduced to a description of *how* relevant individuals *behave*, also the outcome of the normative analysis cannot but incorporate *just* what *single individuals* want to happen without taking into consideration the needs of the system as a whole. These weaknesses make it impossible for the Paretian approach to tackle some of the relevant issues which are currently at stake in a meaningful way. For example, as noticed in the Introduction, it is hard to identify useful benchmarks to orientate income distribution, or to define a desirable degree of financiarisation of an economic system.

Distributive issues can be faced in at least two ways in Neoclassical analysis. One is concerned with the notion of wealth conceived as a *stock*. Consider a pure exchange economy with two individuals, A and B, and two goods, X and Y. Feasible allocations of the economy's endowments of these two goods, $\bar{x}$ and $\bar{y}$, are represented by all points of the Edgeworth box (see the left–hand graph of Figure 1). The set of Pareto–efficient allocations is represented by a subset of this box, the contract curve CC'. The curve on the right–hand side of Figure 1 is built by moving along the CC' curve: it indicates the maximum level of utility assigned to one individual for any given level of utility assigned to the other individual. It constitutes the *utility frontier* (UF) of the society. All movements from any point of the Edgeworth box *toward* the CC' curve — or from any point *below* the utility frontier *toward* it — can be justified on the basis of economic considerations deriving from the notion of Pareto efficiency. All movements *along* the CC' curve — or along the UF curve — entail reallocations of endowments between individuals; they are not ex-

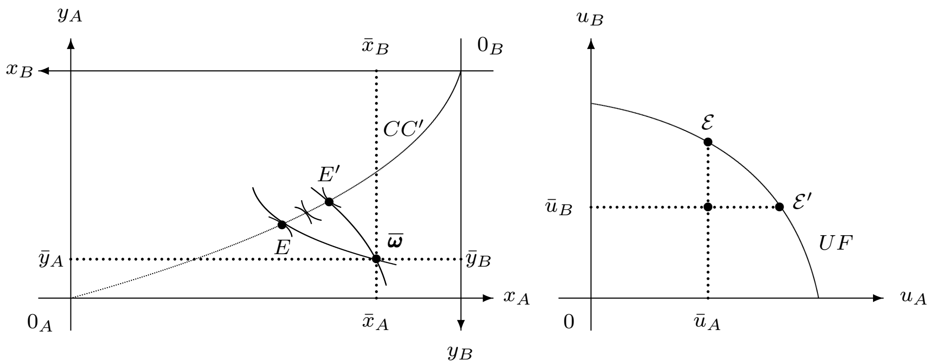

Figure 1: The contract curve (CC') and the utility frontier (UF)

cluded, but they *cannot* be justified by efficiency arguments. Their justification is to be found outside the pure field of economic theory, in the sphere of social choices: in ethical, political, social, in brief 'institutional' arguments. For example, if the property rights on initial endowments are specified by vector $\overline{\omega} = [\bar{x}_A, \bar{y}_A; \bar{x}_B, \bar{y}_B]$, on the basis of efficiency arguments we can justify every movement from vector $\overline{\omega}$ to any point in the subset EE' of curve CC' — or every movement from point $(\bar{u}_A, \bar{u}_B)$ to the subset $\mathcal{E}\mathcal{E}'$ of curve UF. Once the system is on curve CC' — or on curve EE' — every further movement along these curves must be justified on the basis of arguments outside the pure field of economic theory.

Hence, by looking at wealth in terms of stocks, Neoclassical economic analysis gives space, by separating the analysis of efficiency from that of equity, to the possibility of affecting initial endowments on the basis of economic arguments up to the point where the system reaches an efficient allocation; once it is reached, any further movement must be justified on the basis of 'institutional' arguments.

More rigid conclusions can be drawn if we look at distributive relationships in terms of income flows, that is, in terms of factor prices (i.e. wages and profits). Hence, we must introduce production.[3] Consider, for simplicity, a system with two final goods, X and Y, produced by means of capital, K, and labour, L. Given the quantities that must be produced of final goods, $\overline{X}$, and $\overline{Y}$ — here considered as given for simplicity —, a unique (and feasible) allocation of factors among industries (composed of identical firms) is identified:

3. We are not considering here the difficulties for Neoclassical theories to formulate a coherent value and distribution theory when capital is seriously taken into consideration. On this, see Garegnani (1990) and (2003).