

# **The Gower Initiative for Modern Monetary Studies**

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# An Introduction to Modern Monetary Theory

‘Faced with the choice between changing one's mind and proving that there is no need to do so, almost everyone gets busy on the proof’. John Kenneth Galbraith

## A word from JMK

‘The difficulty lies not so much in developing new ideas as in escaping from old ones’.

John Maynard Keynes

# Three R's

- ▶ **Responsibility** to give due attention to the issues
- ▶ **Reframing** the debate: breaking away from neoliberal framing
- ▶ **Recognition** that when the debate is framed a different way different outcomes are possible.

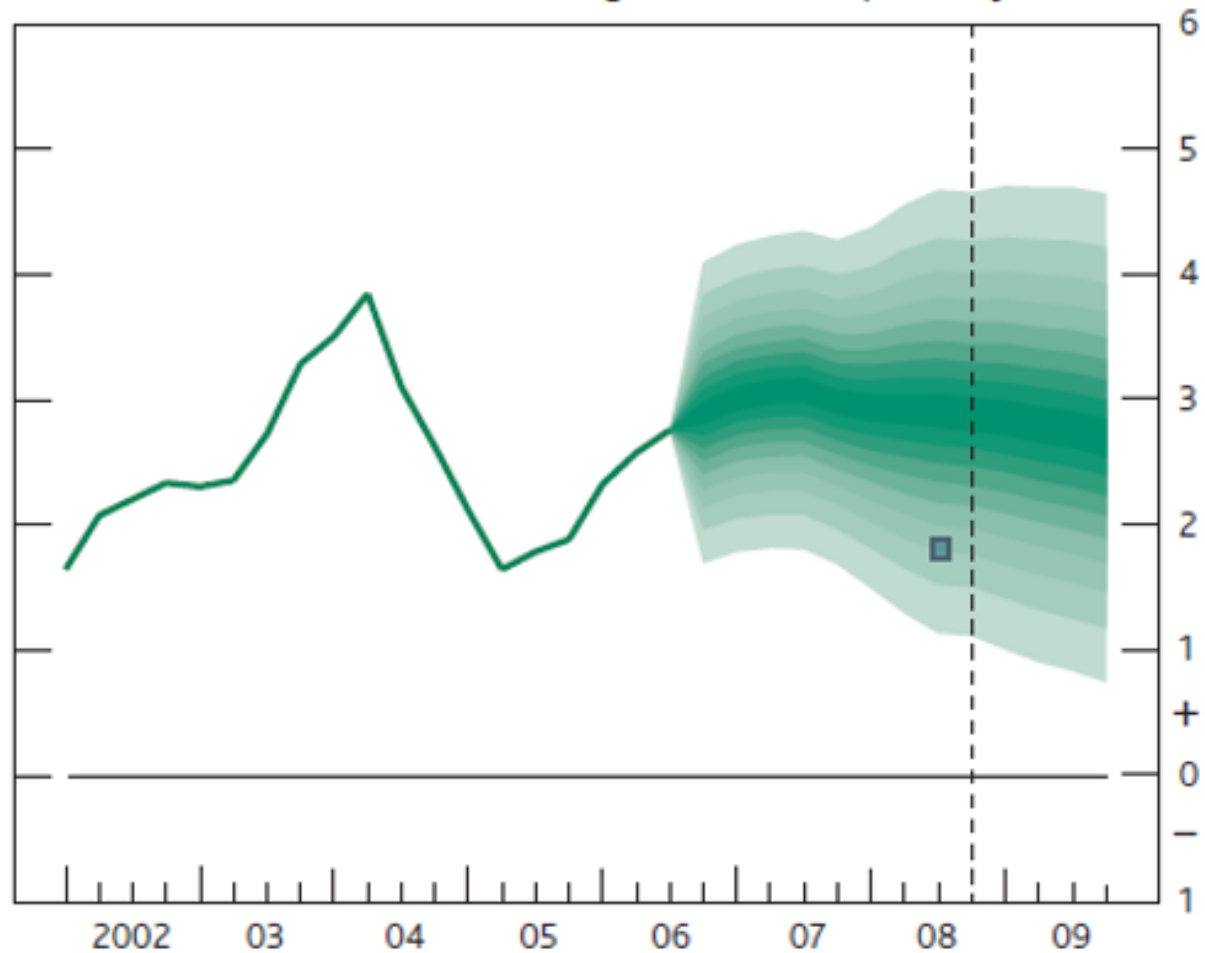
**‘Living successfully in a world of systems requires more of us than our ability to calculate. It requires our full humanity, our ability to sort truth from falsehood, our intuition, our compassion, our vision and our morality.’  
Donella Meadows, *Dancing with Systems* 2003**

**(Next two slides:** Source: Bank of England Quarterly Bulletin

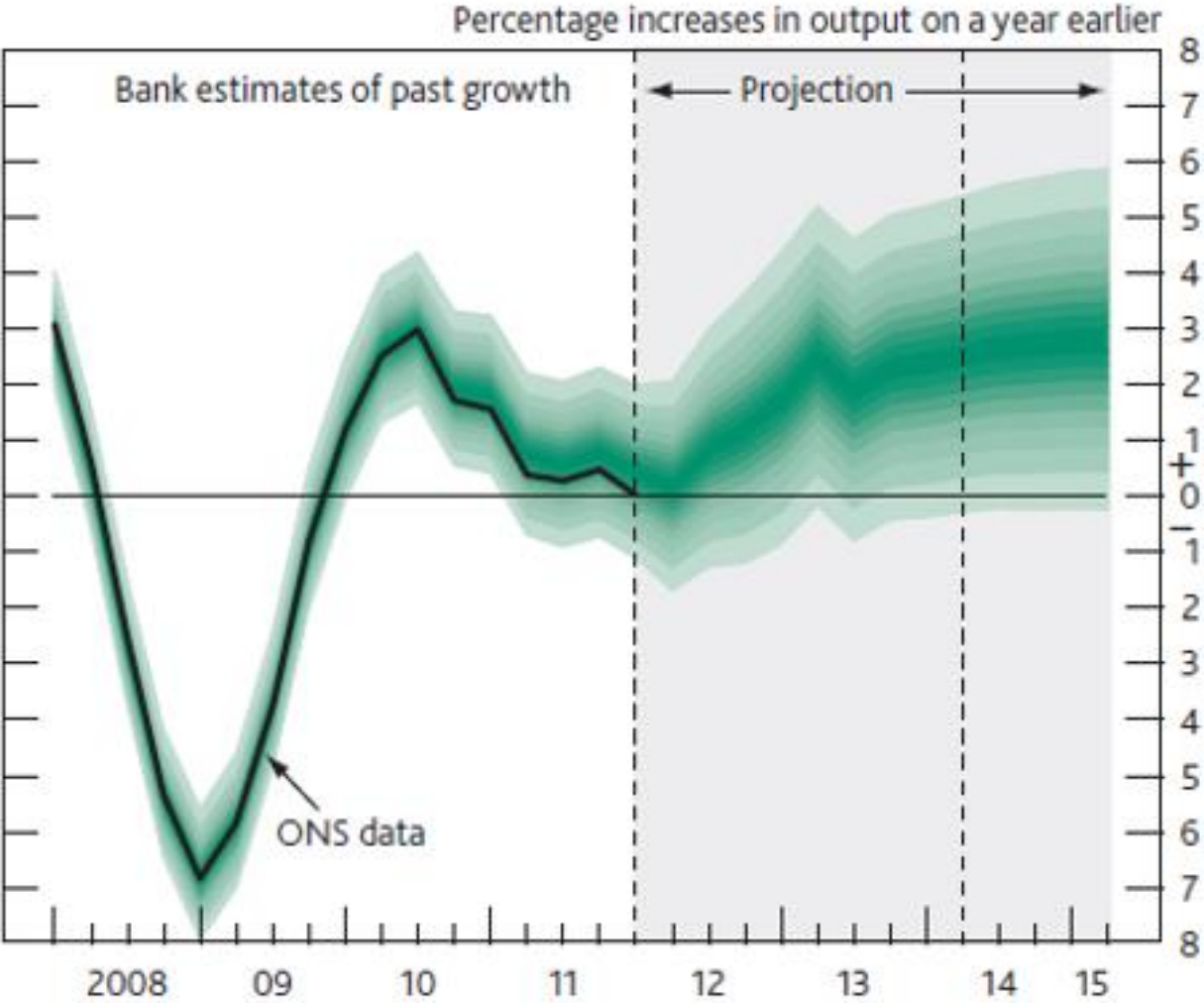
1. 2006 Q3/ 2. 2011 Q2)

# Chart 1 Current GDP projection based on market interest rate expectations

Percentage increase in output on a year earlier



**Chart 1** GDP projection based on market interest rate expectations and £325 billion asset purchases



# The standard view of fiscal Policy.

- ▶ Fiscal policy is a term used to describe the government's approach to taxing and spending.
- ▶ All politicians, journalists and the great majority of economists think they understand the nature of fiscal policy... but they have it backwards.
- ▶ **'In economics, the majority are always wrong...'**  
**J. K. Galbraith**

# The standard view of fiscal Policy.

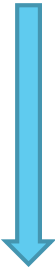
- ▶ Most people think that before the government spends money, it must collect money in the form of taxes.
- ▶ If it wants to spend more than it collects in taxes, it must borrow the difference.
- ▶ If it tries to borrow 'too much', it might not be able to find enough people to lend it money so it might 'go bankrupt'



# The standard view of fiscal Policy.

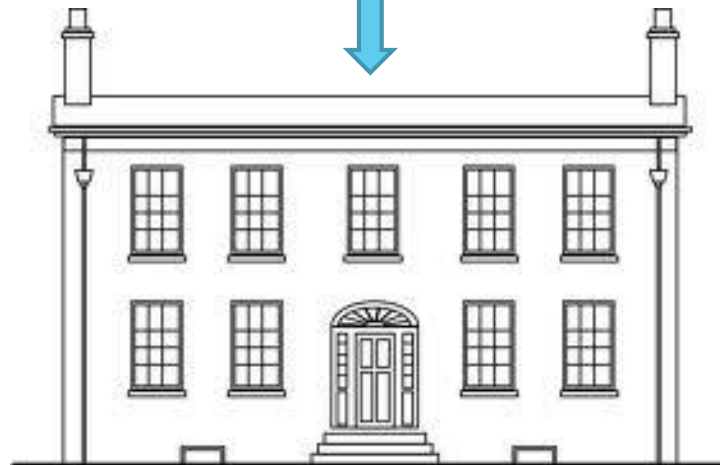
- ▶ If this is right, the government is like a 'giant household'. Before we can spend we must earn or borrow money and eventually our credit might run out and so must the government.....or so the story goes!

Wages and credit



A HOUSEHOLD

Taxes and borrowing



GOVERNMENT

# The standard view of fiscal Policy.

- ▶ Key question:
  - ▶ Where does the private sector (viewed as a whole) get the money it needs to pay taxes?

# The standard view of Fiscal Policy.

- ▶ THE ANSWER:

- ▶ Before the government can tax it must either spend or lend the money!

# The alternative view of fiscal Policy.

- ▶ The government is NOT like a 'giant household'. Before it can tax, it must SPEND or LEND state money Why? The private sector cannot create money (they'd get arrested) so the government must spend or lend the money before the private sector can pay the taxes

# The alternative view of fiscal Policy.

- ▶ Why the confusion? The standard view treats the household and government as currency users.
- ▶ In reality, households are **currency users** and governments are **currency issuers** and different rules apply.
- ▶ At least if you are not in the Eurozone...but we will talk about that later.

# The alternative view of Fiscal Policy.

- ▶ How does the Government actually spend?
- ▶ Key thing to remember - the Government neither has or doesn't have money! It spends by data entry.
- ▶ Try this if you've got online banking. Say your bank account is at ZERO and you get a social security payment of £100. You watch your balance online change from £0 to £100.
- ▶ The money doesn't come from anywhere. Think about it this way - if Joe Root scores a FOUR we don't worry about where the stadium will get the four runs from!

# The alternative view of Fiscal Policy.

- ▶ The Government doesn't need to worry about 'getting anything from anywhere' before it spends. So the question is, if taxes aren't required to 'fund' Government spending what is/ are the purpose(s) of taxation?



# The alternative view of Fiscal Policy.

▶ The answer:

1. Taxes give value to Government money. When the Government spends, we accept the money because we know it's accepted in taxes
2. Taxes '**MAKE ROOM**' for Government spending. Imagine the economy was a giant department store. To give itself room to spend, the Government needs to destroy some of our spending power.
3. The fancy term for this is '**REGULATE AGGREGATE DEMAND**'. Taxes must reduce private sector spending just enough to allow the Government to buy what it needs without causing **INFLATION** .



# The alternative view of Fiscal Policy.

- ▶ What happens if the Government gets it WRONG?
- ▶ If the Government spends too little and/ or it taxes too much, total spending in the economy will be insufficient to fully use all the nation's precious resources such as land, machinery and labour. There will be **UNEMPLOYMENT**.
- ▶ If the Government spends too much and/ or it taxes too little, total spending in the economy will be too much for the nation to satisfy using all its precious resources such as land, machinery and labour. This will cause prices to rise and there will be **INFLATION**.

# The alternative view of Fiscal Policy.

- ▶ So, the trick is getting your Fiscal Policy (balance between spending and taxes) just right so that you get **FULL EMPLOYMENT** without Inflation.
- ▶ Problem - it's not so easy in practice. The Government is never quite sure what the right level of spending and taxing is!
- ▶ Another problem - Inflation can occur even when demand or total spending is low. This might fool the Government if it's not careful. This type of Inflation is what economists call **COST-PUSH INFLATION** e.g. if the price of oil rises, the price of petrol will rise, pushing up the cost of transport. If the price of wheat rises, the cost of food rises, etc.

# The alternative view of Fiscal Policy.

- ▶ What about all the fuss about deficit (the difference between Government spending and taxation in a year) and the debt (the total accumulation of deficits since the monetary system started) - do we really need to worry?
- ▶ Are we passing on our debts to our grandchildren?
- ▶ What do you think?



# The alternative view of Fiscal Policy.

- ▶ We don't need to worry about the deficit, it is simply the untaxed Government spending which remains as net saving in the system.
- ▶ No need to worry - we are **NOT** passing on debts to our grandchildren - we are actually passing on **ASSETS**.
- ▶ Think about it - if you give your grandchild a £100,000 Government bond, they are going to be very happy.
- ▶ **Summary:** The deficit is only a problem at full employment. If it is too large when the economy is operating at full capacity there may be inflation. The trick is getting it at the right level - *Full Employment but No Inflation.*



# The alternative view of Fiscal Policy.

- ▶ In the world, who understands this best?
- ▶ *MMT economists ...Warren Mosler (below), Bill Mitchell and Randall Wray*



# What about the Government?

- ▶ So then, we know the Government CANNOT run out of money. You can't run out of something that you issue in the first place!!
- ▶ Why do they say they can? Possibilities...
  1. They don't understand monetary operations!?
  2. They're stuck in fixed exchange rate or gold standard logic (which ended in 1971!!). Under a fixed exchange rate, the government's money could be exchanged for another asset at a fixed rate?
  3. They believe that democracy needs to be subjugated to markets?
  4. They understand the system but choose to employ 'a useful fiction'?

# They don't know!

- ▶ MMT is not a conspiracy theory. Politicians do not understand how the monetary system works.
- ▶ Governments face real not monetary constraints
- ▶ Education about MMT is the most important issue
- ▶ Governments need to know that they control the sovereign currency, can never go bankrupt and can set interest rates at whatever level they choose to across the whole spectrum.
- ▶ This is not true of Eurozone member govts. who effectively act as currency users and are subject to default

*'There is a tide in the affairs of men, Which taken at the flood, leads on to fortune. Omitted, all the voyage of their life is bound in shallows and in miseries. On such a full sea are we now afloat. And we must take the current when it serves, or lose our ventures' William Shakespeare.*



# *Useful links*

Warren Mosler - key articles

[http://moslereconomics-kg5winhhtut.stackpathdns.com/wp-content/uploads/2018/12/7DIF\\_edited.pdf](http://moslereconomics-kg5winhhtut.stackpathdns.com/wp-content/uploads/2018/12/7DIF_edited.pdf)

<http://moslereconomics.com/mandatory-readings/soft-currency-economics/>

Bill Mitchell - daily blog

<http://bilbo.economicoutlook.net/blog/>

Phil Armstrong - recent articles

<http://moslereconomics-kg5winhhtut.stackpathdns.com/wp-content/uploads/2007/12/Money-and-MMT.pdf>

<https://gimms.org.uk/2018/12/28/magic-money-tree/>

<https://gimms.org.uk/2019/05/27/phil-armstrong-gavyn-davies-response/>

Questions?

The background features abstract, overlapping geometric shapes in various shades of blue, ranging from light sky blue to deep navy blue. These shapes are primarily located on the right side of the frame, creating a modern, layered effect against the white background.