Book Review

Reviewed by Dirk Ehnts

Email: d.ehnts@berlin.bard.edu

Modern Money Theory – A Primer on Macroeconomics for Sovereign Monetary Systems (2nd edition)
by: L. Randall Wray
Published 2015
by Palgrave Macmillan
4 Crinan St, London, N1 9XW, UK, 306pp
ISBN: 9781137539908 (softcover), $39.00

The second edition of L. Randall Wray's textbook *Modern Money Theory: A Primer on Macroeconomics for Sovereign Monetary Systems* was published in 2015, with slightly more pages and a restructured outline. The book is the standard of modern mone(tar)y theory (MMT) – a Post-Keynesian variety centred on monetary macroeconomics, whereby the economy is explained through the examination of balance sheets, heavily focused on the monetary side.

In the preface to the *General Theory*, Keynes (1936[2010], p.7) wrote, "whilst it is found that money enters into the economic scheme in an essential and peculiar manner, technical monetary detail falls into the background". Wray puts this technical monetary detail into the spotlight, resulting in a very different macroeconomics textbook than the typical mainstream text. Indeed new thinking is needed, since many economists have lost their predictive power in recent years, forecasting hyperinflation and debasement of the currency after quantitative easing (QE); that income growth would accelerate given public sector spending cuts and lower wages, etc. Those seeking advice from Wray's first edition would probably have fared well in recent policy discussions.

Modern Money Theory is structured around institutions and their actions. After starting with the basics of macroeconomic accounting, spending by the issuer of the domestic currency is examined; the book then covers banks and central banks before returning to government spending and taxation. A chapter on exchange rate regimes follows, succeeded by two chapters on policy recommendations for government, a chapter on inflation, and the concluding chapter.

Having earlier used the first four chapters of Wray's first edition (2012) in teaching macroeconomics, I can say that the students' reaction was very positive. Imagining the economy as a web of contracts and transactions provides a very insightful point of view, and moving step-by-step is a sensible approach. Boxes on frequently asked questions provide background and ensure that readers are not alone with their questions. Progress in the beginning is slow, but given that "money enters into the economic scheme in an essential and peculiar manner" that is to be expected. After learning that government spends first and taxes later (taxes drive money), and that banks can create money without any need for savings, the student needs some time to think through the consequences. Wray provides plenty of space and issues to ease this thinking..

The changes in the second edition are modest. There are no major revisions of how balance sheets 'work'. The old chapter eight on the nature of money was deleted, which is probably a good idea: Understanding modern money does not require the reader to understand monetary history, and given that since 1971 money has not been fixed against gold or the dollar, it would probably have overburdened the reader to understand how money used to work. The added chapters on inflation and taxation are useful, even though both topics had been discussed in the first edition.

The second edition remedies weaknesses of the first edition, like adding an appendix on the dynamics of the debt to GDP ratio, and addressing critiques of the 1st edition chapters on taxation and inflation. Nevertheless, the latter chapter does not seem to provide a definitive answer. Baumol's disease and the fact that items are more expensive because they are more useful are offered to explain positive rates of inflation. This seems to be quite a simplification, especially since both issues concern the long-run, whereas the book is otherwise focused on the short-run. Surely in a situation of high aggregate demand some demand-pull inflation is possible? Wray addresses inflation arising from market power – unions and oligopolies – in passing, but then concludes, "some inflation is probably a good thing". While I agree, more space should have been given to labour market institutions. Discussing the role of wage-price spirals in the 1970s, for example, would have added significantly to the chapter. The discussion of the Weimar inflation misses the fact that the Rhineland was occupied by French troops and the German government decided to give money to workers who had been on strike.

The chapter on alternative exchange rate regimes now contains a discussion of monetary history, which I found not very helpful. A bit of economic history does not hurt, but does it help to explain sovereign monetary systems of today? The chapter's main idea is to demonstrate that flexible exchange rates are superior, because they give the most policy discretion. Wray admits that China, even though it runs a pegged exchange rate, has kept all its policy space because it has trillions of US dollars in assets. Additional discussion of other issues connected to flexible exchange rates would have strengthened the book, e.g., countries with trade partners, and pegged currencies, if they devaluate, shift demand to the rest of the world while the inflation rate falls, possibly into negative territory. How should a government react? Also, what happens when there is a need for imported inputs to the industrial sector and the exchange rate depreciates, leading to unwanted high rates of inflation? Some words on industrial policy and trade-offs between domestic and external stability would have helped the reader understand the implications of sovereign monetary systems with flexible exchange rates.

The strongest part of the book is the three longer sections covering the eurozone in chapter 5. Sectoral balances are used to explain what happened and also what needs to happen to resuscitate economic growth. In the book's conclusion, Wray returns to the eurozone crisis boasting that 'MMT got it right'. This seems to be correct. However, claiming "the problem [is] not be the Maastricht Criteria", which limited the public deficit and the public debt to GDP ratio, is something that I find very odd. It is true that the Greek Government ran deficits in excess of the allowed 3%, but without the stability and growth pact (not the Maastricht criteria, which determined who would get into the eurozone in the first place) there would have been no political leverage. Governments would have been able to finance themselves, and the European Central Bank would have had to buy up their sovereign securities on the secondary bond markets in order to ensure that the interest rate in Greece did not diverge from that of other members of the European Monetary Union. The vicious circle of increasing interest rates and higher debts did not have to happen – rather, it was the stability and growth pact that gave the power over national budgets to the European Union's institutions. Also, it seems to be a bit much to claim that the ECB was 'operating under the thumb of the Bundesbank'. The ECB repeatedly rejected the advice of the Bundesbank, and former 'Bundesbanker' Jürgen Stark stepped down as chief economist of the ECB in 2012 after claiming that the ECB overstepped its mandate by moving into fiscal territory.

All in all, the second edition is an improvement and is recommended. Students at all levels, and the general public, can profitably read the book.

In times of weak demand, it is crucial to understand the limitations and flexibilities of a sovereign monetary system in order to fight unemployment, deflation and stagnation. *Modern Money Theory* hence is a theory that is descriptive, and opens up policy space for whatever is deemed feasible. It is also crucial to point out flawed arguments, like the savings paradox, from a balance sheet perspective. It is perhaps the best book for anyone who wants to understand the basic functioning of modern money.

References

Keynes, J.M. (1936[2010]) *The General Theory of Employment, Interest, and Money*, Harcourt, Brace and Co., New York.

Book Review

Reviewed by Andy Denis

Email: a.m.p.denis@city.ac.uk

Contending Perspectives in Economics. A Guide to Contemporary Schools of Thought
by: John T. Harvey
Published 2015
by Edward Elgar
15 Lansdown Road, Cheltenham, Glos GL50 2JA, UK, 158pp
ISBN: 9781784719487 (paperback)
ISBN: 9780857932037 (hardback)

John T. Harvey's *Contending Perspectives in Economics. A Guide to Contemporary Schools of Thought* is a contribution to the movement towards a more pluralistic curriculum in the study of economics. The context is made explicit throughout the book. Harvey mentions his six years as director of the International Confederation of Associations for Pluralism in Economics, and he cites the founding of this *Journal* in 2009 in evidence of the steps that that movement is taking.

Apart from the introduction and conclusion, *Contending Perspectives* consists of eight chapters – one on 'Economics as a scientific discipline', and one each on neoclassical, Marxian, Austrian, post-Keynesian, institutionalist, new institutionalist, and feminist economics. Each chapter addressing a specific school of thought has a similar structure:

1 a description of the school
2 a discussion of the methods of analysis adopted by it
3 a brief statement of that school's view, human nature and justice
4 a discussion of the standards of behaviour of its members
5 the contemporary activities of the school – the conferences they hold, the journals the publish in, and so on
6 criticisms of the school
7 how its members might answer such criticisms
8 some further reading.

Each of these chapters has been fashioned with the aid of feedback from members of that school. The aim is to ensure that the discussion of each school is fair and recognisable to adherents of that school. This is perhaps more difficult that it sounds, since most of us implicitly characterise those with whom we disagree by the errors we think they commit.

The book is extremely well-written and will certainly be appreciated by those students who consult it – everything Harvey discusses is made abundantly clear, the author's passion and sense of humour shine through, and he sustains the reader's interest. Harvey's intention – stated in the publisher's blurb on the back cover – is to provide a text that can be used in undergraduate (UG) degree programs in economics in order to break down the monist manner in which the discipline is normally presented to students. This is eminently supportable. Most readers of this *Journal* will need little persuasion that Harvey is absolutely right to condemn the monism of the discipline, with the mainstream, neoclassical economics, constituting itself the orthodoxy and all else, by exclusion, the heterodoxy.

The results, however, are mixed. For courses such as the book is designed to serve as text, it is really excellent. But – in my own country at least – the scope for developing and offering such courses, is almost nil. The problem is this. The book is both short, and, as you will understand from the list of contents given above, quite broad. The consequence is that it is quite general and, consequently, lacking in depth. The assumption is that the reader knows nothing about economics, so the author is limited in what he can say. For any UG course in economics, even in the first year, we should be able to assume that students know *something* about economics, and base our discussion of the various paradigms available in that existing knowledge, or present it as counterpoint: what the student thought was knowledge turns out in fact not to be so. In terms of its level, this book could be suggested as optional additional reading on an AS or A level or first year UG principles module, in the same way that we routinely advise students also to read the *Financial Times* and *The Economist*. But it would hardly fit with the curriculum: sixth form teachers and first year UG lecturers are almost universally not at liberty to design their own syllabus. It would be far more relevant to a second- or third-year module in alternative paradigms within the discipline, but then it would very much lack the depth required at that level of study.

It is possible that the book would work better in educational systems where four-year bachelor's degrees are the norm, such as Scotland and the USA. It is possible lecturers could design their own course, incorporating a text such as this, in such systems, where first year study is roughly equivalent in level to English AS and A levels, in subjects which students have not, or not yet, selected as their 'major', but in which lecturers are not required to follow any particular curriculum.

A second significant problem with the book is its treatment of the 'Neoclassical School' as a school of thought on a par with the others, such as Marxian and Austrian thought. This is not the case – in my own view at least. Firstly, it is perhaps more appropriate to view neoclassical thought as, not a school so much as a family of schools of thought. For example, just within macroeconomics, neoclassical (or 'old') Keynesianism, monetarism, new classical economics, real business cycles, new Keynesianism, and new neoclassical economics, are all schools of thought within the neoclassical paradigm that have emerged in mutual debate and controversy. Moreover, as the mainstream, neoclassicism is the language within which economic debate takes place, and it is therefore essential for scholars working in every school of thought to have a thorough grounding in neoclassical thought in order to participate in that debate. Hence, the weight given to the neoclassical school in *Contending Perspectives* – 20 pages out of 150 – is, in my view, simply inadequate.

Consequences of the constraint of brevity that the author has imposed upon himself include:

- A discussion of neoclassical thought which does not mention the uneasy relationship between Marshallian partial equilibrium and Walrasian general equilibrium approaches which constitutes its history.
- A failure to discuss the significance of econometrics and mathematical economics – which are after all what neoclassical economics consists of today; and, connected with this, an account of neoclassical economics without benefit of diagrams or equations. There is some discussion of a loanable funds approach using the simplest, stripped-down equations of national income and output, showing savings and investment as functions of the rate of interest, and there is a simple production possibility frontier and a demand diagram. But there are no supply and demand equations, and no discussion or graphical illustration of these relationships.
- The absence of any discussion of pluralism *within* the mainstream – take the case of behavioural economics, and behavioural finance, for example: behaviouralism contradicts the neoclassical notion of the rational economic agent, but it is still acceptable to the mainstream, and not excluded as heterodox schools are. This is something worth exploring;

Given these omissions, it is difficult to know what the student is expected to know about neoclassical economics, and how that student is to make sense of the other schools, which can only really be understood via their points of contact and conflict with the mainstream. It would be far better to teach the student neoclassical economics in one module and then alternative paradigms in another module immediately afterwards, each school being taught by reference to what it shares with the mainstream, and where it diverges from it. Both heterodox and orthodox schools can then be treated at the required level of depth and sophistication.

The accounts given of the heterodox schools of thought are likewise constrained by space and by the assumptions made about the previous knowledge of the reader. The result again is a certain lack of depth. In the chapter on Marxian economics, we have no discussion of the two circuits, C-M-C′ and M-C-M′, which are fundamental to understanding Marx's economics. I winced when I read Harvey's psychological interpretation of alienation. Harvey rightly notes that there is too much diversity to permit the identification of a single modern Marxist perspective, and that the appropriate strategy is to revert to Marx himself. But the notion that, for Marx, 'alienation' was a matter of a lack of job satisfaction is very wrong. Alienation is a demanding topic in studies of Marx, and is not essential for understanding Marxian economics. Getting it right would be a lengthy task, and conspicuously above the level of the rest of the book; better to leave it out.

Harvey discusses the seven schools of thought listed above. This is a choice, and I felt that there should have been some discussion of the basis on which that choice was made – what constitutes a school of thought and what motivated the selection he makes. We have a chapter on new institutionalism, although a strong case can be made that it is a member of the neoclassical family of schools of thought. And what about the Virginia School of political economy and Ordoliberalism: can they really be considered less distinct from neoclassical economics, or less significant than new institutionalism? Many more schools exist within the discipline but are not mentioned here, from critical realism and associative economics, to Islamic and Buddhist economics. It is not possible to discuss everything, and Harvey's choice is largely sensible, but we do need to know that this is a selection from a broader population, and that the borders between the various approaches are, not given once and for all, but both porous and contestable.