

## Is Milton Friedman a Keynesian?

Well, **NO**—if you compare Friedman and Keynes in the context of the macroeconomics that was dominant during the heyday of monetarism (which spans roughly a quarter century from the late 1950s to the early 1980s). Consider these half-dozen points of contrast:

### THE KEYNESIAN VIEW

**K1.** Keynesians believe that the interest rate, largely (if not wholly) a monetary phenomenon, is determined by the supply of and demand for money.

**K2.** In the Keynesian vision, a change in the interest rate has little effect on (aggregate) investment. In other words, the demand for investable resources is interest inelastic—a judgment that reflects the Keynesians' short-run orientation.

**K3.** Keynesians conceive of a narrowly channeled mechanism through which monetary policy affects national income. Specifically, money creation lowers the interest rate, which stimulates investment and hence employment, which, in turn, give rise to multiple rounds of increased spending and increased real income. The nearly exclusive focus on this particular channel of effects, together with the belief that investment demand is interest-inelastic, accounts for the Keynesian preference for fiscal policy over monetary policy as a means of stimulating or retarding economic activity. Government spending has a direct effect on the level of employment; money creation has only an indirect and weak effect.

**K4.** Keynesians believe that long-run expectations, which have no basis in reality in any case, are subject to unexpected change. Economic prosperity is based on baseless optimism; economic depression, on baseless pessimism.

**K5.** Keynesians believe that economic downturns are attributable to instabilities characteristic of a market economy. A sudden collapse in the demand for investment funds, triggered by an irrational and unexplainable loss of confidence in the business community, is followed by multiple rounds of decreased spending and income.

**K6.** Keynesians believe that in conditions of economy-wide unemployment, idle factories, and unsold merchandise, price and wages will not adjust downward to their market-clearing levels—or that they will not adjust quickly enough, or that the market process through which such adjustments are made works perversely as falling prices and falling wages feed on one another.

### THE MONETARIST VIEW

**M1.** Monetarists believe that the interest rate, largely a real phenomenon, is determined by the supply of and demand for loanable funds, a market which faithfully reflects actual opportunities and constraints in the investment sector.

**M2.** In the Monetarist vision, a change in the interest rate has a substantial effect on (aggregate) investment. In other words, the demand for investable resources is interest elastic—a judgment that reflects the Monetarists' long-run orientation.

**M3.** Monetarists conceive of an extremely broad-based market mechanism through which money creation stimulates spending in all directions—on old as well as new investment goods, on real as well as financial assets, on consumption goods as well as investment goods. Nominal incomes are higher all around as a direct result of money creation, but with a stable demand for money in real terms, the price level increases in direct proportion to nominal money growth so that all real magnitudes are, in the long run, unaffected.

**M4.** Monetarists believe that profit expectations reflect, by and large, consumer preferences, resource constraints, and technological factors as they actually exist.

**M5.** Monetarists believe that economic downturns are attributable to inept or misguided monetary policy. An unwarranted monetary contraction puts downward pressure on incomes and on the level of output during the period in which nominal wages and prices are adjusting to the smaller money supply.

**M6.** Monetarists do not believe that the perversities envisioned by the Keynesians, if they exist at all, play a significant role in the market process. They believe instead that prices and wages can and will adjust to market conditions. The fact that such adjustments are neither perfect nor instantaneous is, in the Monetarists' judgment, no basis for advocating governmental intervention. A market process that adjusts prices and wages to existing market conditions is preferable to a government policy that attempts to adjust market conditions to existing prices and wages.

But, **YES**—if you consider that Friedman set out his ideas in the context of ISLM analysis, took account of the interest rate only as it affects people's willingness to hold money, failed to deal with the market mechanisms that allocate resources over time, and saw no causal connection (his "Plucking Model") between boom and subsequent bust. Friedrich A. Hayek's criticism applies to both Keynes and Friedman: "[Their] aggregates conceal the most fundamental mechanisms of change."