The Daily Dish

Modern Monetary Theory

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Eakinomics: Modern Monetary Theory

AAF has gotten a lot of attention — ranging from praise to damnation — for its initial analysis of the Green New Deal and, especially, the bumper-sticker price tag of $93 trillion. But perhaps the most controversial policy issue today is the assertion that it is easy to pay for the Green New Deal because of Modern Monetary Theory (MMT). The essence of MMT is that a sovereign nation with its own currency (e.g., the United States) cannot default on its own bonds because it can always print more money to pay principal and interest. This has three important corollaries: (1) there is no reason to worry about the size of the deficit or debt; (2) there is no need to weigh budgetary tradeoffs — just do everything; and (3) there is no tradeoff between private and public uses of money — just print more.

Similarly there are three philosophical approaches to critiquing MMT: (1) Timeless moms' rules — "If something seems too good to be true, it probably is"; (2) Modern moms' rules — "Don't believe everything you read on the internet"; and (3) thinking through the economics. Let's spend a little time with (3).

A key feature is that MMT posits that there is chronic unemployment, which is a bit ironic since its popularity coincides with a sub-4.0 percent unemployment, a 50-year low in new claims for unemployment insurance, and job openings that exceed the number of unemployed. But supposing that to be true, then MMT amounts to bond-financed deficit spending followed by the monetary authority printing money to buy up the bonds. There are three key issues here. The first is that there really are unemployed resources that can be easily deployed in response to the government purchases. But if there is full employment, the same worker cannot install solar panels and work in the dry cleaner at the same time. That also means there is a tradeoff between the Green New Deal and private sector uses of resources. And it further means that there is competition among budgetary priorities, so priorities are needed.

The second key issue is that the private sector has to be indifferent between money and Treasury securities, so that the swap has no real consequences. But most investors don't think of staying in cash as the same as staying in bonds, so the policy will affect the level and allocation of saving and investment. This is especially true of international investors who may flee the dollar in the face of large scale money-printing.

The third key issue is inflation and its consequences. MMT acknowledges that inflation is an issue, but argues that taxes can be raised to control it. But that is just another way of saying that the deficit needs to be smaller and not monetized, which is exactly what conventional analysis would suggest.

As a general rule, it's hard to take MMT too seriously. But it is especially ironic that it is deployed to defend the Green New Deal which has as one if its provisions guaranteed full employment.