Obituary

ELRR

Ronald McKinnon (1935–2014)

The Economic and Labour Relations Review
2015, Vol. 26(1) 160–161

DOI: 10.1177/1035304614567051
elrr.sagepub.com
SAGE

As an engineering undergraduate in 1966, I listened to John Kenneth Galbraith delivering his 1965 Massey Lectures on 'The Underdeveloped Country'. These are the Canadian equivalent of the ABC's Boyer lectures. Galbraith had been John Fitzgerald Kennedy's ambassador to India in the early 1960s, possibly the only economist to have fulfilled such a role in the past 60 years. As such, he had had a great opportunity to examine one of the largest 'underdeveloped' economies first-hand. As I recall, he argued that educated labour (or 'human capital', as we call it now) was not the main impediment to the development of the Indian economy – instead, it was lack of capital.

This diagnosis was not unique to Galbraith: conventional wisdom then was that with more capital, many 'underdeveloped' economies would grow and evolve. It was another Canadian economist, also removed to the United States, who dispelled this notion. In the early 1970s, Ronald McKinnon, who died recently, aged 79, after a fall on an escalator at San Francisco International Airport, had developed the theory of 'financial repression', with another Stanford professor, the late Edward Shaw (1908–1994).

As Galbraith and others had argued previously, conventional wisdom (incidentally, a phrase popularised by Galbraith) was that a lack of capital was the main barrier to economic development. Development economists argued that governments should boost their nations' capital stock through financed investment and foreign aid. McKinnon and Shaw instead focused on the maturity of the nation's financial system. At that time, banks in these countries were often required to hold extensive reserves (which tended to be in government bonds), in order to cap the interest rates charged in loans or paid on deposits. The purpose was sometimes to favour particular sectors, or alternatively to facilitate government funding of its budget deficit, often through lending at below-market rates.

McKinnon and Shaw called this approach 'financial repression', which they saw as resulting in negative real interest rates, impeding economic growth by reducing banks' ability to lend through squeezing the amount of money saved. Different sectors, they argued, paid different interest rates in this fragmented market, a result that discouraged investment, and hence growth.

In his 1993 book, *The Order of Economic Liberalization: Financial Control in the Transition to a Market Economy*, McKinnon outlined how to liberalise government policies in domestic finance and foreign trade so as to create more open markets.

Ronald McKinnon was born in Edmonton, Alberta, on 10 July 1935. He first studied economics at the University of Alberta and completed his doctorate at the University of Minnesota in 1961. He joined Stanford in 1961 and remained there for 53 years. His academic interests included exchange rates, finance, economic development and monetary systems. He contended that immature or distorted financial systems often exacerbated crises, and recently argued against the Federal Reserve's policies of quantitative easing and zero interest rates.

But these monetary policies differed from the interventions in underdeveloped economies outlined in his earlier work, and his fears of inflation, distortions in the banking system and reduced lending in consequence were not realised. The problem since 2008 has been lack of demand and regulatory constraints, not the unprofitability of loans. Ronald McKinnon will be remembered for his pioneering work in highlighting the dangers to economic growth of government-induced distortions in the financial system.

References

Galbraith JK (1965) The underdeveloped country. Canadian Broadcasting Corporation. Available at: http://www.cbc.ca/ideas/episodes/massey-lectures/1965/11/09/massey-lectures-1965-the-underdeveloped-country/ (accessed 13 December 2014).

McKinnon R (1973) *Money and Capital in Economic Development*. Washington, DC: Brookings Institution Press.

McKinnon R (1979) *Money in International Exchange: The Convertible Currency System*. Oxford: Oxford University Press.

McKinnon R (1993) *The Order of Economic Liberalization: Financial Control in the Transition to a Market Economy*. Baltimore, MD: Johns Hopkins University Press.

McKinnon R (1996) *The Rules of the Game: International Money and Exchange Rates*. Cambridge, MA: The MIT Press.

McKinnon R and Ohno K (1997) *Dollar and Yen: Resolving Economic Conflict between the United States and Japan*. Cambridge, MA: The MIT Press.

Robert Marks
The University of New South Wales, Australia