Week 5 (May 16 2022): Context for Chapters 5 & 6

- · Chapter 5: "Winning at Trade"
- · Chapter 6: "You're Entitled"

We have just two sessions left in this course so in today's session we will once again cover two chapters in Stephanie Kelton's *The Deficit Myth*. Those chapters are #5, "Winning at Trade", and #6, "You're Entitled."

Return to Last Week's Bonus Question

In my introductory remarks this week, however, I'm actually going to turn back to the "Bonus Question" we dealt with in Week 4. That question referred you to two media articles reporting on President Biden's May 4 remarks on what he argued are the highlights of his administration's macroeconomic policy. The bonus question then asked you to evaluate Biden's remarks from the MMT perspective.

I decided that if I wanted to understand Biden's thinking better I should go straight to the source: the official White House transcript of [Remarks by President Biden On Economic Growth, Jobs, and Deficit Reduction](). I am going to cite him directly and then evaluate his statements in the way that (I think) MMT advocates like Stephanie Kelton would.

Biden: *"[W]e're on track to cut the federal deficit by … another $1.5 trillion by the end of this fiscal year — the biggest decline in a single year ever in American history. And the biggest decline on top of us having a $350 billion drop in the deficit last year, my first year as President.*"

Biden is boasting about cutting the deficit. MMT would ask, "Is this something we should necessarily be boasting about? If the converse were true, *i.e.*, if the deficit were growing, would that be something we should be worried about?"

Biden is explicitly assuming the validity of what Abba Lerner characterized as the "sound finance" approach to the federal government, as counterposed to the "functional finance" approach which MMT advocates. Biden is implicitly assuming that the federal budget -- the budget of a currency-issuing level of government -- works the same as any currency-using

household's budget. He is further assuming that the size of the federal budget deficit is a policy goal that *can* be targeted and *should* be targeted. MMT argues that the overall well-being of the economy is what should be targeted and that the size of the federal deficit cannot be effectively targeted because it is determined largely by the flows of automatic stabilizers such as tax receipts and unemployment benefits over which the government does not have tight control.

Biden: *"[F]or the first time since 2016, the Treasury Department is planning to pay down the national debt issued to the public this quarter."*

Biden might as well be saying, "For the first time since 2016, we're causing the net financial assets held by the non-government sector of our economy to go down." What happened when the Clinton administration started to pay down the national debt in the late 1990s?

Biden: *"[B]ringing down the deficit is one way to ease inflationary pressures in an economy where a consequence of a war and gas prices and oil and food and — it all — it's just a different world right this moment because of Ukraine and Russia. We reduce federal borrowing and we help combat inflation."*

Hey, Joe, can you tell us *specifically* how reducing the deficit eases inflationary pressures? For the sake of argument, let's assume that U.S. support for one side in the Russia-Ukraine war is a good thing. How is the deficit going to go down if war spending is increasing? If that war is reducing worldwide supplies of oil and wheat, why would we expect the prices of those two key commodities to go down? Can you show us a war during which prices went down?

Biden: *"The previous administration increased the deficit every year it was in office, in part because of its reckless $2 trillion tax cut. I know you're tired of hearing me saying that, but a $2 trillion tax cut that was not paid for. Was not paid for. And a tax cut that largely benefited the biggest corporations — 55 of which earned $40 billion in profits and paid not a single penny in income tax in 2020 — and wealthiest Americans, like the billionaires who on average pay just 8 percent in federal taxes."*

Okay, Joe, we're with you on the inequality in the tax burden. Would that Democrats had

been doing something about that during, say, the Obama administration, in which you were the Number Two guy.

But, hey, Joe, what exactly do you mean when you say that the Trump tax cuts were "not paid for"? That term "pay for" has a specific meaning in the U.S. Congress. It means that any new federal spending program cannot be implemented unless it is "paid for" by some combination of new tax revenues and spending cuts elsewhere. In this framework, the Trump tax cuts should have been "paid for" via spending cuts elsewhere in the federal budget. Where should those cuts have been made?

Biden: *[L]ooking ahead, I have a plan to reduce the deficit even more, which will help reduce inflationary pressures and lower everyone's costs for families. … [M]ost importantly, no one making less than $400,000 will pay a penny more in federal taxes."*

So, once again, Mr. President, how exactly will reducing the federal budget deficit -- even assuming that you can set that as a policy goal -- reduce inflationary pressures? MMT argues that *any* form of spending -- consumer, investment or government -- where real productive resources are in short supply will push prices up. What are the kinds of goods and services whose prices are currently being pushed up by government spending? If the prices of some goods and services are currently being pushed up by excessive consumer spending, how will taxes only on the very rich alleviate those pressures?

Biden: *"You've heard me say it before: I'm a capitalist. I believe you should be able to make as much as you legally can, but just pay your fair share."*

Stephanie Kelton, Bill Mitchell and other MMTers always say that before we can propose macroeconomic policies informed by Modern Money Theory, we first have to articulate our social and political values. I'll give you credit, Mr. President, you have just now articulated your political values very clearly.

Now, Back to Our Regularly Scheduled Program

Let's get back to Chapters 5 and 6 in Stephanie Kelton's *The Deficit Myth*.