

The Rudd Government and the Return of Keynesianism¹

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In November 2007 Kevin Rudd led the Labor Party back into office after 11 years of Coalition government. The Howard government had looked increasingly like it was failing to exercise the degree of fiscal discipline required to keep inflation from breaking out after an unprecedented 16 straight years of economic growth. Labor's challenge on assuming office was to achieve that requisite fiscal discipline while not reneging on its election promises — including over \$40 billion worth of scheduled tax cuts over the next four years. Less than twelve months later, inflation was the last thing the government was worrying about as it launched a major stimulus package to stave off the rapidly mounting effects of the global downturn and released revised figures showing that the healthy surplus projected in its first budget was turning into a serious deficit. Not shying away from task, the government made it clear that it wanted people to spend and that it would do what was required to maintain effective demand. After a long absence, Keynesianism was back.

The Rudd government's enthusiastic and determined embrace of Keynesianism re-opens long-running questions about the scope and means for political control of the economy and the capacity for achieving 'full employment' in a capitalist society. Keynesianism is a touchstone of the left and there has always been a popular view that since the mid-1970s the full employment objective has been sacrificed on the altar of 'neo-liberalism': governments choosing to tolerate persistent and sometimes high unemployment when more humane approaches were available. This paper takes issue with that view, arguing that the return of Keynesianism has only been made possible by the unusual convergence of a number of necessary conditions. In doing so, the paper is influenced by Notermans' (2000) argument that parties of the left and their Keynesian policies are much more suited to times that call for macroeconomic stimulation than those where the price stability is the issue. It is important not to overestimate the contribution Keynesianism made to the post-war golden age and nor to underestimate its contribution to the 'great inflation' of the 1970s. Keynesianism emerged in the very particular economic conditions of the 1920s and 1930s and applies in only a highly qualified way to the very different conditions that have obtained since.

Keynesianism and the 'Full Employment' Objective

It is difficult to exaggerate the significance of the Keynesian revolution to politics and public policy. In the relatively short period of time between the end of the First World War and the end of the Second World War, it transformed our expectations of government — inventing the idea of macroeconomic management and making full employment a primary policy goal. The formative event behind this revolution in economic policy was the Great Depression, a downturn distinguished from anything that has occurred since by its depth, its duration and its deflationary character, as well

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as by the very limited degree of social services governments then provided. What created the conditions for a 'revolution' in economic policy was something else on top of the economic conditions: the fact that the Depression was a "disaster of perverse economic policies", policies that reinforced rather than attempting to counteract the downward spiral (Eichengreen and Temin 2003; Eichengreen 1992; Bernanke 1995; Hall and Ferguson 1998; Kindleberger 1986; Schedvin 1970). In today's language, those policies were 'pro-cyclical' rather than 'counter-cyclical'.

While varying in its severity across countries, the Depression afflicted all the developed economies; it has been described as "an economic catastrophe of the first order" and "the dominating economic event in Australia" of the twentieth century (Valentine 1987:61). Highlighting a more general contrast between that time and this, economist Robert Lucas (2000:159) has made the observation that "economic growth in the second half of the 20th century has been so different from any earlier period in history that anyone educated in the 1950s has been led to a new view of the world economy simply by watching events unfold".

Economics of the free lunch

Put most simply, Keynesianism is the predisposition toward counter-cyclical rather than pro-cyclical economic policy. More specifically, this paper will take Keynesianism to be the view that 1.) markets are not self-equilibrating and in particular are inherently prone to periods of involuntary unemployment; 2) this involuntary unemployment is often caused by insufficient effective demand to stimulate adequate levels of investment and employment; 3) through their influence on effective demand governments have both the capacity and the responsibility to moderate the extremes of the business cycle so as to maintain full employment; 4) fiscal policy is the most powerful instrument for stimulating demand; 5) thanks in part to the 'multiplier' and 'pump priming' effects, budget deficits generated by stimulatory fiscal policy are not to be feared; and 6) there is a psychological component to economic behaviour that increases the returns to policies of economic stimulus.

With the exception of point 6, this account equates closely to what Coddington (1976:1264) labelled "hydraulic Keynesianism", that is, the image dominant in post-war macroeconomics of the economy as a network of flows with given characteristics whose rates and levels can be regulated by government. More colloquially still, this is the so-called "free-lunch Keynesianism", meaning that it postulates a win-win-win result for workers, businesses and the public purse through a virtuous circle of demand stimulation → investment → employment → increased effective demand → further investment, etc, that pays for itself through reduced need for welfare spending and increased flow of tax revenues. While economics is generally seen as being all about explaining how everything has a cost, says Paul Krugman (2008:191), "Depression economics ... is the study of situations where there *is* a free lunch". For Keynes, the preferred way of injecting the desired fiscal stimulus was to initiate large programs of public capital investment since they would yield what the OECD (2009) today terms a "double dividend" of short term cyclical, and long-term structural, benefit.

The Keynesian Consensus

The victory of Keynesianism was, if not total, certainly rapid and extensive. What had been a number of provocative proposals in the 1920s and early thirties, and became a manifesto with the publication of Keynes's (1936) *General Theory*, "had more or less established itself as the new orthodoxy" by 1945 (Bleaney 1985:83).

The acceptance of Keynesianism represented a major watershed in Australian public policy as it did elsewhere. It was officially signalled by the release of the Labor government's 1945 White Paper *Full Employment in Australia*, a policy statement that followed the British lead and had Canadian and American equivalents.² The White Paper's first pronouncement was that "Full employment is a fundamental aim of the Commonwealth Government". Following Keynes's emphasis on the demand side, it also declared that "governments should accept the responsibility for stimulating spending on goods and services to the extent necessary to sustain full employment". And, again following Keynes, it singled-out infrastructure spending as the most expedient way to boost effective demand. "Public capital expenditure is the principal type of expenditure that can be readily varied to offset variation in the unstable parts of expenditure." Of course capital expenditure is actually not quite so 'readily' variable, and this was acknowledged: "Careful and detailed advance preparation will be required if public capital expenditure is to play a significant part in our development".

On the risk side, the White Paper also acknowledged the danger of "unstable public finances" and the need to "ensure...that undue sectional pressure for wage increases does not lead merely to a rising spiral of wages and prices without any real benefit — and perhaps with disadvantage — to the workers themselves". Governments would have to keep public spending within bounds and build in mechanisms for controlling inflation.

What's in a name? Keynesian and the Left

Notwithstanding the fact that Keynes's "patrician liberalism" (Pierson 2001:40) had no time for many of the core elements of social democracy, there has always been a decided affinity between Keynesianism and social democratic politics and policy. While some prominent exercises in Left Keynesianism — the Blum government in 1930s France and the Mitterrand government in 1980s France most notably — have been anything but successful, the affinity is strong. Arguably, it was Keynesianism that made social democracy viable: provided a way to square the circle of social reform in a capitalist economy by giving government responsibility for macroeconomic management and justifying progressive taxation, public spending and redistribution. Keynesianism thereby obviated the need for socialisation of the means of production (Holland 1977; also Whyman 2006:55).

We would thus expect to find parties of the left far more likely to take an actively Keynesian approach to economic management than parties of the right, favouring full employment over price stability. Workers are most concerned about their jobs, the middle class about their savings. As Andrew Glyn (1998:2) puts it, "Maintaining full employment has been the centrepiece of social democratic programmes since the 1930s". The classical reference along these lines is Hibbs (1977), who advanced a two-fold proposition: first, as an economic fact, that the working class not only perceives itself as being best-served by low-unemployment/high inflation policies *but is in actual fact* best-served by such policies; and second, as a political fact, that left-wing parties govern accordingly. While this analysis has been supported by others (e.g., Cusack 2001; Hall 1989:376), more recent research suggests that it is much truer of Hibbs's period — the 1960s and 1970s — than

² The British White Paper, *Employment Policy*, of 1944; the Canadian White Paper, *Employment and Income*, of 1945; and the US *Full Employment Act* of 1946. The American statement was the only one to assume any formal or legal standing; the others remained merely White Papers. That said, the American commitment to Keynesianism in the *Full Employment Act* was considerably watered down by the successful demands of business.

it is of the 1980s and 1990s. After the disaster of loose fiscal and monetary policy in the 1970s, argues Sakamoto (2008), parties of the left came under pressure to reform their ways and became as — or indeed more — fiscally responsible than parties of the right, delivering improved economic outcomes as a result. Significant convergence has occurred.

Does this mean that parties of the left have forsaken their Keynesianism and their commitment to full employment? Critics of Britain's 'New Labour' have argued that it does (e.g., Arestis and Sawyer 2001; Hay 2004, 2007; Whyman 2006). They accuse Labour of having abandoned the Keynesian emphasis on counter-cyclical fiscal policy by transferring primary responsibility to monetary policy and committing to balanced budgets over the cycle. In Whyman's (2006:220) view, this must be reversed: "The revitalisation and evolution of Keynesian macroeconomic strategy is quite simply a prerequisite for a successful progressive–social democratic approach to economics."

The alternative interpretation is much kinder to 'third way' economics, arguing in essence that Keynesianism takes a form relevant to the circumstances in which it is being applied (e.g., Clift and Tomlinson 2007) and that squaring the circle is not as easy as it first sounded. Keynesianism operates, like most other things, in a constrained world.

Constraint factors

Five factors potentially limiting the capacity of governments to operate Keynesian economic policy are of particular relevance to this paper: inflationary tendencies; the need for timeliness; fiscal impact; cyclical asymmetry; and the external economy. It is necessary to highlight a few points about each.

Cautionary note: inflation

The most intrinsic potential constraint on Keynesianism is inflation. There were those who sounded a cautionary note about Keynesian's magic pudding in this regard from the outset. From a Marxist perspective, Keynesianism represents another instance of *naïveté* about the easy reconciliation of the conflict between capital and labour. Much cited in this regard is the political economy analysis of Michał Kalecki. In a 1943 article, Kalecki argued that business would not accept Keynesian demand management because it would diminish their political influence over public policy and diminish their workplace authority over labour. With much greater control over the economy, governments would be much less likely to fear loss of 'business confidence', and in the workplace "the 'sack' would cease to play its role as a disciplinary measure" (Kalecki 1943/1990:351).

In a 1944 article Kalecki put aside the view that Keynesianism would be *politically* infeasible and argued instead that over the longer run it would be *economically* infeasible: full employment is another one of those things that is too good to be true. In the full employment economy's tight labour market the bargaining power of workers "will be very strongly enhanced" and wage pressures will mount. If wage increases are allowed to outstrip productivity increases, inflation will result and workers' gains will be for nought (Kalecki 1944). These observations tilted the balance back from Keynes's focus on the failings of the financial sector to the real economy: "Workers and manufacturers had only walk-on parts in Keynes's play" (Skidelsky 1979:61).

Given the inevitability of inflationary pressures, Kalecki (1944/1990:362) concluded that under full employment "arrangements must be made to prevent prices running away". Those 'arrangements'

would take the form of a system of wage and price controls. The sceptical response to such a program was articulated by F. W. Paish (1958), who agreed that full employment inevitably invited employers to bid up the nominal price of labour, but conjectured that the kind of controls contemplated would require “powers of enforcement more severe than would be tolerated in a free country”. Perhaps it is not surprising that Keynesianism’s greatest success in the 1930s was in Nazi Germany, where labour was completely subordinated to the state (Bleaney 1985:70). The inflationary pressure of full employment seemed to be empirically confirmed by Phillips’s (1958) famous study of British wage rates and employment levels. A century’s worth of data reveal, he advised, “a clear tendency for the rate of change of money wages to be high when unemployment is low and to be low or negative when unemployment is high” (Phillips 1958:290).

It is easy to conclude that Keynes was cavalier about inflation and it was this indifference that gave Keynesianism its inflationary bias, but this seems not to be the case. Keynes was no less concerned about inflation than anyone; indeed, he regarded it as a great evil. His campaign for policies to stimulate demand and inflate prices entirely reflected the overwhelming deflationary nature of the context within which he struggled to reform economic policy. Nothing in the last seventy years even approximates the conditions of those times where a process of economic implosion seemed to be occurring as prices declined over time and output followed suit. The great contrast between interwar conditions and those prevailing ever since is partially obscured by use of the term ‘deflation’ or ‘deflationary’ to describe policies directed at reducing the inflation rate (e.g., Bell 2004:37-39). Disinflationary policies are fundamentally different from deflationary ones and Australia has not experienced deflation since 1932 or deflationary policies since the Premiers’ Plan. It is also worth remembering that Keynes’s (1972a) one sustained piece of explicit policy analysis was entirely focused on how to keep a lid on the inflationary tendencies that would inevitably threaten the British economy in the impending war. To maintain wartime price stability, Keynes recommended a systematic program of forced savings or “deferred consumption” for the population at large.

One strand of Keynesian thinking maintains that full employment and price stability can be reconciled through less draconian arrangements than those of Nazi Germany, ones built on a social democratic commitment to wage and price restraint. In reality, the success of such arrangements is dependent on a reasonably unlikely number of economic, political and organisational conditions being met. Approximations to such arrangements, such as those practised in Australia through the ‘Accord’ in the 1980s, tend to be criticised those on the Left for their tendency to work *too* well in keeping wages down (e.g., Battin 1997:110)

Timing is everything

Keynesian economics took shape in a period when timing was scarcely an issue. The tragedy of the interwar period was the sheer persistence of the slump. In both Britain and (as a consequence), Australia, the economy had already been in a deflationary recession *before* the Great Depression even struck in late 1929. Similarly, the Second World War confronted governments with a challenge of economic management that, although the reverse of the interwar period, was similar in its constancy. For much of the period since the end of the war, the ambitions of Keynesians has been the very different one of moderating short-run cyclical fluctuations in growth rates — sharp rises or falls that last eighteen months or less. This was ‘fine tuning’ — rapid, relatively minor adjustments to monetary and fiscal policy that would anticipate those annual movements. It required a

timeliness and calibration well beyond anything Keynes contemplated. Uncertainty is one of the major sources of difficulty for fine tuning, with modern economic management dependent on reliable forecasts of economic conditions in the immediate future. Australian economist R. I. Downing (1956:279) seemed to be providing a pessimistic answer to his question ‘is an economic policy possible?’ when he commented that “predicting the future is impossible”. The other difficulty arises from the tendency of counter-cyclical measures to lag too far behind the cycle, taking effect either when they are no longer needed or, worse yet, when they have become damagingly pro-cyclical. This is clearly a risk greatest in periods such as the post-war years characterised by short business cycles. On top of the delay involved in recognising the need for a stimulus, lagging occurs as a result of internal delays as policies are activated and external delays as they are implemented and take effect — “decision lags” and “implementation lags” (Blanchard and Perotti 2002). Contemporary proponents of traditional Keynesianism such as Arestis and Sawyer (2003) recognise these risks but insist they are manageable.

Cautionary note: deficits and debt

Keynes sought, above all, to liberate economic policy from the perversely pro-cyclical balanced budget orthodoxy that required governments to cut spending and/or raise taxes to restore public finances in an economic depression. The ‘test’ of Keynesianism in the popular mind thus is the government’s willingness to engage in deficit spending. The thrust of Keynes’ argument was that deficit spending would be self-solving; he did not seek to defend deficits as general policy. It is possible to see Keynes as having been as cavalier about deficits as he seemed to be about inflation given his famous disregard for Victorian virtues of self-restraint and frugality. The impression that Keynesianism is cavalier about deficits has mixed validity. Contributing to the great success of the Swedish Social Democrats in deficit spending was the way they anticipated this objection from the outset — crafting their fiscal framework in a way explicitly directed to returning the budget to balance. For leading Swedish Social Democratic economist Gunnar Myrdal (1939:107), this was a point of great importance. “The chief problem of fiscal policy in the business cycle”, he argued, is “to design formulas for public finance which, as part of the regular system, make room for deficit spending during depressions by securing the building of corresponding surpluses in good years.” This is fundamentally different from the extreme “functional finance” (Lerner 1943) version of Keynesian that sees maintaining full employment as the sole appropriate criterion of fiscal policy. Myrdal (1939:193) also acknowledged that ‘making room’ for counter-cyclical fiscal policy is easier said than done; balancing deficits with surpluses “assumes normal business cycles with good times alternating with the bad ones”.

Cyclical asymmetries

Contributing to both the inflation and the fiscal balance problems is the tendency toward asymmetry in Keynesian counter-cyclical policy making. Logically we would expect the electoral–political pressures to address problems of economic contraction to be stronger than those to address problems of economic expansion. Raising taxes and curtailing spending at the peak of the cycle when the government is already enjoying a strong budgetary position does not make for the most attractive campaign platform and leaves any party in a clear position to be outbid. However, it may be exactly what is optimal for demand-management and fiscal consolidation reasons. An independent central bank utilising monetary policy to compensate for inadequate fiscal resolve may provide some macroeconomic counterweight.

Cautionary note: the external constraint

Much contemporary scepticism about a Keynesian approach to economic policy emphasises the constraints imposed by 'globalisation': counter-cyclical demand management depends on a degree of national economic autonomy that no longer exists. This may represent an accentuation of realities that have always imposed limits on Keynesianism. Trading nations are dependent, first of all, on income earned from export to buyers over whom domestic policy has no influence. Secondly, trading nations face the reality a boost in domestic effective demand will translate into a boost in imports.

Even though Australia's is not as 'open' economy in terms of its trade profile as many,³ it is generally regarded that Australia's room to manoeuvre economically is severely limited by the international context. Valentine (1987:76) concludes, for instance, that the Great Depression in Australia "was almost completely imported" — with a collapse in export prices pulling the rug out from under the Australian economy. Both wage and government debt levels were too high, but the fundamental problem was loss of export earnings. More generally, "data on economic outcomes and policy responses suggests", argues Gregory (1991:111), "that world economic influences are pervasive" in Australia. Macfarlane (2005:2) declares similarly. The French socialists' experiment with economic stimulation in 1982 seemed to demonstrate rather clearly that 'Keynesianism in one country' — other than in a large economy such as the United States with a very small trade exposure — is doomed to fail.

Bring Back the Golden Age

For a number of commentators (Battin 1997; Bell 2000; Dow 2008; Nevile 2000), the question has been why have we waited until now to restore Keynesianism to its rightful place in macro-economic policy making? In their view, Keynesian demand management techniques have been abandoned in favour of an inhumane 'neoliberalism' that has sacrificed workers' livelihoods on the altar of price stability or fiscal rectitude. The crux of this argument lies in the proposition that there has been, in Stephen Bell's (2000:2-3) words, "a major re-orientation away from the postwar commitment to full employment". Either explicitly or implicitly, this re-orientation is interpreted as representing a distinctly *political choice*, not one driven by or reflecting economic imperatives. Battin (1997:8) claims that "a reliance on economics alone to explain something like the shift away from Keynesianism is a barren enterprise".

For the then-Governor of the Reserve Bank, Ian Macfarlane (1997), harking back to the Keynesian golden age of capitalism is the "economics of nostalgia". His criticisms of the universalist interpretation of economic policy history are twofold: only very moderate use was made of discretionary fiscal policy in the post-war period, and the undeniably extraordinary economic performance of the period was the outcome of underlying economic forces. From a different position on the ideological spectrum, Andrew Glyn (1995) judged similarly. "It is doubtful that 'free lunch Keynesianism...was ever very important in accounting for post-war full-employment.'" Presumably Keynesianism played some positive role in the post-war boom — at the very least by its

³ Lane and Ersson (2002:11) define an open economy as one where imports plus exports "constitute about 50 per cent of the GDP". Only in the past decade and a half has Australia begun to push towards that level.

impact on expectations and hence consumption and investment decisions (Boltho 1989; also Nevile 2000); however, this was made possible by the underlying economic vigour.

The overwhelming feature of the post-war experience is the way that economic vigour caught economists and policy makers by surprise. Planning for Keynesian solutions to a post-war slump had to be quickly readjusted for exactly the opposite (Whitwell 1986:83). Immediately the limitations of Keynesianism started to become evident, first of all in the public works program. The kind of massive infrastructure investments that were to form the centrepiece of counter-cyclical policy could not be delayed and would be unavoidably and dangerously pro-cyclical (Whitwell 1986:90-95).

What about short-term cyclical management? Under such benign conditions there is good reason to expect 'fine tuning' to have been a contributing factor to general economic welfare. That even this was the case, however, is not so clear. According to Whitwell (1986:104-7), the first instance in Australia of a deliberately and openly Keynesian counter-cyclical intervention was the budget of 1951, brought down to cool a rapidly overheating economy and reduce inflationary pressures. But the budget came too late to have the desired effect, instead exacerbating a very sharp downturn that was already underway. Similarly, according to Whitwell (1986:134), the failure of the mildly disinflationary budget of early 1961 to have much effect led to additional measures a few months later whose "effect on economic activity was abrupt and considerable and ushered in a recession which persisted well into 1962".

In both instances, at least two constraints seemed to have been at work militating against counter-cyclical demand management. One reason for the failure of Keynesian techniques in this instance was self-imposed: the over-reliance on fiscal policy. Committed to a policy of cheap money, the government had foreclosed the option of using contractionary monetary policy earlier in the cycle to pre-empt the extremes (Whitwell 1986:105; Rowse 2002:232-230; Bell 2004:15). The other was an inherent limitation of economic management. This was the difficulty of have a sufficiently timely response to changes economic conditions. "'Fine tuning' is a marvellously evocative phrase" said Milton Friedman (1968:3), "but it has little resemblance to what is possible in practice". Utterly unlike the Great Depression, all subsequent downturns in the twentieth century were short, sharp downturns. They were extremely brief, and could easily not be fully registered in the typical indices until they were half over. The nimbleness required of macroeconomic fiscal policy by such short time frames completely rules out the dominant technique of Keynesianism — capital works programs, whose long lead times (even if 'off the shelf' in some sense) and long 'tail' mean they would inevitably have their impact far too late.

Milton Friedman was, of course, ideologically ill-disposed to tuning at all, fine or not. However, these conclusions are also consistent with those arrived at from the other side of the political divide by Gunnar Myrdal (1939:187) who judged that "fiscal policy is rather a clumsy instrument in crisis policy when utilized as the mobile factor in fighting against depressive forces which change from month to month and from week to week". As John B. Taylor (2000:27) has noted, monetary policy enjoys a distinct "comparative advantage over fiscal policy" in these regards. "Experience has shown that the implementation lags are much shorter for monetary policy"; and, in addition, monetary policy decisions are much easier to reverse.

Stagflation and the death of Keynesianism?

The prevailing interpretation of the 1970s experience is that it killed Keynesianism as an intellectual framework and policy guide. The extreme version of this thesis comes from Lucas and Sargent (1979). Keynesian “macroeconomic models were subjected to a decisive test in the 1970s” and not only did they have no answer to the stagflation problem, but the “inflationary bias” of Keynesian policy advice exacerbated or even perhaps caused the problem in the first place. “For policy”, they conclude, “the central fact is that Keynesian policy recommendations have no sounder basis, in a scientific sense, than recommendations of non-Keynesian economists or, for that matter, noneconomists.” While such a blanket dismissal is extreme, a number of sources support the finding that the ‘Great Inflation’ in the US was fuelled by loose monetary policy (DeLong 1997; Mayer 1998) that resulted from a Keynesian predisposition against contractionary measures burned into the minds of a generation of economists and policy makers by the experience of the Great Depression.

Defeating inflation

What opposition there was to Keynesianism in the golden age came from the ‘monetarists’ — those who argued that the most important factor in maintaining economic stability was monetary stability. In this view, countercyclical fiscal policy would be ineffectual or insidiously dangerous. In his 1968 Presidential Address to the American Economic Association, Friedman (1968) warned that it is naïve to think that a modest dose of inflation can be applied to lift output and employment in a sustained way. Once unleashed, inflation becomes a self-fulfilling prophecy thanks to the embedding of inflationary expectations. Worse yet, monetary policy has asymmetric potency: while loose monetary policy can unleash an inflationary spiral, it takes stronger measures to restore stability. As Friedman (1968:15) put it, “the potentiality of monetary policy in offsetting other forces making for instability is far more limited than is commonly believed”.

Monetarism was adopted early, consensually and undisruptively in Germany, later and more savagely in the United States. In both cases, it was highly effective (Johnson 1998). One comparative study of the Australian experience argues that Australia’s poor record on inflation in the 1980s reflected governmental failure to embrace monetarism and impose sufficiently contractionary monetary policy (Nelson 2005). The Accord was expected to do the job, but its main objective and achievement was to increase growth and employment instead (see also Bell 2004:39-54). It was not until the recession of 1990 had made its mark that Australia joined the low-inflation club. One criticism of the Accord is that it made workers’ pay the price of economic recovery, engineering “an unprecedented transfer of national income away from wage earners to business” (Bell 1992:196). However, this re-adjustment must be seen against the backdrop of the “exceptional” transfer of national income share away from business to labour in the 1970s (Dowrick 1991:126). Real wage increases well above the rate of productivity increase cannot have been economically sustainable — contributing, presumably, to both stagnation and inflation. If Edwards (2006:31-2) is correct, the Accord’s achievements in this respect were still insufficient and it took the recession of 1990 to really bring real wages back to non-inflationary levels.

While its extreme version, or what Bradford DeLong (2000) calls “political monetarism”, disproved itself in application, the main message of “classical monetarism” has been absorbed into mainstream economic thinking and the practice of economic policy making. In US Federal Reserve Chairman Ben Bernanke’s (2003) words “Friedman’s monetary framework has been so influential that, in its broad

outlines at least, it has nearly become identical with modern monetary theory and practice.” This applies equally to Australia, where the Reserve Bank finally adopted a coherent and determined inflation targeting regime when the opportunity arose in the aftermath of the 1990 recession (Bell 2004).

Keynesianism and price stability

There is no doubt about the ‘inflation bias’ of Keynesianism. Keynesians make clear their view that solving the unemployment problem should not be compromised by concerns about price stability. This has little to do with the views of Keynes himself, who was very clear that price stability was a *sine qua non*. It is easy to forget that he presented his case of demand-side stimulation in an era of chronic deflation and generally ‘morbid’ expectations about the future (Overly 2009). By the time the Great Depression struck, the UK had already suffered through almost a decade of economic stagnation, policy-encouraged deflation and high unemployment. Keynes’s (1939/1972a) only substantial work outlining economic policy strategy was his program for containing inflation in the war economy by means of forcibly deferred consumption.

But enforcing price stability in wartime is rather different from maintaining in peacetime. The fallacy of the so-called Phillips curve lay in the inference drawn that policy makers could simply trade off a little bit of inflation for a bit more employment in the hydraulic engineering sort of a way. Friedman’s (1968) objection to this was controversial at the time but prescient and largely seems like commonsense now: inflation breeds inflation through the effects on behaviour generated by expectations. Real-world Keynesianism is constrained by the pressures that Kalecki and others identified. Under inflation is brought under control, there is little scope for stimulatory fiscal policy.

The new balanced budget consensus

One of the touchstones of current economic policy consensus is the commitment to ‘balancing the budget over the economic cycle’. This was made policy in Australia by the Coalition government when they took office in 1996 (Treasury 1996).⁴ It was made policy in the UK by the Labour government when they took office in 1997. Does it represent a derogation from Keynesianism? Some critics of UK Labour’s so-called ‘third way’ have answered yes (Arestis and Sawyer 2001; Hay 2004), but it is difficult to be sympathetic to such criticisms. The conditions that prevailed from the mid-1970s to the mid-1990s represented precisely the eventuality that Myrdal was flagging. OECD countries have struggled to eliminate deficits, let alone accumulate the “corresponding surpluses” that Myrdal called for. Even in Australia, which has maintained a much stronger record than most OECD countries in this regard, conservative parties have successfully made deficits and the corresponding accumulation of debt a political issue.

A more serious criticism of ‘balancing over the cycle’ has been raised from a free-market liberal perspective (Buchanan and Wagner 1977:148): how can one possibly know what constitutes ‘the cycle’? The term itself is misleading since it carries a connotation of smooth regularity that bears

⁴ “The Government’s medium term fiscal strategy is to follow, as a guiding principle, the objective of maintaining an underlying balance on average over the course of the economic cycle. This approach will ensure that over time the Commonwealth budget makes no overall call on private sector saving and does not detract from national saving; it will provide the Government with the flexibility to allow fiscal settings to change in response to economic conditions over the course of the cycle and to respond to external shocks.”

little relationship to reality. Did the Howard government balance the budget over the cycle? The answer to that question would depend on where one saw the cycle beginning and ending.

Boom to Bust: the Rudd Government and the global recession

Fighting inflation at first

The economic challenge facing the Rudd government when it was elected in November 2007 was inflation. After an unprecedented sixteen years of economic growth, culminating in the minerals boom also unprecedented in its duration, the economy was operating at full capacity in many sectors, unemployment rates had reached lows not experienced since the 1960s, and the CPI was trending upwards. In Treasury's view, the economy had probably reached the NAIRU where any further reduction of unemployment would lift inflation unless considerable investment was made in upskilling the remaining unemployed (Kennedy et al. 2008). By the time the election was called the Reserve Bank had already raised the cash rate nine times since 2002 (from a low of 4.25% to 6.5%). Few things could have signalled the depth of concern about an overheating economy more than the Reserve Bank's also unprecedented decision to initiate another rise in the midst of the election campaign — a move that could only be interpreted as an adverse judgement on the economic credentials of the Howard government and more specifically on the looseness of fiscal policy under the Coalition. While the government was going into the election with a respectable budgetary surplus of \$14.4bn or 1.3 per cent of GDP and very comfortable growth forecasts (Secretary to the Treasury and Secretary to the Department of Finance and Administration 2007), the surplus was modest in its context and the electorally-driven spending commitments seemed by contrast anything but. According to subsequent Treasury analysis, real spending growth in the last terms of the Howard government was extremely high, indeed unprecedentedly so — a "particularly noteworthy" fact given the full capacity conditions that were prevailing (Laurie and McDonald 2008:30).

Inflation thus continued to be the over-riding concern as the Rudd government crafted its first budget in early 2008. National Accounts and CPI figures for the December 2007 and March 2008 quarters showed continuing strong GDP growth and accelerating rates of inflation. By this time the 'Global Financial Crisis' was well underway but having little direct effect on Australia. In February the RBA raised the cash rate another 25 basis points and in March it raised the rate again. After 12 consecutive rises over seven years, the cash rate was now 7.25 per cent. The IMF's 2008 World Economic Report warned of a global slowdown, but still forecast a 3.8 per cent increase in GDP in 2009, saw Australia as being particularly well situated, and continued its emphasis on vigilance against inflation.

Thus the 2008–09 Budget was crafted to be disinflationary yet pro-growth. The government sought to finance its election promises out of spending cuts and ensure that "all tax receipt windfalls since the election" would be quarantined to "deliver a budget surplus of 1.8 per cent of GDP, up from the 1.2 per cent surplus forecast in the Pre-Election Economic and Fiscal Outlook 2007" (Treasury 2008). A surplus of 1.8 per cent of GDP would be the biggest in almost a decade. Of course, the Budget could not really claim to 'deliver' such results, only project them; what it actually delivered would only be known in 15 months time.

How legitimate it was for the Commonwealth to be collecting more revenue than it needed given that all debt had been paid off and pension liabilities covered through the Future Fund had been a matter of public debate for some years. Pressure for the surplus to be returned via tax cuts had been building from the business side. The Labor Party view had been that the Commonwealth was under-investing in economic infrastructure, an under-investment that was being exposed by the minerals boom. The 2008–09 Budget implemented Labor’s agenda by directing the surplus into three capital investment funds: one for infrastructure, one for education and one for health. This followed the Coalition’s lead in establishing the Future Fund and, more recently, the Education Endowment Fund. Of the 2007–08 Budget’s final \$19.7 billion surplus, \$7.5 billion was deposited into the first of these, the Building Australia Fund, \$2.5 billion into the education fund, and \$5 billion into the new health fund.

Towards the crisis

In early October the IMF issued its second 2008 *World Economic Outlook*, revising its assessments downward to describe conditions as a “major downturn” where the “major advanced economies are already in or close to recession” (IMF 2008b). It was also becoming clear that Australia was being dragged down as well. At this point, the Rudd government launched its first Keynesian stimulus: a \$10.4 billion ‘Economic Security Strategy’ revolving around payments to the less well off and subsidies for first-time home buyers (Rudd and Swan 2008). The Mid-Year Economic and Fiscal Outlook reported that “the Budget has felt the full force of the global financial crisis”, with tax revenues “expected to be around \$40 billion lower” than estimated in the Budget. Nonetheless, at this point Treasury was “continuing to budget for surpluses in 2008–09 and across the forward estimates” (Swan and Tanner 2008). Any concern that the government might be jumping the gun was soon allayed when the IMF issued an update subtitled “rapidly weakening prospects call for new policy stimulus”(IMF 2008a). Downgrading its October assessment significantly, the IMF announced that output across the advanced economies would fall in 2009, “the first such fall in the post-war period”. By 8 December, the Treasurer was able to announce that the economic stimulus payments were now flowing through to recipients (Swan 2008).

In tandem, the Reserve Bank began cutting interest rates, bringing them down 25 basis points in September; a full one per cent in October; 75 basis points in November; and another whole percent in December. Australian fiscal and monetary settings had turned, in unison, from disinflationary to stimulatory in the space of only a few months.

Escalation

Only weeks after the government announced its \$10 bn stimulus package, the IMF had issued another ‘update’, “drastically revising down its forecast for the world economy” and calling for new stimulus measures (Swan 2009a). The Rudd government responded with alacrity, announcing a second stimulus package four times the size of its 2008 initiative on 3 February 2009. This time, greater emphasis was placed on funding infrastructure improvements (notably schools and roads) rather than simply cash transfers to individuals. At the same time, the government announced that with the drastic reduction of revenues resulting from the downturn, the Budget was moving heavily into deficit — a situation the government was quick to affirm did not lessen its “commitment to deliver budget surpluses, on average, over the course of the economic cycle”. Once economic growth resumed, fiscal repair would get underway by “holding real spending growth to 2 per cent a year” (Swan 2009b).

Release of the December quarter National Accounts a few weeks later confirmed that Australia was heading into recession, with GDP having contracted by 0.5 per cent. Although the situation was unlikely to have improved in the intervening period — indeed, was overwhelmingly likely to have worsened — the government avoided any mention of the ‘r’ word at this time. Inflation, meanwhile, had predictably fallen, but not dramatically so.

The recession budget

The 2009–10 Budget brought down by the Rudd government on 12 May could scarcely have been more different from the government’s budget of a year earlier. The \$21.7 bn surplus (1.8 per cent of GDP) the government’s first Budget was ‘delivering’ had turned into a \$32 bn (2.7 per cent of GDP) deficit — a \$53 bn fall in 12 months. And that was only the beginning. The 2009–10 shortfall was projected to be \$57.6 billion, continuing into the year following. In large part, this budgetary reversal was the result of a collapse in tax receipts, revenues projected to be down by \$23bn in 2008–09 and \$49bn in 2009–10. At 4.9 per cent of GDP, the Budget was projecting a record deficit, one substantially larger than the Keating deficit at its peak of 4.0 per cent; and at 28.6 per cent of GDP the Budget was projecting a record level of Commonwealth spending (Treasury 2009).

Maintaining a credible fiscal policy

Again, the government was determined that this should not look like fiscal irresponsibility. Consistent with IMF recommendations, the deficit spending was accompanied by a program for deficit reduction. By 2015–16, the government declared, the Budget would be back in surplus. But of course such comforting projections are entirely dependent upon parameter assumptions — and this is where the controversy lay. Critics seized upon the assumption of 4.5 per cent GDP growth in the third and fourth years of the forward estimates to argue that the fiscal recovery program was complete fantasy. Assuming such a rapid turn-around in economic fortunes was not only highly optimistic, they argued, but also at odds with what the IMF was estimating.

Quintessential Keynesianism: the public works program

One of the criticisms of the initial stimulus package had been that it represented a frivolous hand-out, money wasted. Reports that shops were back ordered on imported flat screen TVs following the hand-out certainly suggested that the multiplier effect of the resulting burst of consumer spending would be minimal. As Keynes (1972b/1931:138) put it, people must be buying “home-produced goods if they are to increase employment in this country”. Keynes’s real preference was for a large-scale public works program that would deliver a triple dividend of immediate employment; short-term demand stimulus; and a longer-term legacy of better infrastructure. Capital investment was the cornerstone of Keynesianism as conceptualised in the 1945 White Paper; and more recently there have been calls to reverse the trend towards pro- rather than counter-cyclical public works spending by reviving the notion of an ongoing ‘ready shelf’ of capital works proposals (Hughes 2001).

The Budget confirmed that the government’s strategy was now to focus on infrastructure spending. This was consistent with the message coming from both the OECD (2009) and the IMF: certain forms of deficit spending will deliver a “double dividend” by stimulating recovery in the short term while also providing growth-enhancing capital assets for the longer term. As Myrdal (1939:185) put it, “there are ... important, purely fiscal reasons for concentrating public expenditure in the years when costs are low”. And as Australia’s experience has illustrated at certain points, there are good macro-

economic reasons for not concentrating them in the years when they will be straining capacity. \$22 bn was committed over four years to a range of capital works projects.

Rebirth of Keynesianism?

As is inevitably the case since the rise of the welfare state, a good part of the 2009–10 Budget's stimulatory deficit derived automatically from the downturn's widening scissors effect of declining tax take and rising transfer payments. Indeed, the *Budget Papers* estimate that fully two-thirds to three-quarters of the "deterioration in the budget position" is to be accounted for this way (Treasury 2009). Thanks to the 'automatic stabilisers', any modern budget is a Keynesian budget under these circumstances unless governments take deliberate action to neutralise or moderate their effects (van den Noord 2000; also Darby and Melitz 2008). In addition to being Keynesian in a passive sense, the Rudd government has engaged since late 2008 in active Keynesianism — the explicit and avowed use of discretionary fiscal policy for counter-cyclical demand management. This corresponds very conveniently to the ideological orientation of a party of the left, but, more importantly, it is made possible by the coincidence of a number of key conditions for the first time in over a generation. Keynesian policies are back because of a confluence of developments at the level of theory, in the fiscal position of government, and in the nature of the crisis.

A new Keynesian consensus?

This is the first time since the post-war boom that there has been consensus support for deficit spending. Domestically, this has been most evident in the unusual degree of business support. Both the Business Council of Australia (see BCA 2009), representing large corporates across a range of sectors, and the Australian Industry Group (see Ridout 2009), representing the manufacturing sector, formally endorsed a Keynesian approach. This is consistent with the urgent recommendations of the leading international economic policy bodies, the OECD and the IMF.⁵ Neither institution is noted for a strong belief in governmental activism, but both have pressed the case for aggressive interventionism in this case. Business support has not, of course been unqualified, with the BCA (2009) expressing concern about the tendency of deficit episodes to ratchet up the size of government as governments increase taxation to restore fiscal balance.

A new respectability

Contributing to this consensus is the rehabilitation of Keynesianism within economics. Economic theorists of a neo-classical persuasion had exploited the neglected microeconomic basis of Keynesianism to cast doubt on several of its central assumptions — exploiting the fact that "Keynes did not make any obvious departures from the neoclassical tradition" and "left unclear the relationship between Keynesian and neoclassical theory" (Bleaney 1985:17). Increasingly, though, those weaknesses have been addressed, establishing firmer theoretical bases for the theory's

⁵ As a recent IMF staff paper put it, "The optimal fiscal package should be timely, large, lasting, diversified, contingent, collective, and sustainable: timely, because the need for action is immediate; large, because the current and expected decrease in private demand is exceptionally large; lasting because the downturn will last for some time; diversified because of the unusual degree of uncertainty associated with any single measure; contingent, because the need to reduce the perceived probability of another 'Great Depression' requires a commitment to do more, if needed; collective, since each country that has fiscal space should contribute; and sustainable, so as not to lead to a debt explosion and adverse reactions of financial markets" (Spilimbergo, *et al.* 2008)

originally more intuitive assumptions (Akerlof 2007a; Blinder 1988; Akerlof 2007b; Mankiw 2006, 1992). In the process, the 'New Keynesians' have revised to revive by, among other things, recognising the importance of both fiscal and monetary instruments, taking inflation more seriously, and being more cautious about the possibilities of stabilisation policy.

The return of Keynesian economic pre-conditions

This is the first major downturn since a low-inflation environment was restored in the early 1990s. It is possible to reflate without reigniting inflation. And unlike the last three recessions, this downturn was not triggered by high interest rates; thus, low interest rates are unlikely to suffice for recovery (Feldstein 2009:3). Moreover, the difficulty presented by decision and implementation lags is much less of a problem in the current circumstances. "The delays in starting infrastructure projects and the long tail in that spending are not likely to be as much of a problem now because the current downturn is likely to last much longer than previous ones. ... Once the recovery begins, the upturn will be very slow because households need to increase their saving", comments Feldstein (2009:6) apropos of the American situation.

While Keynesianism entails use of either or both monetary and fiscal instruments, it has a closer identification with the more contentious of those two tools, fiscal policy. This is largely because Keynes himself was writing of a situation where the utility of monetary instruments had been exhausted (Akerlof 2007b: 6). The 1970s crisis of Keynesian represented the opposite, a situation where fiscal instruments had been exhausted, and thus the preference over the next period was to require a more neutral role for fiscal policy and use interest rates as the main tuning mechanism. With the 'death of inflation' in the 1990s, economists have put the more traditionally Keynesian focus on fiscal policy back on the agenda. They advocate a judicious use of counter-cyclical budgeting, noting that "with interest rates at their lower bound of zero, there is no plausible alternative" (Allsopp and Vines 2005:485; also Krugman 2005).

The return of Keynesian fiscal pre-conditions

In addition to changing economic conditions, the improved budgetary position of governments across the OECD had helped reinstate Keynesian fiscal policy. Australia occupies a particularly advantaged position in this respect, not having had a pattern of large and continuing deficits to compete with those of many other OECD countries and having accumulated only very moderate debt through the past two recessions. On the face of it, this was another factor making for ideal circumstances for the Rudd government to engage in active deficit spending. The Howard government had cleared the existing debt and initiated a program of quarantining the budget surplus in 'future funds'.

A shelf-full of public works

The challenge with the public investment strategy, then as now, is timeliness. Frivolous the Rudd government's 2008 stimulus package may have been, but at least it took immediate effect. Major capital works can easily take years from conception to full-scale construction — particularly if, as the OECD (2009) enjoins, they only proceed after being "carefully" selected on the basis of cost-benefit analysis.⁶ Another factor facilitating the current embracing of Keynesianism is the public investment

⁶ This is redolent of Myrdal's (1939:193–4) otherwise very strong endorsement of his government's deficit-spending program in the early 1930s. "Public works were generally begun too late; they were not prepared in advance and were, for this reason delayed and scarcely aimed at the works which should have been selected

situation. Symptomatic of how suitably-timed the crisis was in this regard was the fact that the incoming Rudd government had already made large-scale infrastructure investment a priority and was working through its revived model of cooperative federalism to inject substantial funds through the States into major transportation projects. Within four months of being elected, the government announced the establishment of an advisory body, Infrastructure Australia (Albanese 2008). In addition, proceeds from the 2007–08 Budget surplus were set aside in the three special funds. At this stage, public investment was seen as being necessitated for microeconomic reasons, and insofar as they would serve a macroeconomic purpose, that purpose would be to reduce inflationary bottlenecks on production. Infrastructure Australia was given one year to draw up a priority list for COAG to consider and by the time of the second budget had assessed \$200 plus billion worth of proposals from the States and identified a short list of most eligible candidates.

All this meant that conditions were unusually auspicious for a revival of traditional Keynesian public works spending: the need was there; the plans were there; and, to some extent, the money was there.

A less constraining external constraint

Earlier in this paper it was suggested that the external constraint is widely regarded as seriously diminishing the scope for Keynesian demand stimulation and that Australia is generally seen as a price taker when it comes to economic cycles. Has something changed to diminish these influences in the recent crisis? The general answer has to be no: with globalisation and Australia's significantly increased trade exposure, external influences can presumably be only stronger. For two particular reasons it would seem, though, the external constraint is uncharacteristically mild in this instance. By contrast with the French case of the 1980s, Australia is not trying to buck the disinflationary trend. The world-wide policy response to the global recession has been to inject demand stimulus. Secondly and more importantly, by particular contrast with the Great Depression, Australia's exports have not collapsed. There have been dramatic cuts to the market price of Australia's bulk commodity exports and a reversal of Australia's improving terms of trade,⁷ but the impact of these cuts has been substantially mitigated by two factors. One of those is that the level from which prices have been falling was very high, and even after the cuts the prices are still above what they were only a few years ago. The other cushioning factor has been the way that, at least through the first part of 2009, greatly increased volumes compensated for decreased prices. When the National Accounts figures for the March quarter showed what was to the government a most vindicating stability in the GDP figures, a closer look showed that while household expenditure (the Keynesian component) contributed 0.3 per cent to keeping GDP growth from staying negative despite a large drop in business investment, exports contributed twice that (ABS 2009). It is difficult to imagine the Rudd government's deficit spending doing much other than build deficits if export earnings had not maintained their strength.

Lingering issues

As a number of commentators have noted, budget balances that take years to establish are undone overnight once recession hits (e.g., BCA 2009). This raises the question of well the Coalition had

before all others if a rational choice had been made. They were usually of much smaller scope than would otherwise have been desirable."

⁷ A 7.8 per cent fall in the first quarter of 2009.

positioned the government for a downturn. As noted above, achieving balance over the cycle was a cardinal aim of the Howard government's and by re-establishing a pattern of surpluses, paying off the debt, and quarantining moneys in the 'Future Fund', the government saw itself as having acquitted itself quite credibly in that respect. The government's surpluses, however, were not large — never reaching 2 per cent of GDP. They are even smaller when one takes into account that they were being generated in the extraordinary conditions of the resource boom. Some economists (e.g., Garnaut 2006:10) cautioned at the time that "a major part" of these windfall gains should be set aside for the day when the inevitable collapse occurs. Similarly, Sheehan (2005) argued that the 'surpluses' that were distributed in various election promises by the Howard government would simply not exist were Australia employing accounting methods that revealed the government's underlying fiscal balance. Accounting of that nature requires significant judgement to be exercised in estimating 'normal' revenues and expenses; however, it has the advantage of providing a more sober picture of fiscal conditions. Along these lines, analysis in the 2009–10 *Budget Papers* (Treasury 2009) estimated that "the structural budget balance deteriorated from 2002–03, moving into structural deficit in 2006–07". The Howard government was not alone in cultivating the illusion of balancing the budget over the cycle while letting the surplus run through its fingers. The tendency has been endemic across the OECD and might reasonably be seen as an inherent challenge for democratic governance in resolving issues of the political business cycle (Joumard and André 2008).

Arm's Length Fiscal Policy?

The challenge of economic management under political constraint leads to suggestions for autonomising fiscal policy. This was flagged by Myrdal (1939:188), for whom the "big problem" was "how to tie the hands of government and legislators in good times and hinder them from expansion beyond the trend at that time, but to be able to release their hands and spur them to action in depressions. The Swedish approach was to have appropriate budgeting practices in place — a suggestion also made more recently by Hou (2006). That is likely, though, to be only part of the answer.

The cybernetic approach

One option is to enhance the automatic stabilisers and rely on them to do the job, as was suggested quite early on in Australia by Downing (1956:282) and by others more recently (e.g., Solow 2005; Taylor 2000). Given the size and responsiveness of stabilisers in the modern welfare state, this is not an unreasonable suggestion. It would entail, as Downing (1956:282) noted, maintaining or reinforcing the taxing and spending programs that have highly counter-cyclical qualities — such as reliance on a progressively-structured income tax system and a responsive system of unemployment benefits. A cybernetic approach would hold discretionary fiscal policy in reserve for more genuinely depression-like circumstances.

An independent fiscal authority

But this may not be enough, particularly in regard to the kind of capital investment program that plays such a central role in a Keynesian approach to economic revival; what Myrdal (1939:188) called "appropriate alternations in the institutional setup" may be required. Following the apparent success of independent monetary policy in recent years, one particularly provocative alteration has been proposed: the farming out of responsibility for fiscal policy to an independent agency (Blinder

1997; Gruen 1997, 2000; BCA 1999). Like Odysseus when imperilled by the sirens, democratic politics needs self-binding constraints to resist fatal temptation (Gruen 2000). While this is entirely consistent with Keynes's own technocratic desire for the "euthanasia of politics" as far as making economic policy is concerned (Schaefer and Schaefer 1983:60; also Smithies 1951), it conflicts rather directly with democratic norms. Quite unlike monetary policy, which in many ways is ideally suited to independent, apolitical, management, fiscal policy is entangled fundamentally with the intrinsically political questions of how and to what extent governments raise revenue and where and to what extent they spend.

Conclusion

Commentators such as Hay (2007) or Bell (2000) have the peculiar idea that being Keynesian means engaging continually in fiscal stimulus or that a merely steady reduction in unemployment is somehow "a major reorientation away from the full employment objective". This is the fallacy of 'fiscalism' — the idea that Keynesianism is defined by a fiscal rather than a monetary approach to counter-cyclical demand management and the use of fiscal stimulus regardless of potentially adverse effects. Keynesianism is about investing in fiscal stimulus in conditions where monetary policy has been exhausted; substantial economic resources, both capital and labour, are idle; inflationary dangers are minimal; and current account problems do not threaten. Commitment to balancing the budget over the cycle is in no way contrary to Keynesianism and indeed is integral to Keynesianism-in-practice as emphasised by Myrdal. Deliberate deficit spending — the 'hydraulic' approach — to provide demand-side stimulation is the epitome of Keynesianism but it is by no means everything Keynesianism is about or implies. Conveniently for a party of the Left, the Rudd government came to office when an unusual combination of fiscal and economic circumstances made such classically Keynesian methods applicable once more: public debt had been retired, interest rates were low, other countries were following suit, infrastructure backlogs beckoned. This does not mean that they were the deciding factor in the gentleness of Australia's recession or that the resulting fiscal bias will not present political problems and the reality is that Keynesianism was developed as an alternative to pro-cyclical policies in an era of deflation. There has been no deflation in this crisis and the risk of pro-cyclical impacts is very slight given the size and responsiveness of today's automatic stabilisers.

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