

Murphy Takes on MMT
Guest: Robert P. Murphy
November 13

Bob Murphy holds a Ph.D. in economics from New York University. He is the author of Chaos Theory, The Politically Incorrect Guide to Capitalism, The Politically Incorrect Guide to the Great Depression and the New Deal, and Lessons for the Young Economist. He blogs at consultingbyrpm.com/blog.

WOODS: You're going to be the guy who does two things for us today. First, explain to us what Modern Monetary Theory is, and then let's talk about what the shortcomings are. How should somebody answer when this comes up?

But first of all, this seems to me like a relatively new school of thought. I'm not an economist, so maybe this has been percolating for a long time, but I don't remember anybody using the term Modern Monetary Theory ten years ago. Where did this come from, and who are the people associated with it?

MURPHY: I don't know exactly when the term Modern Monetary Theory was coined. The ideas in it, I think, would be considered part of the same worldview held by Oskar Lange, for example, the same person who was part of the socialist calculation debate. They refer sarcastically to me as being a credit to the socialists raising the issue, and then Lange, of course, solved it with the market socialist solution. A lot of the ideas associated with what we now call MMT actually go back to Oskar Lange, so these ideas have been around.

Nowadays, I think one of the leading gurus of the movement is this guy called Warren Mosler, and he's the guy that I debated at Columbia University over the summer. Incidentally, Tom, this guy is extremely charming, so just be careful if you ever cross paths with him. He might convince you with his natural witticisms, and before you know it, you'll be advocating inflation.

WOODS: Bob, if only people would say that of me someday. "If you just meet Woods, he may just, through his sheer charm, win you over."

MURPHY: You have to work on that, then.

WOODS: All right, go on.

MURPHY: He was telling me that he actually thinks of the phrase "Modern Monetary Theory" as a complete misnomer. He said that, first of all, it's not modern if these ideas have been around. He also said it's not really monetary, and unfortunately, I can't remember what his problem was with that term, whether he meant that it's also fiscal policy. I think that might have been what it was, but I honestly can't remember. There's

some reason he was saying that even the term “monetary” is not quite right. Then he said it’s not really a theory, that it’s, if anything, a theorem. He was saying that he thinks the whole phrase is kind of silly. I don’t think he said the word “silly”; he was saying it’s a misnomer.

To answer your question, nowadays I think Mosler is the guy associated with it. One thing I should be clear about is, it’s not the same thing as Keynesianism as the way Paul Krugman and Brad Long and guys like that advocate. MMT, in some respects, from an Austrian perspective, might appear to be, “That’s just what those crazy Keynesians are saying,” but actually, if you’re going to put it on a spectrum, I think Modern Monetary Theory is more extreme, and in fact, even Krugman once in a while will occasionally point out that he differs from the MMT guys, that they only match up with the recommendations during what Krugman calls a “liquidity trap.”

WOODS: Let’s go back to the beginning here, and set the stage this way. Often you hear these MMT people say, “Even though it may seem superficially plausible, it is illegitimate to compare your household budget with a government budget, and say that the rules that constrain me in my household budget also constrain the government.” Am I wrong to think that, in talking about that comparison between a household budget and the government budget, we’re hitting the real heart of what MMT is all about?

MURPHY: I think you’re exactly right. Another big guy, by the way, is James Galbraith, if people know who that is.

WOODS: I didn’t know he was an MMT guy.

MURPHY: I believe he is. With all this stuff, too, you get into different sects, just like who’s an Austrian economist, you and I might quibble about certain people, but I think, relative to everyone else, Galbraith is definitely closer to that MMT camp than the other camps. But, the point they’ll make is, when anybody like a politician or other more conventional economists – certainly Austrians – will complain about or worry about, “Hey, the government is in the hole with all these liabilities with Social Security and Medicare and so forth. This is really going to cause disaster down the road. Americans need to wake up to these fiscal realities.” They’re saying things along those lines, or saying, “Hey, Social Security is broken,” that sort of language, their first response will be to roll their eyes and say, “You guys are thinking as if we’re on the gold standard still, and you don’t realize that in modern times, with modern monetary and banking systems – we see it in money in particular – that’s just not how it works anymore. It’s not true that governments have a budget constraint the same way that an individual household does, because, from the government’s perspective, when they have to pay a bill, they just effectively credit the bank account of the individual in question or the creditor in question. So there’s no issue about them being able to meet all their financial obligations, because they can just issue more money. This is the tie-in with the title or the description of Modern Monetary Theory. They’re trying to distinguish it from the

system that ruled under the classical Gold Standard, when it really did make sense, they said, for government to worry about being able to pay their bills.

WOODS: So they're saying, then, that governments are not subject to the type of constraints that you and I are, because you and I can't just create money to pay our bills? Is that really what they're saying?

MURPHY: Yeah. I think you just hit it on the head. They're saying an individual is using currency issued by some other entity, whereas, if we're referring to sovereign governments that have fiat currencies that they themselves issue, then they face no such constraints. That's why they might contrast it and say the U.S. government is in a different position from, say, the government of Spain, because they're part of the euro system, so the Spanish government can't unilaterally just issue more euros, whereas they're claiming the U.S. government can unilaterally create more dollars. You do get into an issue of, "They must be including the Federal Reserve and the federal government as part of the same entity." In case your listeners are confused about that step, that is the way the MMTers typically talk.

WOODS: Let's unpack this, then. Would they admit that there could be some drawbacks to money creation? In other words, surely, they would say that, if the federal government or the Federal Reserve created – just think of some astronomical amount of money – and that they injected it right into the economy and it was being spent, that this would have negative consequences, but they would say that's a separate issue. The point is, there's no constraint in terms of the government budget. Yes, there could be some unfortunate side effects of inflation, but that's a different issue? How do they handle the issue of inflation?

MURPHY: You, again, are correctly describing it. The more careful MMTers – people like Mosler and others, actual economists – the way they will phrase it is to say, "Don't get us wrong – if the government creates too much money, then yes, you'll see prices rise" (they'd call that "inflation" of course) "at a rate that is undesirable, and so that might be a drawback to the policies. We're not saying that there's no longer economic scarcity." What they're saying is that the entire debate, as it typically unfolds, consists of people worrying about the government having the ability to say – for example, if someone proposes the government spends money on some new program, MMTers do not want someone to object and say, "Well, how are we going to pay for that?" They think that's a silly question that's no longer relevant, because of course the government can pay for that. It can just create money and pay for it that way. They'll say that the only issue is whether this will cause too much inflation or more inflation than we desire. As I said, if they're careful, and especially if you press them on it, they will concede, "Right. If we create too much money, then we'll have more inflation than we want." But they still think that they're setting the issues up properly and giving us the proper framework within which to have a policy discussion by getting rid of this silly idea that the government can't afford certain things.

WOODS: What is your response to that? To me, this seems like a silly thing to want to emphasize. I suppose I could yield to them, in a very technical sense, yes, I understand that the federal government has a monopoly on money creation, and yes, it can create a lot of money, but I still feel like there are, at some level, constraints to building fifteen colonies on Mars. That would take trillions of dollars. I suppose the U.S. government could print up the money for that. But how helpful is it to emphasize that aspect of the question when the more relevant aspect is: does the rest of society really want to see its resources transferred to this institution on that scale?

MURPHY: I again agree with you totally here, Tom. I think, at this point, my presence on your show is superfluous.

WOODS: I'm just groping my way through this stuff here, Bob! I'm glad I'm hitting a bullseye every time, but I assure you, I don't really know that much about this. I'm just going on what you're telling me, and just trying to see what I think a guy on the street would say in response.

MURPHY: What you just said a minute ago is exactly how I dealt with it. For your listeners, if you just go to YouTube and search *Robert Murphy Warren Mosler Debate Columbia U*, because it's Columbia University, I'm sure you'll see it, if you're curious to see the actual debate we had. He laid out his position. Actually, he didn't lay it out; he just went right into his policy recommendations and I tried to make sure everybody in the crowd and online knew what his position was, and the way I dealt with it was exactly as you just tried to do, and I said, "Yes, there is a sense in which everything he's laying out in his book" – and his book is called *Seven Deadly Innocent Frauds of Economic Policy*, if you want to look that up. I said, "Yes, there's a sense in which the points you're making – or at least many of them – are technically accurate, but to me, it seems like that's not really changing the fundamentals of the discussion."

I used an analogy. I said, "Suppose there's a couple and they're looking over their bills at the dinner table, and the wife is really stressed out, and she says, 'You know, honey, with the amount you're making from your job and all these bills that we owe and so forth, I just don't think we're making ends meet. I'm going to have to take a job and bring in some income as well, because I don't see how this is going to work.' Then, imagine if the guy said, 'No, no, dear. You're thinking in terms of the gold standard. You're thinking of this Ozzie and Harriet notion that there's a household budget constraint. We aren't constrained by the amount of income we bring in. I can just go put on a ski mask and start holding up 7-11s to get more money that way.' The wife says, 'What are you, crazy? You're going to get arrested and go to prison!' And he'll say, 'I'm not denying that there are drawbacks to my recommendation, but what I'm saying is, you're wrong to be focusing on how we need to boost our reportable income, but what I'm saying is, really, the only constraint on what we can buy is when the police are going to arrest me and how many 7-11s I can get away with knocking over.'"

Is what the husband said incorrect? Did he lie to her? Is what he said wrong in terms of accounting and the reality of the way the world is, in a world of being able to rob 7-11s and so forth? No. What he said technically is true, but does that really change the way the wife is thinking about it? Is that really a realistic thing to take into account, or is it pretty much fine for her to be saying, "If we want to keep spending like this, I'm going to have to take a second job. We're going to have to boost our income." That's kind of my reaction to the MMT people: if it is true to say that just regular tax revenues and possibly running budget deficits and borrowing, that the government can't possibly live up to the spending obligation it's committed to, then you don't really change that reality by saying, "Wait a minute; there's a printing press right here. Make sure you guys don't leave that out of the equation!" That just means people are paying for it through higher prices and having dollar-denominated assets become worth less in real terms. The public is still paying for it. If they don't want to pay for it without use of the printing press, all it's going to do is possibly make them not realize how much they're being ripped off with the printing press, but it doesn't mean all of a sudden these programs are now more affordable.

WOODS: If the MMT people make these points about the government's unique ability to pay for things in ways that you and I can't pay for things, and about there not being a constraint on the government in the way there's a constraint on us, in order to set the stage for policy discussion, where do they take this? Where do they go with this insight? On a very technical level, we can concede this point to them, as you say. It's not strictly wrong; it's just that it begs every important question. Where do they then go with it?

MURPHY: You're right there. I should warn people that, unfortunately, my unbridled honesty gets me into trouble, because after I said that in the debate, not Mosler himself – Mosler is really a cool guy; it's just that I think his ideas are nutty – but a lot of the MMT people went to the airwaves and blogs and stuff, and said, "Oh my gosh, within the first eight minutes, Murphy just conceded the entire debate! He said that Mosler was right, end of story. Murphy just has personal qualms about liberty and printing money and 'counterfeiting,' as he calls it, blah, blah, blah, but he conceded that Warren is right." When you say that, yes, technically, you guys are correct in an age of fiat money, no government ever has to tell a creditor, "We lack the means to pay you our contractual obligation," then they're going to say that you conceded, but of course, as you're bringing up here, Tom, that doesn't really change the nature of the fact that, if governments are spending too much, then they're spending too much

And you're right: where they take it, invariably, is to say, "The government should be spending more." Mosler in particular had all sorts of recommendations, including that the federal government should pledge to give everyone a job who wants a job. Off the top of my head, I don't remember what the hourly wage rate was, because he's saying there's no reason for there to be involuntary unemployment at this point. The government can just pay everyone to do it. In his mind, that would just get people a

chance to then find a better job in the private sector. He's not assuming that half of Americans are going to be on the dole indefinitely, but the point is, that's just one of several of his proposals that sound like it's an incredible potential transfer of resources from the private sector, into the hands of politicians and bureaucrats to be doled out to various people of their choosing. Yes, if they were just making the technical point then calling for massive spending cuts, that would be one thing, but what they do is, they look around and see that right now price inflation is very moderate. We have slack demand. There's excess capacity. The factories are idle. There are millions of people looking for work. So, clearly, the government could get away with creating a bunch more money that wouldn't lead to massive price increases, so there'd be no downside to it, and it's just this obsolete gold standard thinking that's preventing the politicians from having the wisdom to go ahead and put everyone back to work. You crazy Austrians and other goldbugs need to stop tying their hands, thinking, "We can't afford it," when clearly the problem right now is that we need more people to go to work. When they look at the economy right now, they see unemployed workers, so in their mind, the government could just spend money that it creates out of thin air and get them back to work, and then real output increases. Clearly, that has to be a good outcome. We don't have to worry about making sure the accounts balance, because the government can always just create more money, so that's not the issue.

WOODS: Suppose we leave out of account the subject of price inflation. Let's say we concede that that's not a problem. From the Austrian standpoint, there are other problems that are associated with the idea that you just create money, and there's slack demand for reasons that are never explained. There are idle resources that are idle for reasons that are never explained. We'll just create money out of thin air and then, like a lubricant, it'll get the whole machine running again. An Austrian just doesn't think that way. Price inflation or not, that's another matter. An Austrian doesn't look at the economy this way, like it's a single entity, like it's an ignition that needs to be turned. Can you talk like an Austrian here in explaining exactly what's wrong with the way they're thinking about this?

MURPHY: Sure. From an Austrian perspective, we had a regular economy that was in a normal equilibrium, let's say, where things were running smoothly, and then the government were to come on the scene and create a bunch of new money and start buying things and giving money to the military and cranking out more tanks, and giving money to other construction companies to start building bridges and highways and what have you, and giving money to other people for food stamps or whatever it is, the point is, that would redirect resources from where they originally would have gone into now the channels that the government picks. Clearly, from an Austrian perspective, you'd say, "That can't be a good outcome, because there are many reasons for thinking that the private sector and voluntary transactions are the best way to allocate resources. Now a Keynesian would say, "Oh, yeah, okay. Sure. You're saying if there's already full employment, and then there's crowding out and there are tradeoffs. If the government wants to increase government output, then the private sector has to

restrict itself. Fair enough.” What if there’s slack capacity? What if there’s unemployment when this scenario unfolds? You’re right, Tom – even there, the Austrians are going to say, “No, you have to ask why is there this involuntary unemployment in the first place. It’s because of the fallout from a previous unsustainable boom. Because of a previous bout of inflation coming in through the credit markets that lowered interest rates below where they should have been that misled entrepreneurs – they started longer projects than there were real savings to finance, and at some point, you hit a wall physically. It’s not just a matter of having enough dollars or whatever the monetary unit is, but there are physical constraints in the structure of production, in the capital structure. That leads to a situation where the authorities either have to back off or else the currency collapses. Either way, that unsustainable boom is unsustainable, and it will end, and that’s what leads you to the depression – or “recession,” in modern parlance. It takes time for those unemployed resources to get redirected back into useful niches, and if the government comes in while they’re still idle and try to print up a bunch of money and get everybody back to work, it just short-circuits that recovery process.

WOODS: Let me jump in here, because we had G.P. Manish on a few weeks ago, and he was talking about Keynesianism, and he made a valuable distinction between what you might call physical idleness and economic idleness. It’s true that some factory may be physically idle – it’s not in use – or a hotel, maybe it closes for one season of the year and it’s physically idle, but can you say it’s economically idle? Is there really no economic purpose served by withholding its services? Is the owner a complete idiot, or might he have some reason for doing what he’s doing? What you’re describing is a situation in which the owners of a lot of these resources are trying to figure out exactly where they fit into the structure of production right now in the wake of the bust. They need to rearrange things, and so they need to watch and see how they fit in, right?

MURPHY: Exactly. Even in normal times, even in a purely free market where there were no boom-bust cycles, at any given moment there’d be workers in between jobs. If a business goes out of business – that particular entrepreneur miscalculated what the demand would be, or he miscalculated what the costs would be, whatever – and so a commercial building that has a bunch of little stores in it, at any given moment, one of those units might be vacant, and they’d have a sign up that said, “Office space for rent” with the phone number. You have to ask, why don’t they just rent it out immediately after the next day so that there’s no discontinuity and output from these various things? It’s because the owner, the landlord of that building, of course, wants to hold out to get a tenant in there to get a better price for it. If he just had to rent it out immediately, he’d have to drop the price pretty drastically. He leaves it vacant while people are searching. The same thing with workers – if you quit your job or get laid off, you don’t just take the first job offer. If you’re driving down the street and see that McDonald’s is hiring and you previously were an engineer, you’re not going to take that job right away, even though technically you could be working the next week. You hold out. You send your resume around and you look for a better spot. That sort of search process happens

all the time. That's going to happen even in a normal free-market economy. It's just that, in the wake of massive government distortion with interest rates that screw everything up, when the entrepreneurs realize that, it takes them longer to adjust, and the best solution to that is for the government to stop interfering and let the market do its work.

WOODS: Bob, any parting thoughts on Modern Monetary Theory? Do you feel like we hit everything, or is there anything we left out in terms of a basic overview course?

MURPHY: I guess one thing I'd like to take on is one of the ways they try to show how silly the conventional approach is. They'll say they have this apparently wise statement that says the only way for the private sector to accumulate net financial assets is for the government to run a budget deficit. The way they're thinking about it – you can do it with various forms of accounting – is that if you divide the world up into the government sector and then the private sector, only if the government runs a deficit and owes the rest of the world money can the rest of the world then increase what it's owed. See how that works?

WOODS: Yeah.

MURPHY: So they think it's a very profound statement to show, "See? You guys are crazy if you want the government to run a balanced budget, or, even worse, to run a budget surplus. That necessarily decreases net financial assets held by the private sector. You're crazy!" There are various flaws with that, but one way to see it is to say, look, suppose the government comes up to me and gives me a \$1,000,000 IOU. I'm holding a Treasury bond, and Uncle Sam is going to give me \$1,000,000. I feel rich – I have \$1,000,000 more now, and my net financial assets have gone up. Now, next year, to pay that off, Uncle Sam points a gun at me, takes \$1,000,000 from me at gunpoint, and then redeems that bond and gives me the \$1,000,000 and takes the treasury back, and says, "There you go! We just paid you." Clearly, that process didn't make me any richer. That's what happens in the aggregate when the government runs a budget deficit with the rest of the world, and then we say, "The rest of the world now is richer." How is the government going to redeem those bonds? Just by taxing the rest of us. It's completely ludicrous when you think through the implications of what they're saying, and yet they run around with these accounting tautologies that yes, technically are accurate mathematically, but how they deploy them in policy discussions is completely misleading.