IPB University
Bogor Indonesia

New Keynesian Economics

oleh

Bambang Juanda

Departemen Ilmu Ekonomi

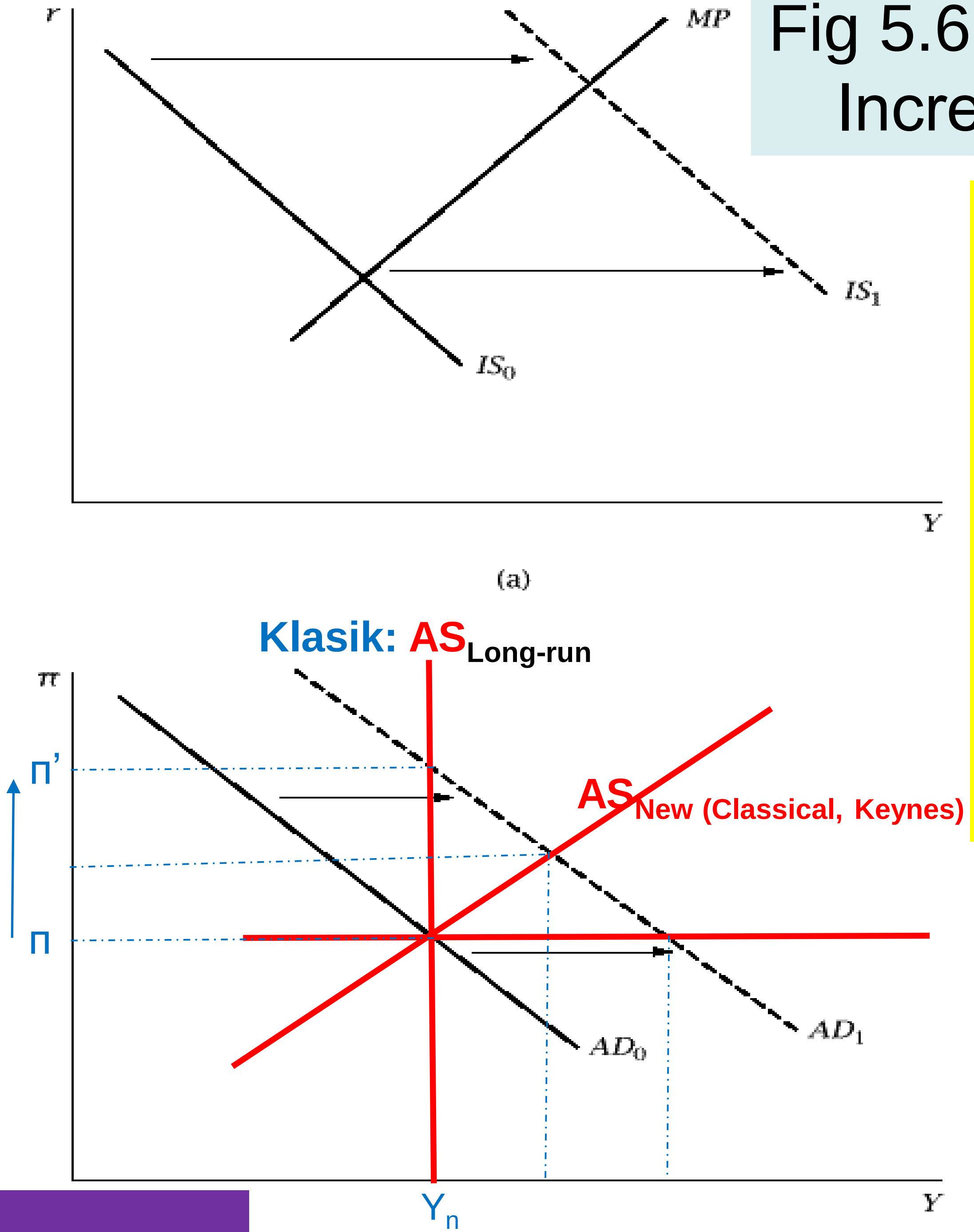
Fakultas Ekonomi dan Manajemen IPB

https://bambangjuanda.com/

Review

Fig 5.6 The Effects of an Increase in Gov't Purchases

The Impact of this change in AD on output and inflation depends on the AS curve. If it is vertical, only inflation increase. If it is horizontal, only output increase. And if it is **upward-sloping but not vertical, both output and inflation increase**



New Keynesian economics is a school of macroeconomics that strives to provide microeconomic foundations for Keynesian economics. It developed partly as a response to criticisms of Keynesian macroeconomics by adherents of new classical macroeconomics.

Two main assumptions define the New Keynesian approach to macroeconomics. Like the New Classical approach, New Keynesian macroeconomic analysis usually assumes that households and firms have rational expectations. However, the two schools differ in that New Keynesian analysis usually assumes a variety of market failures. In particular, New Keynesians assume that there is imperfect competition in price and wage setting to help explain why prices and wages can become "sticky", which means they do not adjust instantaneously to changes in economic conditions.

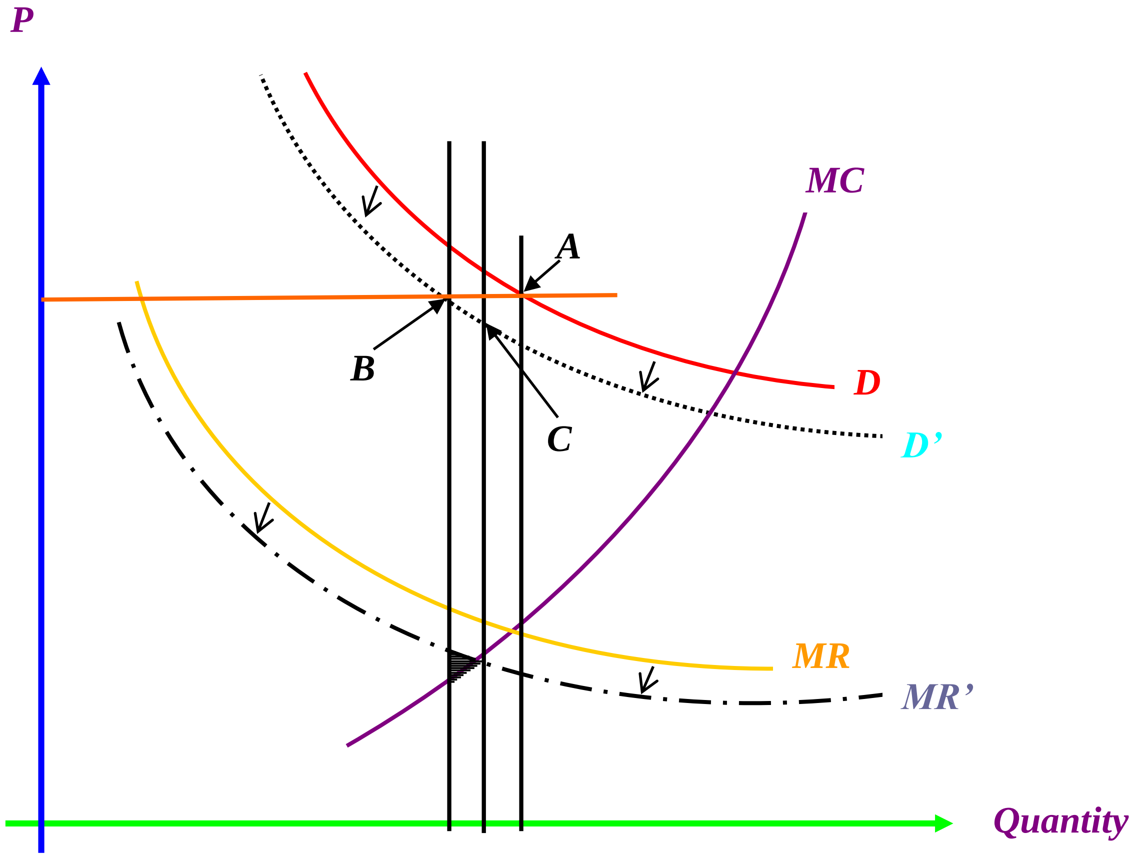
Wage and price stickiness, and the other market failures present in New Keynesian models, imply that the economy may fail to attain full employment. Therefore, New Keynesians argue that macroeconomic stabilization by the government (using fiscal policy) and the central bank (using monetary policy) can lead to a more efficient macroeconomic outcome than a *laissez faire* policy would.

New Keynesianism became a part of the new neoclassical synthesis, which incorporated parts of both it and new classical macroeconomics and forms the theoretical basis of much of mainstream economics today.

- Para Ekonom *New Keynesian* percaya bahwa model "*market clearing*" tidak dapat menjelaskan fluktuasi ekonomi dalam jangka pendek, karena upah dan harga bersifat rigid (kaku)
- Fischer dan Taylor: fakta bahwa upah atau harga ditentukan dengan kontrak secara periodik
- Implikasinya akan berdampak pada penyesuaian terjadi secara bertahap dari tingkat harga terhadap *nominal disturbance*.
- Salah satu alasan harga tidak segera menyesuaikan untuk *market clearing* karena penyesuaian harga membutuhkan biaya penyesuaian (*menu cost)*

  Menu cost : biaya yang dikeluarkan perusahaan untuk *updating*, seperti mencetak menu baru, daftar harga, brosur dan berbagai keperluan lain ketika harga berubah

Kapan Perusahaan Merubah Harga



A Representative Firms Incentive to Change its Price in Response to Fall in Aggregate Output

- Awalnya perekonomian di keseimbangan A. Perusahaan memaksimisasi keuntungan ketika MR=MC.
- Jika terjadi penurunan AD dan harga-harga lainnya tidak berubah maka mengurangi agregat output dan kemudian menggeser kurva demand yang dihadapi perusahaan
- MR bergeser ke MR' (menurun) sementara MC tetap
- Jika perusahaan tidak mengubah harganya, maka output ditentukan oleh permintaan pada titik B.
- Pada tingkat output tersebut, MR > MC, dan dengan demikian perusahaan punya insentif untuk menurunkan harga dan meningkatkan output
- Jika perusahaan mengubah harganya, maka MR'=MC, sehingga tingkat output dan harga berada pada titik C
- Daerah yang diarsir menunjukkan tambahan keuntungan yang diperoleh karena pengurangan harga dan peningkatan jumlah produksi.
- Perusahaan tertahan pada harga yang lama, jika luas daerah tambahan keuntungan tersebut haruslah kecil, sehingga perusahaan tidak punya insentif untuk mengubah harga (adanya AD *externality)*

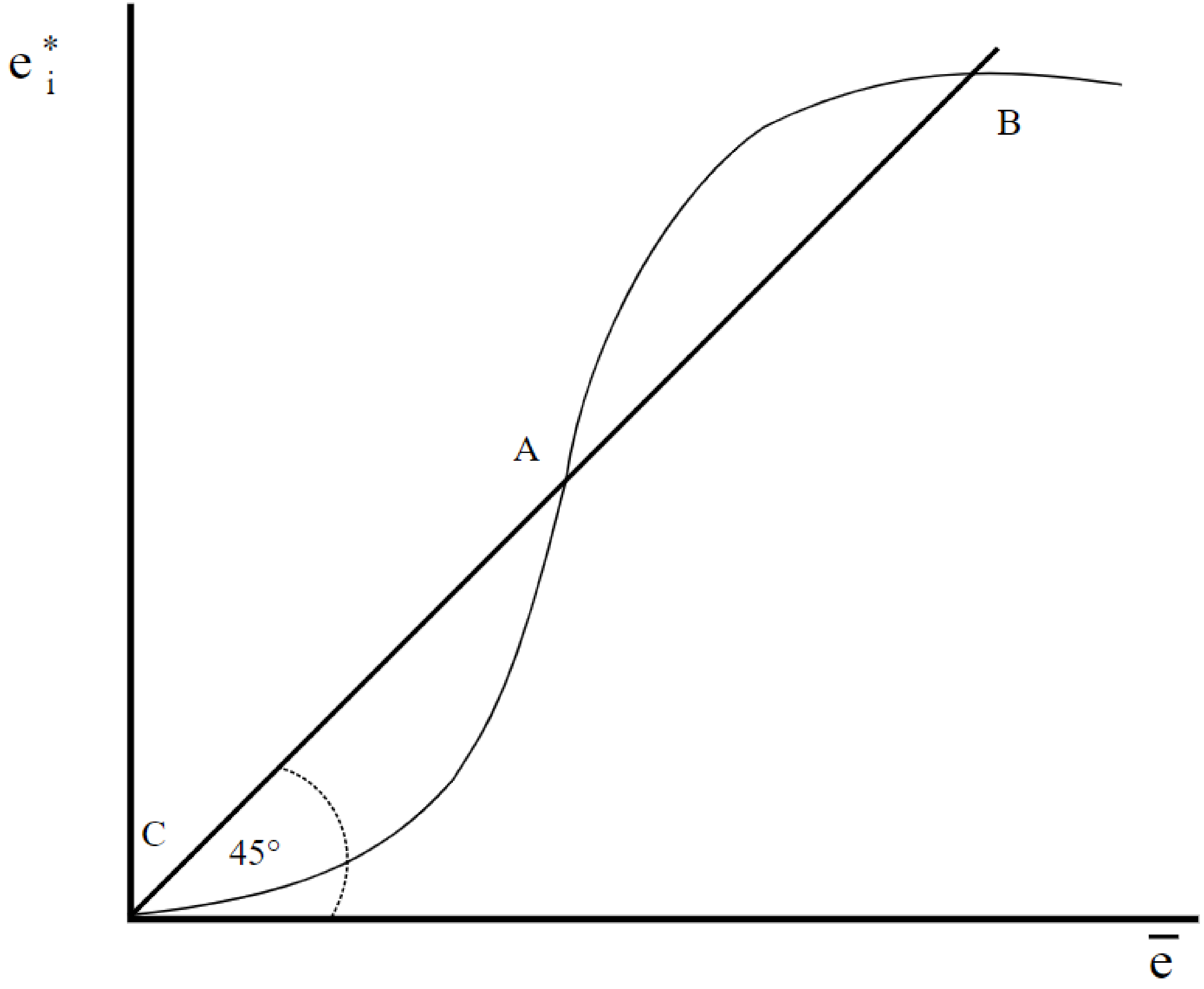
Coordination failure was another important new Keynesian concept developed as another potential explanation for recessions and unemployment. In recessions a factory can go idle even though there are people willing to work in it, and people willing to buy its production if they had jobs. In such a scenario, economic downturns appear to be the result of coordination failure: The invisible hand fails to coordinate the usual, optimal, flow of production and consumption.

Paper *Coordinating Coordination Failures in Keynesian Models* expressed a general form of coordination as models with multiple equilibria where agents could coordinate to improve (or at least not harm) each of their respective situations (Cooper & John,1988).

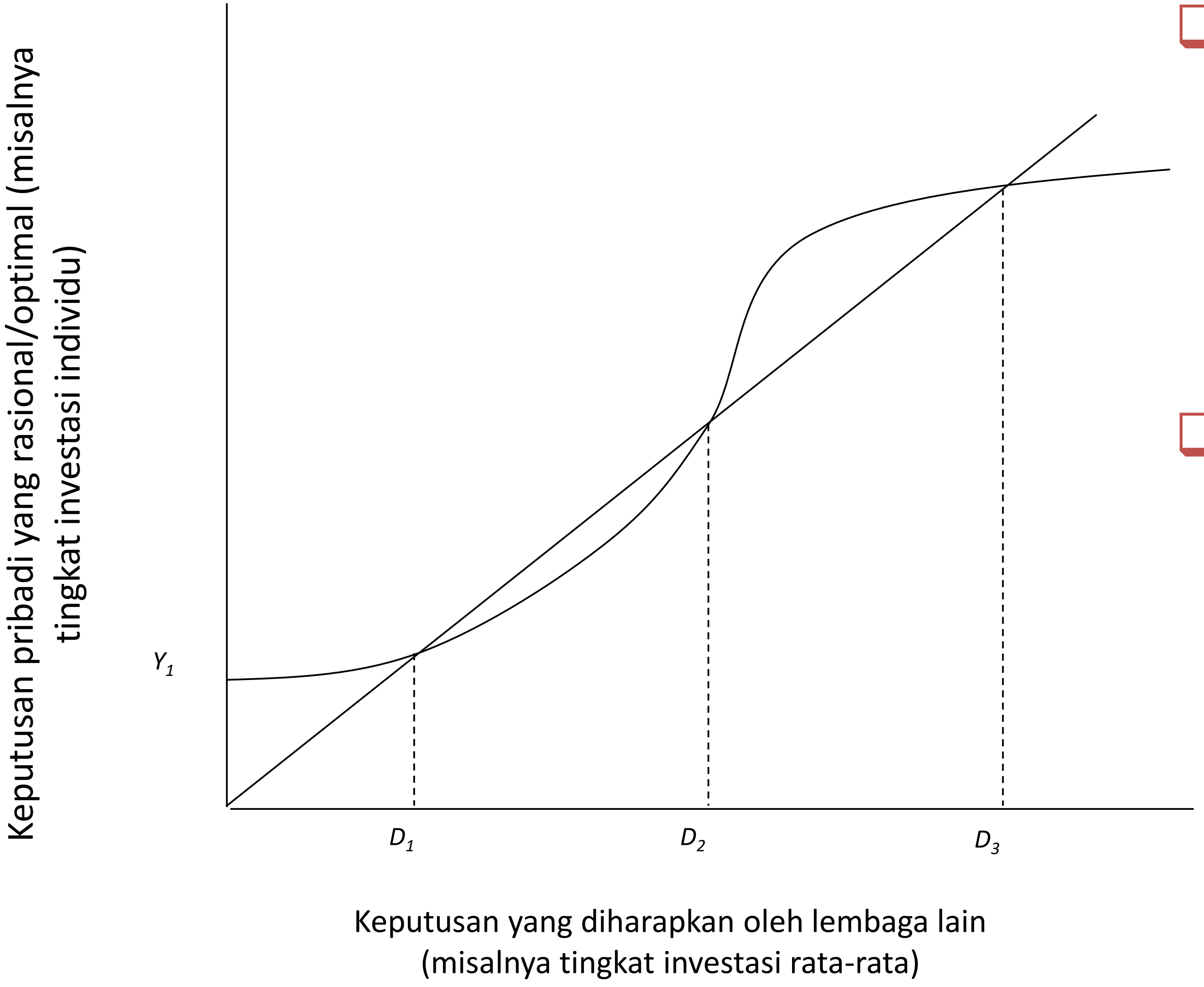
In Diamond's coconut model (1982) producers are more likely to produce if they see others producing. The increase in possible trading partners increases the likelihood of a given producer finding someone to trade with. As in other cases of coordination failure, Diamond's model has multiple equilibria, and the welfare of one agent is dependent on the decisions of others. Diamond's model is an example of a "thick-market externality" that causes markets to function better when more people and firms participate in them.

Other potential sources of coordination failure include self-fulfilling prophecies. If a firm anticipates a fall in demand, they might cut back on hiring. A lack of job vacancies might worry workers who then cut back on their consumption. This fall in demand meets the firm's expectations, but it is entirely due to the firm's own actions

Ilustrasi ***Coordination Failure***



In this model of coordination failure, a representative firm e_i makes its output decisions based on the average output of all firms ($\bar{e}$). When the representative firm produces as much as the average firm ($e_i = \bar{e}$), the economy is at an equilibrium represented by the 45 degree line. The decision curve intersects with the equilibrium line at three equilibrium points. The firms could coordinate and produce at the optimal level of point B, but, without coordination, firms might produce at a less efficient equilibrium



Ekuilibria Jamak

- Kemungkinan gagalnya koordinasi akan mengarah ke keseimbangan yang *underemployment*; yang berarti output berada dalam kondisi dibawah & tidak efisien karena setiap orang percaya bahwa hal tersebut akan terjadi.
- Dalam kondisi demikian, tidak ada sumber yang mendorong perekonomian bertahan pada output yang normal. Sebagai hasilnya, ada ruang bagi kebijakan pemerintah untuk mengkoordinasikan ekspektasi sehingga menuju pada keseimbangan output yang tinggi. Sebagai contoh, stimulus temporer mungkin secara permanen akan menggerakan ekonomi kepada keseimbangan yang lebih baik

Efficiency Wage Theory

The idea of the efficiency wage theory is that **increasing wages can lead to increased labour productivity** because workers feel more motivated to work with higher pay. Therefore if firms increase wages – some or all of the higher wage costs will be recouped through increased staff retention and higher labour productivity.

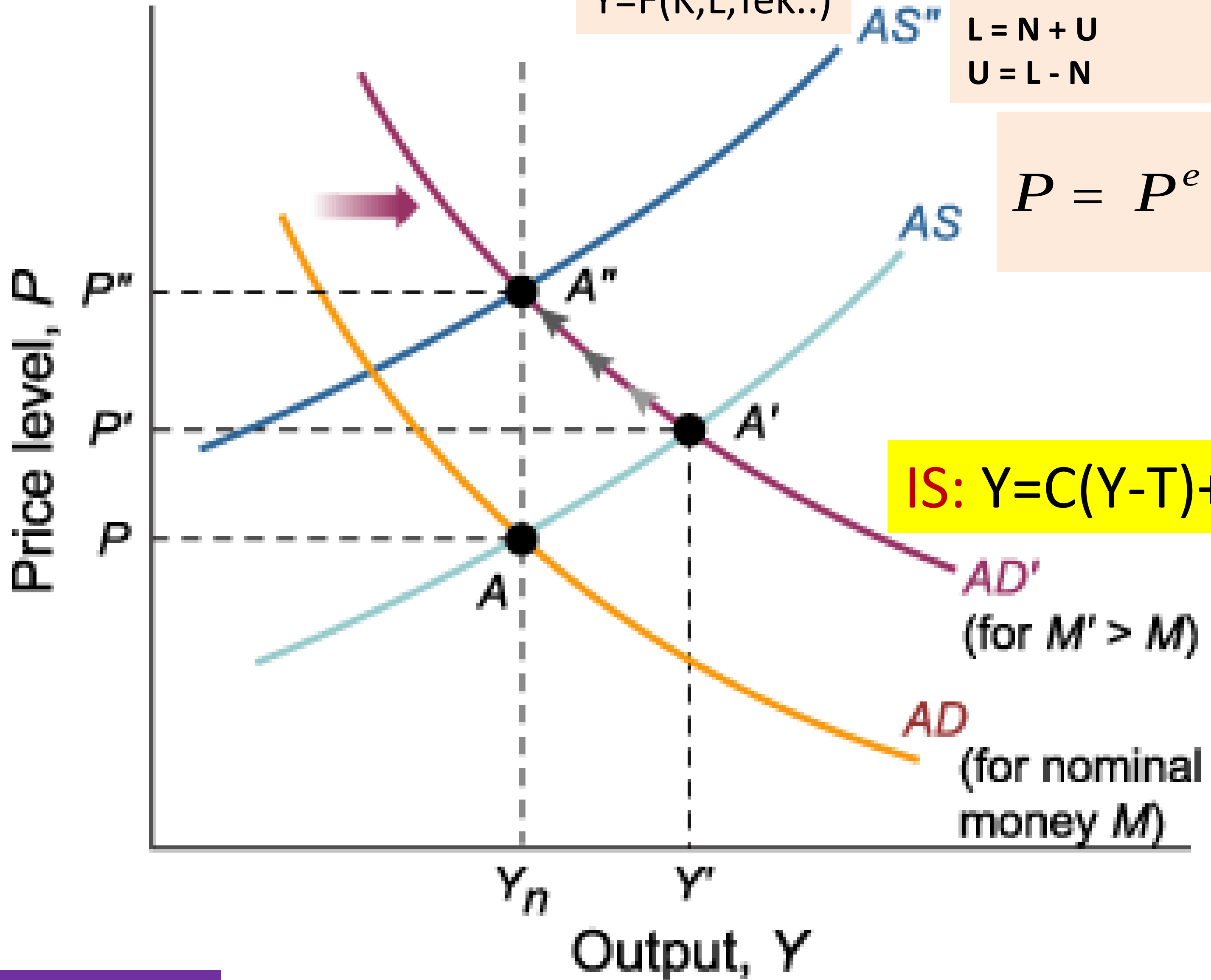
Economists call the theories that link the *productivity* or the *efficiency* of workers to the wage they are paid.

These theories also suggest that wages depend on both the **nature of the job** and on **labor-market conditions**:

- Firms that see employee morale and commitment as essential to the quality of their work, will pay more than firms in sectors where workers' activities are more routine.
- Labor market conditions will affect the wage.

Perkembangan Output akibat peningkatan AD dan/atau AS

Y=F(K,L,Tek..)



Misal Y = A.N = N
L = N + U
U = L - N

$$W = P^e F(\overset{-}{u},\overset{+}{z})$$

$$P = (1+\mu)W$$

$$P = P^e(1+\mu)F\left(1-\frac{Y}{L},z\right)$$

IS: Y=C(Y-T)+I(Y,i)+G+(X-M)

$$\text{LM relation: } \frac{M}{P} = YL(i)$$

$$Y = Y\left(\underset{+}{\frac{M}{P}},\underset{+}{G},\underset{-}{T}\right)$$

Sumber: Blanchard (2017)

The Effects of a Monetary Expansion

The Dynamics of Adjustment

$$IS\ relation:\ Y = C(Y - T) + I(Y, i) + G$$

$$LM\ relation:\ \frac{M}{P} = YL(i)$$

$$W = P^e F(u, z)$$

$$P = (1 + \mu)W$$

Figure

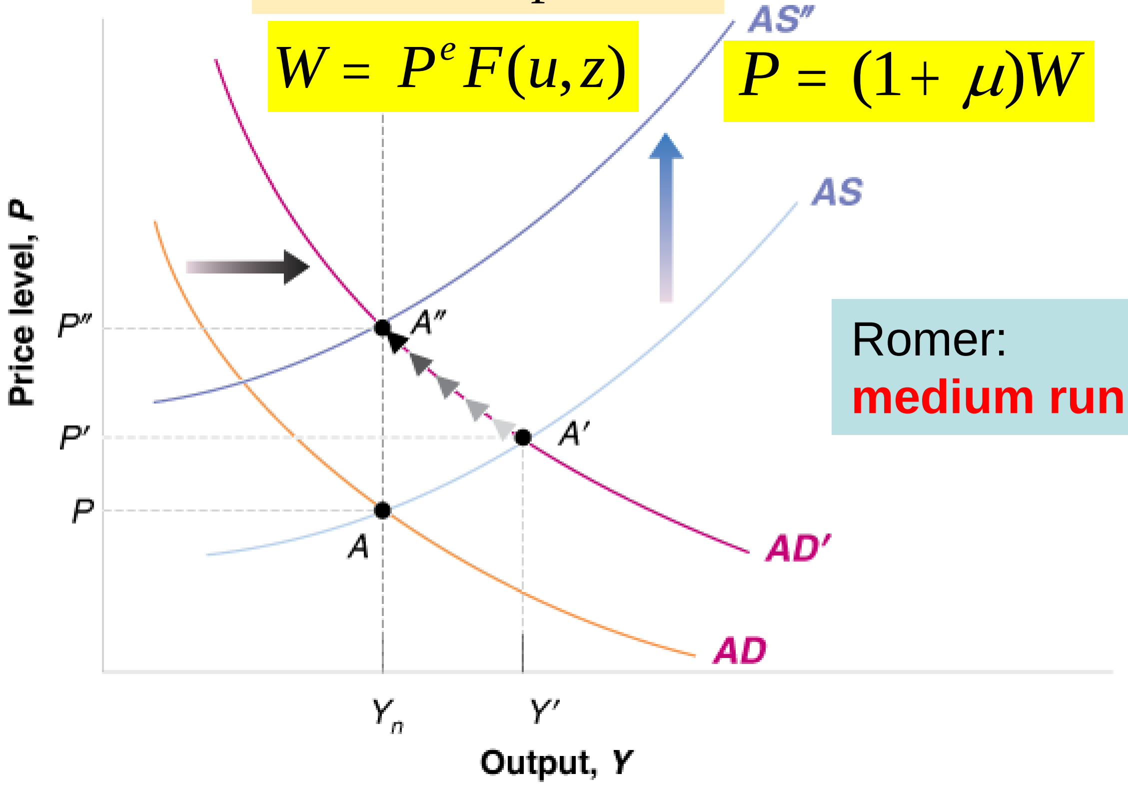
The Dynamic Effects of a Monetary Expansion

A monetary expansion leads to an increase in output in the short run but has no effect on output in **the medium run**.

The difference between Y and Y_n sets in motion the adjustment of price expectations.

In the medium run, the *AS* curve shifts to *AS''* and the economy returns to equilibrium at Y_n.

The increase in prices is proportional to the increase in the nominal money stock.



Romer:
medium run = long run

$(P\nearrow > P^e) \rightarrow P^e\nearrow \rightarrow$ **(AS ke atas)** $\rightarrow W\nearrow \rightarrow P\nearrow$

Ps Uang & Barang: $M^s\nearrow$ & $P\nearrow$ proporsional

$\rightarrow$ Y tetap $\rightarrow$ i ?

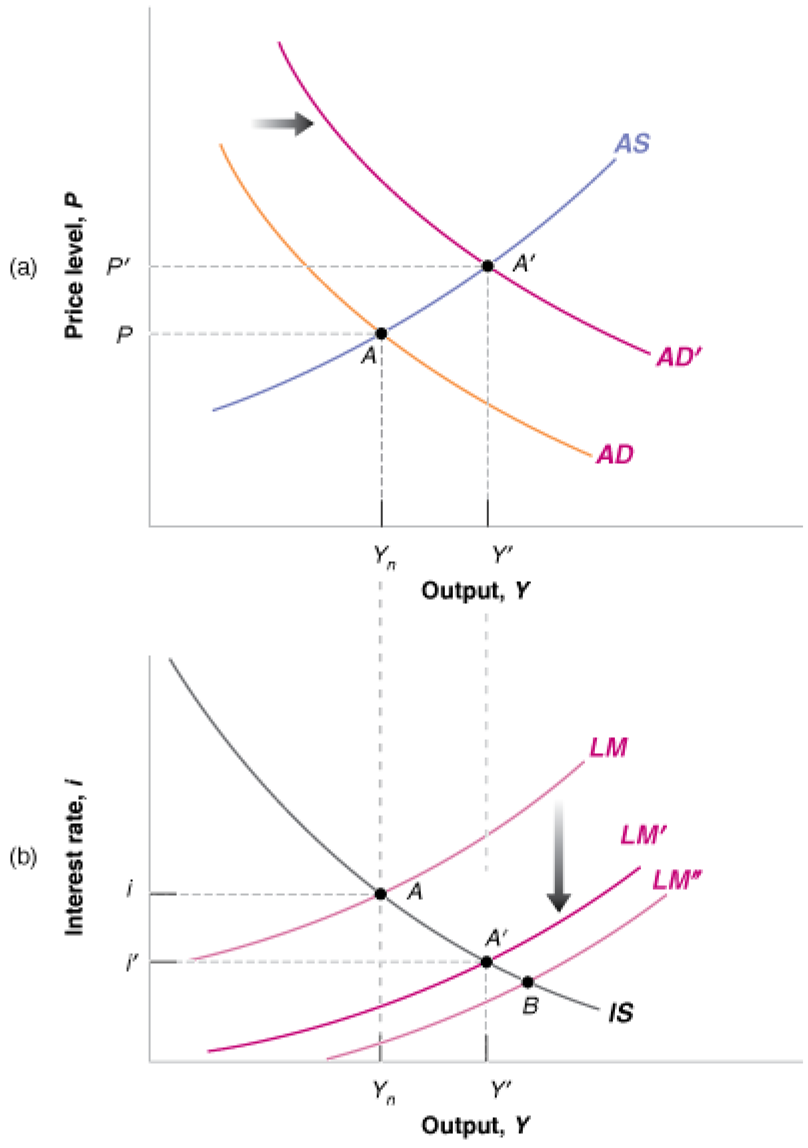
The Effects of a Monetary Expansion

Going Behind the Scenes

The impact of a monetary expansion on the interest rate can be illustrated by the *IS-LM* model.

The **short-run** effect of the monetary expansion is to shift the *LM* curve down. The interest rate is lower, output is higher.

If the price level did not increase, the shift in the LM curve would be larger—to LM''.



The Effects of a Monetary Expansion

The Neutrality of Money

- In the *short run*, a monetary expansion leads to an increase in output, a decrease in the interest rate, and an increase in the price level.

- In the *medium run*, the increase in nominal money is reflected entirely in a proportional increase in the price level. The increase in nominal money has no effect on output or on the interest rate.

The **neutrality of money** in the medium run does not mean that monetary policy cannot or should not be used to affect output.

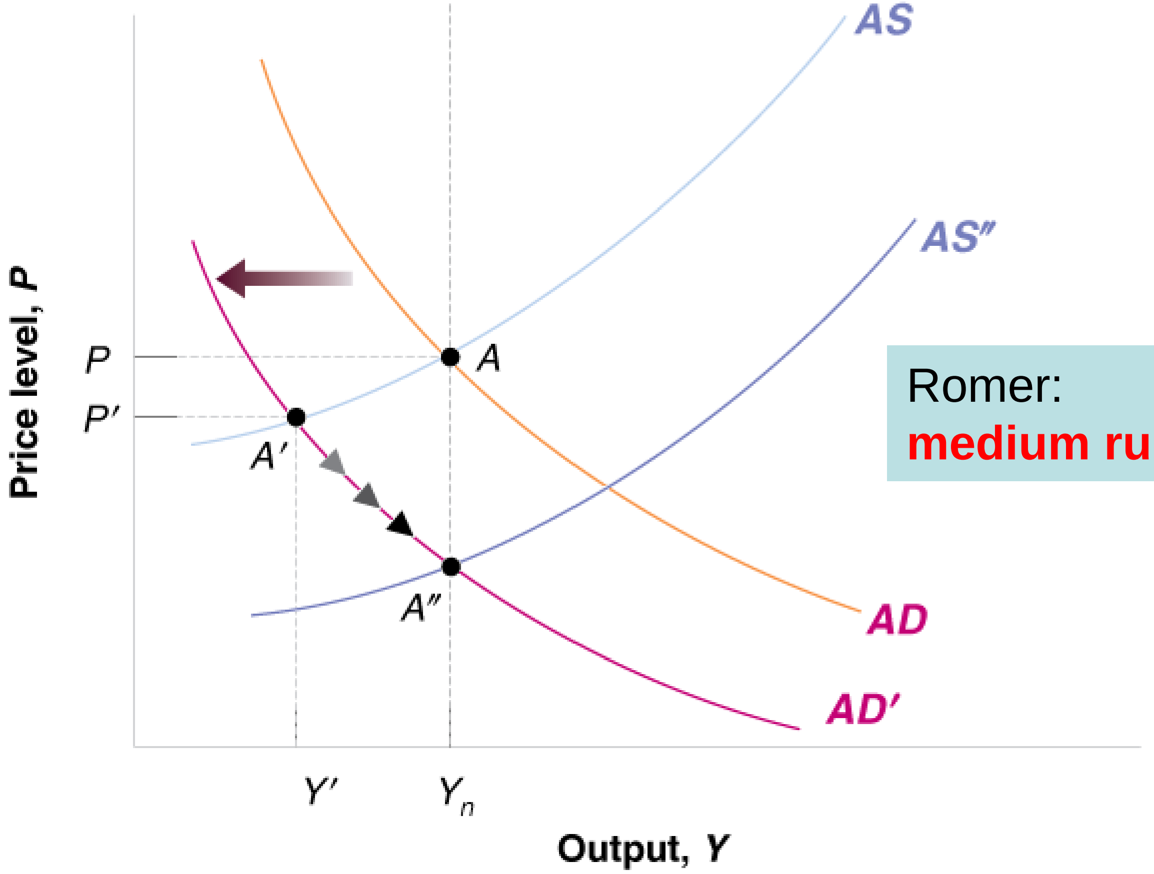
Romer:
medium run = long run

A Decrease in the Budget Deficit

Figure

The Dynamic Effects of a Decrease in the Budget Deficit

A decrease in the budget deficit leads initially to a decrease in output. Over time, however, output returns to the natural level of output.



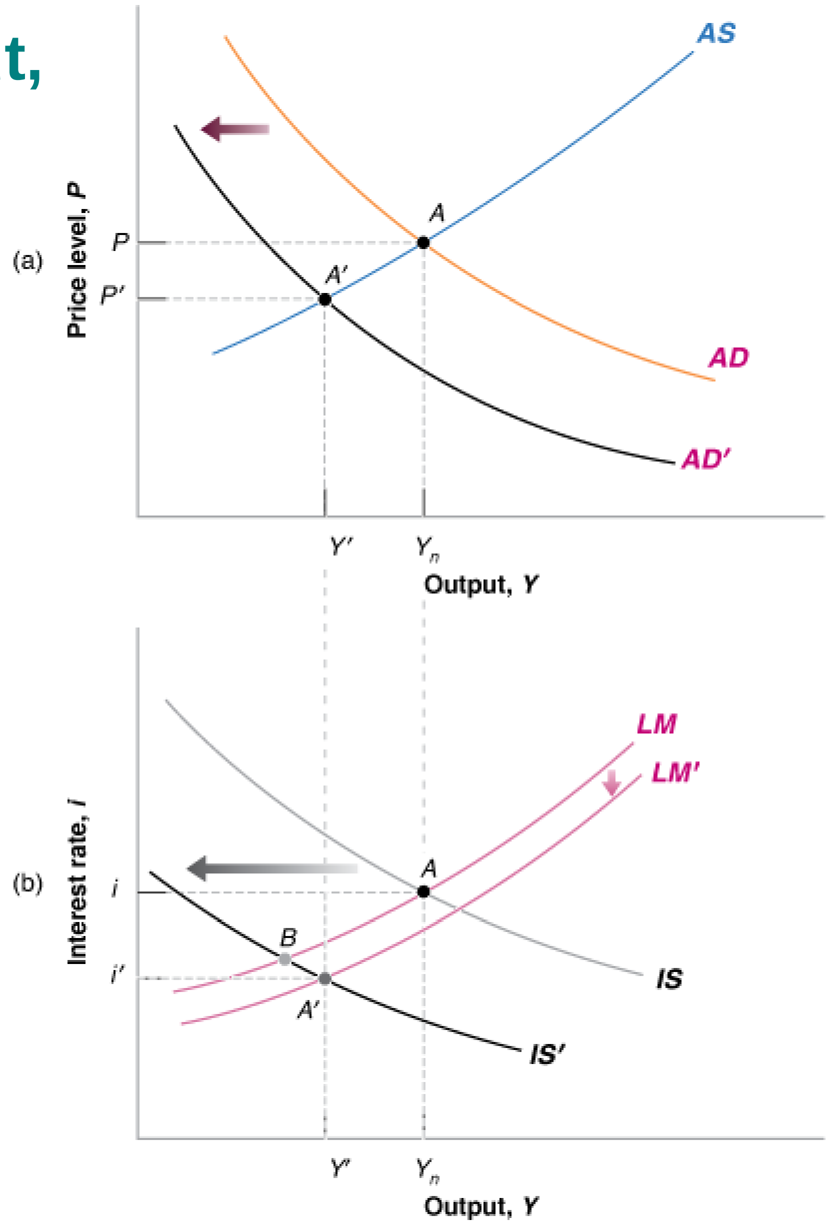
Romer:
medium run = long run

A Decrease in the Budget Deficit

Deficit Reduction, Output, and the Interest Rate

Since the price level declines in response to the decrease in output, the real money stock increases. This causes a shift of the *LM* curve to *LM’*.

Both output and the interest rate are lower than before the fiscal contraction.



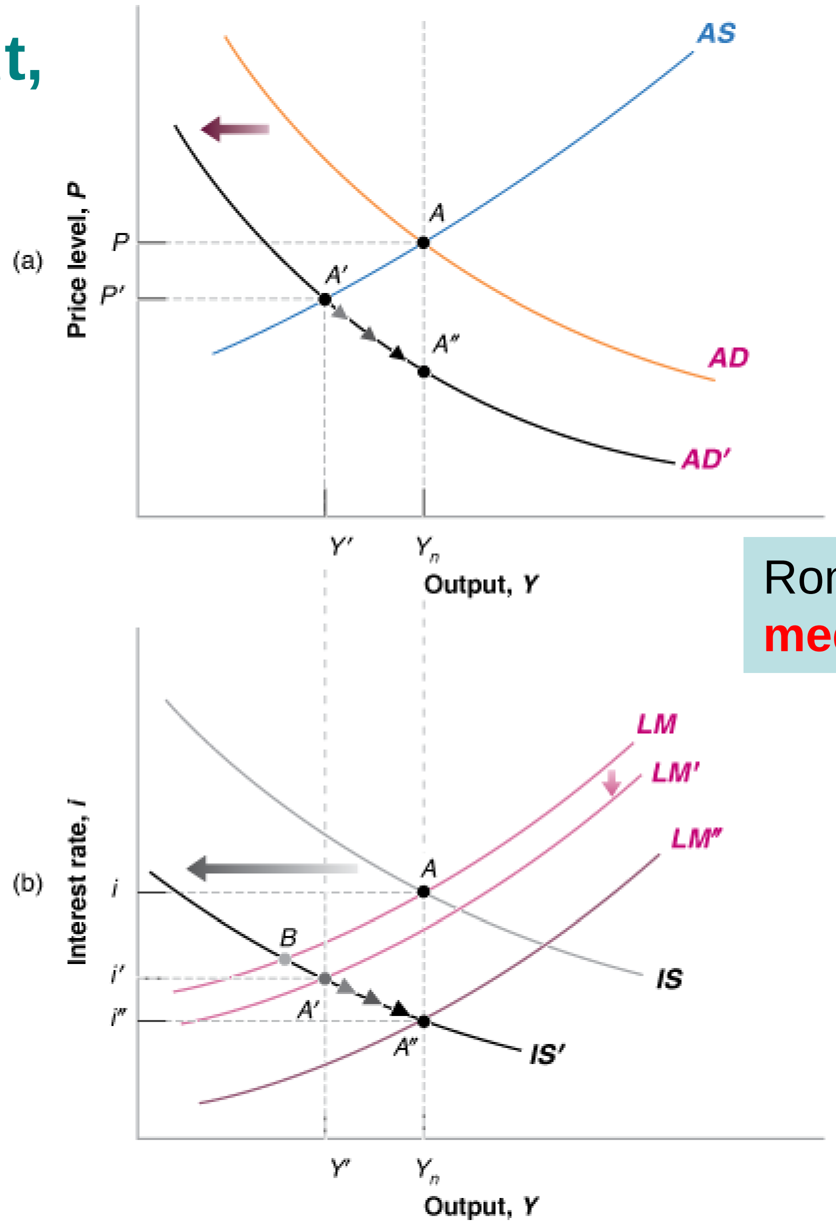
A Decrease in the Budget Deficit

Deficit Reduction, Output, and the Interest Rate

Figure

The Dynamic Effects of a Decrease in the Budget Deficit on Output and the Interest Rate

A deficit reduction leads in the short run to a decrease in output and to a decrease in the interest rate. In the medium run, output returns to its natural level, while the interest rate declines further.



Romer:
medium run = long run