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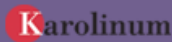
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Keynesian Macrodynamics: Convergence, Roads to Instability and the Emergence of Complex Business Fluctuations

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Abstract: We reformulate the traditional AS-AD growth model, with a Taylor policy rule replacing the conventional LM-curve. The essential features of the model are gradually adjusting wages and prices, perfect foresight on current inflation rates and an adaptive revision of the inflationary climate in which the economy is operating. We compare this approach with the New Keynesian approach with staggered price and wage setting and find that whilst both approaches have common components, they have radically different dynamic implications due to the treatment of the forward-looking part of our wage-price spiral. We show that an estimated version of our model implies local asymptotic stability, due to stable interaction of goods market dynamics with the interest rate policy rule of the central bank, and due to a normal working of a real-wage feedback chain. These results are however endangered when there is a global floor to money wage inflation rates, leading in fact to economic breakdown. In this latter case, the return of some money wage flexibility in deep depressions is of help in restoring the viability of the model, thereby avoiding explosive dynamics and the collapse of the economy.

JEL classification: E24, E31, E32

Keywords: Keynesian dynamics, wage and price Phillips curves, persistent business cycles, complex dynamics

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