

Post-Keynesian Analysis of the Fed's Policy Response to the Financial Crisis

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ABSTRACT. *Combining the historical lessons of the Great Depression, from the perspective of post-Keynesianism, explain the Fed's policies to cope with the global financial crisis, analyze the pros and cons of post-Keynesian economic crisis theory, and make suggestions for the economic crisis from the perspective of post-Keynesianism. Provide useful historical reference and practical guidance for maintaining stable economic development.*

KEYWORDS: *Post Keynesian; Federal reserve; Economic crisis*

1. Introduction

The global financial crisis that broke out in 2008 had a considerable impact not only on the development of the U.S. domestic financial market but also on the growth of the U.S. real economy. In order to avoid the further development of the financial crisis and trigger the global economic crisis, the Fed has carried out a lot of practical operations in the field of monetary policy. Among them are not only the application of traditional price-based monetary policy tools, for example, the federal funds rate and the legal reserve rate. There are also traditional quantitative policy tools that supplement market liquidity, such as open market operations.

Although the financial crisis in 2008 has a significant impact on the world, many scholars have conducted continuous exploration and research on how similar economic crises are caused. However, no unified answer has been obtained so far. The post-Keynesian theory has attracted widespread attention. It was after the global economic crisis in 2008. This argument, which was put forward decades ago, was correctly verified in the crisis. This article elaborates on the application of the Fed to the traditional monetary policy in the economic crisis after the Great Depression based on collecting reading literature and then analyzes the economic crisis from the perspective of Keynesianism and finally draws the pros and cons of Keynesian economic crisis theory.

Finally, combine the theoretical content with the actual situation. The logical sufficiency of the post-Keynesian economic crisis theory is obtained, which provides a brand-new theoretical basis for interpreting the economic crisis, and also provides useful historical reference and practical guidance for maintaining stable economic development.

2. The Practice of the Federal Reserve's Monetary Policy after the Global Financial Crisis

The article first reviews the 2008 financial crisis. The outbreak of the crisis is first reflected in two aspects, the collapse of the real estate industry and the bankruptcy of banks. (Burton and Brown, 2014; CGFS, 2018) Therefore, the article will analyze the Federal Reserve's response to the economic crisis from these two aspects combined with the experience of the Great Depression.

To stimulate economic growth, the Fed adopted a quantitative easing monetary policy after the Great Depression. (Kennedy, Kennedy and Jay, 2017) The outbreak of the subprime mortgage crisis in the United States triggered the financial tsunami, and the economies of various countries were deeply involved. (Jin, 2020) In order to respond to the financial crisis, not only developed countries but also emerging market countries have adopted corresponding measures, such as increasing fiscal expenditures and lowering benchmark interest rates, to continue to stimulate economic growth. Correspondingly, at the end of 2008, the Fed lowered the benchmark interest rate to the level of 0-0.25%, and other countries followed suit to increase investor confidence and stabilize the financial market. (Elliott and Atkinson, 2016) The U.S., real estate market, has begun to recover in a more liquid

market environment, with new housing rapidly rising from the steady monthly sales of 800,000 to 900,000 units in 2001 to 1.4 million units in July 2005. Under the influence of the right real estate market, commercial banks and housing loan companies began to place large amounts of subprime mortgage loans, which led to subprime credit lenders with low repayment ability entering the market. At the same time, securitization and derivation of subprime mortgages have also developed rapidly. (Рыманов and Rymanov, 2018)

The U.S., real estate industry, experienced bubbles, and the Fed began to tighten monetary policy. (Cargill, 2017) The real estate market at the peak of the market has accumulated up to \$ 600 billion in subprime mortgages, accounting for a quarter of new mortgage loans in the country, and most subprime mortgages have been Used for asset securitization. (Block, 2010) The U.S. housing index continued to decline. By the second half of 2006, the risks of the real estate market began to be exposed, the trend of U.S. real estate prices showed an inflection point, and housing prices continued to decline since the peak in early 2007. The quality of subprime mortgages has deteriorated extensively. (Pezzuto, 2014)

The Fed continues to raise interest rates, and bank liquidity deteriorates. As the main body of subprime mortgage loans, banks have been the most affected by the subprime mortgage crisis. During the period from April to June 2004, the Fed continued to raise interest rates 17 times, raising the federal funds rate to 5.25%. (Martin and Morrison, 2012) The substantial increase in the cost of housing mortgage loans in a short period makes the burden of home buyers' loan repayments surge. Moreover, the U.S. real estate market has contracted rapidly since the end of 2006, and the continued decline in house prices has prevented many subprime mortgage borrowers from repaying their debts on time, or even their homes are insolvent. Under this influence, not only has the sub-prime default rate of the real estate market increased, but the non-performing loan rate of the affected banking sector has also increased. (Seko, Sumita and Naoi, 2015)

The subprime mortgage crisis broke out, and eventually, banks closed, and many enterprises went bankrupt. The asset-liability structure of many banking institutions has deteriorated sharply. (Wang, 2019) Investment institutions and insurance companies that have invested heavily in subprime mortgage securities also generally face financial difficulties. Among them, some systemically important financial institutions such as Fannie Mae and Freddie Mac, Lehman Brothers and Merrill Lynch face bankruptcy. (Brigo, Morini and Pallavicini, 2013) The subprime crisis has spread and spread from the real estate market to the banking sector to the entire financial system. The financial crisis finally broke out and spilled out to the world through various channels. (Rude, 2010) had a significant impact on the stability of the financial market and economic growth. This became the most severe global economic crisis after the "Great Depression" in the 1930s. (Grossman, 2014)

3. Post-Keynesian Explanation of the Economic Crisis

The currency problem and the growing problem are the foundation of the post-Keynesian crisis theory, and the defects of the capitalist system have caused the root of the economic crisis.

Post-Keynesian crisis theory shows. First of all, financial investment will cause an economic crisis, and a stable environment will produce unstable factors. For example, a prosperous economic environment before 2006 caused excessive investment. This behaviour led to increased market vulnerabilities, a lack of real economic support, and caused a bubble economy. Eventually, the financial market collapsed in 2008. Secondly, the market always pursues the maximization of profits, and it is easy to fall into class solidification. And it is easy to cause problems such as people's income injustice, and thus fall into the situation of economic growth.

The direct cause of the subprime crisis is credit default, and the fundamental reason for credit default is relative overproduction. The United States has highly developed productivity and produces surplus products, but the income of ordinary residents in its society is insufficient to pay them. In order to cope with this situation, the U.S. government has adopted a policy of continuous interest rate cuts to encourage residents to borrow from banks for early consumption and investment. However, the accumulation of liabilities is only temporary for economic development, and it is impossible to continue to support economic development. The essence of the economic crisis is imbalanced income distribution and relative overproduction. Therefore, the economic crisis is rooted in the capitalist system and cannot be eliminated by some means or form, nor does it have the ability to heal itself.

Therefore, only external means are used to reduce the number of crises and the degree of disruption. The main measures include: strengthening financial market monitoring, reasonable and fair redistribution, and always paying attention to changes in demand and supply.

Post-Keynesian thinking on crisis theory is more comprehensive, and it is carried out from multiple angles and in many fields. It has the characteristics of openness and inclusiveness and focuses on the achievements and ideas of various economic theories in many aspects. At the same time, the post-Keynesian attention also has its perfect complement.

First, pay too much attention to investment behaviour and ignore consumption behaviour. After Keynesianism, a large amount of analysis of its investment behaviour, except for the impact of interest rates, but why it caused its investment behaviour-consumer demand, did not further dig into it. Only the impact of investment demand is considered, and the role of consumer behaviour is not further considered. The second is that the focus is mainly on the demand side, and there is little research on the supply side. Most of its policy recommendations are aimed at social needs, distribution systems, and financial systems, and lack supply-side considerations.

4. Pros and Cons of Post-Keynesian Economic Crisis Theory

Post-Keynesian considerations of the crisis are careful, involving a more extensive range of fields and a more open and tolerant attitude towards various economic theoretical achievements. At the same time, we can also see what needs to be added and perfected in the post-Keynesian crisis theory.

One is to pay too much attention on investment behaviour and ignore the impact of consumer behaviour. In the analysis of the crisis, the post-Keynesians used much space to analyze the impact on investment behaviour. However, in addition to the role of interest rates, they did not continue to tap the nominal consumer demand that caused excessive investment. In the post-Keynesian analysis, only the impact of investment demand was discussed, and the fundamental role of consumer demand was not recognized.

Second, it is too focused on the demanding field and lacks research on the supply field. The post-Keynesian policy recommendations mostly involve the regulation of total social demand, the improvement of the distribution system and the supervision of the financial system, while ignoring the role of the supply level.

5. Suggestions and Enlightenment for Post-Keynesian Economic Crisis

Through the understanding and interpretation of the crisis from the perspective of post-Keynesianism, the following three points of reference to the economic crisis can be proposed.

1) To improve demand management and deepen supply reform. The idea of sufficient demand is the core of post-Keynesianism, and the level of total social demand mainly determines economic performance.

2) Be cautious about financial liberalization. With the economic globalization, the trend of international financial liberalization is inevitable, but it must have strong risk control capabilities.

3) To establish a sound financial supervision mechanism. The smooth progress of corporate investment and production activities is the foundation of the national economic development, and its volume determines the credit needs of the enterprise.

6. Conclusion

In order to raise the post-Keynesian economic crisis thinking from the theoretical level to the practical level and prove its practical reliability, this article introduces the Fed's monetary policy during the 2008 economic crisis. It makes an explanation based on post-Keynesian logic. Support was given to provide new ideas and guidelines for the analysis of the economic crisis.

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