Stephanie Kelton Primer

In Mid-2020, Stephanie Kelton released her New York Times Bestseller, *“The Deficit Myth: Modern Monetary Theory and the Birth of the People’s Economy”,* which largely popularised what is called Modern Monetary Theory (MMT). In the book, Kelton explains what the most important conclusion to draw from MMT is – namely, that it is a myth that if the government runs large budget deficits and borrows the difference, eventually the public sector debt will become unsustainable, leading to sharp increases in taxation or cuts in public spending and possibly a foreign creditor run on the national currency.

While MMT found inspiration in Keynesian and neo-Keynesian concepts, it goes a step further by positing that money is merely an instrument of exchange created by governments through taxes and budget spending. Money creation is not something that commercial banks do, as classic economic theory would suggest. Moreover, according to MMT, governments that print and borrow in their own currency cannot be forced to default since they can always print more money to pay their creditors. MMT draws many of its conclusions from George Knapp’s theory of chartalism, which states that, historically, “*it’s the state’s ability to make and enforce its tax laws that sustains a demand for them, which in turn makes those dollars valuable.”* In essence, the idea that money emerged in modern economies is therefore a direct result of the state needing to spend and needing to invent a unit of currency that it can tax people in. Furthermore, MMT supporters suggest that the lack of inflation over the past few years is a sign that there is not enough ‘money’ (ie. Budget deficits) in the system, and that governments should respond by using their budgets to boost demand by extending more public debt. They think that governments have a lot of room to issue debt, and that they can (and should) better coordinate both fiscal and monetary policy levers to boost the economy. In short, they argue that the main lever of economic policy should be the federal budget rather than interest rates and that the main job of elected officials should be to decide on the regulation of money supply through budgetary spending.

As of late, MMT has started to gain credibility as governments continue to rack up debt on the back of the coronavirus crisis. MMT advocates believe it is wrong to think of government spending as analogous to the budget of an individual household, which must live within its means and avoid spending more than its income. They argue that governments that issue their own currencies are incapable of running out of money, because they have the power to create more. Government spending should, therefore, be constrained not by deficit levels, but by their implications for inflation. The only other limiting factors are real resources such as workers or supplies. Advocates of MMT point out that the quantitative easing (QE) programmes launched by the Federal Reserve in the wake of the 2008 financial crisis have not led to the surge in inflation feared by some classical monetarists who simply link inflation to growth of the monetary base. Even before the covid-19 outbreak, several economists and political leaders voiced at least implicit support for MMT. An instrumental moment came at the beginning of 2019 when Olivier Blanchard, the International Monetary Fund’s former chief economist, declared that *“public debt may have no fiscal cost”* and that the price of public debt may be *“smaller than typically assumed”*. In November 2019, the House of Representatives’ Committee on the Budget organised a hearing on ‘Re-examining the cost of debt’. One could argue that the bold steps taken to tackle the covid-19 crisis imply that MMT has become more mainstream. The massive increase in the US budget deficit this year, combined with unprecedented Fed activism in response to the crisis could be seen as bordering on MMT.

What's more, MMT advocates believe that many of the traditional roles of monetary policy – such as keeping prices stable and pushing toward full employment – should be fulfilled by fiscal policy. Taxes should function not to fund government spending, but as a tool to remove currency from the economy to prevent it from overheating. One of the most central tenets of MMT is simple: that thinking differently about 'balancing the books' would radically improve governments' ability to push towards full employment and fund ambitious spending projects that would improve citizens' quality of life. That the theory is now being taken more seriously than ever is largely because of Stephanie Kelton. A professor of economics and public policy at Stony Brook University, she was an adviser to Bernie Sanders' presidential campaign in 2016, when she was named by Politico as one of the top 50 'thinkers, doers and visionaries transforming American politics'. Kelton's, and MMT's, place in mainstream politics was confirmed earlier this year, when she became a member of Joe Biden's economics 'taskforce', with some of Biden's spending pledges, such as a $2 trillion climate pledge, appearing to bear Kelton's mark. The main objections to MMT, from those who are reluctant to take it seriously, are that it is irresponsible, and that excessive deficit spending risks hyperinflation. Attempts to mitigate this through taxation, critics say, would lead to biting recessions. In this webinar, we will discuss the fundamental theories of MMT, the budget deficit myths that Prof. Kelton has identified, and the future for MMT as a valid regime for governments around the globe.