Book Review

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Modern Monetary Theory and its Critics,
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The book edited by Fullbrook and Morgan is a collection of articles published in Issue 89 of the journal, *Real-World Economics Review*. It assembles eighteen articles from experts who offer their vision or criticism of Modern Monetary Theory (MMT) that has been popular in the media given fiscal austerity, stagnating wages, rising inequality, and climate change. This review focuses on salient ideas that could be presented to economics students in a way that would challenge mainstream viewpoints including that budget deficits crowd out private investment, that government spending is constrained by taxes and borrowing, or that money is solely created by the central bank. Another motivation for this review comes in the context of the economic crises faced by countries like Pakistan that reel under currency depreciation, dependence on imports for food, medicines, and energy, and the unhelpful conditions stipulated by IMF loans. The idea is to explore whether MMT has any hope to offer such countries or whether it is predominately applicable to the U.S. whose dollar serves as the world reserve currency. Thus, the key ideas presented in this book are systematically delineated below.

A Review of Salient Ideas

In his article, Wray introduces the readers to a primer on MMT. He highlights the conditions for monetary sovereignty that forms the basis of MMT. These include a government that borrows and collects taxes in a currency that it issues, and which therefore faces no financial budget constraint (p. 10). Additionally, this currency issuing government can set the interest rate on its obligations by buying bonds (p. 11). Wray emphasizes that MMT does not justify that the government “spend without limit” or that the central bank “print money” to finance deficits (p. 11). Instead, while downplaying financial constraints, MMT upholds real resource constraints so that it recognizes that excessive spending or poorly targeted spending can cause inflation (p. 12-13). However, Wray adds that the size of deficits and debt do not accurately reflect the “inflation potential of additional government spending”, as modern economies operate with enough underemployment and unused production capacity (p. 13).

Wray states that MMT is critical of monetary unions, pegged exchange rates, dollarization, borrowing in foreign currency, tight budgets or austerity, and independent monetary policy with high interest rates, as despite being promoted by institutions like the IMF, they have not helped either advanced or developing countries (p. 15, 16). He rejects the textbook theory that money developed as a medium of exchange to replace the inefficient barter system and instead states

that money arose as a unit of account to facilitate tracking debt and credit and also to pay taxes (p. 17-18). He adds that taxes are not to generate revenue but to incentivize people to hold money and to withdraw money from circulation to curb inflation (p. 19-20). Moreover, in contrast to the textbook idea that savings lead to deposits, he highlights the endogenous money theory where banks issue loans that create deposits and that therefore banks create money (p. 28-29). Thus, MMT challenges the textbook depiction of the creation of money.

According to Wray, MMT challenges the ideas that deficits crowd out private investment, that the government is leaving debt for future generations, and that the U.S. is dependent on Chinese lending (p. 29-30). Instead, he states that budget deficits create private sector income and crowd in private investment, that such income supports imports, that current account deficits lead to the Chinese buying safe American assets where the U.S. government can meet obligations by issuing currency and by setting the interest rate and that therefore the U.S. is not dependent on Chinese lending (p. 30, 34, 35). Similarly, MMT challenges the idea of central bank independence to prevent hyperinflation as illusory for such independence is limited to choosing the overnight interest rate (p. 38-39). Finally, Wray states that capital flight causing an interest rate hike and exchange rate depreciation in response to government debt is overblown, as the central bank controls the interest rate by simply announcing a target rate (p. 42).

Overall, Wray provides a useful primer on MMT, stating that a currency issuing government faces real resource constraint on inflation but not financing constraints, that spending is not dependent on taxes and borrowing, that austerity measures proposed by institutions like the IMF are unhelpful, that budget deficits crowd in private investment, that the U.S. can meet its domestic and foreign obligations denominated in dollars, that monetary unions reduce monetary sovereignty, and that deficit and debt concerns are overblown for a government that issues its own currency and controls the interest rate.

In his article, Andresen highlights injecting electronic parallel money (EPM) that would help countries facing crisis in the eurozone. Addressing the debt crisis, he states that raising taxes is problematic, selling public property is unsustainable, and raising net exports is difficult for it entails having wage and price devaluation to increase competitiveness (p. 48, 49). Instead, he supports circulating a parallel electronic currency with the euro to mobilize unemployed workers and unutilized capacity (p. 50). Countering the criticisms, he argues that people would accept EPM due to economic need and because of a positive feedback loop that would engender trust, and that they would not immediately get rid of it by paying taxes because of the time delay between EPM injection and taxation (p. 56, 57). Finally, he critiques that MMT has not offered much for euro countries except the suggestion to revert to national currencies (p. 63). Overall, Andresen states that an EPM can help countries that have abandoned monetary sovereignty to achieve full employment by mobilizing unemployed workers and unutilized capacity and critiques that the MMT prescription of reverting to national currencies is insufficient.

In his article, Armstrong states that according to mainstream thinking the government is constrained by taxing, borrowing, or printing money to finance its spending and that taxing leads to disincentives to work, borrowing crowds out private investment, and printing money leads to inflation (p. 67-68). In contrast, according to MMT, a currency issuing government with floating exchange rates is not constrained to spend and can choose interest rates at which it borrows (p. 68-70). Armstrong states that mainstream theory treats banks as intermediaries that take deposits to issue loans, whereas according to MMT, bank loans create deposits (p. 72).

Moreover, in contrast to the crowding out effect in mainstream theory, MMT indicates that there is no positive correlation between deficits and interest rates and that issuing bonds is not about borrowing but maintaining the overnight interest rate (p. 74, 87). Armstrong adds that according to the mainstream, higher interest rates are contractionary and lower interest rates are expansionary, whereas according to MMT, it is the other way around, as higher interest rates add interest income and that decades of near zero interest rates have not instigated aggregate demand or inflation (p. 82).

He states that the mainstream argument against debt monetization or the government borrowing from the central bank was to curb inflation, whereas according to MMT the central bank cannot monetize debt by buying government bonds, as government spending would increase reserves in the banking system, which the central bank would reverse by selling government bonds to support the target overnight interest rate (p. 85-87). He mentions that under the gold standard it made sense to limit debt as higher spending increased the risk of conversion to gold, whereas with fiat money, government spending can be maintained to achieve full employment (p. 85). Overall, Armstrong contrasts mainstream theory with MMT, highlighting that currency issuing governments are not financially constrained, that bank loans create deposits, that deficits do not crowd out private investment, that issuing bonds is about targeting the overnight interest rate, that higher interest rates are expansionary, that debt monetization is not possible, and that without a gold standard, government spending can be maintained to achieve full employment.

In their article, Bonizzi, Kaltenbrunner, and Michell argue that MMT does not help much in the context of developing countries with limited monetary sovereignty, as they face debt denominated in foreign currency and the need for fixed exchange rates to import food and energy (p. 98, 115). This is even though MMT prescribes policies including sufficiency in domestic food and energy through employer of last resort or job guarantee programs (p. 98, 115). However, the authors critique that MMT contributes little, as much of what it offers is already found in post-Keynesian economics except for job guarantee programs and debt monetization (p. 99, 124). The authors state that many developing countries may have to devalue exchange rates to boost exports to get foreign exchange, but such a strategy is problematic due to low price elasticity of exports and cost push inflation due to food and energy imports (p. 116-117). Alternatively, developing countries can attract foreign portfolio and direct investments but the former can lead to exchange rate and asset price volatility, whereas the latter may encourage a race to the bottom to attract such investments and lead to outflow of dividends and remittances (p. 117-118).

The authors reiterate that MMT prescriptions of flexible exchange rates and no foreign currency debt for monetary sovereignty do not apply to developing countries that manage exchange rates to import food and energy. They highlight that dismissing balance of payment constraints is problematic as developing countries are dependent on food and energy imports, that deficit monetization is problematic because of capital flight, and that the strategies of boosting exports or attracting foreign investment have limitations. Overall, they critique that MMT has not much to offer much beyond post-Keynesian economics save for the job guarantee program and debt monetization (in contrast to Armstrong).

In his article, Colander critiques that while MMT has received attention in the mainstream, it has not been much of an “intellectual success” (p. 132). He upholds money as arising from society than the state to eliminate the need for recording credits and debits in a ledger (p. 136,

139). This credit theory of money suits the rising use of cryptocurrencies (p. 141). As such, he critiques MMT for connecting money only to the state (p. 142). He also states that MMT could be supported by "supply siders" if it were framed as justifying lower taxes instead of supporting government spending (p. 146). Additionally, he critiques the idea that the government maximizes a social welfare function with only an inflation constraint by highlighting the rent seeking pursued by various political groups that vie for government power (p. 147). Therefore, he states that policies including balancing the budget, limits on debt, and monetary expansion can be explained as upholding a social contract between such groups (p. 149). Overall, Colander critiques aspects of MMT that connects money only to the state, the idea that the government acts in the interests of the people whilst ignoring rent seeking by political groups and provides a rationale for balancing the budget and having limits on debt.

In their article, Ehnts and Hofgen state that governments don't need taxes to finance spending but to create demand for currency, lower inflationary pressures, address inequality, and disincentivize some behaviour (p. 162). Similarly, they don't need bond sales to raise funds but to drain excess reserves because of government spending to curb downward pressure on interest rates (p. 162-163). On the eurozone, they state that fiscal deficit rules are a major reason behind anemic aggregate demand and high unemployment, which could be relaxed by the European Central Bank buying government bonds (p. 167-168, 171). Finally, they highlight job guarantee programs on community and environmental care as stabilizing the economy at full employment and providing the national minimum wage (p. 172-173). Overall, Ehnts and Hofgen present the MMT perspective that taxes and bond sales are not required to finance government spending but to temper inflation and manage interest rates, that fiscal deficit rules cause anemic demand, and that job guarantee programs help achieve the goal of full employment.

In his article, Lavoie states that MMT is part of post-Keynesian economics, as both are skeptical of proposals on universal guaranteed income but supports new policies like job guarantee programs where the government acts as the employer of last resort (p. 208-209). He adds that both MMT and post-Keynesian economics state that the main tool to stabilize the economy should be fiscal policy not monetary policy and that both reject that deficits crowd out private investment (p. 214-215). However, he critiques the efficacy of flexible exchange rate for countries with low monetary sovereignty, and the potential impact of job guarantee programs on wages and prices (p. 216). He also critiques that it was post-Keynesian economics and not MMT that first pointed out that loans create deposits (p. 219). Overall, Lavoie states that MMT and post-Keynesian economics share ideas on the primacy of fiscal policy and rejection of the crowding out effect, criticizes that several ideas like loans creating deposits were initiated by post-Keynesianism not MMT and highlights the limits for countries with low monetary sovereignty and the potential consequences of job guarantee programs.

In her article, Mayhew critiques that MMT exponents provide simplistic solutions to complex problems and that they come close to rejecting the endogeneity of money, which is a major tenet in MMT (p. 279). She critiques that money has value not because the government accepts taxes in the issued currency, but that money has value because people accept it as payment (p. 282). Additionally, she critiques that the MMT treatment of the political context that informs fiscal policy is inadequate (p. 289). She adds that MMT has focused on the affordability of job guarantee programs instead of the political difficulties in having them approved (p. 290). She also critiques that the MMT prescription of not worrying about debt works in the context of the U.S. dollar that is used as an international reserve currency but that such a condition may not

hold forever (p. 293). Finally, she criticizes MMT downplaying of debt in the context where such debt is acquired for “frivolous expenditures” (p. 294). Overall, Mayhew critiques that MMT offers simplistic solutions, that some MMT exponents come close to rejecting the endogeneity of money, that MMT ignores the political context that informs fiscal policy, that MMT downplaying of debt is problematic in the context of “frivolous expenditures” and the context where the dollar no longer remains the international reserve currency.

In his article, Murphy argues that if MMT is to succeed then it must be accompanied by MTT that focuses less on balancing the budget and more on social and economic policy (p. 313-314). He critiques that MMT focuses on the role of taxes in managing aggregate demand, as taxing more than spending causes unemployment but that it ignores taxing the wealthy, as it suggests that taxation is not required for redistribution (p. 299-300). He goes on to state that modern taxation theory (MTT) would not focus on revenue maximization but on supplying public services through reallocation of resources (p. 305-306). Moreover, the tax rate under MTT would be different from the standard optimal efficient tax rate (p. 310). Overall, Murphy critiques that MMT upholds taxes to manage aggregate demand but does not deem it necessary for redistribution (unlike Ehnts and Hofgen that mention taxes to address inequality) and that MMT should be accompanied by MTT that focuses on social and economic policy including the provision of public services.

In his article, Palley states that mainstream economics has embraced the effectiveness of counter cyclical fiscal policy, as fiscal stimulus has been successful in addressing the recession of 2009 whereas fiscal austerity has been “disastrous” (p. 318). He adds that it is now accepted that the Keynesian multiplier is larger under recession and that debt is sustainable if the interest rate is less than the growth rate (p. 319). However, he critiques the MMT claim that spending can be financed by printing money without causing inflation (p. 320). He also critiques that the MMT rejection of interest rate policy by keeping interest rates close to zero would exacerbate the inflation situation (p. 324). He adds that debt monetization would cause inflation in both asset and goods markets and would lead towards exchange rate depreciation (p. 327). Moreover, the combination of budget deficits and high inflation would cause a financial crisis and necessitate tax increases that could lead towards a voter backlash (p. 328-329). Overall, Palley recognizes the role of fiscal stimulus under recession but critiques MMT for debt monetization (a charge rejected by Wray), as it would cause inflation, exchange rate depreciation, and a financial crisis.

In his article, Rochon states that, unlike post-Keynesian economics, MMT has succeeded in simplifying complex ideas (p. 333). He states that both MMT and post-Keynesians agree on full employment, endogenous money, the primacy of fiscal policy over monetary policy, and rejection of the crowding out effects but that disagreements remain on issues including whether MMT applies to developing countries (p. 339). He also mentions that in making the case for the government role in circulating money, MMT seems to have undermined the idea of endogenous money (p. 340). Finally, he states that it is important for MMT scholars to engage with post-Keynesians that have raised legitimate arguments and who can help in the development of arguments (p. 349). Overall, Rochon expresses concern that despite the similarity between MMT and post-Keynesianism on full employment, the primacy of fiscal policy, and the rejection of crowding out effects, there are issues on the applicability of MMT to developing countries and the undermining of endogenous money, which necessitates a dialogue between the two.

Finally, in his article, Sawyer dismisses claims that job guarantee programs or employer of last resort programs would cause inflation, stating that inflation could be curbed through more productive capacity (p. 354, 367). Additionally, he argues that while MMT has argued for the consolidation of central bank and the government, the central bank should be recognized as independent and constrained in the creation of money (p. 359-360). On job guarantee programs, he critiques that labour is not homogeneous or paid uniform wage, that such jobs must be offered at minimum wage to prevent people avoiding other employment, that a Green New Deal requires workers qualified beyond minimum wage workers, and that beneficial jobs in social care are long term that cannot be based only on declines in private employment (p. 366-370). Overall, Sawyer states that the MMT prescription of job guarantee programs has several issues including the duration of jobs offered, the qualifications of workers required and the concern on drawing workers away from other sectors, but that inflation is not a concern, as it can be mitigated by additional productive capacity.

Consolidating the Salient Ideas

The following salient points can be distilled from the review above. Supporting MMT, Wray provides a useful primer, stating that a currency issuing government faces real resource constraints on inflation but not financing constraints, that spending is not dependent on taxes and borrowing, and that budget deficits crowd in private investment. He is clear that MMT does not justify deficit monetization and that excessive spending can cause inflation. Similarly, Armstrong highlights MMT ideas that issuing bonds is about targeting the overnight interest rate, that bank loans create deposits, that debt monetization is not possible, and that government spending can be maintained to achieve full employment. Likewise, Ehnts and Hofgen reiterate the MMT perspective that taxes and bond sales are not required to finance government spending but to temper inflation and manage interest rates and that job guarantee programs help achieve the goal of full employment.

In contexts beyond the U.S., Bonizzi, Kaltenbrunner, and Michell reiterate that MMT prescriptions of flexible exchange rates and no foreign currency debt for monetary sovereignty do not apply to developing countries that face balance of payment constraints especially as they are dependent on food and energy imports. They critique that MMT has not much to offer much beyond post-Keynesian economics save for the job guarantee program and debt monetization in contrast to Armstrong, who states that debt monetization is not possible. Similarly, in the eurozone context, Andresen critiques that the MMT prescription of reverting to national currencies is insufficient and instead propose an electronic parallel money (EPM) that could help countries that have abandoned monetary sovereignty to achieve full employment by mobilizing unemployed workers and unutilized capacity. However, it is not clear whether EPM would help developing countries like Pakistan to address their balance of payment crisis.

In terms of criticisms, Mayhew critiques that MMT offers simplistic solutions, that some MMT exponents come close to rejecting the endogeneity of money, that MMT ignores the political context that informs fiscal policy, and that MMT downplaying of debt is problematic. Similarly, Colander critiques MMT for ignoring rent seeking by political groups and for downplaying the rules on balancing the budget and limits on debt. Additionally, Sawyer critiques that the MMT prescription of job guarantee programs has several issues including the duration of jobs offered, the qualifications of workers required and the concern on drawing workers away from other sectors. In the context of taxes, Murphy critiques MMT for not deeming taxes as necessary for

redistribution unlike Ehnts and Hofgen who mention taxes to address inequality. Likewise, while Wray is clear that MMT does not justify deficit monetization Palley critiques MMT for debt monetization, as it would cause inflation, exchange rate depreciation and lead to a financial crisis.

Finally, both Lavoie and Rochon draw similarities between MMT and post- Keynesian economics whilst critiquing MMT on its limitations. Thus, Lavoie depicts the limits of the applicability of MMT to countries with low monetary sovereignty whilst highlighting that both MMT and post-Keynesian economics share ideas on the primacy of fiscal policy and the rejection of the crowding out effect. Similarly, Rochon expresses concern on the applicability of MMT to developing countries and on the undermining of endogenous money. While he reiterates the similarity between MMT and post-Keynesianism on full employment, the primacy of fiscal policy, and the rejection of crowding out effects, he calls for a dialogue between the two to flesh out arguments in MMT circles.

Overall, this book offers a detailed and nuanced read on MMT, as it draws out the central points of MMT, the inconsistency of its claims when various MMT exponents undermine the endogeneity of money, and the criticisms especially from post-Keynesian economics (with whom MMT shares much in common) on issues of debt monetization, the goal of taxes, downplaying of debt, and the issues of job guarantee programs. The book shows the limitations of MMT for developing countries like Pakistan but also offers ideas like the EPM that could prove promising in contexts beyond the U.S. Additionally, this book would be a difficult read for ECON 101 students, who may be directed to the more popular books including Kelton (2020) and Wray (2022). Nonetheless, this book makes for an effective reading for advanced undergraduate students and instructors who require a more comprehensive perspective on MMT.

References

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