



MODERN MONETARY THEORY AS POST-
NEOLIBERAL ECONOMICS:
THE ROLE OF METHODOLOGY-
PHILOSOPHY

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Useful economics

- When we look at world around us, we see the effects of sets of processes which cause changes from place to place and from time to time.
- **The main job of economists is to explain the mechanisms at work in the economy and shed light upon the causes of the effects we observe.**
- However, the development of method and theory in economics has made achieving this aim highly problematic. This is particularly true in mainstream economics.
- We might highlight the distinction between open and closed systems definitions
- A closed system characterised by event regularities i.e., *whenever a happens b follows*. In an open system a multiplicity of mechanisms is operating, conjointly bringing about a series of events. Thus, outcomes are *complexly codetermined by a plurality and a multiplicity of causes*.

The Failure of Mainstream Economics

- The dominance of the use of methods appropriate for analysing closed systems (in particular, mathematical modelling) rather than using an open system approach which is appropriate for theorising about the real world hampers the ability of mainstream economists to develop meaningful explanations.
- In contrast, we stress the importance of uncertainty within a world characterised by a complex interaction of relatively enduring mechanisms.
- **Our conceptualisation of MMT as a historic open system underpins our analysis. We aspire to be 'useful economists' (as described by James K Galbraith) and both specify and analyse the mechanisms which explain real world events.**

Useful economics: Modern Monetary Theory (MMT)

- 'MMT recognizes that the currency is a public monopoly, taxes function to create unemployment and the funds used to make payments to the government come from the government. The price level is a function of prices paid by government and loans create both deposits and required reserves.
- The national debt is nothing more than the dollars spent by the government that haven't yet been used to pay taxes and remain outstanding as 'net savings' in the economy until used to pay taxes. They 'rest' in the form of cash, reserve balances at the Fed and balances in securities accounts at the Fed' (Warren Mosler).

Modern Monetary Theory (MMT): The Importance of Institutions

- MMT contains an explicit recognition of how institutional change impacts on the real mechanisms present in an economy. For example, MMT stresses that the social structures and institutions extant under the Gold Standard – those necessary for its survival - determined the actual behaviour of the authorities of observed by economists as policy outcomes or ‘events’.
- MMT highlights the contrast between these Gold Standard institutions and the nature of contemporary institutions and mechanisms at work in monetary systems when a nation issues its own non-convertible currency where state and central bank must work hand-in-hand on a daily basis.

Realism in Economics: MMT Research

- Observed phenomena may take the form of partial regularities or *'demi-regularities'* which require explanation by economists.
- *Over restricted regions of time-space certain mechanisms may come to dominate others and/or shine through... Although the social world is open, dynamic and changing, certain mechanisms may, over regions of time-space, be reproduced continuously and come to be (occasionally) apparent in their effects at the level of actual phenomena, giving rise to rough and ready generalities or partial regularities, holding to such a degree that prima facie an explanation is called for (Lawson 1997: 204).*
- **'Contrastive demi-regularities'** (or patterns that stand out as unexpected) against the usual course of events in the **'flux of experience'** are especially likely to prompt an economist to carry out research.

MMT and explaining the 'unexpected'

- The rapidly increasing government deficits as a percentage of GDP that occurred in the immediate aftermath of the GFC provided excellent data with which to evaluate the mainstream contention that higher deficits tend to lead to higher long term interest rates
- **When nations issue their own sovereign currency and operate under floating exchange rates, the expectation of mainstream economists that expanding government deficits as a percentage of GDP tend to cause increased long term interest rates on government debt was not borne out.**
- **The general trend of rising deficits was accompanied by falling rather than rising long term interest rates (Armstrong 2018).**

MMT and explaining the 'unexpected'

- Table 1 below (countries with their own sovereign currency). Table 2 (next slide) Eurozone nations
- a. Government net lending/net borrowing as a percentage of GDP, surplus (+) or deficit (-) for selected nations, 2006-11 (OECD data)
- b. Long term interest rates (secondary market yields of long term -usually 10 year- bonds, annual percentage) for selected nations, 2006-11 (OECD data)

Country	2006	2007	2008	2009	2010	2011
Australia; govt. deficit	2.1	2.1	0.5	-4.1	-4.8	-3.3
Australia; interest rate l. t.	5.59	5.99	5.82	5.04	5.37	4.88
Canada; govt. deficit	1.6	1.4	-0.4	-4.9	-5.6	-5.0
Canada; interest rate l. t.	4.21	4.27	3.61	3.23	3.24	2.78
Japan; govt. deficit	-1.6	-2.4	-2.2	-8.7	-7.8	-8.9
Japan; interest rate l.t.	1.74	1.67	1.47	1.33	1.15	1.10
United Kingdom; govt. deficit	-2.7	-2.8	-5.0	-11.0	-10.4	-9.4
United Kingdom; interest rate l.t.	4.50	5.01	4.59	3.65	3.62	3.14
United States; govt. deficit	-2.2	-2.9	-6.6	-11.6	-10.7	-10.0
United States; interest rate l.t.	4.79	4.63	3.67	3.26	3.21	2.79

MMT and explaining the 'unexpected' : The Eurozone

Country	2006	2007	2008	2009	2010	2011
France ; govt. deficit	-2.34	-2.54	-3.18	-7.16	-6.79	-5.10
France ; interest rate l. t.	3.80	4.30	3.98	3.22	2.74	2.61
Germany ; govt. deficit	-1.72	0.19	-0.18	-3.32	-4.22	-0.96
Germany ; interest rate l. t.	3.76	4.22	3.98	3.22	2.74	2.61
Greece; govt. deficit	-5.95	-6.71	-10.18	-15.14	-11.20	-10.28
Greece; interest rate l.t.	4.07	4.50	4.80	5.17	9.07	15.75
Ireland; govt. deficit	2.81	0.27	-6.98	-13.78	-32.03	-12.73
Ireland; interest rate l.t.	3.79	4.33	4.55	5.23	5.99	9.58
Italy; govt. deficit	-3.59	-1.53	-2.69	-5.27	-4.25	-3.71
Italy; interest rate l.t.	4.05	4.49	4.68	4.31	4.04	5.42
Netherlands; govt. deficit	0.21	0.21	0.22	-5.43	-4.99	--4.29
Netherlands; interest rate l.t.	3.78	4.29	4.23	3.69	2.99	2.99
Portugal; govt. deficit	-4.33	-3.01	-3.77	-9.81	-11.71	-7.38
Portugal; interest rate l.t.	3.91	4.42	4.52	4.21	5.40	10.24
Spain; govt. deficit	2.20	1.92	-4.42	-10.96	-9.38	-9.61
Spain; interest rate l.t.	3.78	4.31	4.36	3.97	4.25	5.44

MMT and explaining the 'unexpected'

To a limited extent the data for euro-using nations provide support the general expectation of mainstream economists; that higher government deficits lead to higher long term interest rates.

However, this outcome is by no means universal. For France, Germany, Italy and the Netherlands there was no apparent significant relationship between deficit size as a percentage of GDP and long term interest rates; **in fact if simple correlation coefficients are calculated for these four countries from 2006- 11 the result is negative, i.e. an inverse relationship exists between higher deficits and long term interest rates .**

However, for **Greece, Ireland, Portugal and Spain, higher deficits seem to be accompanied by higher long term interest rates . Thus, there appears to be a relatively complex 'contrast' which has become manifest; one which may constitute a 'surprise', for mainstream economists at least.**

First, the expected relationship between elevated deficits and higher long term interest has been notably absent in countries with their own currencies operating under floating exchange rates, and second, even within the Eurozone, the relationship is apparent only in some cases. However, from the point of view of the advocates of MMT, this apparent contrast is explained by their understanding of the different nature of the real underlying mechanisms at work in the monetary systems for and those with their own sovereign currency operating under floating exchange rates.

MMT provides satisfying explanations

- **MMT distinguishes clearly between these countries and, for example, nations using the euro. Euro-using nations have ceded their money-issuing power to another entity, the European Central Bank.** Each nation's government is forced to act as a 'currency user' (rather reminiscent of US states). In this case taxes do fund spending, borrowing from private sector euro holders may be necessary to fund spending, default is technically possible and, in the absence of ECB assistance, the need to sell debt on bond markets may drive yields to very high levels.
- **Thus, in the case of nations such as Ireland, Greece and Portugal, where default risk seemed significantly heightened we might expect bond yields to rise. In contrast, in countries such as Germany, The Netherland and France where default risk was perceived as being very low demand for bonds remained high.** In fact, given fears about the future value of private financial assets and expectations of relatively low short-term interest rate policy settings by the ECB, bond yields for these nations actually fell despite significantly higher public sector deficits as a percentage of GDP.

Conclusion

- We show that Modern Monetary Theorists are able to posit the underlying mechanisms behind observed phenomena and provide explanations for what we see.
- We argue in favour of 'useful economics', an economics which aims to shed light on an uncertain world.
- We suggest that the explanatory power of MMT is superior to mainstream economics and that Modern Monetary Theorists are 'useful economists'.

References

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Questions?