The Concept of Trust and the Political Economy of John Maynard Keynes, illustrated using central bank Forward Guidance and the democratic dilemma in Europe

Introduction

Trust is an issue to which Keynesians and post-Keynesians have paid relatively little attention. However, properly understood it is an aspect of almost all activity, including key elements of socio-economic reality. Without trust market exchange is at the very least problematic, if not impossible. Moreover, trust is intrinsic to a variety of issues with which Keynes, and subsequent Keynesianism have been concerned. In the following paper we provide a general social theory conceptualisation of trust and then set out some of the areas where this concept resonates with the work of Keynes in terms of the role of conventions. Conventions quintessentially involve trust and that trust can be unstable, can be withdrawn, and can require rebuilding. We illustrate this with reference to central bank policy and the Bank of England's introduction of Forward Guidance. Exploring the problem of trust in the context of banking also highlights a challenge for the continued relevance of Keynes' work. We now live in a neoliberal world and this provides a quite different context for state intervention than was previously the case. Keynes' work is now an argument for the alternative, and as such it requires more than a technical economic argument, it must also address the problem of trust in state policy makers. We briefly illustrate the challenge this poses with reference to Europe.

1. The concept(s) of trust

Trust might first be considered as a quality of conduct, a quality that enables or facilitates the completion of some activity. Following this line of thought the general received meaning (expressed then in ordinary language use) tends to be focused around trust as a personal attribute, usually related to ethical conduct and articulated along the lines of s/he is (is not) trustworthy (see the work of O'Neill, 2002). This individualisation as a focus is not incorrect, as such, but it is limited. It can lend itself to a reductionism where one neglects the context which causes the individual to (perhaps collectively) give or withdraw trust and can, inter alia, serve to also neglect the broad range of things that trust can be given to or in. It is a focus that does not necessarily or consistently emphasise that trust is relational and that, since social relations can be of many kinds, trust can also be a complex issue beyond traditional ethical context dilemmas (see Luhmann, 1979; or Archer, ed. 2014).

One way to think about this is to consider how trust inheres in the classic agent-structure problem. An agent is more than the sum of their socialisations and agency cannot be reduced to structural determinism. Conversely, structure is more than simply an aggregate of individual actions at any one moment in time, it has some form of significance for the nature of activity that can be engaged in over that time. If agents are considered individually only then it is difficult to make sense of what causes them to be more or less trustworthy and to give more or less trust, and it is difficult to consider the many institutional and systemic components that may influence whether in fact trust is given and whether in fact that trust is appropriate. As many in organization studies and some within economics have noted in recent years, this has created particular problems in terms of the aftermath of the global financial crisis (see Bachmann and Inkpen, 2011; Dow, 2012a and 2012b).[1] It has also, following a longer timeline, proved a difficult issue for mainstream economics (in ways one can easily imagine in terms of issues of tractability and conformity to utility functions, rationality, methodological individualism, differentiations of social capital as an attribute etc.; see work focused on Williamson, 1993; and also Davis, 2009; Christoforou, 2013; Latsis and Repapis, 2014).[2]

What we want to briefly suggest here is that trust has multiple relevant components. In particular these seem to resonate with a broadly realist social ontology (see Lawson 1999 & 2012; Collier, 1995, Chp 5). For the sake of brevity and to allow us to move quickly to the work of Keynes we draw on previous work and list key aspects here (see Colledge et al 2014, pp. 1-2):

1. Trust is about activity that is intended in some sense *to* occur (and other activity and outcomes that are not): it is forward directed.
2. Trust involves significant relations: the activity involves others and relies upon them in a variety of ways; to do something, to be something, to allow something, to complete, facilitate, or not impede something…
3. Trust is given or placed, it may be placed in a person, a person in a role in an organization, or in increasingly anonymous and impersonal entities such as governmental and corporate actors and also the web of configurations that affect any role, organization etc (e.g. codes of conduct, industry bodies, relevant law and broader norms). Trust may be given quickly or slowly and over different distances (based on physical presence or mediated by technology).
4. Trust may be mutual or reciprocal, but is not necessarily symmetrical in either its extent or significance to the parties. The greater the significance of some circumstance to the party the greater the sense of confidence that is likely required in order for trust to be given or placed.
5. Trust is a means by which the scope for activity is extended or expanded (it is an operative aspect of emergence); what is done is affected by the scale and scope of the original commitment; if the original commitments are fulfilled it can be agreed that the extent of the commitment should be increased.
6. Trust involves judgment: the activity requires the anticipation of some outcome and to expect that this will be achieved and this is part of the reason for the activity actually occurring (one is doing more than merely hope, blind trust is not trust).[3]

[1] Trust has been a significant area of research in organization theory for some time (see e.g. Zucker, 1986; Kramer, ed. 2006)

[2] Consider how the problem of trust underpins issues in environmental economics – the tragedy of the commons, the work of Ostrom (e.g. 2010) etc – as well as game theory; whether in fact trust is reasonable and how this is reasoned out is at least implicit in game theory and is also investigated in neuro and experimental economics (e.g. Charness et al 2004; Cox 2004). Within social economics, the most significant work on trust has been done by those who work on aspects of the gift economy, and also issues of care and reciprocity, van Staveren, for example, contrasts heterodox and mainstream models of care (2005, contrast this with Baron, 2013, who explores wage premiums in a more orthodox context). See also Davis (2003)

[3] Note, this focus on judgement is one which places an emphasis on the existence of reasons as causes and notes also, as old institutional theory following Hodgson also claims, that behaviour may become routine in a certain sense but is always initially grounded in reasons and can be reconstructed in terms of particular forms of reasoned conduct. This focus, however, does not address certain kinds of primary relationships

Judgment may be based on experience – the repeated dealings with another individual or entity, the repeated achievement of something in terms of an activity; or it may be based on the experience of others or on some form of advice, information or research. The judgment may be directed to all or only some aspects of the relations in terms of which trust is given or placed.

7. Trust involves uncertainty: there is the possibility that what is intended may not occur (otherwise trust seems a semantically inappropriate term for the situation). One may be aware that an activity can simply fail to realise a particular outcome based on chance or one may be aware that the activity involves antagonistic parties and interests that can confound subvert or redirect the activity.
8. Trust is exhibited through the activity engaged, but not necessarily by its successful completion. That trust has been given is only revealed by following through to engage in that activity. However, an observable act need not be evidence of trust nor can the failure of an outcome to be realised be evidence that there was an absence of trust. The existence of trust is a interpretive issue.
9. Trust is a means by which the possibility of an activity is reproduced through the activity, and the activity helps to *build* and reproduce trust… Trust may be built in a narrow sense, through repeated dealings with a given person, organization etc, and/or built in a broader framework of institutions through repeated dealings with different participants in that framework.

Clearly, trust can be considered in mutliple ways and in many contexts. One need only think of a personal example of where you have given trust and then translate it through 1-9 to consider this. In the most generalised sense trust seems to be no more or less than a term for the situational social glue that expresses some aspect of *how* relations are engaged (or refused) with a view to (in)completion. It involves the *aboutness* of the individual or group within the wider complex of social reality. Considered in this way, the study of trust is simply a relevant frame of reference for investigating the multi-form of social reality, and this includes issues in economy. It is then curious that relatively little attention has been paid to the significance of trust for the work of Keynes and then for the contemporary significance of the work of Keynes in the twenty first century. Keynes was acutely aware of the importance of trust to the workings of capitalism and also its varieties. In what follows we attempt to ilustrate rather than comprehensively establish that this is the case.

2. Keynes on trust, uncertainty and (in)stability

Keynes' seminal contribution to economic theory, *The General Theory of Employment, Interest and Money* is intimately concerned with issues of trust. This is not surprising given that the work is an attempt to make sense of the inherent instability of capitalism, which relegates the theoretical construct of necessary full employment based on contemporary precepts to a special case (e.g. Pigou's *Theory of Unemployment* where unemployment is voluntary and temporary because real wages fail to adjust; a claim that neglects that demand for labour is derived etc. and that defaults to a form of Say's law). The *General*

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where trust may well be blind (up to some significant threshold), such as the parent child relation (we thank Robert McMaster for this point).

Theory provides an economic specification of basic insights regarding social reality: it recognizes that the system is a complex, multi-relational and historically conditioned process (see also Martins regarding this, 2014). What people decide to do individually and collectively matters to the aggregate of outcomes. Any decision-making context involves trust based on some combination of elements 1-9 in the previous section. As such, trust is one of the features that both accounts for capitalism's periods of relative stability and expansion and its tendency towards instability and collapse. There are multiple points of entry one might consider in terms of Keynes' theory, but responses to the nature of uncertainty are perhaps of primary significance. As Keynes states:

> The outstanding fact is the extreme precariousness of the basis of knowledge on which our estimates of prospective yield have to be made. Our knowledge of the factors which will govern the yield of an investment some years hence is usually very slight and often negligible. If we speak frankly, we have to admit that our basis of knowledge for estimating the yield ten years hence of a railway, a copper mine, a textile factory, the goodwill of a patent medicine, an Atlantic liner, a building in the City of London amounts to little and sometimes nothing; or even five years hence. (2007/1936: pp. 149-150)

And:

> By uncertain knowledge, let me explain...The sense in which I am using the term is that in which the prospect of a European war is uncertain, or the price of copper and the rate of interest twenty years hence, or the obsolescence of a new invention, or of the position of private wealth owners in the social system [thirty years hence]. About these matters there is no scientific basis on which to form any calculable probability whatever. (1973: pp. 113-114)

For Keynes, following his earlier work on probability, social reality is intrinsically uncertain (for analysis see Davidson 1991; Lawson, 1988). However, it is not thereby either inexplicable (rather than slavishly predictable) nor is it lacking in attempts to shape the present and future. Human conduct is intimately concerned with attempting to find and construct ways to cope with uncertainty – the very basis of society is concerned with this and economic activity is merely a subset of this. Keynes was aware that for economic theory to be adequate one must apprehend the general way in which uncertainty is managed and then explore more specific systemic problems that actually arise, including as a product of the limits of how one does or can manage that uncertainty. These, for example, are the underlying issues in Keynes' development of the marginal efficiency of capital. Keynes is intimately concerned with the psychology of the human but also with the nature of the rules through which psychology operates. In capitalism:

> How do we manage in such circumstances to behave in a manner, which saves our faces as rational, economic men? We have devised for the purpose a variety of techniques, of which much the most important are the three following.
> (1) We assume that the present is a much more serviceable guide to the future than candid examination of past experience would show it to have been hitherto. In other

> words we largely ignore the prospect of future changes about the character of which we know nothing.
> (2) We assume that the existing state of opinion as expressed in prices and the character of existing output is based on a correct summing up of future prospects, so that we can accept it as such unless and until something new and relevant comes into the picture.
> (3) Knowing our own judgment is worthless, we endeavour to fall back on the judgement of the rest of the world which is perhaps better informed. That is, we endeavour to conform with the behaviour of the majority or the average. The psychology of a society of individuals each of whom is endeavouring to copy the others leads to what we may strictly term a conventional judgement. (1973: p. 114)

Here, knowledge is not simply a matter of epistemology based on some concept of truth as an identified/achieved correspondence, it is rather a matter of judgment and the basis of judgement i.e. the justifications – it is thus, in a real and practical sense in a capitalist system, an issue of convention and the reliance on convention (for a variety of issues of convention see Latsis et al, 2010; Al-Amoudi & Latsis, 2014); it is a matter of where and in what trust is placed. Keynes was quick to see that reliance creates a basic problem since that in which trust is placed may simply be unreliable or become so. There is to some degree a performative-adaptive tension within this issue of reliability. As Keynes recognized, decision makers can continue to use given conventions even where they appear already to be failing (insecurity can cause one to fall back on the familiar). However, the failure of conventional behaviour to result in anticipated outcomes can then affect further responses. Keynes connects the two by the state of confidence as a general term for the flow of behaviour based on the ongoing use and response to convention, which is then significant for its influence on the schedule of the marginal efficiency of capital (Keynes, 2007/1936: p. 149). One can then consider this in more technical terms based on the inherent positive feedback loops that occur in Keynes' system as investment, employment and consumption decisions are made – creating different interacting dynamics through aggregate demand, and including the derived demand for labour (hence the possibility of involuntary unemployment that violates Say's law and refutes Pigou). Trust is of central importance here because the term captures an intrinsic judgement regarding the reliability of convention and then is also significant in terms of changes in behaviour. A feedback loop can also be described as a progressive ripple of trust being withdrawn and perhaps of new conventions or behaviours being sought and constructed. For Keynes, a practical theory of the future has the following shape:

> In particular, being based on so flimsy a foundation, it is subject to sudden and violent changes. The practice of calmness and immobility, of certainty and security, suddenly breaks down. New fears and hopes will, without warning, take charge of human conduct. The forces of disillusion may suddenly impose a new conventional basis of valuation… At all times the vague panic fears and equally vague and unreasoned hopes are not really lulled, and lie but a little way below the surface. (Keynes, 1973: pp. 114-115)

The reliability of convention is only one aspect of Keynes' work in which the concept of trust seems to be significant. The nature of the conventions and institutions in which trust can be placed are also significant in a different sense. Keynes recognizes that a system can be subverted by the conventions that it encourages to emerge and that then shape the behaviour of participants. In particular he focuses on the speculative nature of investment, where activity forecasts the psychology of the market (Keynes, 2007/1936: p. 58), famously stating:

> [P]ersons are, in fact, largely concerned not with making superior long-term forecasts of the probable yield of an investment over its whole life, but with foreseeing changes in the conventional basis of valuation a short time ahead of the general public. They are concerned, not with what an investment is really worth to a man who buys it 'for keeps', but with what the market will value it at, under the influence of mass psychology… professional investment may be likened to those newspaper competitions in which the competitors have to pick out the six prettiest faces… [where we reach] the third degree where we devote our intelligences to anticipating what average opinion expects the average opinion to be. (Keynes, 2007/1936: pp. 155-156)

Here Keynes is drawing attention to the general context of the casino qualities of investment and the role of animal spirits (Keynes, 2007/1936: pp. 159 & 161). One can bring together these issues for trust (the reliability of convention, the withdrawal of trust, seeking to construct new conventions and the problem of the context in which trust is placed) using the example of recent central bank policy in the UK.

3. Central banking and a crisis of trust

Central bank policy is concerned with matters of trust in many ways and central banks were developed based on a variety of historical issues; for example, the financing of war. One important justification for a central bank was to create a solution to the problem of runs on banks. The very existence of the lender of last resort function was deemed significant not just because it created an actual means to resolve problems, but because the existence of that means created confidence in retail and commercial banking that meant the lender of last resort function may not need to be used. A conventional basis for trust was built in a general situation of economic uncertainty, and this has served to enable banking activity. The aim was to forestall positive feedback loops within the finance system – to reduce the potential for a progressive withdrawal of trust. However, since the system has always remained one where banks are private organizations run for profit in a fractional banking system then the degree to which one can manage uncertainty here has always been both limited and conditional on the wider context of the general economy and of financial activity.

The role of central banks has qualitatively changed as the structure and significance of the finance system has changed, and conventions have been a significant contemporary issue here for central bank policy, both in terms of the causes of the Global Financial Crisis and in terms of responses to it (Arestis and Sawyer, 2004; Angeriz and Arestis, 2007; Morgan, 2009). Prior to the Global Financial Crisis, during the period commonly referred to as the Great Moderation, central bank policy across the major economies, including in the UK, prioritised price stability (see Morgan, 2013). The Bank of England targeted an inflation rate and did so based on an economic model that sought to balance a growth trajectory based on inflation, unemployment and an output gap. Though the Bank drew on many data sources, its basic model of the economy was (and continues to be) of a dynamic stochastic general equilibrium

(DSGE) form, making use of a Taylor Rule to manage the growth trajectory. Specifically, adjustments are made to nominal short-term interest rates (as a base rate). The dynamics of this in terms of the DSGE are technical but the process has also been one that fundamentally relies on influencing behaviour through the way interest rate policy is positioned and communicated. The operational independence of the Bank of England granted in 1997 was intended to provide the Bank with a credible basis for stable policy that would be well-understood by economic actors. The (somewhat flexible) use of models and rules contributed to the sense that policy was understood, but so also did the concomitant way in which interest rate policy was intended to be broadly interpretable.

A conventional basis thus arose for interest rate policy: small, well-signalled and regular changes in nominal interest rates. The intention was that trust could be placed both in the general competence of the Bank of England and then in the specific policy trajectory of the Bank of England and this would contribute to a stable context for economic activity. The problem, however, was that the consequences of the conventions exceeded the intentions and oversight of the Bank of England. Since changes in interest rates were small and well-signalled (though this did not mean entirely transparent prior to the crisis) economic actors realised they could manage interest rate policy, reversing the intention of the Bank to manage the behaviour of actors. Clear policy tendencies (as well as low interest rates) meant that more debt could be generated and more leverage applied to that debt with apparent degrees of confidence. Moreover, this could be done in the context of financialised economies where the organizations and institutions of finance created great scope for the use of financial instruments and strategies (which then meant further unintended consequences in terms of originate and distribute strategies, which translate in mainstream economics theory into problems of agency alignment and moral hazard). Central banks, including the Bank of England were paying relatively little attention to the trends in financial activity and one reason for this was that the primary focus had become price stability, where it was assumed financial stability would flow from an economic environment that exhibited price stability (financial crisis would be localised, could always be managed, and in any case the dominant position was that such crises could not be adequately predicted).

Clearly, though central bank policy was not *the* cause of the Global Financial Crisis, it was a contributory factor and part of its contribution was the construction of the basis for conventional behaviour. As such it provides an archetypal example of the relevance of a Keynesian approach to convention and trust; an unstable situation of reliance is created and tends to persist for some time despite accumulating problems. This is in addition to any other issues that might arise in terms of a technical Keynesian critique of banking based on the money multiplier, or any Post-Keynesian argument regarding endogenous money and the claim that banks have discretion in a fiat system to create credit at will rather than in response to deposits and savings. In terms of the Global Financial Crisis the problem of conventions and trust arose in a context of interconnection with issues of growing speculative investment opportunities and trends. The complex that arose then resulted in a variety of feedback loops or points of withdrawal of trust as specific problems manifested. One might point to the run on Northern Rock that began in September 2007 and was the first on a UK bank since 1866. One might point to the gradual realisation among key economic actors that the valuation of assets could not be trusted and that one could not trust particular counterparties to be sufficiently liquid (or solvent) to repay loans or redeem deposits, creating a situation of distrust in inter-bank lending markets from August 2007, and in commercial paper markets and primary broker relations from early 2008, which resulted in what were effectively runs on the investment banks and the investment arms of universal banks (as counterparties ran down assets and reduced credit availability), culminating then in the Federal Reserve's refusal to bailout Lehman Brothers in September 2008, an event that exacerbated all other existing problems because it signalled the Fed would not or could not be relied upon.

It is important then to note that the Global Financial Crisis was not just a failure of models and of the mechanics of financial strategies that had economic consequences, it was also a crisis of trust that had compounding real world consequences. One can then view central bank responses to the crisis as also attempts to rebuild trust in their own competence as part of rebuilding the conventional aspects of economic activity. The eventual response (though there are arguments regarding timing and whether in fact central banks waited longer than necessary) was to commit to resolving the immediate problems of the Crisis by any means necessary. In the UK this meant making liquidity available from the Bank of England via existing facilities as well as new ones, equity investments into the banks in the form of partial and temporary nationalisations, suspending market concentration concerns and encouraging mergers and acquisitions, reducing short-term nominal interest rates rapidly and in large percentage terms towards a zero bound threshold (in the UK to 0.5% since March 2009), and introducing quantitative easing (Joyce et al, 2011; Goodhart and Ashworth, 2012; McLaren and Smith, 2013).

4. Rebuilding trust? Forward Guidance, 2013-14

In July 2013 Mark Carney took over as Governor of the Bank of England, and in August 2013 introduced Forward Guidance as a new form of the interest rate signalling policy utilised prior to the Global Financial Crisis (Carney et al, 2013). Prior to the crisis the strategy was to position the major Bank of England publications, particularly, the quarterly *Inflation Report* and its various forecasting scenarios, within a narrative that indicated a trend in interest rate policy, where the form of changes in interest rate were then also well understood (small incremental movements). Forward Guidance adds to this a set of commitments or thresholds that are to be met *prior* to any interest rate change. The context is one in which there is a perceived need to address concerns over when historically low interest rates will begin to rise and what it is that will enable that to occur without major dislocations in the economy. The intent is then to create confidence amongst economic actors, of which there is a significant range from households concerned with their mortgages, credit cards and car loans, to businesses, institutional investors, and various other actors in the finance system such as investment banks. Specifically, the point was to firm up longer-term expectations regarding the cost of credit and hence the management of debt, (and within the finance system this then also creates scope to anticipate trends and changes in bond yields, exchange rates and so forth). When first introduced the core guidance was that the base rate would not increase from 0.5% until unemployment fell below 7%.

Here, Forward Guidance can be categorised as an attempt to reconstruct the pre-crisis conventions by which interest rate policy was made interpretable, thereby creating a basis for trust through the conditional management of uncertainty (§1, aspect 7). The context is clearly one in which trust must be rebuilt (aspect 9) and so the intention is that trust can become an emergent property (aspect 5). One might argue here that rebuilding trust is achieved on the basis of the clarity and consistency of the procedures (aspect 3), and how that is judged (aspect 6), where the main criterion seems to be the reliability of the conventions. Trust typically involves the bridging of a gap where relations or activity can but need not occur, it involves connectivity, like a social synapse. Starkly stated the core of Forward Guidance appears to be an attempt to harden the basis of communication by the Bank, creating a tighter specification. It seems to provide some basis for reliance, encompassing some of the characteristics of a contract but without the further important characteristics of enforceability of terms or recompense for any violation.

However, the form of the commitment was not as clear as it might at first seem. The point of the threshold was to communicate to economic actors that the Bank had no immediate intention of raising the base rate whilst recovery from recession remained precarious ('escape velocity' had not been achieved). As such, the threshold was stated as a point beyond which the Bank *may* consider increasing the base rate – it was not a definite trigger. This was particularly so since the Guidance was presented in the context of further 'knockouts' or reasons why it might be suspended or simply not followed. If inflation (CPI) continued to exceed 2.5% (and so deviates from the Bank target of 2%), then the Bank signalled that it may raise rates, but again, this provided no definite trigger, since the inflation rate was 2.8% at the time of the introduction of Forward Guidance and had exceeded 2% for significant durations of the post-crisis period without any such rise (though it had begun to trend down in 2013). In addition, it was stated that the commitment might be suspended if a significant financial event was to occur (a threat of deflation, some renewed source of financial crisis, such as adverse movements in the Eurozone or a housing market problem or where some other form of asset bubble phenomena was to arise).

The important point here is that it became immediately obvious that the Bank did not control the context that would cause it to modify, adjust, or suspend the commitment it had stated as Guidance. Stating the procedures as Guidance simply emphasised the degree to which the contexts exceeded the control of the Bank (much as they had prior to the Global Financial Crisis). Significantly, since all economic actors were already aware that the Bank was operating in a context where the timing of interest rate rises had become problematic because any rise would affect the cost of debt and may cause many whose real incomes had eroded to suffer (with various economic consequences for consumption, housing etc), then the new guidance threshold did not seem to be adding any constructive basis for Bank policy to be clarified in a way that contributed to a stable basis for economic activity (intended then to encourage growth) i.e. what it was that would cause interest rates to rise and when they would rise remained ambiguous. Moreover, consider the actual institutional basis of policymaking at the Bank; the Monetary Policy Committee (MPC) sets interest rates. The point of the MPC is that decision-making should arise from debate between designated experts based on available data (of many kinds). The debate may result in consensus but it need not do so, it needs merely result in a majority decision. Forward Guidance, in so far as it actually has force, undermines the basis of the MPC as a broad based forum for debate since it seeks to impose harder rule systems that affect the scope of action of members (it potentially imposes a more narrow conformist technocratic set of disciplines on a Committee already previously criticised for being technocratic). At the same time, there is no actual statutory/regularity force to Forward Guidance that requires members to conform to its strictures (such that they are) when voting and so its status is both contradictory regarding the constructive purpose of having a policy setting committee and in terms of the actual institutional framework of that organization, creating further ambiguity.[4]

Ambiguity, however, is not always cause for the absence of activity, it merely means that it takes on additional forms and characteristics, as Keynes notes and we have previously referred to in §2. Distrust rather than the rebuilding of trust is just as significant here. One area of distrust had become the very basis of Bank forecasting, since this had proven inaccurate for key economic metrics up to and following the Crisis.[5] As such, Guidance could do little in and of itself to construct a credible narrative around the forecasting built into the Bank's periodic publications, such as the *Inflation Report.* If actors dispute the future figures that are intended to shape policy then they will place limited credence in policy having that particular shape and timing at some future point. They will begin to anticipate in different ways. Consider this in terms of the centrality of the unemployment threshold for Guidance. When Guidance was introduced in August 2013 UK unemployment was 7.8%. At the time the Bank was forecasting that unemployment would not fall below 7% before mid 2016 (on the basis of a net increase of 250,000 jobs per 12 months for 36 months). This was met by considerable scepticism. Ten-year government bond yields immediately rose, implying an expectation of more rapid interest rate rises and this tended to reflect also a basic contradiction in Forward Guidance. If the policy proved credible then it would provide an additional basis for increased investment and consumption and so for more rapid economic growth resulting in greater employment, bringing forward the anticipated fall in unemployment and putting the forecast for the threshold in question (any credibility success undermined the convention). Even if this mechanism did not apply there was still widespread scepticism regarding the basis of forecasting because of the poor track record of the Bank in this regard.

As such, other market actors (analysts, institutional investors, hedge funds etc) were encouraged to apply their own forecasting. At the same time, though they could place no definite confidence in the Bank increasing interest rates because unemployment fell below 7% they had to at least model as if this would be the case for the Guidance to be of any relevance at all. The net result was then to create a new form of focus and opportunity for market activity based on the range of forecasts for unemployment that could then be constructed. Moreover, this range was one that created further opportunities for trading profits in financial markets (including via arbitrage based on different forecasts and through derivatives – focused on any area related to interest rate movements, such as exchange rates). Unemployment data is provided monthly by the Office of National Statistics and so Guidance immediately had the unintended consequence of creating a focus on and around the

[4] Edited minutes from MPC meetings are published with a short delay. The August 2013 meeting minutes include dissenting comments from Martin Weale concerning the conditionality and construction of Forward Guidance. In a speech to the national Institute for Economic and Social Research, December 2013 Weale also states: 'If Forward Guidance has done no more than codify what people had expected the MPC to do anyway then its [real/additional effects] should be expected to be small.' Note also that matters regarding asset bubbles and financial stability are the remit of the Bank's Financial Policy Committee (FPC) and not the MPC; as such, there is a further problem of institutional integration regarding decision making created by Forward Guidance.

[5] This had caused sufficient concern at the Bank that the Court of the Bank of England commissioned FED researcher David Stockton in 2012 to produce an analysis of the Bank's forecasting performance. This has also been followed up by Bank commissioned research by Andrew Wood at University of Essex 2013/14.

publication of unemployment data – something notoriously volatile from month to month. So, the introduction of Guidance creates not only ambiguity and a contradiction, but also scope for further exploitation of that ambiguity (since monthly data was now to be matched to an expectation of a net change over a 12 month period). As such, Guidance can be seen as feeding problems of the psychology of markets that exceed the conventional intentions of the Bank (a new form of an old problem for the Bank).

By January 2014 unemployment had already fallen to 7.1%.[6] The Bank's response was to reiterate its commitment to maintaining low interest rates *despite* the apparent imminent achievement of the Guidance threshold. At the January World Economic Forum meeting in Davos Mark Carney announced that the Bank would now be considering a 'broader range' of factors and options. The Bank's initial response simply served to increase scepticism regarding Forward Guidance; rather than a genuine firming of rules to create clarity and reliance it seemed to have been revealed as a failed attempt to provide spurious quantitative credibility to what was essentially a deeper de facto commitment – the maintenance of historically low interest rates. Whether that commitment has been appropriate is not the point here. The point is that Forward Guidance was undermined as a conventional approach to rebuilding trust. Both the failure of forecasting and the original ambiguity of Forward Guidance are significant – since both, in context, encourage multiple responses to uncertainty.

In February 2014 the Bank tried to recover its credibility by introducing Forward Guidance Mark II (Bank of England, 2014: pp. 8-9). Instead of identifying a single threshold, subject to knockouts, Guidance was now explicitly focused on a complex dynamic data problem expressed in terms of 'spare capacity'. Rates would now only rise when spare capacity was used up, on the basis that this creates inflationary pressure as an economy grows. Spare capacity is then defined in terms of an evolving equilibrium unemployment rate – one that shifts as investment and productivity change - and the context of absorption of the unemployed is assumed to change as the economy grows (it is therefore not quite the same as the output gap in the Bank's DSGE). In the *Report* the Bank estimated spare capacity at 1-1.5% of GDP. Here, one can point out that this version of Guidance simply exacerbates the problems of Mark I. The whole relies on the credibility of forecasting but in this case also allows the Bank to adjust the parameters. If the equilibrium rate of unemployment is reduced then the pressure for a rate rise at any given level of growth also reduces because the Bank has effectively introduced additional spare capacity into the calculation. This may seem like a data driven exercise but a great deal of the process relies on the weight given to different sources of evidence and to ongoing events and changes. One might consider the developing role of different types of employment (zero hour contracts, the self-employed, part-time employed etc) and other issues such as changing age structures or demographic elements in employment (older workers taking retirement but then returning to the workforce in new capacities) and how these seem to be influencing the further development of wage growth, and so then also one aspect of the significance of spare capacity in terms of potential price pressures.

Potential is the operative word here since Guidance is referenced by a whole set of complexly interconnecting and changing factors rather than some simple clearly stated set of

[6] The rate of growth of employment without clear signs of wage growth or productivity growth then also exacerbated contemporary debate regarding the UK's 'productivity puzzle' – economic growth appeared to be employment led rather than investment/productivity led.

fixed relations. This may well be more realistic but it is also grounds for dispute regarding when a given threshold has been achieved for the purposes of Guidance (spare capacity is elastic *and* ambiguous as a concept). This in turn creates both a problem of modelling, since the basis of the credibility of the modelling process is the isolation of key dependable relations, and then a problem of concepts – what does it really mean to talk about an equilibrium rate of unemployment? Scepticism was then further exacerbated because unemployment continued to fall more quickly than expected in 2014 and economic growth began also to unexpectedly accelerate. The Bank's response has been to reduce its equilibrium rate of unemployment from 6.5% to a range of 6 to 6.5%. Office for National Statistics data reported unemployment had fallen to 6.4% for June 2014 but that wage growth for the first two quarters of 2014 was actually negative 0.2%. Since this implies changes to spare capacity it then creates also pressure for the Bank to continue to justify and specify its Guidance. This has then created a curious reversal; rather than Guidance acting as an underlying commitment in the building of trust, scepticism regarding Guidance has become a focus and source of critique to which the Bank now finds itself responding – it has exacerbated issues of competence over and above its relation to interest rate setting. This was clearly reflected in the questioning Mark Carney faced, when presenting the August 2014 *Inflation Report* to the media (Hopkins, 2014). Carney is adamant that the Bank has a consistent approach, but in the end this is not the point, it is what is communicated and how this is used that is significant in terms of trust. Actual expectations in terms of when interest rates will begin to rise have varied considerably during the period of Forward Guidance. At the time of the August 2013 *Inflation Report*, many analysts were anticipating the base rate would start to rise in May 2015, when Mark Carney appeared before the Treasury Select Committee in June 2014 that date had been brought forward to November 2014, whilst the new data on wage growth and the *Inflation Report* of August 2014 then put the date back again to February 2015 (Hopkins, 2014). The only constant has been that when interest rates do start to rise it will be in small increments and to a level that will not exceed 3% in 2017.

So, bringing the analysis together, one can state that central bank policy involves conventions, those conventions involve the attempt to manage uncertainty and involve building trust. However, the very basis of that trust is always at issue. Keynes recognizes that a system can be subverted by the conventions that it encourages to emerge and that then shape the behaviour of participants. The Global Financial Crisis highlights that the context for trust exceeds the intentions of any given organization and this can be highly problematic. The net result can be a collapse of trust and this was something that the Bank of England experienced. Trust must then be rebuilt and this too involves matters of convention. However, the same issues arise. The context may seem new, a post-Crisis world, but the basis of conventional activity does not seem to be particularly new.[7] It carries typical hallmarks identified by Keynes that remain relevant today. There is, however a further problem that then arises *for* a

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[7] There are of course new challenges: as former MPC member Andrew Sentence argues central banks, incuding the Bank of England have so far failed to state a clear and coherent strategy regarding how to unwind quantitative easing (Sentence, 2013); the Bank of England has also failed to effectively encourage appropriate credit provision by banks for small and medium enterprises – the recent economic recovery seems to be despite rather than because of bank commitment to supporting investment. See also BIS, Monetary and Economic Department analysis (2013)

Keynesian approach, or any other that seeks to make the case for greater intervention in economies.

5. Keynes in a neoliberal world

Keynes makes the general point that 'there is no clear evidence from experience that the investment policy which is socially advantageous coincides with that which is most profitable' (Keynes, 2007/1936: p. 157). This is a point that highlights a distinction regarding that which trust is placed in. 'I trust a behaviour to succeed' is a conditional statement and may be based in some criteria of judgement, but it is not necessarily also a deliberation on the *nature* of the conventions in which trust is placed. These are not separate issues for any real economic context in terms of consequences, though they are clearly distinguishable issues. As the work of Minsky, Kindleberger and many subsequent post Keynesians (e.g. Palley, 2013) highlight, in a purely functional sense a set of conventions may facilitate economic activity for some period, but the very form of those conventions may ultimately undermine the system in which they operate – notably in terms of scales of debt, leverage, the extraction of returns and the problem of servicing.[8] This point follows from our analysis in §3. This is not to suggest that either Keynes or subsequent fellow travellers emphasise a subjectivist account of the economy, where conventions free float. It suggests rather that conventions form part of the structures of relations, which we then seek to express technically, and that we should also be sensitive to the real consequences of the quality of those conventions. This is a matter of trust as a key aspect of facilitating economic activity but then also of the quality of that in which trust is placed, i.e. whether in fact it is a social good. Social goods are ultimately matters of deliberation within a democracy – what kind of society do we choose; and this implies then a role for democratic deliberation regarding the nature of society, and of the economy as a subset of society, and then of the appropriate role of the state in terms of the structure of society and economy.

Mainstream economics in general tends to deform through game theory or incorporation into assumptions for functions the nature of convention, and also tends to neglect the problem of normative deliberation, and thus fails to adequately address the basis of trust (see Fehr, 2008; Fehr et al, 2006). However, a Keynesian position on the nature of aspects of the good society is one that faces a challenge in terms of how trust is placed in the state, and this is a problem that requires careful consideration.

We currently live in a period dominated by neo-liberalism. Neo-liberalism articulates a focus on the individual and their responsibilities, expressed as an empowered individual freed from constraint to realise themselves, and claims that a minimal state and the extension of market disciplines will help facilitate this realisation (see Harvey 2007; Mirowski, 2013; Wrenn, 2014). The reshaping of law and regulation to create space for activity, rather than to define and discipline or undertake that activity, means that there is now more of a scope for trust to be significant than was previously the case. This may seem counter-intuitive since

[8] Consider also the basic contradiction created by reference to a 'Minsky moment'. The term was first used by Paul McCulley, managing director of Pimco to refer to the 1998 Russian financial crisis as a post speculative market contraction. The term has gained traction since the GFC but is often used to refer to the periodic relevance of Minsky. However, Minsky's point is that the processes that result in financial problems are endogenous and continuous i.e. that instability emerges out of the conditions of stability. The phrasing 'Minsky moment' thus provides an inappropriate sense of the relevance and signfiicance of his work.

markets are represented as depersonalised (often distanced) mediums for exchange, but consider that it is people who must engage in social and economic interaction and the extent of that engagement has increased.

Consider again the aspects of trust 1-9 in §2; aspect 3 in particular highlights the range of ways trust can be given: persons, roles, organizations, codes of conduct etc, but also the distances and technological mediums that may contextualise how trust is given. There has been a great proliferation in the diversity and significance in the range of ways we give trust and how we give it based on technologies. Moreover, the more we engage in exchange relations and the more we are required to take individual responsibility, and to use technological mediums, then the more aspect 7, uncertainty, becomes a concern. As such, trust is now a quite different issue than it was during the social welfare Keynesian consensus period, and arguably is more significant. To realise this is the case one need only refer to §§'s 3 and 4 and the way trust has been eroded in the banking system with which central banks are engaged. This, however, raises the issue of trust in the alternative.

In the Preface to *The General Theory* Keynes emphasises that a major impediment to thinking and acting differently is 'escaping habitual modes of thought and expression' (Keynes, 2007/1936: p. viii). To some degree *The General Theory* was successful in breaking the mould, paving the way for macroeconomics and for interventionist fiscal and monetary policy that sought to manage the business cycle, and with a focus on effective aggregate demand. However, modern mainstream economics has gradually shed its Keynesian components and has developed a contemporary form of pre-Keynesian economics (despite reference to a Keynesian synthesis, or claims to incorporate Keynes through the IS-LM in aggregate demand and supply analysis, see Colander, 1995; Moseley, 2010). Labour is treated primarily as a unit cost, subject to marginal productivity of labour, and the labour market is treated as any other market, rather than as a site of derived demand, so unemployment becomes voluntary, subject to a natural rate, and the focus shifts to supply side economics. Unemployment (and matching investment to savings) has become a short-term problem resolved by adjustments in interest rates. Effective demand has simply been neglected as a key issue that justifies state intervention through expansionary fiscal policy and active demand management, and one rarely hears of any positive discussion of multipliers or socialised investment; rather there is a focus on policy ineffectiveness, on price stability as taking priority over full employment (even if both are ostensibly targets) and also a general further context that identifies government failure as a greater problem than market failure. One important issue here then is that there is now distrust in the political and economic elites capacity to manage an economy with a greater role for interventionist policy. This seems to be the antithesis of a Keynesian position.

6. Keynes on trusting economists and state policy-makers

Keynes was an elitist, in the sense of placing great faith in the technical capacities and potential for moral conduct of a specialised few in the service of the many (see Skidelsky, 1992). However, in terms of solving real world problems he was a pragmatist, whose pragmatism combined his theoretical critique with solutions that addressed the fundamental changes that theory seemed to imply (Skidelsky, 1992: p. 224). Specifically, the context of capitalism (as Marshall had previously also noted in 1890) was changing to larger more complex forms, based on joint stock ownership, and where there were also competing models of the organization of production (cooperatives) and, increasingly, new power blocks within industry, such as unions. With this in mind Skidelsky states Keynes:

> Was never interested in institution-building, whether creating markets or organs of state planning. He took existing institutions as given and tried to work with their grain. A new ideology was required for a capitalism evolving into more organized forms. This was quite different from the robust liberal or socialist approach of remoulding institutions to fit theory. The institutional shifts which Keynes observed were the eclipse of the independent entrepreneur, maximising his profits, by the joint stock company, mainly interested in the general stability of trade; the organization of the labour market by trade unions; the increasingly dominant role of the banking system in determining monetary conditions; and growing state responsibility for investment through the rise of the public corporation. (Skidelsky, 1992: p. 229)

Keynes, of course, did advocate the desirability of more state planning as a solution to the instabilities of capitalism, '[I]f the bulk of investment is in public or semi public control and we go in for a stable long-term programme, serious fluctuations are enormously less likely to occur' (Keynes, 1980: p. 326).[9] Keynes' work is thus antithetical to neoliberalism in terms of the content of theory as a resource for policy – and this extends to demand management and fiscal stimulus. Concomitantly, his work is also antithetical in terms of its refusal to place a greater weight on government failure than market failure; specifically, one could place some confidence in the architects of state planning for right conduct. This is explicitly stated in a letter to Hayek regarding *The Road to Serfdom*:

> I should say that what we want is not no planning, or even less planning, indeed I should say we almost certainly want more. But the planning should take place in a community in which as many people as possible, both leaders and followers, wholly share your own moral position. Moderate planning will be safe if those carrying it out are rightly orientated in their own minds and hearts to the moral issue[...] But the curse is that there is also an important section who could almost be said to want planning not in order to enjoy its fruits but because morally they hold ideas exactly the opposite of yours, and wish to serve not God but the devil[...] Dangerous acts can be done safely in a community which thinks and feels rightly, which would be the way to hell if they were executed by those who think and feel wrongly. (Keynes, 1980: pp. 386-387)[10]

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[9] Keynes also discusses institutions in 'The End to Laissez-Faire' (1972). Here he considers the need for 'semi-autonomous bodies within the state. I thank an anonymous referee for this point.

[10] Keynes also comments: 'In my opinion it is a grand book. We all have the greatest reason to be grateful to you for saying so well what needs to be said…[M]orally and philosophically I find myself in agreement with virtually the whole of it; and not only in agreement with it, but in a *deeply moved agreement.*' (Keynes, 1980: p. 385, emphasis added). However, Keynes took great exception to Hayek's review of his *Treatise* noting 'Hayek has not read my book with that measure of good will which an author is entitled to expect of a reader. Until he can do so, he will not see what I mean or whether I am right.' (Skidelsky, 1992: pp. 456-457)

Here, Keynes adopts a more balanced position than is traditionally read into Hayek (who bases his thesis in *The Road* on the inevitable degeneration of even good intentions as well as on the coordination problem inherent in planning). Keynes' position implicitly emphasises the conditions or institutional dynamics of trust. In the hands of an appropriately educated elite, planning can be made safe, and protect the essentials of a free society.

Here it is worth again emphasising that Keynes' work has not been decisively refuted. Rather it has been deformed, distorted and gradually neglected by mainstream economics over the last thirty years (Grieve, 2014). Yet mainstream economics from within which Keynes' work has ceased to be recognizable itself lacks explanatory credibility, and has played a significant role in the recent global financial crisis and subsequent global recession (see Morgan, 2013). There is also a general lack of public trust in economists. Moreover, despite the clear limitations of doing so, political and economic decision makers have persisted, much like the actors of the 1930s, with contemporary conventions and associated knowledge frameworks of those conventions, despite that the fundamentals of those frameworks helped to create the conditions in which they find themselves (see Morgan and Sheehan, 2014). One need only consider the dynamics of austerity and of the measures imposed by the Troika in Europe to see old behaviours repeating in new contexts (see Patomaki, 2013). Involuntary unemployment of the kind identified by Keynes in *The General Theory* (Keynes 2007/1936: p. 6) is widespread across Europe, and particularly in the key states subject to conditionalities. The scale of human suffering created by policy may not be of the order endured during the 1930s, thanks to welfare nets and automatic stabilisers (the last legacy of a Keynesian approach), but it is still significant. Though Keynes' position is radically at odds with contemporary mainstream economics and with neoliberalism both his technical economic argument regarding the instability of capitalism, extending to solutions to any manifest crisis, and his focus on conventions, where trust matters, remain important alternative positions today (see also Dow, 2012c). However, one might also consider what is required for trust to be collectively placed in a specific contemporary context and it is with this we conclude.

Conclusion: trust, elites and democracies with reference to the European Union

Keynes was of the view that in the hands of an appropriately educated elite, planning could be made safe, and protect the essentials of a free society. However, thereafter, he pays little attention to the further context of Hayek's concern as it is expressed in the Platonic problem of *Quis custodiet ipsos custodes* (who will watch the watchers/guard the guards?). This is an associated problem of whether trust is to be collectively given. It implies also a context of democratic oversight, deliberation and participation to create checks and balances and to help shape the form of any institutions and organizations. This also is a situation antithetical to neoliberalism in a general sense, since neoliberalism has been associated with the carving out of technocratic spheres of influence regarding policy (see e.g. Moran, 2007; Wolin, 2010). Here, one might argue that the difference between Keynes and later approaches revolves around the nature of technocratic solutions to problems: more substantive shaping and control and intervention versus more market-conforming regulation and limited oversight. However, some post-Keynesian inspired political economists have also worked on the issue of a greater role for the many that addresses *Quis custodiet ipsos custodes* and so also implicitly addresses the deliberative aspect of how trust can be built in and given to forms of institution and organization (see Martins, 2014; and the many works of Patomaki, e.g. 2013).

Such work regarding both the nature of policy (a Keynesian alternative) and of the democratic context in which trust is to be given is particularly significant for contemporary Europe. Across the European Union's constituent states it is recognised that the EU-wide institutions are both deeply undemocratic and unpopular (see Duroy, 2014). The elections of 2014 speak directly to this; right-leaning parties with a profound scepticism regarding the EU as a potential federal organization, and as a highly bureaucratic distanced and alienated entity, made gains across the member states, as did some left-leaning parties that also responded to the way the Troika has imposed punitive policies that have served mainly to socialise costs (financial and human) from the global financial crisis. The broader context here is a long-recognised democratic deficit that has never been fully or adequately addressed, which only encourages disillusionment and pessimism.[11] This then causes popular disengagement with the very limited democratic procedures to elect the European Parliament.[12]

Data suggests a pronounced withdrawal of collective trust from the institutions of the EU in the aftermath of the global financial crisis. According to the Standard Eurobarometer, those willing to trust EU institutions peaked in 2007 at approximately 60% of member state citizens; by 2013 that figure had fallen to just above 30%. Member state citizen's positive image of the EU, meanwhile, significantly deteriorated, reducing from 52% in 2007 to 30% in 2013; relatedly, support for the Euro has markedly declined, and opposition to it strengthened (see Standard Eurobarometer, 2013). Data on trust in the European Commission is not published, but it is likely to be at least as unpopular as other EU institutions. One might then infer that European citizens have increasingly withdrawn trust from those EU's institutions. This creates a dilemma, calls for increased EU powers to fundamentally reshape economic policy, for example, a profound new approach to debt within greater integration regarding fiscal policy and a reshaping of the European Central Bank's remit, are currently inconsistent with European popular sentiment. This, however, extends also to trust levels in member state governments, which, according to the Eurobarometer, are even lower than those for EU institutions. As such, the dilemma at the European level is reproduced in the domestic politics of many member states. A withdrawal of trust from elites, authority, and government needs to be addressed as part of the argument for *why* a Keynesian alternative might be preferable to current policy formats. This is clearly a matter that Keynesians need to pay greater attention to. This is not least because there is a *zeitgeist* problem here. Keynes was the product of a paternalistic society where it was simply assumed, the existence of democracy notwithstanding, that an elite had both the right and the powers to shape policy. The existence of arguments for socialism and for reformist democratic socialism was not antithetical in reality to deference, hierarchy, or paternalism. This seems deeply

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[11] Consider, for example, that the EU has a transparency register for organizations seeking to influence EU bodies, but registration is not mandatory. As of May 2014 the register had 6588 registrant organizations. According to the campaign working group Corporate Europe Observatory there are at least 30,000 lobbyists working in Brussels (compared to 31,000 EU staff), there is a widespread problem of revolving door employment of MEPs with large corporations and many corporate interests dominate consulting and advisory committees for EU.

[12] In the EU Parliamentary elections of 2013, approximately 60% per cent of the electorate did not vote, whilst of those who did, approximately 25% supported explicitly anti-EU parties.

rooted in Keynes' confidence that one could trust planners to serve 'God not the devil'. It also flowed easily from the demonstrable successes of world war, where victory had relied heavily on generalised state planning and control. We do not live in that world anymore. It may well be that trust is intrinsic to many issues with which Keynes, and subsequent Keynesianism have been concerned; notably regarding issues of conventions, judgement and uncertainty, but there is also great scope for further elaboration on issues of how trust is built in institututions and how those institutions and any constituted organization operate, and such work is of great contemporary significance.

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