Reserve Bank of India Occasional Papers
Vol. 42, No. 1: 2021

The Deficit Myth: Modern Monetary Theory and How to Build a Better Economy by Stephanie Kelton, 325 pp., John Murray (2020), ₹799

There are quite a few thought provoking books in economics which have been revolutionary in proposing new concepts with powerful messages; the book, Deficit Myth: Modern Monetary Theory and How to Build a Better Economy, is one of them of our times. The book raises some of the most fundamental questions and contemporary issues in public finance and monetary economics and tries to examine them using research findings and cogent arguments. Though the topics discussed are debatable and contentious, the narrative of the book is lucid, comprehensible and rich with illustrations from real life examples. Stephanie Kelton, its author, is a professor of economics and public policy in Stony Brook University and has been named as one of the most creative people in business by Fast Company, an American monthly business magazine.

The uniqueness of the book is that it has mass appeal and caught the imagination of readers world-wide across diverse fields. The author has tried to bust six myths that are deeply rooted under the shelter of conventional economic theories. By using the framework of modern monetary theory (MMT) she has challenged the new consensus macroeconomics head-on and repudiated many common economic beliefs by providing diametrically opposite perspectives.

The first popular myth is that federal governments should live within the means like a household. According to the author, central governments, however, should not constrain their spending like households as they are the creator of money. While households are users of money that they receive as payments for work, in exchange of goods and services or as transfers, central governments through their respective central banks can print legal tenders as they only have the exclusive authority to do so. The author nevertheless cautions that this principle should be applied with utmost care. Countries that lack control over issuance of their domestic currencies in normal times, borrow in foreign currencies and have fixed exchange rate regimes, adoption of this principle may prove fatal for them.

The second myth is that fiscal deficit implies over spending. According to the author, real overspending however, occurs, only when inflation rises after an economy attains full level of employment. She further explains that, one would have worried about deficit spending if a country was still under the Bretton Woods System. The system requires issue of currencies backed by gold in contrast to the system of fiat currencies without the backing of gold reserves after the collapse of bretton wood system. The author postulates that higher inflation could be a sign of overspending and not deficit budget. The author advocates that government budget deficit is not a cause of concern, as long as resources remain unemployed or underemployed. Once the economy reaches its full employment level, however, deficit spending can lead to a rise in demand, which in turn may lead to a situation of scarcity of resources, resulting in a rise in prices. She questions the mainstream economics that propagates that there exists a tradeoff between inflation and unemployment, *i.e.*, to reduce inflation the economy has to live with certain amount of involuntary unemployment. Through the lens of MMT, she recommends federal job guarantee schemes as a solution which could help to keep in check both unemployment and inflationary pressures.

According to the book, the third myth is that public debt is a burden. The author views public debt of the US economy from a different perspective, viewing them as mere adjustment in holding of assets and liabilities instead of borrowing. In her illustrations, China holding large US Treasury securities does not pose a threat to the US economy as these are not borrowings by the US, rather these are China's investment arising as a result of its huge trade surpluses. Even when China sells off the assets held in the form of US Treasury securities, it may not influence bond yields since the US has command over management of both short-term and long-term interest rates. Countries like Greece, Italy and Spain *etc.*, who have abandoned their local currencies and adopted the Euro faced the sovereign debt crisis because they had borrowed from markets at market interest rates and they had no control over these interest rates. So, borrowing in domestic currency is not a burden.

Public borrowing crowds out private investment is the fourth myth. Conventional economic theories state that higher budget deficit leads to higher public borrowing, leading to competition for funds between government and the private sector. As savings are limited, the rate of interest rises, private investment gets discouraged and production activities get hampered leading to a reduction in wealth of the society. According to the author, however, it is the government budget surplus that is detrimental to a society. MMT rejects the loanable funds theory which emphasises that borrowing is limited by access to limited financial resources. Any borrowing supplies equal amount of bonds, leaving total saving in the economy unaltered. When government spends more than taxes, it leaves the banking system with larger cash reserves. Moreover, interest rate on government bonds is a matter of policy choice. The Fed has the ability to retain rates lower even if deficits soar. The crowding-out theory, hence, may not work in countries like the US, UK and Japan that borrow in their own sovereign currencies. In fact, well targeted public spending can crowd-in private investment and improve disposable income.

Trade deficit as a bane rather than trade surplus is the fifth myth. She argues that countries need not worry about trade deficit as long as fiscal policy ensures full employment at home. Further, since the USA is the sole issuer of dollar, the principal reserve currency of the world, it may not face great difficulty in financing imports; the same, however, may not hold for developing nations. If developing nations run huge trade deficits, they have to make payments in dollar, which could undermine their monetary sovereignty. Further, they do not have deep capital markets and can experience sharp swings in exchange rate.

The sixth myth is that government funded entitlement programmes are financially unsustainable. The power of funding social security schemes comes from the exclusive right of the government to issue currency. Instead of fiscal deficit, therefore, greater attention should be given to the other deficits of real concern, *i.e.,* deficit in jobs, health infrastructure, education facilities, clean climate, *etc.*

Post-COVID-19 ultra-accommodative monetary policy and expansionary fiscal policy provide the relevant context to examine the utility as well as futility of MMT as a guide to conduct macro-economic policies for the future. The Deficit Myth, though persuasive, can be misleading for emerging market economies (EMEs). Fiscal deficit can cure economic malaise if utilised judiciously. As the entire world is reeling under the impact of COVID-19, governments are facing the dual challenge of falling revenues due to subdued economic activities and rising expenditure to mitigate the impact of the pandemic. Application of MMT can provide breathing space to nations, which may be difficult to justify under conventional economic theories. It is important to recognise, however, that, this book is written keeping the US economy in mind; the analysis and examples that relate to the US economy may not be suitable for EMEs, in particular high fiscal deficit and debt, and unrestricted expansion in money supply which have been the well-established sources of macro-economic instability in these countries. The book nevertheless provides an intellectual challenge to the established norms guiding the conduct of macro policies and may necessitate a revisit of policy frameworks to prioritise real economy issues while safeguarding sustainability.

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