<u>The Third Diagram and J. A. Kregel in GPKE, pp. 51-56.</u>

What J. A. Kregel establishes about wages and profits, with not a few simplifying assumptions, can be read off the third diagram in terms of aggregate living costs and aggregate

Aggregate living costs are <u>fE'</u>, which derive from basic consumer income, <u>c'fO'</u>, and surplus consumer income, <u>c"fO"</u>, with adjustments from <u>fD' - sfO'</u>.

Aggregate investment expenditure, <u>fE"</u>, is derived from basic investment income, <u>i'fO'</u>, and surplus investment income, i"fO", with adjustments from <u>fD" - sfI"</u>.

Circuit equilibrium requires that i'fO' (directly or indirectly) equals c"fO", so that basic investment equals surplus consumption.

demand/fE'/   Cf. GPKE 55: In the wage good [basic] sector/is equal to wage [cost of living] bill in both the consumption [basic] and investment [surplus] sectors and, as a result, its receipts will exceed its wage [cost of living] bill by an amount equal to the wage [cost of living] bill in the investment [surplus] sector. This provides funds for the purchase of investment goods by the wage good [basic] sector.

What follows on p. 55, follows the same analogy.

Note the final sentence: A higher proportion of investment in total output... leads to a higher share of profits relative to wages (investment income to living income) in national income, and vice versa.

In other words, the surplus expansion is anti-egalitarian and the basic expansion, were it carried through, would be egalitarian.

P. 56: .. not only do firms have the ability to determine their investment plans..., they also have the ability to determine the prices at which they will sell their output... Cf. p. 34 on <u>flex</u>price and <u>fix</u>price markets.

Monetarists assume that the growth of real income, $\dot{y}$, can be treated as a constant trend and that the money market is constantly cleared. On these assumptions it follows that the rate on inflation, $\dot{p}$, is the excess of $\dot{M}$ over $\dot{y}$. Hence Friedman's rule (1969) for price stability that $\dot{M}$ increase 3% to 5% per annum to balance the 3% to 5% of $\dot{y}$.

the rate of change of

The PK view is that $\dot{W}$, the average level of nominal money wages, $\dot{w}$ the rate of change of the average real wage, and $\dot{p}$ the rate of change of the price level, are related by

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$$\dot{w} = \dot{W} - \dot{p}$$

Over the long run, $\dot{w}$, which depends on
$\dot{z}$, the rate of growth of labor productivity, average dQ,
the ratio import to domestic prices,
the levels of indirect taxation and the mark-up,
may be expected to have a fairly steady trend. Hence,

$$(4) \quad \dot{p} = \dot{W} - \dot{z}$$

the rate of inclation equals the rate of increase of money wages minus the rate of increase of average GNP.

If both the level and the rate of change of wages and prices are inflexible downwards, equations (1) and (4). taken together imply that if monetary authorities do not permit the nominal money stock to accomodate the rate of increase of money wages, aggregate demand will not be suffic-ient to maintain the secular growth of real output.

[By (4) average dQ ($\dot{z}$) is no more than the excess of the rate of increase of money wages over the rate of inflation.

rate of increase of

[By (1) the effective demand for money, $\dot{M}$, has to equal the sum of the rise of the price level plus average dQ.

[Re_fusing accomodation to rising prices forced_by rising money wages blocks rising dQ.]

As a result there will be downward pressure on the growth of real income, a rise in interest rates, and an accompanying rise in unemployment rates.