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Are Dynamic Stochastic Disequilibrium Models Keynesian or Neoclassical?*

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Abstract

Dynamic Stochastic Disequilibrium (DSDE) models share the micro-foundations of Dynamic Stochastic General Equilibrium (DSGE) models based on inter-temporal optimization and rational expectations. Yet, it features the principle of effective demand which is at the core of Traditional Post-Keynesian (TPK) models and follows from the perception that the wage inflation is a policy variable rather than a labor-market clearing variable. In order to locate the DSDE model among the traditions of economic thought, the paper compares DSDE first-order conditions of optimal behavior with TPK rule-of-thumb behavior. It further compares the economic propagation of a DSDE model to those of a DSGE and TPK model as well as a Synthetic Neoclassical (SNC) model which features TPK behavioral assumptions and labor-market clearing. We arrive at two core conclusions: First, apart from assumptions regarding expectation formation, orthodox micro-foundation is, to a considerable extent, consistent with the behavioral hypotheses underlying TPK models. Second, the economy characterized by the DSDE model is essentially post-Keynesian rather than neoclassical because it features the principle of effective demand.

Keywords: Dynamic stochastic disequilibrium, dynamic stochastic general equilibrium, post-Keynesian economics, micro-foundations

JEL Classification: B41, E12, J52

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