

Modern Money Theory and European Macroeconomics – *an Alternative to the Policy of Austerity?*

Dr. Dirk Ehnts

Austerity Equals Confidence: Trichet

Patrick Allen

Published 4:23 AM ET Fri, 3 Sept 2010 | Updated 4:28 AM ET Fri, 3 Sept 2010

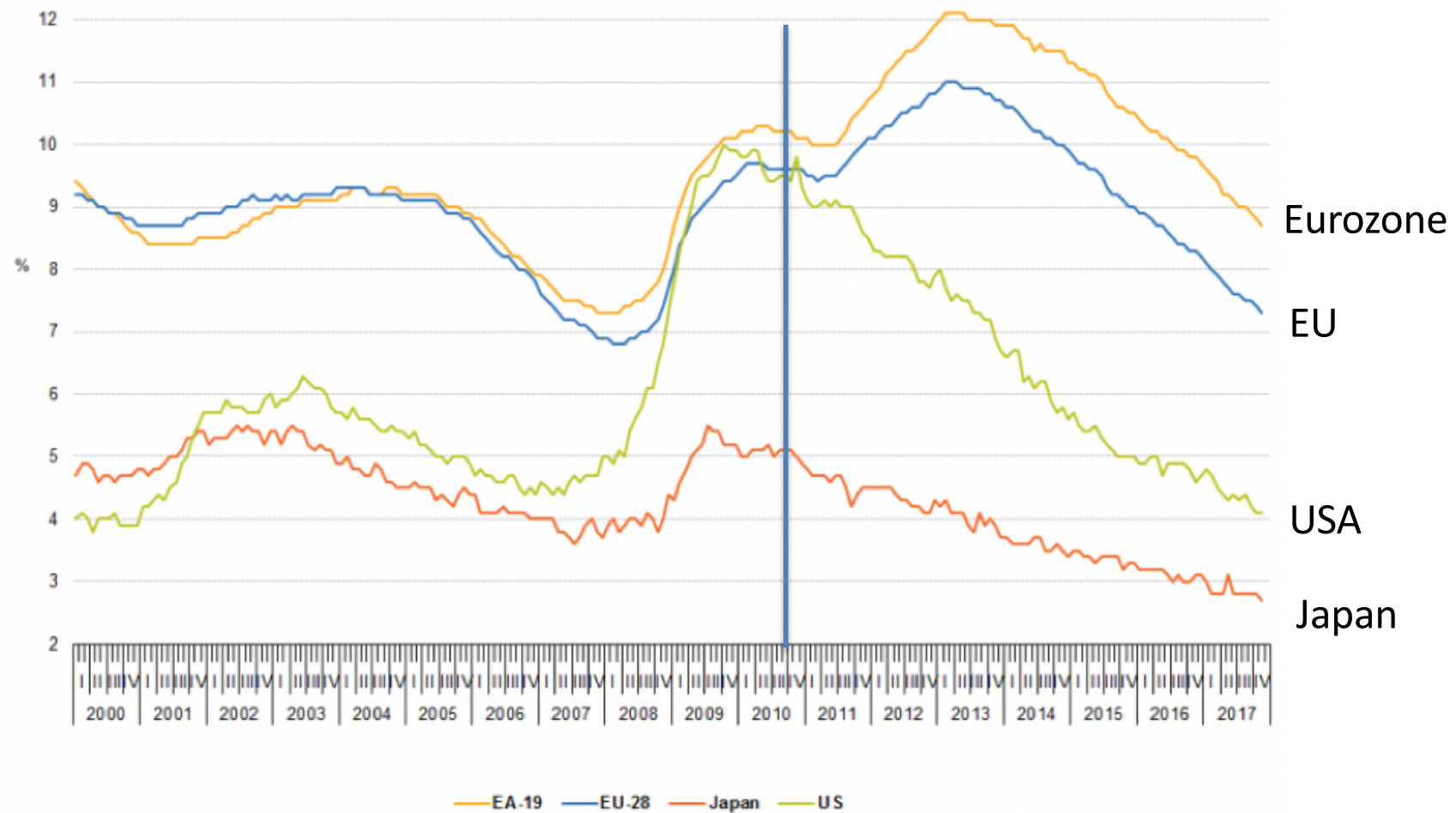


Prudent fiscal policy will help foster confidence within the euro zone, European Central Bank President Jean-Claude Trichet told CNBC.

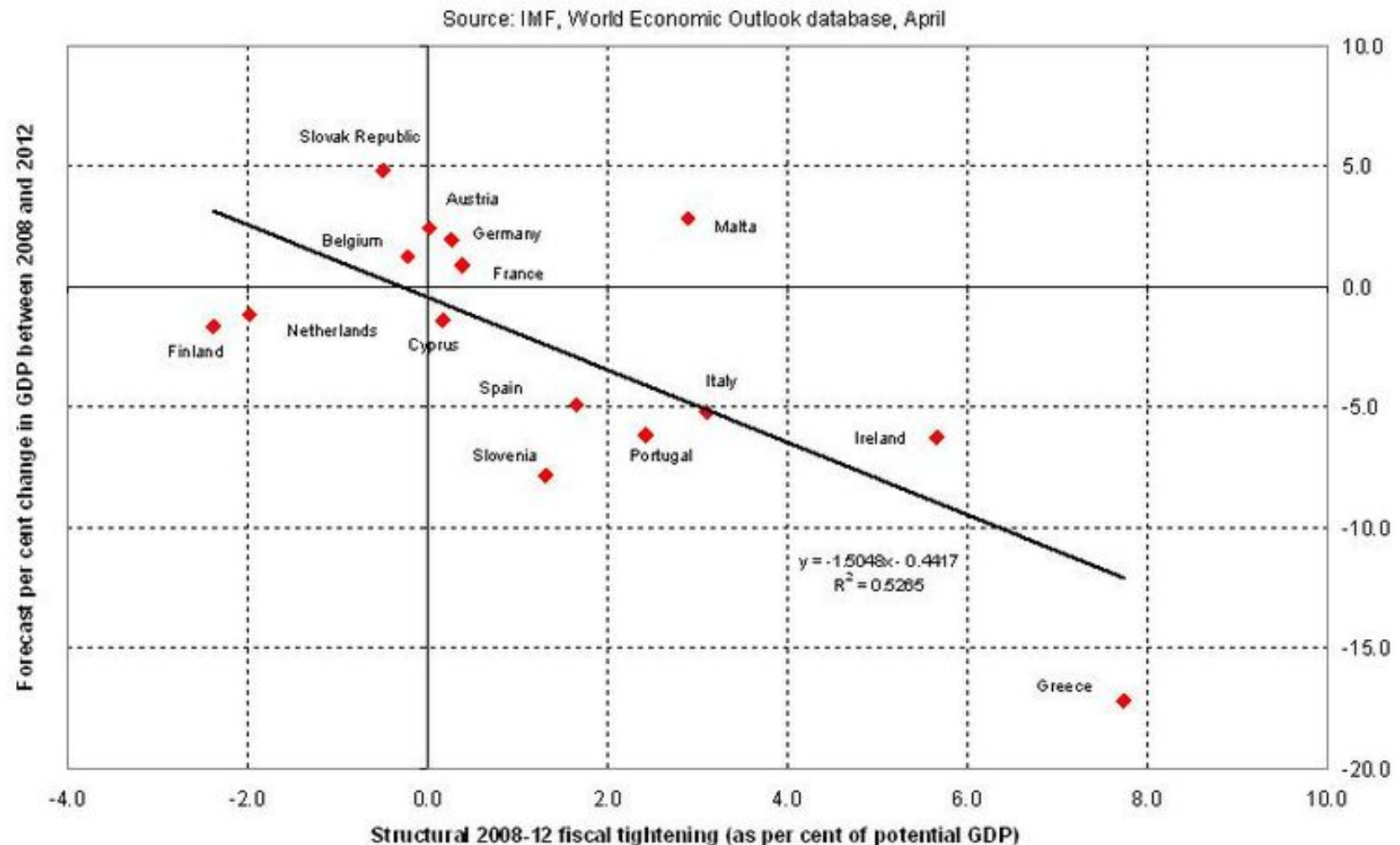
"We encourage all countries to be absolutely determined to go back to a sustainable mode for their fiscal policies," Trichet said, speaking after the ECB rate decision on Thursday. "Our message is the same for all, and we trust that it is absolutely decisive not only for each country individually, but for prosperity of all."

"Not because it is an elementary recommendation to care for your sons and daughter and not overburden them, but because it is good for confidence, consumption and investment today," he said.

Seasonally adjusted rates of unemployment



Fiscal tightening and the Eurozone



„ ... we're living in a **Dark Age of macroeconomics**. Remember, what defined the Dark Ages wasn't the fact that they were primitive — the Bronze Age was primitive, too. What made the Dark Ages dark was the fact that so much knowledge had been lost, that so much known to the Greeks and Romans had been forgotten by the barbarian kingdoms that followed. And that's what seems to have happened to macroeconomics in much of the economics profession.“



Macroeconomic Priorities[†]

By ROBERT E. LUCAS, JR.*

Macroeconomics was born as a distinct field in the 1940's, as a part of the intellectual response to the Great Depression. The term then referred to the body of knowledge and expertise that we hoped would prevent the recurrence of that economic disaster. My thesis in this lecture is that macroeconomics in this original sense has succeeded: Its central problem of depression prevention has been solved, for all practical purposes, and has in fact been solved for many decades. There remain important gains in welfare from better fiscal policies, but I argue that these are gains from providing people with better incentives to work and to save, not from better fine-tuning of spending flows. Taking

American Economic
Association 2003
Presidential Address



<http://pages.stern.nyu.edu/~dbackus/Taxes/Lucas%20priorities%20AER%2003.pdf>



The Federal Reserve Board

Remarks by Governor Ben S. Bernanke

At the meetings of the Eastern Economic Association, Washington, DC
February 20, 2004



The Great Moderation

One of the most striking features of the economic landscape over the past twenty years or so has been a substantial decline in macroeconomic volatility. In a recent article, Olivier Blanchard and John Simon (2001) documented that the variability of quarterly growth in real output (as measured by its standard deviation) has declined by half since the mid-1980s, while the variability of quarterly inflation has declined by about two thirds.¹ Several writers on the topic have dubbed this remarkable decline in the variability of both output and inflation "the Great Moderation." Similar declines in the volatility of output and inflation occurred at about the same time in other major industrial countries, with the recent exception of Japan, a country that has faced a distinctive set of economic problems in the past decade.

<http://www.federalreserve.gov/BOARDDOCS/SPEECHES/2004/20040220/default.htm>



Alan
Greenspan,
2005

[...] The new instruments of risk dispersal have enabled the largest and most sophisticated banks, in their credit-granting role, to divest themselves of much credit risk by passing it to institutions with far less leverage. Insurance companies, especially those in reinsurance, pension funds, and hedge funds continue to be willing, at a price, to supply credit protection.

[...] These increasingly complex financial instruments have contributed to the development of a far more flexible, efficient, and hence resilient financial system than the one that existed just a quarter-century ago.

<http://www.federalreserve.gov/boarddocs/speeches/2005/20051012/default.htm>

“I think there is an element of truth in the view that the superstition that the budget must be balanced at all times [is necessary]. Once it is debunked [that] takes away one of the bulwarks that every society must have against expenditure out of control. There must be discipline in the allocation of resources or you will have anarchistic chaos and inefficiency. And one of the functions of old fashioned religion was to scare people by sometimes what might be regarded as myths into behaving in a way that the long-run civilized life requires.”



- Paul Samuelson, in a movie by Mark Blaug (1995)

MMT and history of economic thought



John Maynard Keynes
(1883-1946)
Founder of modern
macroeconomics

Post-Keynesianism: Not mainstream. Emphasizes risk, irrationality of economic actors (businesses, consumers, etc.) and inherent instability of the financial sector. Tends to favor aggressive government intervention in the economy but is skeptical of monetary policy.

Neo-Keynesianism: Left wing of mainstream economics, believes that governments can play a role in fighting recessions, through both deficit-financed spending and monetary policy.

New Classical: Right wing of mainstream economics, believes that recessions and booms are inevitable and that government can't or shouldn't do much to boost the economy in the short run.



Joan Robinson
(1903-1983)
Applied Keynes to growth theory, criticized Hicks/Samuelson-style Keynesianism.



Abba Lerner
(1903-82)
Developed "functional finance," a forerunner to Modern Monetary Theory.



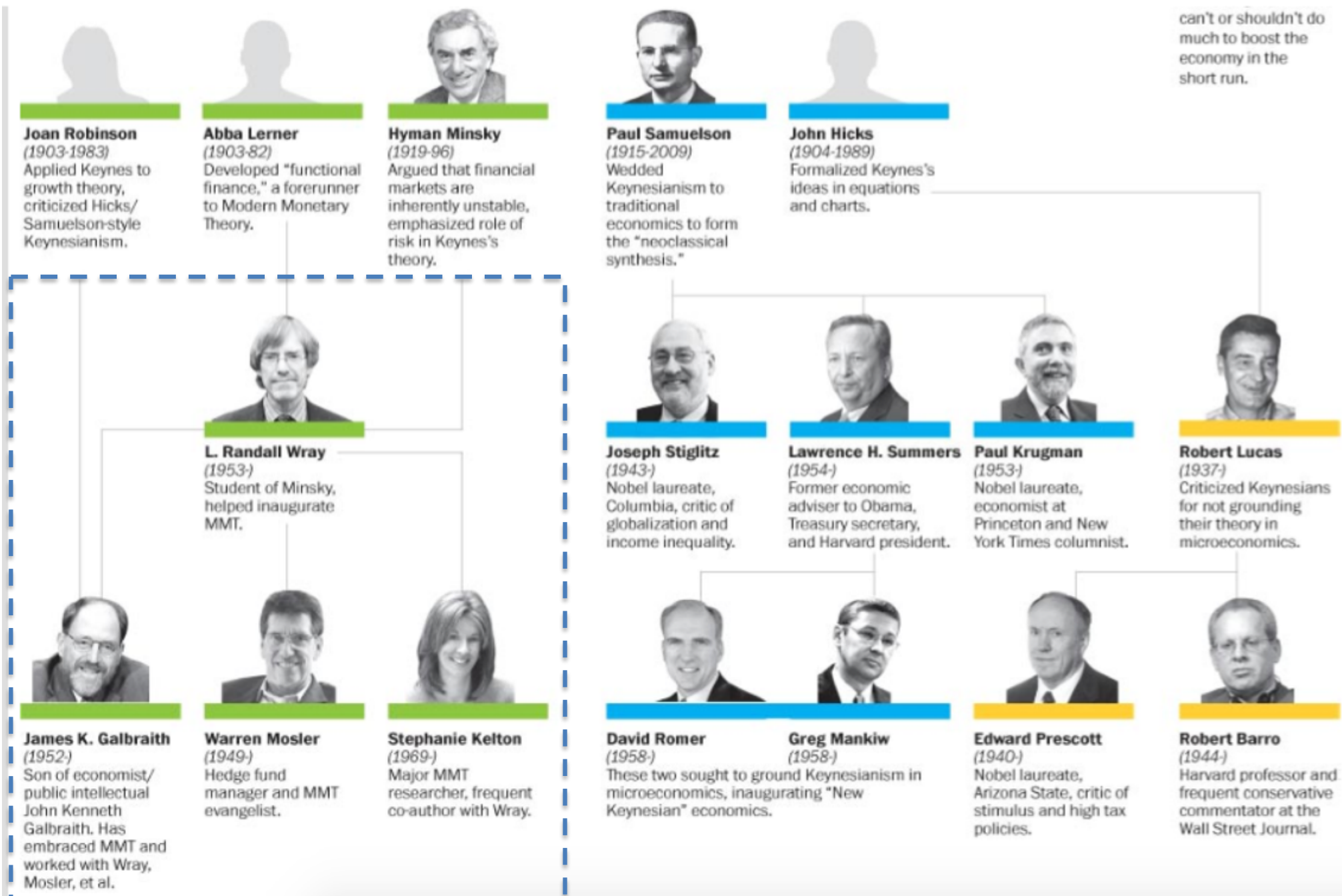
Hyman Minsky
(1919-96)
Argued that financial markets are inherently unstable, emphasized role of risk in Keynes's theory.



Paul Samuelson
(1915-2009)
Wedded Keynesianism to traditional economics to form the "neoclassical synthesis."



John Hicks
(1904-1989)
Formalized Keynes's ideas in equations and charts.



Some core MMT insights

- Banks create bank deposits through an accounting operation
- Central banks create reserves (deposits) through an accounting operation
- Government cannot go bankrupt as long as it spends its own currency run by the central bank
- Unemployment and lack of demand can be cured through an increase in gov. spending

Money creation in the modern economy (2014)

by Michael McLeay, Amar Radia and Ryland Thomas of the Bank of England's Monetary Analysis Directorate.

In the modern economy, most money takes the form of bank deposits. But how those bank deposits are created is often misunderstood: the principal way is through commercial banks making loans. **Whenever a bank makes a loan, it simultaneously creates a matching deposit in the borrower's bank account, thereby creating new money.**

The reality of how money is created today differs from the description found in some economics textbooks:

- Rather than banks receiving deposits when households save and then lending them out, bank lending creates deposits.
- In normal times, the central bank does not fix the amount of money in circulation, nor is central bank money 'multiplied up' into more loans and deposits.



Heutige Lehrbücher liegen falsch:

Sparen führt nicht Investitionen, und die Zentralbank kontrolliert die Geldmenge nicht. Zentralbankgeld wird durch Kreditvergabe multipliziert.

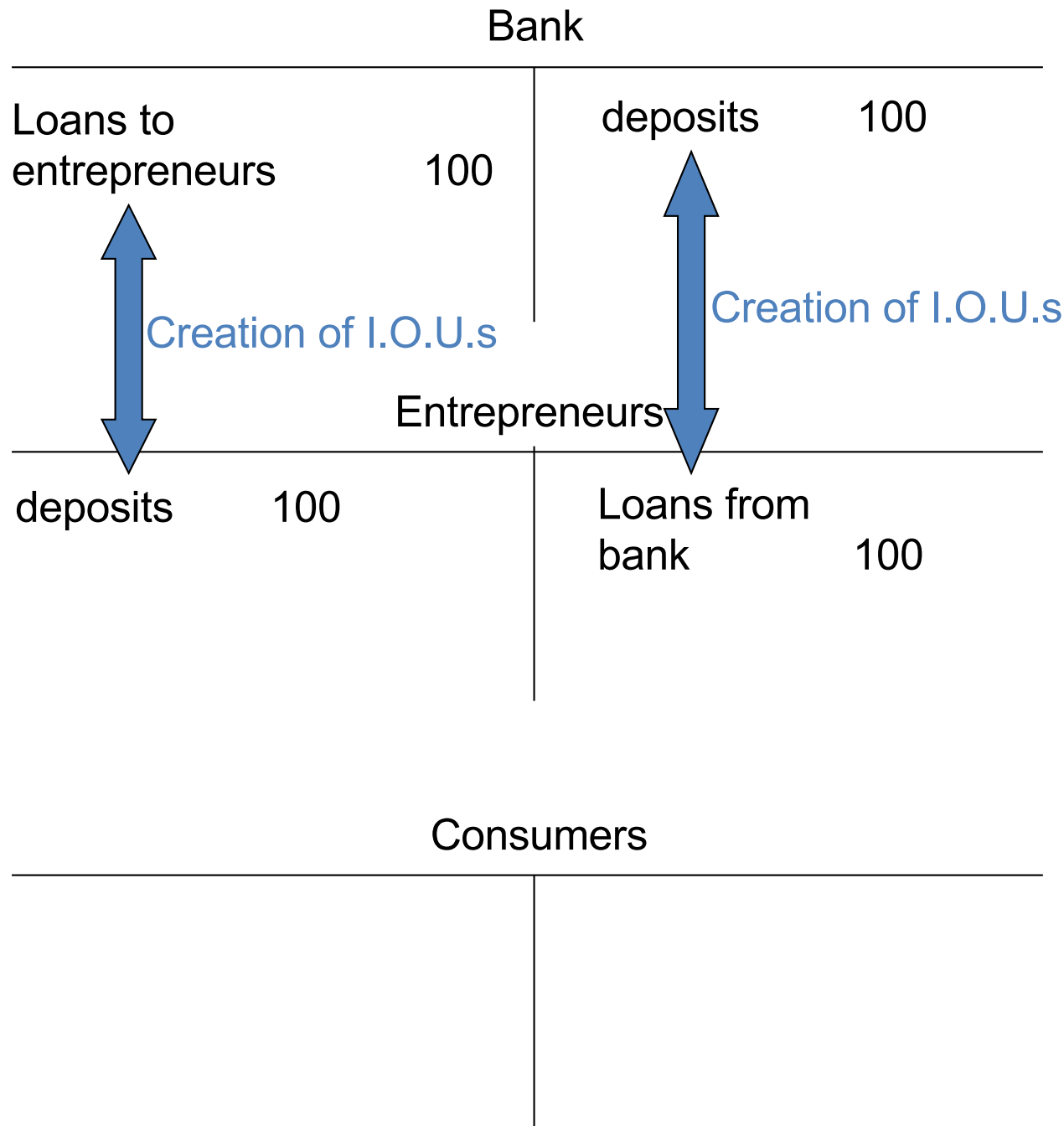
Die Rolle von Banken, Nichtbanken und Zentralbank im Geldschöpfungsprozess

Bereits die rein buchungstechnische Betrachtung der Entstehung von (Buch-)Geld verdeutlicht, dass die Kredit- und Geldschöpfung das Ergebnis komplexer Interaktionen zwischen Banken, Nichtbanken und Zentralbank ist. Dabei hängt die Fähigkeit der Banken, Kredite zu vergeben und Geld zu schaffen, nicht davon ab, ob sie bereits über freie Zentralbankguthaben oder Einlagen verfügen. Vielmehr wird der Geldschöpfungsprozess durch eine Reihe von ökonomischen und regulatorischen Faktoren begrenzt. Bankseitig findet die Geldschöpfung ihre Grenzen im Ertrags-Kosten-Kalkül der einzelnen Banken sowie in mikro- und makroprudenziellen Regulierungsvorschriften. Darüber hinaus wird deutlich, dass auch die Kreditnachfrage und das Portfolioverhalten der Nichtbanken die Geldschöpfung beschränken. Die Zentralbank beeinflusst den Geld- und Kreditschöpfungsprozess in normalen Zeiten über die Zinspolitik, die über verschiedene Transmissionskanäle auf die Finanzierungs- und Portfolioentscheidungen der Banken und Nichtbanken wirkt.

A financial theory of production

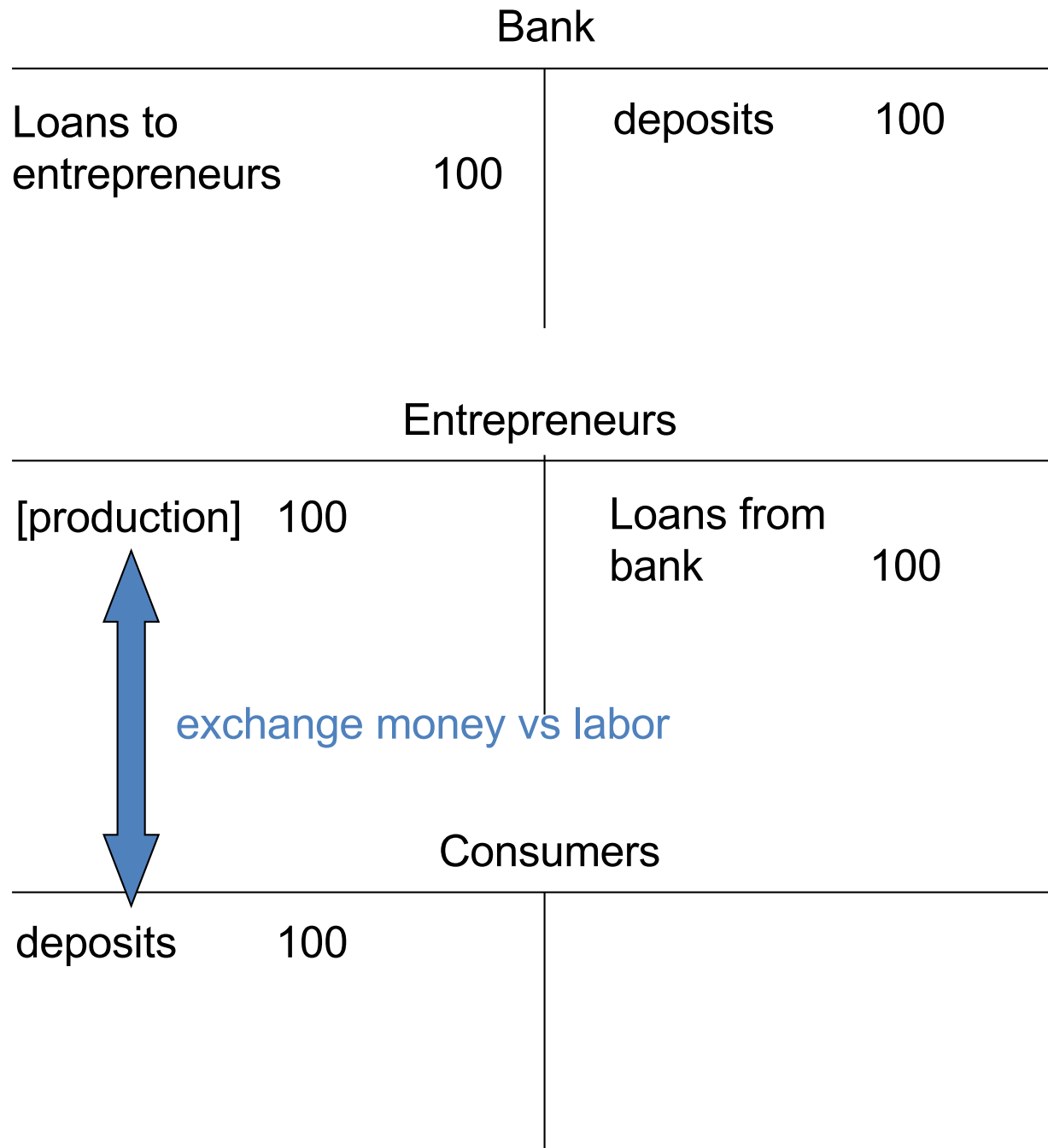
- Perhaps it is best to go all the way back to Wicksell (1898) *Geldzins und Güterpreise* [Interest and Prices]. On page 170 ff., he develops a model.
- The model includes a bank, entrepreneurs and consumers.
- It shows a *circuit* of money and could be described as *‘a credit theory of production’*.





Step 1:

Entrepreneurs demand loans from banks given the interest rate. Banks create deposits which are used as money.

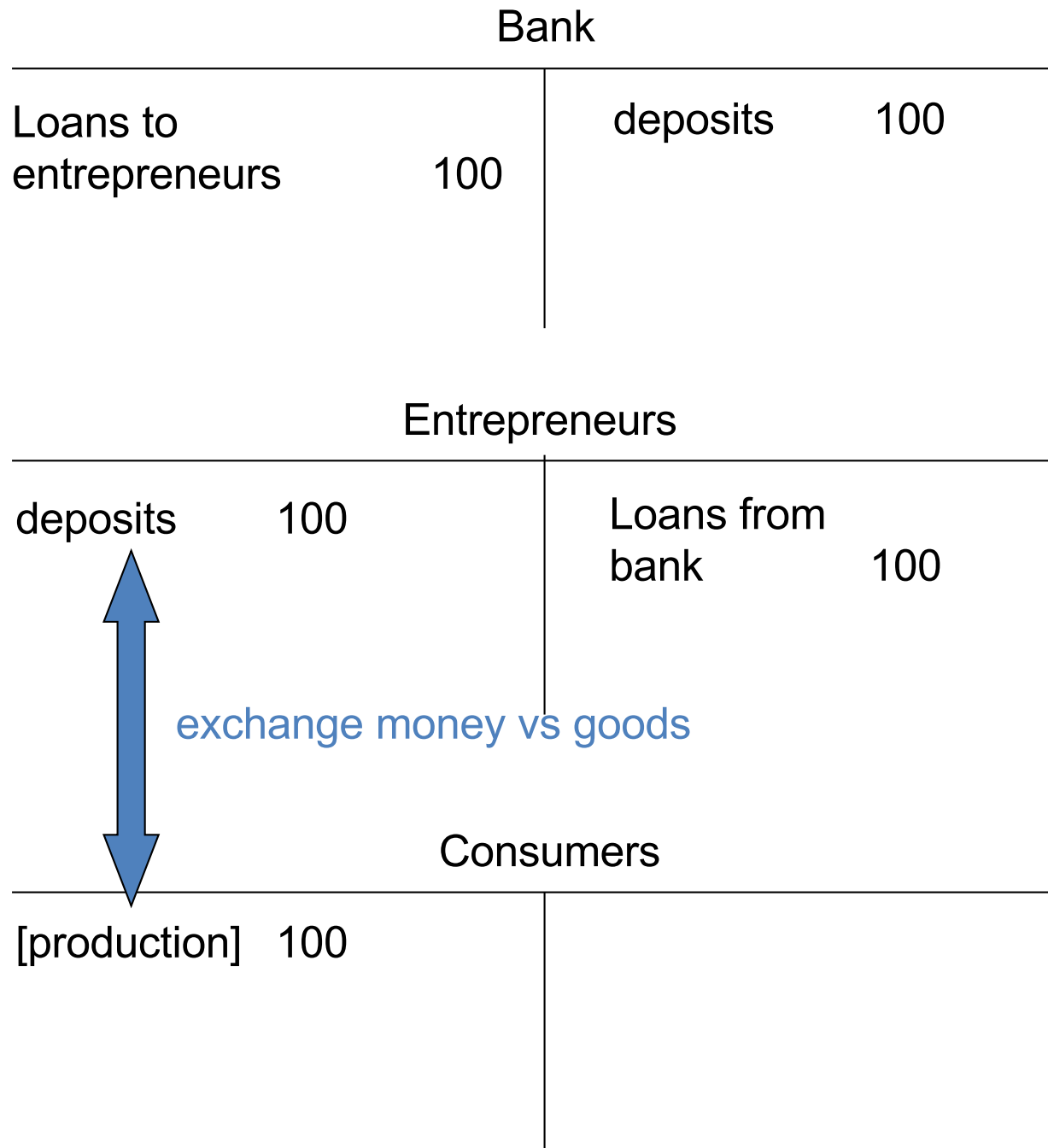


Step 1:

Entrepreneurs demand loans from banks given the interest rate. Banks create deposits which are used as money.

Step 2:

Entrepreneurs pay households to buy their labour and produce.



Step 1:

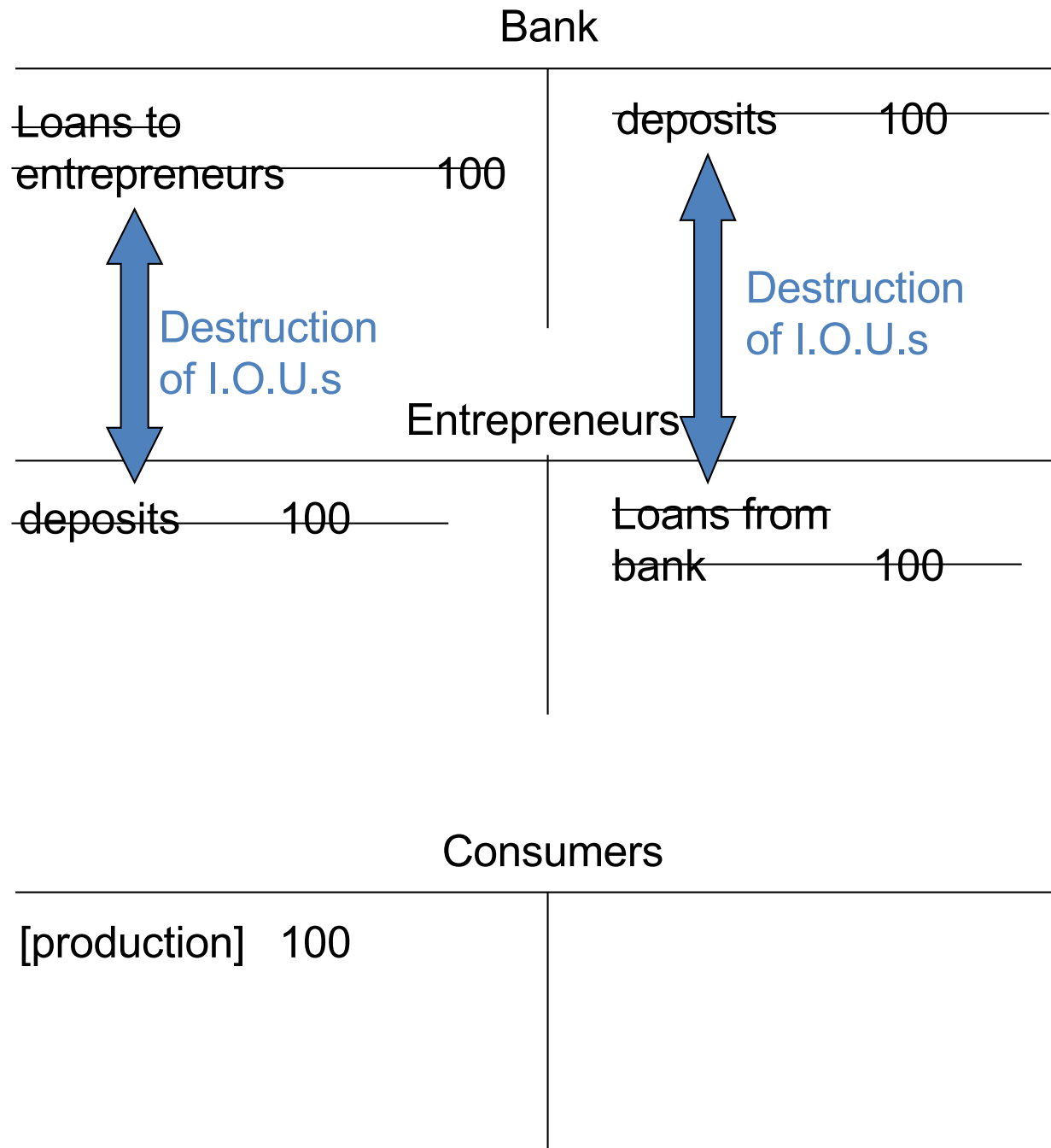
Entrepreneurs demand loans from banks given the interest rate. Banks create deposits which are used as money.

Step 2:

Entrepreneurs pay households to buy their labour and produce.

Step 3:

Households buy goods.



Step 1:

Entrepreneurs demand loans from banks given the interest rate. Banks create deposits which are used as money.

Step 2:

Entrepreneurs pay households to buy their labour and produce.

Step 3:

Households buy goods.

Step 4:

Entrepreneurs repay bank loans.

Bank

Summary:

We have here a credit theory of production. Credit is created by the banks driven by demand, deposits are circulated in the economy by the private sector (entrepreneurs and households) and finally deposits are destroyed when bank loans are repaid.

The goal of the *credit circuit* is to enable production and consumption, i.e. to make entrepreneurs produce goods and services, and then let consumers buy them.

If banks can create bank deposits without needing reserves, then ...



RatingsDirect®

Economic Research:

**Repeat After Me: Banks Cannot And
Do Not "Lend Out" Reserves**

Credit Market Services:

Paul Sheard, Chief Global Economist and Head of Global Economics and Research, New York (1)
212-438-6262; paul_sheard@standardandpoors.com



EUROPE'S DEBT CRISIS

ECB loans out €529.5 billion to European banks

By Ben Rooney and Chris Isidore @CNNMoneyInvest February 29, 2012: 8:15 AM ET

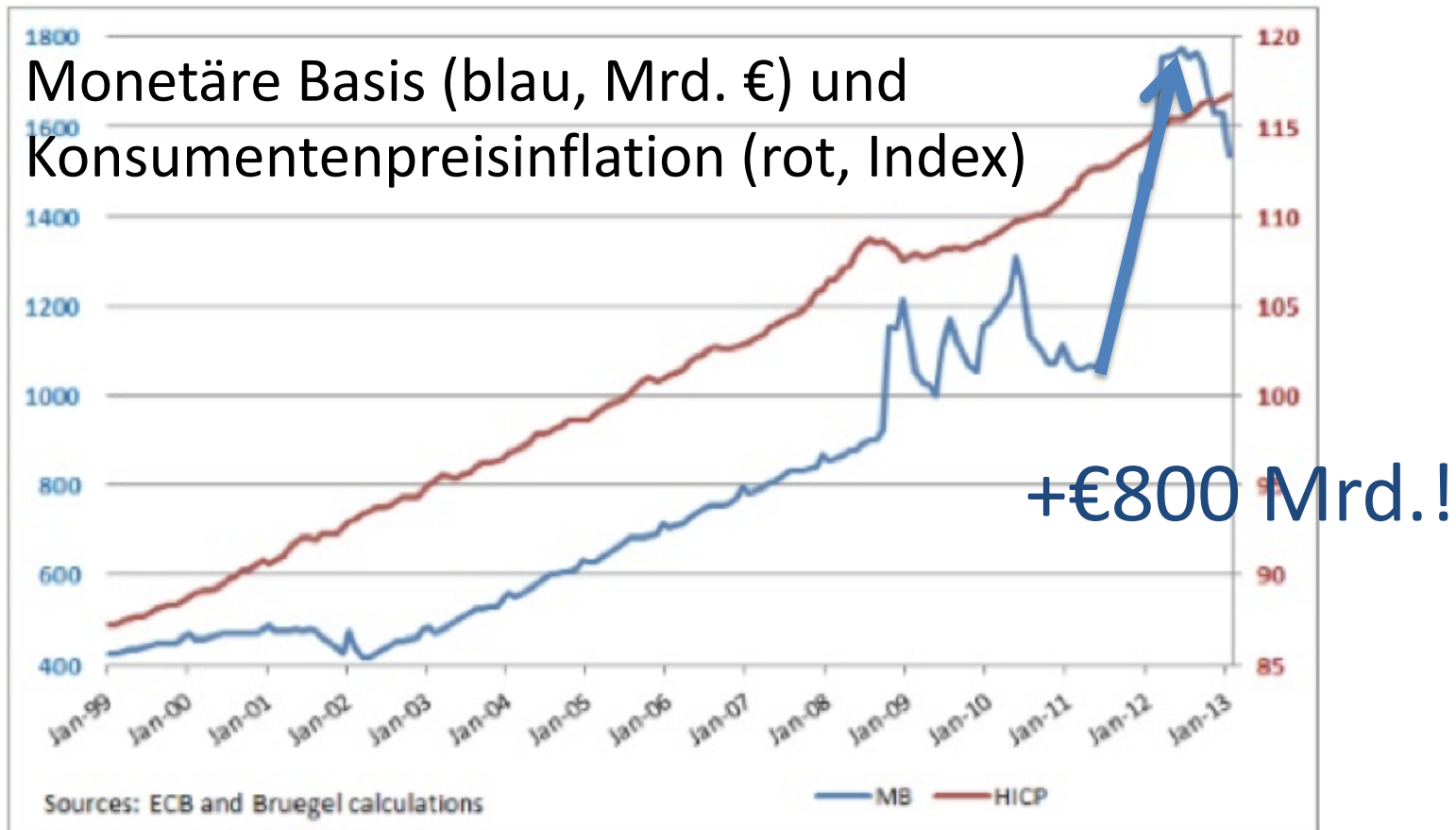
NEW YORK (CNNMoney) -- The European Central Bank announced Wednesday that banks borrowed €529.5 billion, or \$712.4 billion, under a highly-anticipated lending program aimed at preventing a credit crunch in Europe.

In its second long-term refinancing operation (LTRO), the ECB offered banks unlimited three-year loans at interest rates as low as 1%. The ECB allotted nearly €500 billion in the first round of the operation in December.

The borrowing was a bit more than expected, as banks were expected to have taken up roughly €500 billion, although estimates ranged from €300 billion to €1 trillion.

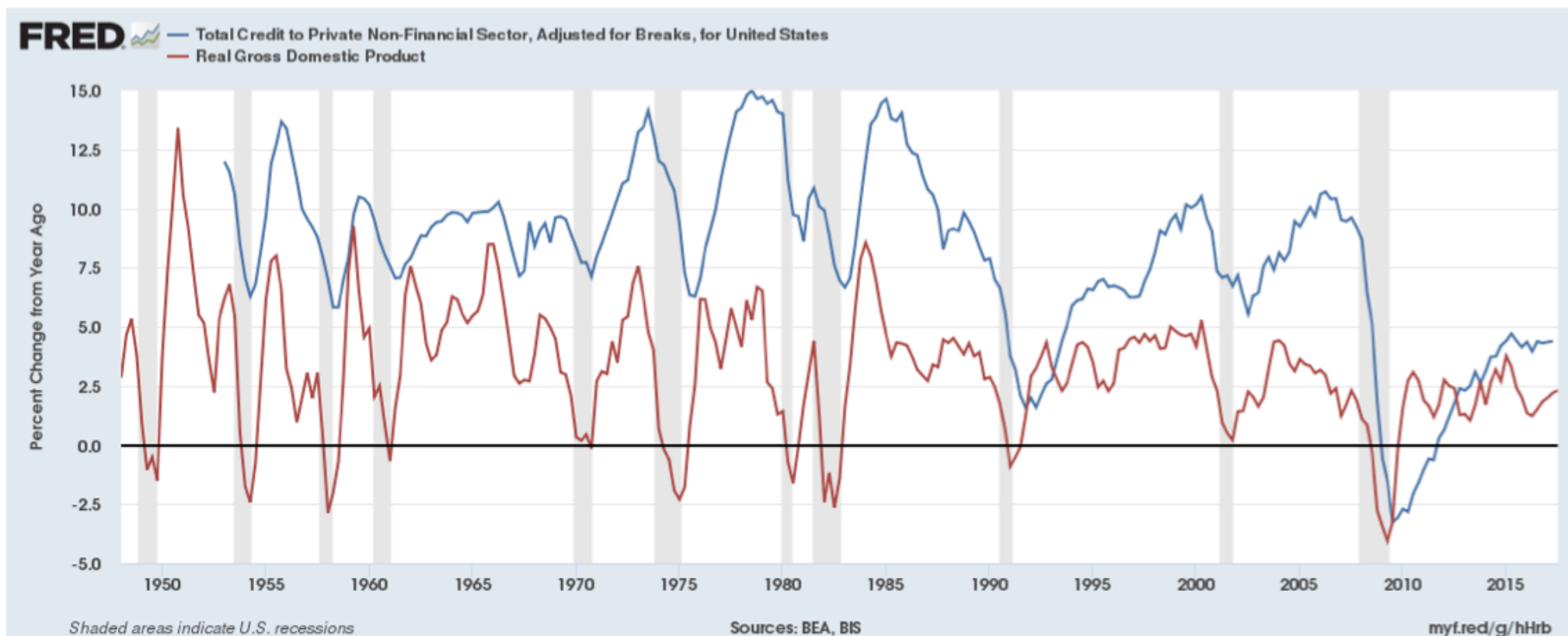
http://money.cnn.com/2012/02/29/markets/ecb_bank_loans/

Chart 2 – Monetary Base and Harmonised Index of Consumer Prices in EA (1999-2013)



<http://www.bruegel.org/nc/blog/detail/article/1056-where-has-all-the-base-money-gone/>

DSGE models are no help at all.



„... and with a representative agent, so that there is no credit extended in equilibrium and hence no possibility of cyclical variations in credit.“

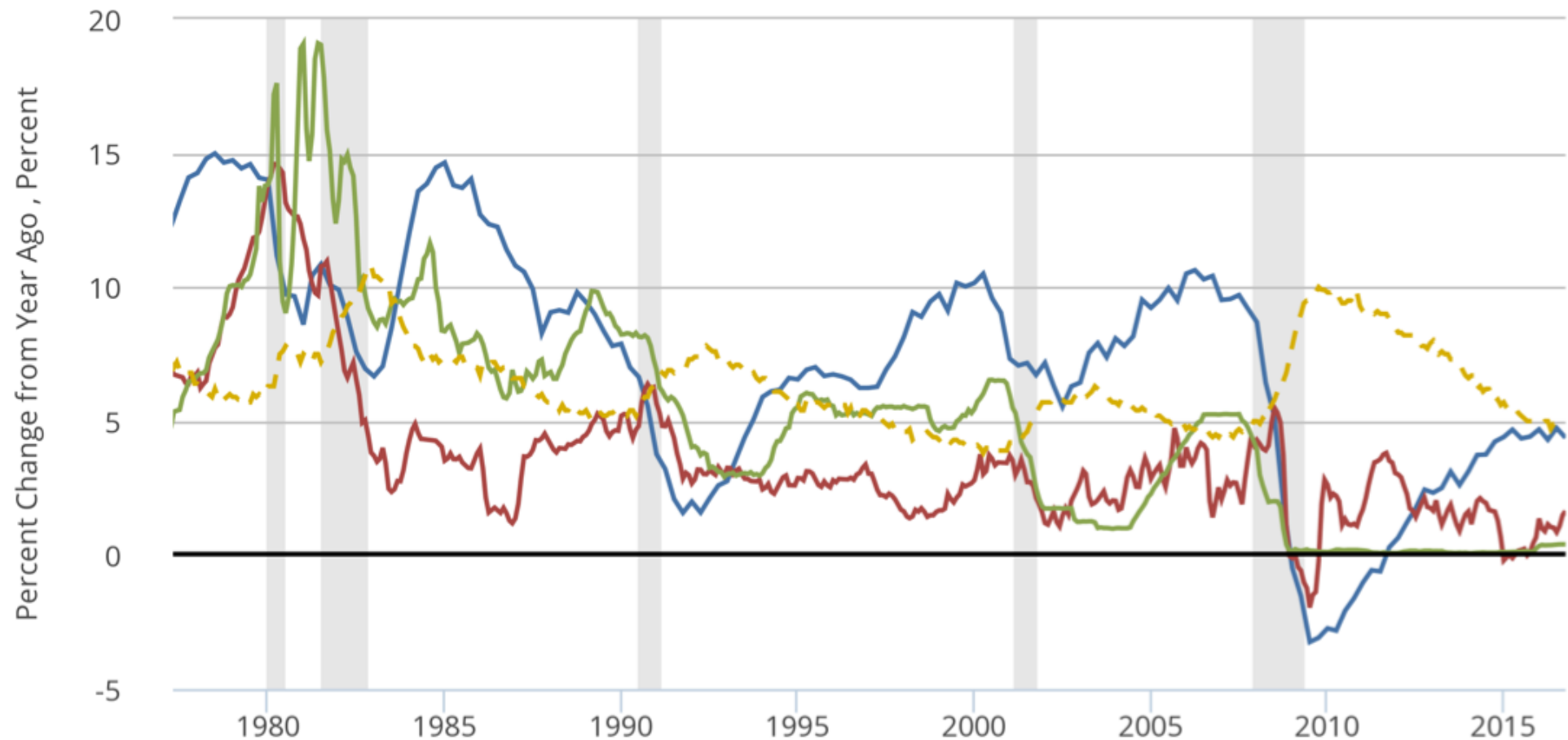


Cúrdia and Woodford, Credit Spreads and Monetary Policy, 2009

B-u-s-i-n-e-s-s c-y-c-l-e



- Total Credit to Private Non-Financial Sector, Adjusted for Breaks, for United States©
- Consumer Price Index for All Urban Consumers: All Items
- Effective Federal Funds Rate
- - Civilian Unemployment Rate



Sources: BIS, BLS, Board of Governors

fred.stlouisfed.org

myf.red/g/eJoc

The role of fiscal policy

- As a matter of logic, Government spends first, then collects taxes
- "State Money" is tax credits
 - $G > T$: deficit – more tax credits given to private sector than taken away
 - $T > G$: surplus – more tax credits taken away from than given to private sector
- That's all, folks!

The case of Canada

Government exchanges bonds for reserves at central bank ...

central bank		treasury	
bonds	reserves	reserves	bonds
bank		private sector	

The case of Canada

... and pays private sector through bank transfer ...

central bank		treasury	
bonds	reserves	reserves widgets	bonds - net worth
bank		private sector	
reserves	deposits	deposits widgets	+ net worth

The case of Canada

... with banks preferring to hold interest-bearing bonds and the private sector ready to spend the additional deposits created.

central bank		treasury	
bonds	reserves	widgets	bonds - net worth
bank		private sector	
reserves bonds	deposits	deposits widgets	+ net worth

The case of Canada

If the private sector prefers t-bonds to deposits it looks like this:

central bank		treasury	
bonds	reserves	widgets	bonds - net worth
bank		private sector	
reserves bonds	deposits	deposits widgets bonds	+ net worth

The case of the Eurozone

Banks borrow from central bank to purchase bonds later...

central bank	
loans	reserves

treasury	

bank	
reserves	loans

private sector	

The case of the Eurozone

... Treasury sells bonds to banks for reserves at account at CB.

central bank		treasury	
loans	reserves	reserves	bonds
bank		private sector	
reserves bonds	loans		

The case of the Eurozone

The Treasury pays private sector by bank transfer...

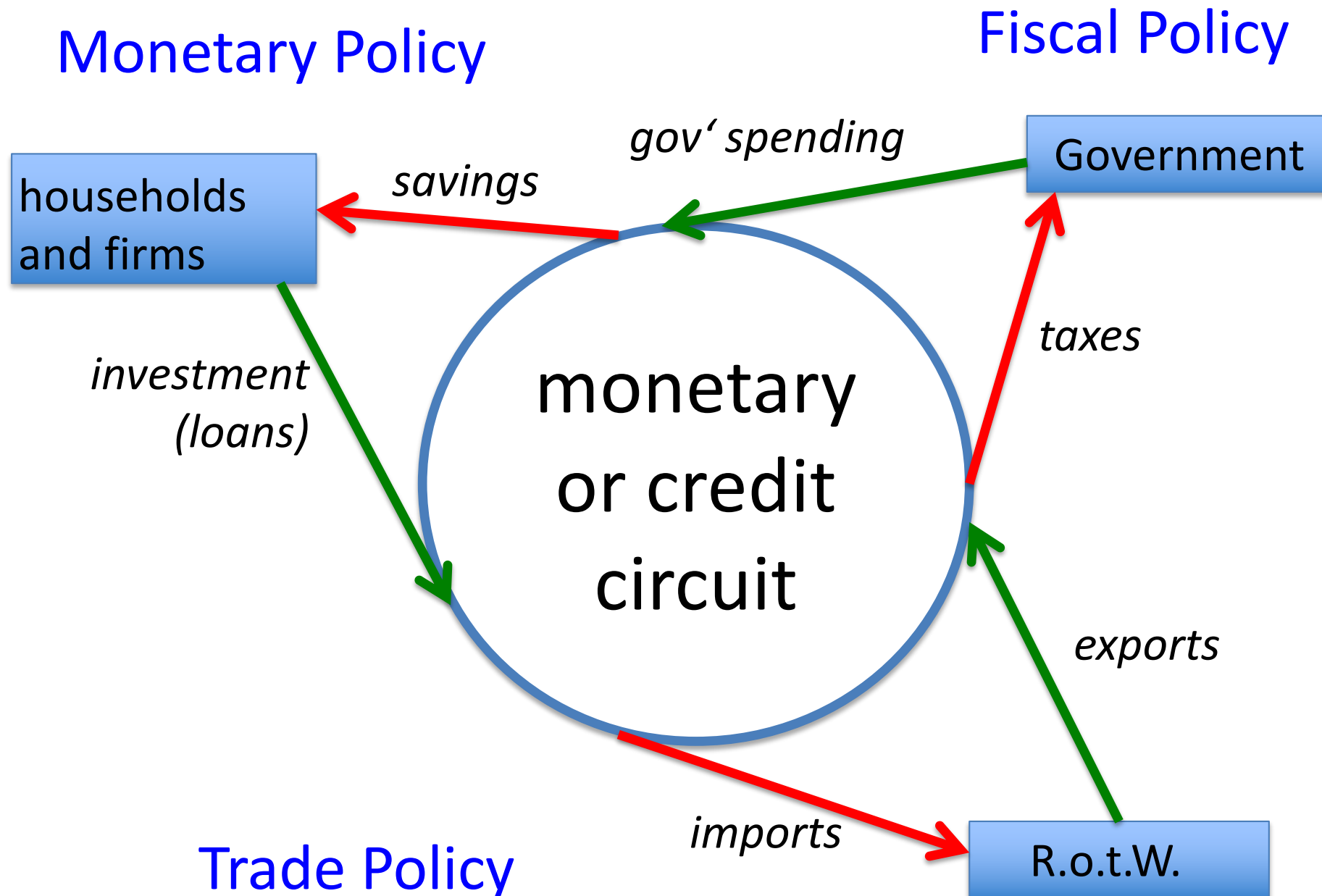
central bank		treasury	
loans	reserves	reserves	bonds - net wealth
bank		private sector	
reserves bonds	loans deposits	deposits	+ net wealth

The case of the Eurozone

Banks prefer to repay debt and hold less reserves or the CB intervenes to stop the interbank market rate from falling.

central bank		treasury	
loans	reserves	reserves	bonds - net wealth
bank		private sector	
reserves bonds	loans deposits	deposits	+ net wealth

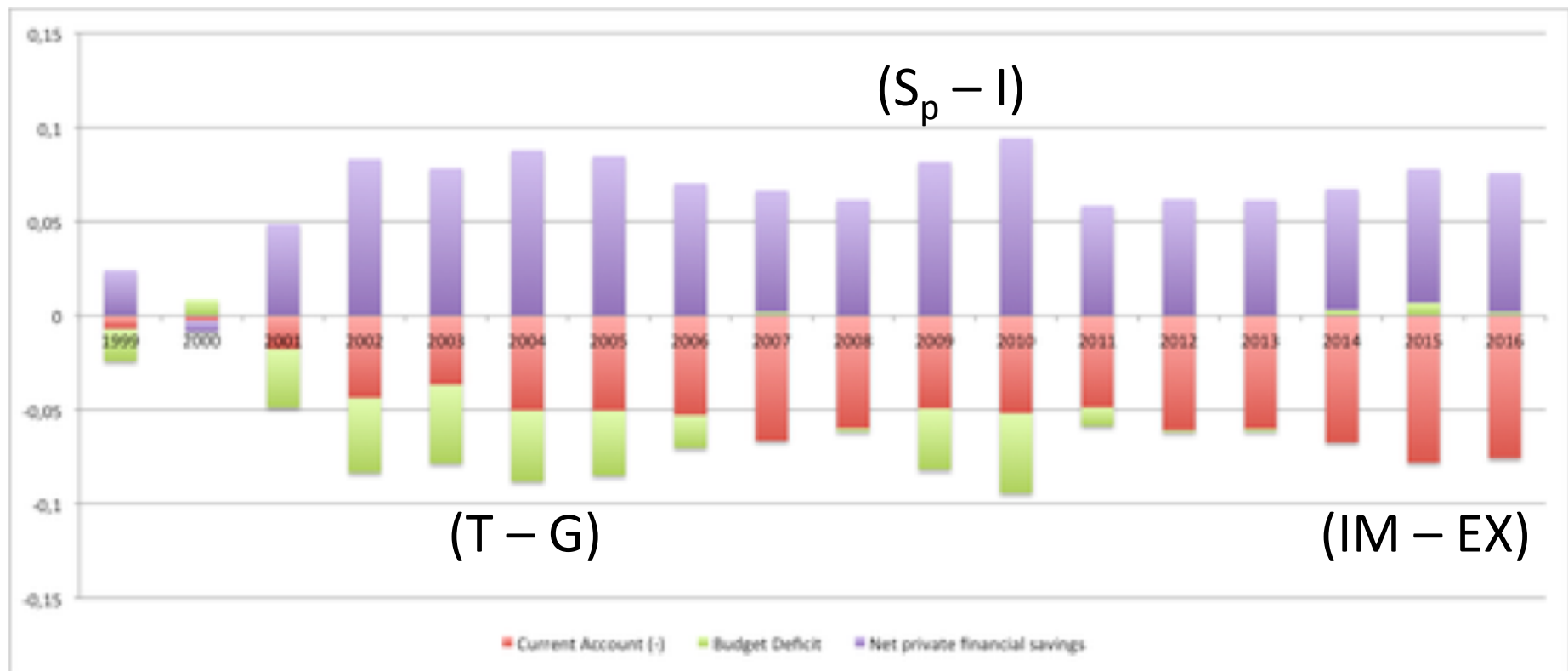
If you want to raise national income...



$$(S_p - I) + (T - G) + (IM - EX) = 0$$

Private sector + public sector + external sector = 0

Sectoral balances: Germany



How to overcome austerity policies?

- Persuasion, persuasion, persuasion!
- Eurozone is a special case (see US, UK, China, Japan, etc.)
- MMT provides strong foundations for economic policy (analysis)
- (I am currently writing a macroeconomics textbook based on MMT)

More MMT stuff

- Wray, L. R. (2015): Modern Money Theory: A Primer on Macroeconomics for Sovereign Monetary Systems, 2nd ed.
- <https://alittleecon.wordpress.com/academic-mmt/>
- <http://neweconomicperspectives.org/>
- <http://bilbo.economicoutlook.net/blog/>
- Ehnts, Dirk H. (2016): Geld und Kredit: eine €-päische Perspektive, Metropolis, 2. Auflage
- Ehnts, Dirk H. (2016): Modern Monetary Theory and European Macroeconomics
- Samuel-Pufendorf-Gesellschaft für politische Ökonomie e.V.
 - <http://www.pufendorf-gesellschaft.org/>

Warren Mosler ist ein einschlägiger Experte auf dem Gebiet Geld und Kredit. Durch seine lange Berufserfahrung an den Märkten weiß er am besten, wie Zentralbankgeld in Umlauf kommt, wie genau Banken funktionieren und warum Staaten bei ihrer Finanzierung nicht mit einer schwäbischen Hausfrau zu vergleichen sind. Arbeitslosigkeit ist ein politisches Problem und kein finanzielles. Warren Mosler hat mit seinen Ideen der modernen Geldtheorie neuen Schwung verliehen und eröffnet dadurch die Möglichkeit, das Primat der Politik wieder in der Gesellschaft zu verankern. *Die sieben unschuldigen, aber tödlichen Betrugereien der Wirtschaftspolitik* trägt dazu bei, die Öffentlichkeit aufzuklären über die Gestaltungsmöglichkeiten einer modernen Geldwirtschaft. Vor dem Hintergrund der andauernden Probleme in der Eurozone ist dies vielleicht wichtiger als je zuvor.

Dr. Dirk Ehnts, Technische Universität Chemnitz

Dirk Ehnts

Geld und Kredit:
eine €-päische Perspektive



metropolis

ROUTLEDGE INTERNATIONAL STUDIES IN MONEY AND BANKING

Modern Monetary Theory and
European Macroeconomics

Dirk H. Ehnts



Die sieben Betrugereien der Wirtschaftspolitik

WARREN MOSLER



WARREN MOSLER

Die sieben unschuldigen, aber tödlichen Betrugereien der Wirtschaftspolitik



Theorie

Deutsche Bundesbank: Geldmultiplikator ist falsch!

26.04.2017



[Bundesbank](#) [Aufgaben](#) [Themen](#) [Statistiken](#) [Service](#) [Presse](#) [Publikationen](#)

Startseite > Service > Schule und Bildung > Schülerbuch Geld und Geldpolitik digital

Bankdienstleistungen für
Zentralbanken

Vertiefung: Häufig gestellte Fragen
zum Thema Geldschöpfung

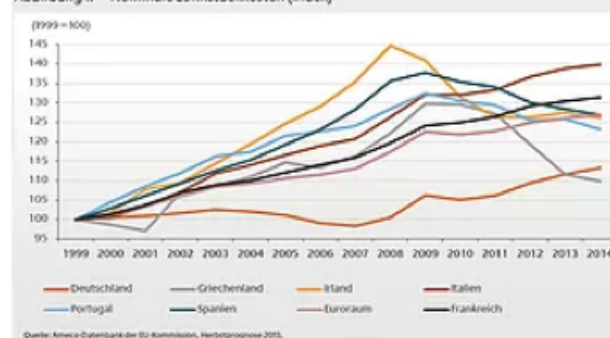
Die Deutsche Bundesbank hat auf ihren Webseiten eine interessante Seite mit Fragen und Antworten ([Link](#)). Die Seiten gehören zu einem Schülerbuch Geldpolitik (digital) und sind geldtheoretisch spannend. In den Lehrbüchern zur Makroökonomie steht ja bis heute, dass die Zentralbank Geld an die Banken verleiht, welches es dann weiter verleihen an Haushalte und Unternehmen. Da Banken jeden Euro an Zent...

Theorie

Lohnpolitik in einer Währungsunion

24.04.2017

Abbildung 1: Nominale Lohnstückkosten (Index)



Vor 20 Jahren wurde in der Frankfurter Rundschau ein Artikel von Heiner Flassbeck veröffentlicht, der auch heute noch lesenswert ist. Unter dem Titel "Und die Spielregeln für Lohnpolitik in einer Währungsunion?" ([pdf](#)) fragte Flassbeck, wie sich denn in der Eurozone

Suche

newsletter

primers

videos

mitmachen

Alle Beiträge:



Suche



Deutsche Bundesbank:
Geldmultiplikator ist falsch!
26.04.2017

Suche



Lohnpolitik in einer
Währungsunion
24.04.2017

Suche



Die Europäische
Zentralbank kann
unbegrenzt Geld schaffen
10.04.2017

Suche

Der Multiplikatoreffekt,
Investitionen und die
Ersparnis
04.04.2017

Kann eine Regierung Pleite
gehen?
23.03.2017

Wie reden wir über Geld
und Verschuldung?