

Title; Trying to make sense of the principle of effective demand

Author: Jocken Hardwig, University of St. Gallen

Abstract

The aim of the paper is to shed light on the principle of effective demand. This is necessary because, although every trained economist has probably heard of this principle and somehow “knows” it, the connotations of it are not unanimous amongst the different schools of the economic science. Furthermore, most of the scholarly reinterpretations of the principle of effective demand are not in line with Keynes’s original presentation of it in chapter 3 of the *General Theory*. To substantiate this claim, Keynes’s definition is first reproduced and then compared with different reinterpretations of the principle by mainstream, Neo-Ricardian, Kaleckian, and Post Keynesian economists. As will be shown there are differences between the schools of thought as far as the understanding of the principle of effective demand is concerned, with some scholars coming closer to the original than others. Those who come closest to Keynes’s own presentation are Post Keynesians and adopt the so-called D/Z-diagram, but there are differences even amongst the adherents of this model with no agreement as to how to draw and interpret the two curves of this diagram. It is argued in the paper that this disagreement stems from the fact that Keynes’s own presentation of the principle of effective demand poses some interpretative problems; and these problems are tried to be overcome. To this end it will be necessary to carefully think out the implications of Keynes’s model and to do that in a scheme which distinguishes between the two departments of the economy, the consumption and the investment goods sector.