The core of Keynesian theory can be summed up in two propositions. The first is that in a capitalist economy the level of production in general is not determined by the availability of resources but by effective demand which determines how much of potential resources are effectively utilised. The second is that demand is the sum of two components: an endogenous component which varies in proportion to the costs incurred by entrepreneurs (which constitute the incomes of wage and salary earners), and an exogenous component which is financed out of capital – by borrowing, or by the sale of financial assets, which comes to the same thing – and which Keynes treated as a given factor in the short period, determined by expectations. The principle of effective demand asserts that there is an equilibrium level of output (or employment) at which the proceeds of entrepreneurs (as a group) are neither greater nor less than the proceeds the expectation of which is the necessary inducement to cause them (the entrepreneurs) to incur expenses on the scale required to produce that output. If we call the latter the ‘aggregate supply price’ (ASP) (consisting both of the costs incurred on hiring labour etc., and the profits necessary to induce entrepreneurs for incurring costs on that particular scale), the equilibrium level of output will be that at which the sum of endogenous (D1) and exogenous (D2) demand (which could be termed as the ‘aggregate demand price’, ADP ≡ D1 + D2) is equal to ASP.

Keynes identified exogenous demand with Investment (I) and endogenous demand with Consumption (C). If consumption is assumed to be a simple linear function of Income, Y

\[ C = cY, \text{ with } 0 < c < 1, \]

and Investment is regarded as given. \( I = \bar{I} \), the equilibrium level of output, \( Y^* \) is given by

\[ \bar{I} = Y^* - cY^* \]
subject to the constraint

\[ Y^* \leq \hat{Y} \]

where \( \hat{Y} \) is the maximum level of output in the short period which Keynes identified with the position of Full Employment.\(^1\)

Professor Malinvaud published a number of papers\(^2\) to the effect that effective demand is only one of a number of possible constraints on output in the short period; it is possible to have unemployment due to insufficient productive capacity, which causes 'classical' or 'Marxian' unemployment; or if capacity, as measured in terms of places of employment (\textit{postes du travail}), is greater than the labour supply, it could be full employment. Depending one one's definition of what constitutes an 'economy' – whether it relates to a region, a sovereign political entity (like France), or an association of countries (like the European Community) or the world as a whole – there can also be a \textit{third} type of constraint, determined by the economy's propensity to import in relation to its exports. In this case, exports play the role of the exogenous component in demand, while imports, investment and consumption of home-produced goods are all endogenous.

In Harrod's\(^3\) original formulation of the theory of the 'foreign trade multiplier', exogenously given exports (\( \bar{X} \)) together with the propensity to import which is assumed to be a simple function of income (\( M = mY \)), determine the equilibrium level of output at the point at which exports and imports are equal, so that \( \bar{X} = mY \), which can be expressed, in terms analogous to the Keynesian model as

\[ Y^* = \frac{1}{m} \bar{X} \]

This is more likely to provide the critical constraint when we consider the problem not in the context of a short-period static equilibrium, but of the equilibrium of an 'economy' (which may be a region, a country, or a group of associated countries, etc.) in a state of steady growth where all components – the physical output potential, the labour potential (as determined by the sum of the rate of growth of employment and the rate of growth of productivity), exports and imports – grow at a steady rate (though not, or not necessarily, at the \textit{same} rate). Under these conditions, investment must be treated as an endogenous factor, depending on the rate of change of demand (on the so-called 'accelerator principle') and so must imports, the growth-rate of which is given by the growth-rate of output multiplied by the income elasticity of demand for imported goods.