

Report on Steve Keen's "Solving the Paradox of Monetary Profits" 6-2-2010.

The paper is in a continuation of an earlier paper addressing the question of monetary profits, or rather the old question of the monetization of real-profits. (Chapman and Keen, 2006 "Hic Rhodus, hic Salta! Profit in a dynamic model of the monetary circuit") An explicit question in political economy at least since the works of K.Marx.

The paper contains several models. In order of appearance they are, a monetary flow model including the specification of the distribution of national income, on top of which a physical production system is specified and linked to the monetary model by money-prices, some further additions allowing for a discussion of money as a stock in a revolving fund and money destruction. Ending up with a multisectoral, that is including a capital good sector, a "strictly monetary version of Goodwin's model" (p.19) That is, Richard Goodwin's growth cycle model from 1967.

In the authors own evaluation the multisectoral model "is preliminary only ...much checking of its structure is needed to validate that it is logically consistent.." but it is supposed to show "the basic insights of the single-sectoral model....that industrial capitalists can and do make a monetary profit in a pure credit economy."

Contrary to the statement above the paper does not dissolve the paradox as it has been stated in the history of political economy up til now. Of course not, that is exactly imbedded in the concept of 'paradox'. The logical and arithmetical problem is not addressed in the first 9 pages of the paper. On p.9 a result of the calculation of equilibrium balances is presented, using values scattered in the text for parameters taken as stylized facts. In itself an instructive method. The result, with a workers equilibrium deposit balance of 9.333 and a turnover of 26 times p.a. and an assumed wage-proportion of 70%, total national-income is 346.654. Which gives 99.819 as the net profit for the 26 turn-overs pr. year. Successive sequences of fortnights pay in and pay out of wages and consumption out of wages, without saving. If we increase the turnover, profits will increase. If we reduce the turnover it will decrease. Given the amount of money, i.e. the reciprocal debts of the Firm and Bank.

Now the paper is suggesting that 99.819 is very close to the basic debt of the firms, the amount of credit money of 100, so just increasing the rate of turnover to 27, and we will have a monetary profit, not only as a flow but also as a stock magnitude, within a year. The accumulated accounts of the firm will show a difference of 3.7 between the debt of the firm = 100 and the accumulated deposits of the Firm of 103.7.

So in this case the Bank owes the Firm 103.7 and the firm owes the bank 100, hence the 'money' profit of 3.7. But as the Bank is not doing deficit spending in consuming out of its positive income, the differential between 5% in and 1% in on loans and out on deposits, how comes the debt of 3.7 to the Firm?

The logical problem can not be solved in this way, we have an equilibrium distribution of the credit money totalling 100, and we have a net-income flow account for a year as 346.5 in *value*. That's it. No dissolving of the paradox is produced. The numbers 100 and the 346 are not in *pari materia*. They can not appear in a consistent accounting of stocks.

To handle credit-money demands accounting of movements, changes in, the Banks and all other stock accounts, balancing credit and debit. Liabilities and assets. In the books of the Bank liabilities adds up to the total amount of credit money, and the assets are in the models of the paper the debt of the Firm. Implying to introduce a revolving fund as a phenomenon to dissolve the paradox, is a *non sequitur*. And the question of not destroying the ‘stock’ of money as (or rather how?) the Firm is repaying its debts, keeping incomes rolling, saving of Banks and Workers still=0, is not at all intelligible. It is a prototypical fallacy of composition, as it can be found in Hicks’ “A market theory of money” 1989, p. 106, in the chapter “The credit economy: Wicksell”. The clue: if there is money, it must be somewhere, and the debt as the collateral must be somewhere too. They grow and shrink together. Credit cum giro or overdraft.

The methodology of the paper, not the announced solution of a paradox, is an interesting contribution in itself. But the presentation is burdened by several infelicities. As of p.18 ‘unemployment % p.a.’ is dimensionally disturbing. The same goes for figure 21, p.23, what does ‘Profit/Capita (percent)’ mean? Returning to the credit money sphere, p.17, figure 17, has ‘compound interest of A’ not necessarily paid out, that is as an increase in the Firm’s debt to the Bank, but that must be an income for the Bank, not necessarily paid in. But nowhere to be found (or included in the calculations?). Is the Bank giving credit to itself?

Infelicities like these makes it difficult for the reader of the paper, as it stands, to follow and appraise the value of the methodological approach as such. And staying in the monetary sphere, continuous time, and its representation by differential equations, is not really meaningful. Monetary payments and their accounting are discrete, by definition, law and convention. No time elapses between payment and receivment, they are strictly simultaneous. No amount of money is travelling in real time and space. Physically yes, if we are considering material money as gold, silver etc., but not even physically when we talk of credit-money. Their movements are strokes of pens or electrons.

As a last critical point. In the logical paradoxical corner, P as an index, priceindex in the paper, no qualms. But simulating on stylized facts, any P will lead our minds astray. P will be, has to be, implicit. This we have learned from Keynes. Chapter 4 in G.T.

So for the simulation of how profits manifests themselves in a capitalistic monetary circuit, the logically non-compromising “Volkswirtschaftliche Saldenmechanik” by Wolfgang Stützel, the second edition is from 1978, is still helpful in the outmost.