

Potential output, actual output and demand-led growth

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Abstract:

The paper explores into the different definitions of potential output to be found in economic literature, given their relevance for policy. It firstly addresses the theoretical shift, in the mainstream of literature, from the Keynesian notion of potential output as a ceiling on actual production to the idea of a permanent tendency of actual production to gravitate towards potential production, and the empirical counterpart of that shift as regards the very way in which estimates of potential output are currently built. It then explores the complex relationship between actual and potential output in the theories of demand-led growth. Finally it tentatively addresses the question of the possible relationships between output and inflation in a Classical-Keynesian theoretical context.