

TERM AND BASIC CHARACTERISTICS KEYNESIAN THEORIES

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Review article

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Abstract

The Keynesian theory was named after its founder, John Maynard Keynes (1883-1946), one of the great thinkers of the 20th century. Keynes was a student of Alfred Marshall at the University of Cambridge (where he later taught himself) and his teaching is under a certain influence of Marshall. He is the author of many economic works, which were intended to "save capitalism" and which were greatly influenced by the social and historical circumstances of that time. He was extremely educated and capable of economically analyzing and describing the reality and problems of the society in which he lived in a short period of time. Of his numerous works, the most significant is certainly: General theory of employment, interest and money¹. In that part, he summarizes and criticizes his earlier understandings, while developing his analysis (theory) in which the idea of effective search occupies a central place.

Key words: *Keynes, economic efficiency, employment.*

Introduction

This work caused, and still causes, numerous expert discussions in academic circles, but it certainly made a great contribution to economic science on a theoretical level and at one time had a significant influence on the creation of British economic policy. Not intending to give an overview of his theory as a whole, because that would in many ways exceed the character and purpose of the work itself, we will try to present only the most important postulates and characteristics of

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Keynes's theory, as well as a certain review of the views of the author's contemporaries.

The work conceived in this way will be based on the articles of good experts on Keynes theory, published in professional magazines of the English-speaking area, with the use of a certain amount of literature, of our speaking area, which was available to the author (Jakšić, et. all, 2001).

These are the main reasons why this paper may have a little original approach in presenting the content and characteristics of Keynes's theory, while there is also the possibility that certain parts of the theory may be incompletely (imprecisely) interpreted to a small extent.

1. Introduction to Keynesian theory

Keynesian economics is a theory and a way of thinking, in the center of which is the functioning of the aggregate (macro) economy and which draws its inspiration from the works of John Maynard Keynes - especially his kwiga *The General Theory of Interest, Employment and Money* (1936), as well as the works of Keynes's contemporaries - R. Harrod, N. Kaldor, R. Kahn, X. Robinson and M. Kalecki, who expanded Keynes's analysis and on the developing economy, as well as the relations of wages and profits in the functional distribution of incomes, which Keynes otherwise neglected (Jakšić, Pejić, 1996).

Keynes' theory was designed to systematically fill the gaps in our knowledge, within three major areas, namely (Jovanović et. all, 2001):

1. propensity to spend;
2. the theory of the interest rate; and
3. the importance of the marginal efficiency of capital.

The propensity to spend and the propensity to save are essential elements of Keynes' teaching. Income is divided into consumption and savings, whereby people necessarily spend one part of their income, and the other part they save, if they have the means to do so. If we denote income by D , consumption by P , and savings by $[$, then we can express the earlier statement in the form of the following equation: $D =$

$P + I = Y$. From this equation, we can state with certainty that consumption and savings are complementary quantities, i.e. if more is saved, less remains for consumption and vice versa.

According to Keynes, the amount of employment depends on the social effective demand, which in turn depends on the total social (national) income, which depends on the amount of consumption of the population, as well as on the amount of investment, i.e. from the division of social income into consumption and savings, which represents a source for investment (Vujović, Vujović, 2021). Keynes managed to differentiate as many as eight factors (goals) of a subjective nature, which determine the tendency to save, namely (Komazec, Ristić, 1992):

1. creating a reserve for unforeseen cases;
2. providing funds for old age, or taking care of the family;
3. enjoying the interest and the increase in value;
4. provision of opportunities for a gradual increase in consumption;
5. enjoying the feeling of independence and power;
6. provision of reserve capital for speculation;
7. inheritance of property; and
8. satisfying the need for hoarding (hardship).

Without the intervention of the state, it is not possible to ensure the volume of investments, which would lead to full employment, as an unusually important condition for the stabilization of the capitalist system (with the condition that inflation is also prevented at the same time) (Avakumović, et.all, 2021). The decline of the economic activity curve brings unemployment and depression, and the highest level of the upward phase, under conditions of full employment and utilization of production capacities, brings with it inflation. Various non-economic factors, such as optimistic and pessimistic expectations, taxes, etc., affect the variability of the volume of investments. In capitalism, not only entrepreneurs save for investment, but other people also save for completely different reasons, but not only for investments. According to Keynes, savings and investments determine the volume of national income, and therefore the volume of employment. In doing so, it should

be borne in mind that savings depend on income, and that investments depend on various other factors as well (Ivanova, **Ristić**, 2020).

Keynes, therefore, still gives priority to investments and says that only that level of national income (equilibrium level) can be maintained, where the population voluntarily saves, exactly as much as the capitalists would voluntarily invest. Investments lead to an increase or decrease in national income until savings are adjusted to the level of sustainable investments.

2. Basic characteristics of the Keynesian theory

The basic characteristics of Keynes' teaching might be best understood by comparing it with pre-Keynesian economics, which has been done in the literature (Legradić, 1975), in the following four steps:

1. In the pre-Keynesian economy (theory), investments are guided by the propensity to save and there is no independent function of investments (**Nikolić, Tasić, Petrović**, 2022). On the contrary, Keynes emphasizes the primacy of investment decisions and their importance for explaining the level of employment and growth. Investments determine production, which determines savings through a multiplier increase in income (both at the level of less than full employment and at the level of full employment, through a change in the ratio between wages and profits). Capitalists, not savers, are the ones who make investment decisions.

2. In pre-Keynesian economics, there is a separation between the theory of money and the theory of value. Money affects only the absolute level of prices, not the relative prices of goods and services in the economy. Money is demanded exclusively for transactions, and an increase in the money supply affects exclusively the price level. In the Keynesian theory, money is sought as an asset, and interest is determined exclusively by the supply and demand for money due to speculative motives, while the influence of money on prices depends on how interest rates affect the relationship between consumption and production.

3. In pre-Keynesian economics, it is assumed that the aggregate labor market functions like any micro market and that supply and demand are equalized by changes in the price of labor (real wages). Unemployment is voluntary due to workers' refusal to accept a reduction in real wages. Keynes turned the classic driving unemployment into non-driving unemployment, asking if and when workers could determine their real wage, given that they have no control over the price level (unemployment is not necessarily driving).

4. Keynesian economics rejects the idea that the functional distribution of income is determined by a mechanism that ensures that the reward to the factors of production is equal to the marginal productivity, derived from the aggregate production function. This assumes constant returns in a linear production function, because otherwise factor prices would not equal total output (Zekić, Brajković, 2022). An even more important fact is that, since capital goods are heterogeneous, they can only be aggregated when the price, interest or profit is known. Hence, marginal products cannot be produced independently and independently. The Keynesian theory of distribution points to the dependence of profits on the investment decisions of the company and on the propensity to save, which we assume for the holders of wages and profits.

One of the basic shortcomings of the Keynesian theory is the fact that it assumes a closed economy, i.e. ignores the problem of the balance of payments, which is not close to economic reality.

3. Contemporary views of Keynesian theories and a partial critical review

In his article, entitled "The Reincarnation of Keynesian Economics" (Slaveski, 1988), the author, in his commentary on Lucas's article - "The Death of Keynesian Economics", made a very important and we would say correct statement, which is that the announcement of the death of Keynesian economics is premature, to say the least (Bardžić, 2023). It is true, Menkiw says, that Keynes' theory does not inspire

much today, so if it even died in the eighties of the 20th century, it has revived today.

In the same article, the author states that his goal is to approximate the views of the pre-Keynesians and Keynesians and that he would like to try to clarify (consider) six ambiguous (suspicious) claims of Keynes, which he singled out himself and which will not be the subject of interest in this paper.

Many other, well-known and lesser-known authors, wrote about Keynes and his theory, and they all agree at least on one statement, made by Blaug (7), and it reads: that even in the 1930s, and especially not today, one could not speak of a rounded theory, but rather of a group of ideas, which are not uniform in their meaning. This statement was most likely made as a comment on the following Keynes thought: "The ideas of economists, both when they are right and when they are wrong, are far more powerful than they think. Practical people, who believe that they are completely free from intellectual influences, are in fact the slaves of long-dead economists." Blaug expresses his opinion about Keynes's theory, as revolutionary, only to the extent that it (the theory) influenced the creation of economic policy (primarily in the inter-war and post-war period).

One can therefore speak of the Keynesian revolution in the sphere of practical economic action, primarily bearing in mind that the economic science of that time was in a great crisis. Keynes managed to discover important truths about the economic system, above all about the possibility of imbalances. Later (and it is still mostly the case in developed economies today) there was the advancement of the theory of general equilibrium and the introduction of mathematical models, which made it possible to identify and express the causes of imbalances far more precisely than was possible in Keynes' time.

Milton Friedman, in his evaluation of Keynes' theory, points out that despite its great influence, it is nothing more than a failed experiment, whose only merit is that "one ineffective dead end has now been examined and the others will not stray there" (Šoškic, 1985). Basic elements of Keynes' theory: consumption as a passive variable, and domestic investments; the claim that money has a secondary role, that the state should replace the market, and official's citizens, proved to be very harmful, because the state, after the war, started an inflationary

spiral and threatened the competitive position of those economies with its redistributive policy. Although Keynes himself may not have believed that inflation could be reduced below 2%, according to Friedman, it was neglected and subordinated to the needs of real growth in production and employment.

The best assessment of the time of origin and rise of Keynes' theory was given by Kindleberger (Mankiw, 1992): "The depression of 1929 was so long, comprehensive and deep, because the leading powers were neither theoretically nor practically prepared for it. They were theoretically attached to the neoclassical automatism of the gold standard, and practically did not have an intervention mechanism. The British were incapable, and the Americans were unwilling to stabilize world economic flows in the domain of free trade, capital movements and monetary movements". The absence of global coordination led countries to protectionism, which manifested itself on the international level in fluctuating interest rates and stock prices.

According to Corey's opinion, Keynes is a significant (revolutionary) phenomenon in economic theory and politics. He defends his claim with the argument that Keynes made the labor market a function of the aggregate level of production. In addition to employment determined on the product market, depending on the size of effective demand, the same is true of investments and wages. Thus, Keynes' greatest contribution was putting employment in the function of production, which resulted in the linking of investments and factor prices to the desired income.

Conclusion

Keynes's work was (we can also say the rest) the inspiration of many great men of economic thought. Arguments for and against the revolutionary nature of Keynes' theory have often been emphasized. The most frequently used argument against the revolutionary nature of Keynes' theory is that the basis on which the theory is based (effective demand, multiplier, uncertainty, rigidity, imbalance) was known even before Keynes. The biggest argument in favor of the revolutionary

nature of Keynes' theory could perhaps be: the rejection of the quantitative theory of money (Gordon, 1990).

And yet, the author of this work, studying Keynes's work, could not escape the impression, probably not exactly original, that Keynes's theory was to a good extent revolutionary. In support of this, I would like to point out the most important contributions of Keynes' theory (Cicmil, **Jakšić, Đaković**, 2023):

1. Keynes managed to make a turnaround:
 - from micro to macro analysis,
 - from short to long term,
 - from monetary to real aggregates, i
 - from price variations to quantity variations;

2. Keynes proved the hypothesis of aggregate consumption and savings as stable functions of income;
3. Keynes emphasized the separation of savings and investments, which can only be balanced by changes in income;
4. Keynes explained the demand for money with the help of speculative and transactional motive; and
5. Keynes emphasized the determination of real wages by the volume of employment.

Keynesian theory, as a whole, made an immeasurable contribution to the development of economic thought and economic policy (especially at that time). In spite of numerous flaws, which to a good extent remained outside of consideration in this paper, the importance of the work is all the greater, because the possibilities for its modernization and improvement have not been completely exhausted even to this day.

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ОСНОВНЕ КАРАКТЕРИСТИКЕ КЕЈНЗИЈАНСКЕ ТЕОРИЈЕ

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Rezime

Кејнзијанска теорија је добила име по свом оснивачу, Џону Мејнарду Кејнсу (1883-1946), једном од великих мислилаца 20. века. Кејнс је био студент Алфреда Маршала на Универзитету у Кембриџу (где је касније и сам предавао) и његово учење је под извесним Маршаловим утицајем. Аутор је многих економских дела, која су имала за циљ да „спасе капитализам“ и на која су у великој мери утицале друштвене и историјске околности тог времена. Био је изузетно образован и способан да економски анализира и опише стварност и проблеме друштва у којем је живео у кратком временском периоду. Од његових бројних дела, свакако је најзначајније: Општа теорија запослености, камате и новца. У том делу сумира и критикује своја ранија схватања, док развија своју анализу (теорију) у којој идеја ефикасне претраге заузима централно место.

Кључне речи: Кејнс, економска ефикасност, запосленост.

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