

The logical flaws of neoclassical economics and why we should not teach it

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Abstract: For decades, post-Keynesians and other heterodox scholars have repeatedly and strongly argued that neoclassical economics was logically and theoretically flawed, that it was “wrong” (King, 2013), and that it was, following Keynes, “misleading and disastrous” if we taught it to students. Some attacked its many assumptions, others its methodological weaknesses; others still its neglect of institutional, historical, political, and social factors, focusing too heavily on static, mathematical models. This paper makes the case that given the flawed nature of neoclassical theory, we should not teach it to undergraduates, and instead make them stronger in data and empirical analysis to make them better job candidates.

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1 Introduction

At a conference at Queen Mary University, in November 2023, one of us presented our joint paper on the state of neoclassical theory and whether we should be teaching it at the undergraduate level. While the audience consisted mainly of heterodox and heterodox-friendly economists, the presentation nonetheless led to some intense discussion on whether we should be teaching neoclassical economics to undergraduate students. While we were of the opinion that we should not teach neoclassical economics, as the title of this paper suggests, many of the attending heterodox economists reacted negatively – which surprised us.

Subsequently, we wrote a blog for the *Monetary Policy Institute* (Rochon and Rossi, 2023), which commanded considerable attention. The reaction, once again, was mixed and led to some strong reactions in defence of both sides of the argument. Again, this left us rather confused.

After all, for decades, post-Keynesians and other heterodox scholars have repeatedly and strongly argued that neoclassical economics was logically and theoretically flawed, that it was “wrong” (King, 2013), and that it was, following Keynes, “misleading and disastrous” if we taught it to students. Some attacked its many assumptions, others its methodological weaknesses; others still its neglect of institutional, historical, political, and social factors, focusing too heavily on static, mathematical models.

In light of this long history of criticizing neoclassical economics, why then shy away from taking what we think is simply the logical next step: ban it altogether from the classrooms? Why are some heterodox scholars suddenly defending its teaching? Are heterodox economists consciously choosing to take the blue pill over the red one?

In sciences, for example, no one is teaching theories of geocentrism or even heliocentrism, or the so-called ‘flat earth theory’ – theories that at one time dominated science, but that were eventually rejected by evidence-based models like the ‘Big Bang’ or the theory of general relativity. In this sense, we agree with Keen (2021, p. 1), who argued that “I would keep as much of Neoclassical economics as modern astronomy kept of Ptolemaic astronomy – which is to say, nothing at all. [...] Neoclassical economics is fundamentally flawed – much like the geocentric Ptolemaic system – and should be completely replaced rather than reformed.”

A simple reason of this conclusion is clear. As Keynes (1931) tells us in “The great slump of 1930”, economic policies derived from neoclassical theory led to the Great Depression. As he writes, “[w]e have involved ourselves in a colossal muddle, having blundered in the control of a delicate machine, the working of which we do not understand. The result is that our possibilities of wealth may run to waste for a time – perhaps for a long time” (Keynes, 1931, p. 135). The same could be said about the global financial crisis, the COVID-crisis, the ecological and climate crises. Bad theory leads to bad policies with devastating consequences.

The reasons some heterodox economists give for continuing to teach neoclassical economics – on its own or alongside heterodox theories – are two-fold. First, neoclassical economics is the dominant approach in economics, and, as such, it is a mistake not to teach it. Indeed, much of the so-called pluralistic movement agrees with including neoclassical economics among the various approaches in economics. In other words, supporters of pluralism advocate for using diverse theories, methods, and viewpoints, including mainstream neoclassical and various heterodox schools, such as institutional, feminist, ecological, Marxist, post-Keynesian and Kaleckian economics to understand complex economic realities. Second, it is argued that if students do not learn the vocabulary and concepts associated with neoclassical or mainstream economics, they would be at a disadvantage in the job market and risk losing potential employment. After all, the private sector and governments are dominated by mainstream economists looking to hire those who share their theoretical view.

Our position is clear. Neoclassical economics is flawed, both in theory and practice, as it asks the wrong questions, and provides limited answers to the correct questions. It does not reflect the real world. So why would we teach something we know to be false? Why spend decades debasing neoclassical economics, only to not take the brave final step and refuse to teach it, and introduce students to heterodox economics that better reflect the real world? In fact, accepting to teach it, in any way, simply perpetuates the cycle of bad economics.

In our opinion, armed with solid theoretical and empirical evidence, we believe students would instead be at a clearer advantage in the labour market, not at a disadvantage. In this sense, if we wish to help students, we should replace the teaching of neoclassical theory with data-driven, empirical and statistical modelling.

All this, of course, is quite well known to the heterodox community. For the purpose of this article, nevertheless, we will provide a number of areas where neoclassical economics is wrong and that, as a result, should be rejected as a teaching method. In this regard, let us note that the following list is not exhaustive, and neither is our analysis in this paper. We do not cover for instance the ‘humbug’ production function, or the role of real wages and income and wealth inequality. That would require a much longer article.

In the next section, we will address the failure of neoclassical economics to explain both the nature and the main characteristics of our economic system. The third section points out the lack of empirical evidence supporting the main axioms of neoclassical economics. The fourth section focuses on the (endogenous) nature of money, which neoclassical models ignore completely. In the fifth section we will explain the supply and demand problems ignored by neoclassical economics, while the sixth section focuses on inflation, pointing out its conflict origins in contrast with the monetarist view. The last section concludes.

2 The economic system

Before discussing some specific arguments, as we do below, let us begin with the widest possible one: the nature of the economic system. After all, economic theory ought to shed light on the complexities and intricacies of the economics system in which we live, or what post-Keynesians like calling the ‘real world’, from which we can draw and propose appropriate policies for inflation, unemployment, economic growth, and more. After all, good theory leads to good policies, and in turn good theory must be based on a realistic view of how the system as a whole and its individual parts function. As Lavoie (2022, p. xv) states, post-Keynesian theory precisely provides us with a “more realistic description of the world.”

As such, the differences between neoclassical and post-Keynesian economics, however, are stark, and offer diametrically opposing views of how our economic system operates. Yet, neoclassical theory does not seem to “get things quite right” (Syll, 2018, Internet). Post-Keynesians are fond of saying that it describes an imaginary world, which is not representative of the real world.

The 2007-8 global financial crisis is a case in point. Why was neoclassical theory unable to propose relevant policies, let alone see the crisis coming? Indeed, recall how in November 2008, following the collapse of Lehman Brothers, Queen Elizabeth had asked this precise question to British economists at the London School of Economics, which the economists blamed on the “failure of collective imagination” (see Davidson, 2015, p. 1) In fact, they were just being true to their models.

As we argued elsewhere (Rochon and Rossi, 2021), the reason neoclassical theory is unable to consider the possibility of economic crises is due to the simple fact that it describes a system that has built-in mechanisms that force this system to converge toward some long-run position of stability and equilibrium. A crisis, therefore, or a prolonged period of disequilibrium, cannot exist: the economic system is self-correcting and markets clear. Of course, the system can be out of equilibrium – whatever that means relative to the real world – in the short run, but eventually it must converge to equilibrium where some ‘natural’ values of output, economic growth, inflation, and unemployment prevail.

Usually, these mechanisms have to do with flexible prices – a wholly unrealistic assumption, at least in most markets for produced goods and services. Indeed, since at least 1945 in the United States, market prices have not been flexible in the sense of going up and down. For the most part, except in 1949 and 1954, prices always went up as inflation was positive, albeit at a different pace. Inflation rates, however, have been flexible. Textbooks, nevertheless, depict goods markets as having flexible prices, and it is this price mechanism that guarantees a return to stable positions of equilibrium. This simply does not fit the data in advanced economies.¹

To be clear, this has nothing to do with the concept of price ‘stickiness’ (which in fact may be stabilizing) but rather with the nature of price setting. Prices are typically set by firms, not by invisible hands in so-called markets: they are administered through the imposition of some mark-up over some level of normal costs. As such, this suggests that they typically do not vary often: firms will leave prices at current levels for some time. Moreover, they tend to be asymmetric: firms will raise prices in light of rising normal costs, but will typically not pass cost saving unto consumers. Again, this is not due to some market stickiness, but rather because of the price setting nature of firms. As Melmiès (2010, p. 450) wrote, “prices are rarely reviewed, and even more rarely changed”. In fact, post-Keynesians argue that even if prices were flexible, this would not force the system to converge to stability and equilibrium, but would rather usher in a period of great instability (see Lavoie, 2022).

Contrast that with post-Keynesians, who are “distrustful of unfettered markets” (Lavoie, 2022, p. 26) and for whom crises are endogenous to the economic system; as such, the system is always on the possible verge of some crisis, as it is characterized by fragility and instability (see Rochon and Rossi, 2021). As a matter of fact, if one considers the performance of our economies over, say, the last two thousand years, crises have become more frequent and more pronounced. This is the nature of our economic systems, or the new reality. Economies do not converge; they are openly chaotic and subject to uncertainty.

¹ Marc Lavoie and Mario Seccareccia tell the story of the time they tried to replace flexible prices with flexible inflation rates in the AS-AD diagram in their introductory textbook (see Lavoie and Seccareccia, 2009). It was a lost cause, as the reviewers of the manuscript insisted the story had to be told in terms of flexible prices. In an email confirming this story (February 16, 2026), Seccareccia writes: “Unfortunately, all seven readers (?) were against our exposure in this framework for an introductory textbook, and the publisher literally begged us to revert to an analysis of aggregate supply and demand based on price and output levels, rather than in an inflation/output space.”

In terms of economic policies to contain or reverse the consequences of crises, neoclassical theory offered very little. In fact, in 2008-9, the official policies were calling for more fiscal austerity. As Stiglitz (2015, p. 43) argued, reminiscent of Keynes, “the models/theories that guided policy were not just innocent bystanders in the crisis that unfolded beginning in 2008. They were critical in the creation of the crisis and in the inadequate responses to it”. As we mentioned above, good theory leads to good policies, whereas, of course, the opposite is true: bad theory must therefore lead to bad policies, and it is in this sense that neoclassical theory is “misleading and disastrous.”

Post-Keynesians, following Keynes (1936), consider the economy as demand-led, so austerity is only bound to make things worse. Stability is not inherent, and the purpose of policy is to search for ways of “stabilizing an unstable economy” (Minsky, 1986). In this regard, we need more aggregate demand, not less. In fact, Summers and Stansbury (2019) came to agree with this post-Keynesian position, arguing that “we have come to agree with the point long stressed by writers in the post-Keynesian (or, perhaps more accurately, original Keynesian) tradition: the role of particular frictions and rigidities in underpinning economic fluctuations should be de-emphasized relative to a more fundamental lack of aggregate demand” (quoted in Vernengo, 2026, p. 311, fn. 16). So, it is not about convergence to an equilibrium position, but about ensuring sufficient aggregate demand in the economic system.

3 Ignoring empirical evidence

Another weakness of neoclassical theory is its lack of empirical validation or rather its refusal to accept empirical rejection. Indeed, one must wonder the usefulness of a theory that has remained steadfast in its core beliefs, as well as its refusal to change in its more than 250-year existence. Neoclassical theory can thus be described as ‘the more economies change, the more the theory remains the same’. We must wonder if this is a wise approach to economics. As everything in economics is empirical, how does neoclassical theory and neoclassical economists fare in the area of empirical validation?

Neoclassical economists are often criticized for failing to adequately respect empirical evidence, particularly when the latter challenges their core theoretical assumptions. At the heart of neoclassical economics lies a set of strong foundational premises – such as rational, utility-maximizing individuals, profit-maximizing firms, market equilibrium, and efficient allocation through price signals. Critics argue that these assumptions are treated less as testable hypotheses and more as axioms to be defended, even when real-world data contradicts them.

Consider, for instance, Friedman’s ‘irrelevance of assumptions’ doctrine, formulated in his 1953 essay on *The Methodology of Positive Economics*, which argues that the validity of an economic theory should be judged by the accuracy of its predictions, not by the realism of its assumptions. Friedman argued that ‘unrealistic’ assumptions are not only acceptable but

necessary for a theory to be useful, as they allow for simplification of a complex reality.² Critics – and there are many – reject this view. For instance, philosopher of science Ernest Nagel, in a 1963 response to Friedman, argued this approach is flawed because “a theory with an unrealistic assumption [...] is patently unsatisfactory; for such a theory entails consequences that are incompatible with observed facts so that on pain of rejecting elementary logical canons the theory must also be rejected” (Nagel, 1963, p. 215). Friedman’s instrumentalism encourages abstraction from historically specific monetary institutions, thereby weakening explanatory power. Predictive accuracy in limited contexts does not justify ignoring causal mechanisms rooted in money, contracts, and expectations.

Another key area of tension concerns the assumption of rational behaviour. Empirical findings from behavioural economics repeatedly demonstrate systematic biases, heuristics, and deviations from strict rationality. For instance, behavioural economist Dan Ariely (2008, p. 239) argues that “[o]ur irrational behaviors are neither random nor senseless – they are systematic and predictable. We all make the same types of mistakes over and over, because of the basic wiring of our brains.” Ariely’s concept of ‘predictably irrational’ shares much in common with the post-Keynesian notion of bounded rationality (for instance, see Lavoie, 2022).

Yet many neoclassical models either downplay these findings or incorporate them only superficially, preserving the broader rational-choice framework. Similarly, evidence of persistent market failures – financial crises, asset bubbles, inequality, and involuntary unemployment – often sits uneasily with models that emphasize self-correcting and efficient markets.

However, it is important to note that not all economists within the neoclassical tradition ignore evidence. Many engage deeply with econometrics and empirical testing. The broader critique, though, is that the dominant framework shapes how evidence is interpreted, often filtering data through pre-existing theoretical commitments rather than allowing empirical results to drive fundamental revisions.

Specifically, with regards to monetary policy, to ensure the stability of the system as well as the effectiveness of policies, neoclassical economics relies on specific elasticities to ensure a quick return to equilibrium. Yet, empirical tests suggest that much of these assumptions are false. For instance, in an inflation targeting scheme, the effectiveness of monetary policy rests on a well-behaved and elastic IS curve. Indeed, changes in the rate of interest must lead to changes in produced output, which in turn must lead to changes in

² In the Preface to his *General Theory*, Keynes (1936, p. xxi) has said that the aim of his book is “to re-examine critically certain of [neoclassical theory’s] basic assumptions”, since “the postulates of the [neo]classical theory are applicable to a special case only,” and that “the characteristics of the special case assumed by [neo]classical theory happen not to be those of the economic society in which we actually live” (p. 3). Finally, at the end of the book, in Chapter 24, he argued that neoclassical theory’s – which Keynes called classical – “tacit assumptions are seldom or never satisfied, with the result that it cannot solve the economic problems of the actual world” (p. 378). It is for this reason that its teaching is “misleading and disastrous” (p. 3).

unemployment and inflation, via a well-behaved Phillips curve. Yet, as post-Keynesians have argued, both relationships are very much in doubt, with the Phillips curve flattening over the last few decades (see Rochon, 2022).

For instance, consider these two quotes:

“A large body of empirical research offers mixed evidence, at best, for substantial interest-rate effects on investment. [Our research work] find[s] that most firms claim their investment plans to be quite insensitive to decreases in interest rates, and only somewhat more responsive to interest rate increases” (Sharpe and Suarez, 2014, p. 1).

“[T]he response of inflation to a measure of labour market slack has tended to decline and become statistically indistinguishable from zero. In other words, inflation no longer appears to be sufficiently responsive to tightness in labour markets” (Borio, 2017, p. 2).

The literature is full of such empirical criticism in fact, which, if true, would make monetary policy less effective in fighting inflation (Rochon, 2022), which according to neoclassical theory must be the result of some excess demand forces (see below for a fuller discussion). In New Consensus models, these two quotes correspond to an IS-type or aggregate demand equation, and a Phillips curve, respectively. The monetary policy transmission mechanism must operate through these two equations in order for monetary policy to be effective in bringing inflation rates down. Yet, with both of these not “well-behaved” factors, then the central banker has no clothes, and we must rethink what monetary policy is and what monetary policy does.

If post-Keynesian empirical and theoretical criticism is correct, there is then no justification for using austerity to fight inflation. In addition, much research, especially in the post-COVID era, has shown how much of the post-pandemic inflation was related to supply issues over which monetary policy has no influence (see Brooks et al., 2024).

This said, there appears to be plenty of empirical evidence that seems, at least on the surface, to confirm the validity of neoclassical theory and its assumptions, and contradict our conclusion. In other words, it would appear that neoclassical economists do rely on empirical results and these confirm the validity of their models. Yet, as Lavoie (2008, p. 10, fn. 31, italics in the original) has cogently argued, “[t]he numerous studies of empirical ‘evidence’ supporting neoclassical production functions or other derived constructs are worthless. This empirical evidence is nothing but spurious findings, or as the title of the paper suggests, this empirical evidence is nothing but an *artefact* [... or] purely imaginary results.”

The end result, of course, is that neoclassical theorists prefer to ignore the empirical reality and continue relying on their flawed model. This is precisely the case with monetary policy, for instance. If central bankers admitted the true nature of inflation, or the limited empirical

support of well-behaved IS and Phillips curves, it would open a Pandora's box of questions regarding what monetary policy is and what it really does. As such, "[a]ll of the forgoing examples show that central bankers are not yet willing to discard the Phillips curve as a policy tool, even though the evidence for a downward sloping curve is meager" (Dorn, 2020, Internet).

As Syll (2018, Internet) argues, "[n]eoclassical economic theory still today consists mainly in investigating economic models. It has since long given up on the real world and contents itself with proving things about thought up worlds. Empirical evidence only plays a minor role in neoclassical economic theory, where models largely function as substitutes for empirical evidence".

4 The nature of money

Having discussed 'big picture' issues above, we now turn our attention to some specific arguments within neoclassical theory that post-Keynesian economists have argued are flawed or wrong, and as such, diminish the theory and model as an effective teaching tool. We cannot possibly cover a whole range of issues, and therefore will focus our attention on a selected few of them.

We begin our discussion with a reflection over the nature of money. This choice is not random, as it highlights precisely everything that is flawed about mainstream economics – an approach that finds its roots in the fictitious story of barter. It follows the discussion laid out by Keynes that any explanation of economic activity must incorporate a discussion of money, "on the ground floor" as Schumpeter (1954, p. 278) told us. So, money must be integrated into the analysis of capitalism from the very start, as post-Keynesians do. This is the very definition of endogenous money. In other words, there cannot be a discussion over any aspect of capitalism or of economic activity without a parallel discussion of money.

This obviously clashes with neoclassical or mainstream economics. Consider how we teach macroeconomics. The first half of courses focus on explaining to students how labour and capital markets work, while referring to prices, wages, and interest rates. We draw demand and supply functions, production functions, and discuss investments while asking students to calculate rates of return. We do all this while not once referring to money. In fact, in most textbooks, money only appears later, as does its discussion in classes. This is what Schumpeter (1954, p. 277) calls "real analysis".

The reason, we are told, is that money is a veil that only impacts prices, leaving all aspects of the 'real economy' unaffected. Prices are considered as relative prices, thereby eliminating the need to incorporate money.

This is one of the most fundamental principles of neoclassical economics. It explains why the money supply was considered exogenous and independent of any real discussion of the economy, and why money is scarce and therefore must be rationed. Moreover, banks are financial intermediaries whose lending decisions are dictated by the availability of prior

deposits. Finally, and perhaps most of all, inflation is considered a monetary phenomenon, thereby giving central banks immense power in fighting it – what Rochon and Setterfield (2007, p. 13) labelled “monetary policy dominance”.

In post-Keynesian, monetary circuit, and heterodox traditions, however, money is considered endogenous, that is to say, it is created through the needs of trade (Kaldor, 1982; Moore, 2025). In a non-Say’s Law world, production requires financing, which must come from banks. As Keynes (1930/1972, p. 197) explains, “[c]redit is the pavement along which production travels and the bankers if they knew their duty, would provide the transport facilities to just the extent it is required in order that the productive powers of the community can be employed at full employment”.

This post-Keynesian analysis suggests many relevant implications. For instance, the strong relationship between money and debt: “money always emerges as a debt” (Parguez and Seccareccia, 2000, p. 101). But also the questionable link between money and inflation, to name a few. And while it is correct to argue that New Consensus models have ‘some sort’ of endogeneity, there remains important differences with post-Keynesians, notably, *i*) they remain committed to the existence of a natural rate of interest (for true endogeneity, we must reject the natural rate of interest (see Rogers, 1989; Rochon, 1999; Lavoie, 2022)); *ii*) inflation is still seen as a result of monetary policy decisions, such that the link between money and inflation is never broken, thereby justifying the use of monetary policy in fighting inflation.

The post-Keynesian approach, however, leads to a panoply of questions regarding the role of banks and financial markets, which is absent from the pure neoclassical model. By including banks and the need to finance production, money can never be an afterthought. Rather, it becomes a “by-product of a balance sheet operation of a third agent who, in modern parlance, can be dubbed a ‘bank’” (Parguez and Seccareccia, 2000, p. 101).

5 Supply and demand

Neoclassical theory remains firmly entrenched in a market-based approach to goods, where their supply and demand determine simultaneously the price and the quantity of any specific good. In other words, the theory of price is the same as the theory of output. This approach makes it easy, therefore, to argue in terms of the convergence property discussed above. Any discrepancy between supply and demand gets resolved internally within the market, fairly quickly through the appropriate price mechanism. In this sense, government policies must aim at eliminating all impediments to the well-functioning of the price mechanism. In fact, if any discrepancies between supply and demand persist for any length of time, it is usually attributed to the breakdown of the price mechanism resulting from government interference in markets.

This approach carries a number of implications. First, to analyse the ‘problems’ within a given industry, there is no need to consider the ‘going-on’ in other markets. The solution

must be found within that specific market. The analysis is therefore very much isolated from the outside world.

Second, the demand curve is constructed via the theory of utility, a concept that cannot be measured, yet forms the very core of consumer behaviour. It is a concept that is static, a-historical and a-cultural. It relies solely on the concept of rationality (see below).

Moreover, demand curves assume constant income, rationality and given preferences, and fail to account for insights from behavioural economics, where irrationality, impulse buying, and a lack of information drive choices. Finally, static and well-behaved demand curves fail to explain Giffen goods as well as Veblen goods.

Perhaps more importantly, static demand curves do not take into account income distribution, in the sense that changes in the prices of goods often change the distribution of income, which directly alters the demand curve itself, making the curve endogenous rather than exogenous.

In post-Keynesian economics, going back to Keynes and his *General Theory*, we understand that the solution to a given market problem must be found in other markets, notably the goods market: this is the principle of aggregate demand. Hence, the solution is not caused by a price problem in a given market (the real wage in the labour market), but by a lack of aggregate demand altogether. This applies not only to problems arising in the labour market, but is extended to all markets.

Moreover, post-Keynesians argue that the theory of prices is not the same as the theory of output, as explained above, which suggests, therefore, that they move independently from one another. Prices are set administratively, whereas produced output is determined by aggregate demand. It is therefore not inconceivable that prices and output might move in the same direction.

6 Inflation

Inflation has remained rather subdued in the last four decades, and as such stopped being a main reoccupation for many central banks. This, of course, changed with the post-COVID inflation surge, which reignited interest in the topic along with possible causes and policy prescriptions. Yet, it is important to note, as does Storm (2024, p. 248), that all mainstream and central bank models of inflation have failed to properly predict or anticipate the resurgence of inflation, and as such the “recent increase in inflation took monetary policy-makers by surprise.” This is akin to their inability to predict the global financial crisis. Bad theory is detached from the real world and cannot be relied upon to predict real world events.

As discussed above, the neoclassical theory of inflation is a simple one: excess demand leads to inflation. What drives this excess demand might be excessive public spending, or an excess supply of money, or rather, in a Wicksellian setting, low interest rates, which are

set below the natural rate of interest. In this sense, inflation is the result of too much money chasing too few goods, or seen from Friedman's world, inflation is always and everywhere a monetary phenomenon.

There is also the expectational theory of inflation, also emanating from the mainstream. In this case, today's inflation is driven from expectations of what inflation is believed to be in the future. Accordingly, the role of the central bank is to manage expectations, or rather to anchor such expectations. In this sense, an independent central bank must be conservative, and even more conservative than the population (see Rochon and Vallet, 2025, for a criticism).

There is much damage here done to students. First, whether inflation is an excess demand phenomenon is open to criticism. The stakes cannot be higher. If inflation is not driven by excess demand, then monetary policy loses much of its effectiveness, in addition of course to the empirical collapse of the Phillips curve (see Rochon, 2022, for a discussion of the general ineffectiveness of monetary policy). Monetary policy rests precisely on the ability of changes in interest rates to impact aggregate demand. Yet, there has been much research done on the weak elasticity of demand relative to incremental changes in interest rates.³

The post-Keynesian theory of conflict inflation, in contrast, explains persistent inflation as the outcome of a distributive struggle between social groups, primarily workers and firms, over the division of national income. Rather than viewing inflation as purely a monetary phenomenon, as in monetarist theory, post-Keynesian economists argue that inflation can emerge from real economic conflicts embedded in capitalist institutions. This approach is closely associated with economists such as Joan Robinson, Nicholas Kaldor, and Michal Kalecki, who emphasized the importance of income distribution, bargaining power, and mark-up pricing. In short, as Hein (2024) stated, according to heterodox economics, inflation is always and everywhere a conflict phenomenon.

Indeed, as Hein (2024, p. 203) explains, "inflation is always and everywhere a conflict phenomenon in the sense that it can only be generated if the claims on real income by different groups persistently exceed real output". This view is echoed by Arestis and Sawyer (2005, p. 959), who argue that "inflationary pressures arise from, inter alia, conflict over income shares, and from cost elements, with the price of raw materials, especially oil, being the most important". Finally, Rowthorn, who put forward perhaps the original conflict inflation some five decades ago (see Rowthorn, 1977), revised his paper for the *Review of Political Economy* in 2024. He concludes by saying that "[c]onflict theories explain inflation as the outcome of conflicting claims in staggered markets. The extent to which claims conflict can in principle be measured by some variant of the aspiration gap. The recent cost of living crisis in the United Kingdom (and many other advanced economies) can be usefully analysed from a conflict theory perspective" (Rowthorn, 2024, p. 1313).

³ We are keenly aware, however, that aggregate demand remains sensitive to cumulative changes in interest rates.

At the heart of conflict inflation is the idea that different groups in the economy have target real income shares (see Rochon and Setterfield, 2007). Workers aim to secure higher real wages to maintain or improve their standard of living, while firms seek to preserve profit margins. In modern economies, wages are often determined through collective bargaining, while prices are set by firms using mark-up pricing over some level of normal costs. When workers demand higher nominal wages – perhaps in response to rising living costs –, firms may respond by increasing prices to maintain their mark-ups. This interaction generates a wage–price spiral.

Unlike the traditional Phillips curve framework, which posits a stable trade-off between unemployment and inflation, the post-Keynesian view rejects the notion that inflation is simply a function of excess demand in the market for produced goods and services. Instead, inflation can persist even without excess aggregate demand, if there is an unresolved conflict over income shares. If workers successfully raise wages beyond productivity growth, firms may raise prices. If firms raise prices to protect profits, workers push for further wage increases to defend real wages. The result is ongoing inflation driven by incompatible claims over output.

A key component of this theory is the role of bargaining power. The relative strength of trade unions, employer associations, and government institutions shapes the inflationary process. In periods of strong unionization and low unemployment, workers may have greater power to demand higher wages. Conversely, in times of weak labour organization or high unemployment, firms may be better positioned to resist wage demands. Inflation, therefore, reflects the institutional balance of power within the economy rather than simply a monetary expansion.

Post-Keynesians also emphasize the importance of cost-push factors. For example, an external shock such as a rise in oil prices can shift the distributional struggle. Firms facing higher input costs may attempt to pass these costs onto consumers. Workers, in turn, attempt to protect their real wages. The initial shock thus becomes embedded in a broader distributive conflict, sustaining inflation even after the original cause dissipates. Now, even an oil shock can be interpreted as conflict inflation. Indeed, according to Rowthorn (2024, p. 1309), “an example would be a tug of war between oil producers and consuming countries. If the consuming countries raise their own prices in response to a higher oil price, the producing countries may retaliate by raising the oil price a second time, and so on”.

Policy implications differ significantly from monetarist prescriptions. Since conflict inflation arises from incompatible income claims, simply raising interest rates may lead to unemployment without resolving the underlying conflict (Rochon, 2022). Post-Keynesians often advocate incomes policies, social compacts, or institutional coordination to align wage and profit expectations with productivity growth. By negotiating acceptable income shares and stabilizing expectations, governments can reduce inflationary pressures without resorting solely to contractionary monetary policy.

In summary, the post-Keynesian theory of conflict inflation provides a structural and institutional explanation of inflation. It views inflation not merely as a macroeconomic imbalance but as a manifestation of social conflict over income distribution. By focusing on bargaining power, mark-up pricing, and distributive claims, this theory offers a nuanced understanding of persistent inflation and highlights the importance of political and institutional solutions.

One last argument pertaining to the neoclassical view of demand inflation is the issue about inflation expectations, as we noticed above. The question is whether they matter or not. In other words, do inflation expectations impact current or future rates of inflation? Some research seems to indicate that they do not. For instance, from a post-Keynesian perspective, Neville and Kriesler (2008, p. 314) argue that inflation expectations bear no influence on labour bargaining: “here inflation is explicitly acknowledged, it is usually the previous period’s inflation, so that the negotiation is an attempt to recover real wages to the pre-inflation level, rather than to have them anticipate inflation [...]. Wage demands usually represent an attempt to regain previous losses caused by inflation, they do not attempt to anticipate inflation”.

Similarly, Federal Reserve researcher Rudd (2022, p. 25) argues that “[e]conomists and economic policymakers believe that households’ and firms’ expectations of future inflation are a key determinant of actual inflation. A review of the relevant theoretical and empirical literature suggests that this belief rests on extremely shaky foundations, and a case is made that adhering to it uncritically could easily lead to serious policy errors”.

7 Conclusion

In conclusion, as we argued above, we consider there is no merit in continuing to teach neoclassical economics. Some argue that it would be acceptable to teach it, provided we then expose its flaws and criticize it. We believe this is too confusing for undergraduate students who are exposed to economics for the very first time.

In fact, neoclassical theory is wrong and bears no resemblance to the real world. Of course, this is hardly a surprising conclusion for heterodox scholars. On this, there is virtually unanimity. If this is the case (and it is indeed), then whether we should teach it at all becomes a most bizarre scenario. We are not convinced by the arguments advanced by many that students are at a disadvantage if they do not learn it. Surely, employers do not insist on knowledge of demand curves. Rather, equipped with empirical and technical skills, students can fare much better. Hence, the solution would be to enrich undergraduate programmes with more classes focused on data gathering and analysis, econometric courses and even courses in stock-flow consistency. Accepting pluralism in economics is perhaps a political strategy within departments, but one that gives too much to neoclassical doctrine.

This conclusion conflicts with the one we reached in our own blog. However, that is the beauty of time, because it allowed us to rethink the question over the last three years, as we discussed the issue with many scholars.

In the end, if our purpose is to give students the better education, why should we teach them theories that we know are false? It is time for the members of the heterodox community at large to take the red pill.

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