



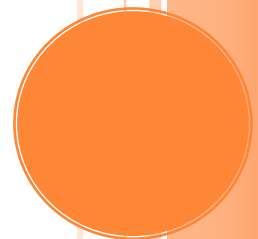
MACROECONOMIC  
Analysis & Policy Studies

## **Rethinking the Taboo of Public Debt from an MMT Perspective**

Student Research Internship Report

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July 2021



# Rethinking the Taboo of Public Debt from an MMT Perspective

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Recently, with the Covid-19 outbreak, the governments are starting to introduce new schemes and plans for economic revival; and these plans cost trillions, ultimately increasing the public debt. Should we be worried about the debt growing in numbers? Or are these plans essential in a time of crisis like this. Public debt is often misinterpreted without knowing how the money system actually works in the modern economy. With the continuous misconceptions portrayed by the mainstream media, politicians & other orthodox economists --it is important to understand the consequences of public debt, government's power in a sovereign nation, its constraints and RETHINK the ongoing narrative. Here we will analyze these under the framework of heterodox school of thought "Modern Monetary Theory." MMT researchers have introduced studies regarding how public debt is repaid, what factors to consider, role of taxes, etc. This paper evaluates my understanding of the workings of Public Debt (PD) in an economy (focusing on the USA) and is presented in a simpler way for general insight.

Public Debt or national debt is the amount of debt owed by a government to the lenders. It is the accumulation of fiscal deficits (government spending exceeding government revenue/income). Public/federal debt is the financial liability of the government. There's an ongoing debate around the term 'public debt' regarding its involvement in the economy or the taxpayers in general. To put it bluntly, orthodox school of thought frames public debt as 'bad' or something that should be avoided and MMT economists argue against it. Looking at it this way, in times of a financial crisis or the case of a global pandemic, government spending must exceed its revenue to spend ON the society. In order to deal with an unforeseen crisis, the government may have to incur costs or spend more to save the economy from a more serious issue like Recession!

## Public Debt Trend

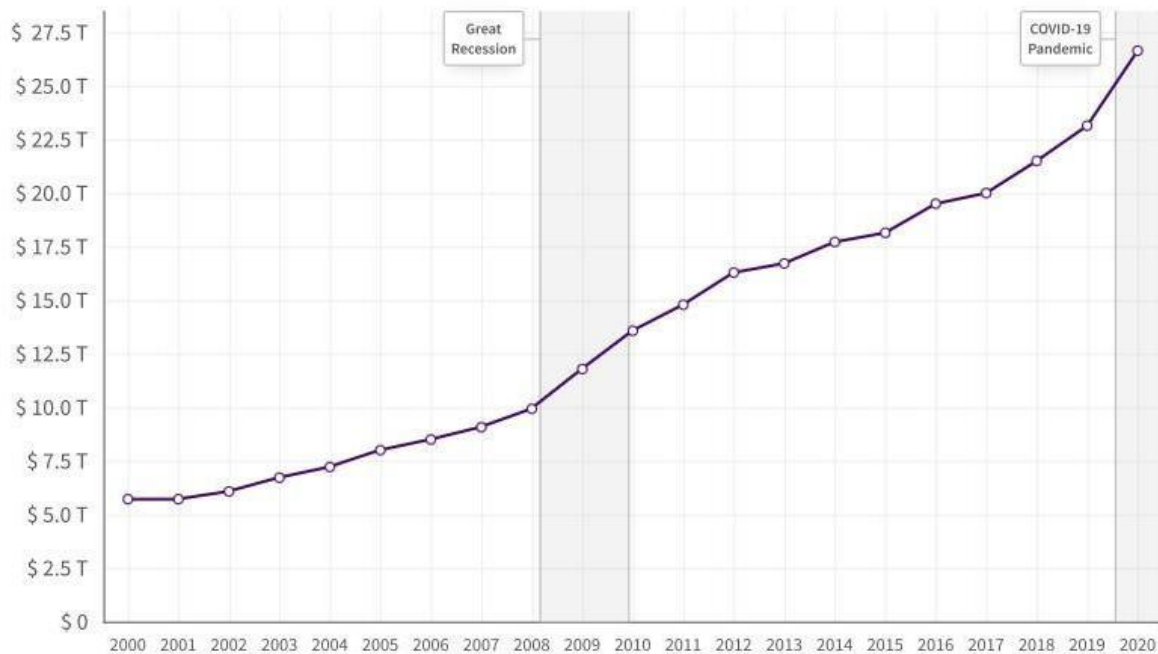
"USA is one the countries with the most amount of public debt which is estimated at around 28.53 trillion U.S dollars, over two trillion more than a year earlier, when it was around 26.48 trillion U.S dollars." (Statista.com). The following public debt graph shows the trend how the accumulation of debt has been increasing over the years:

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This article is written as part of my internship at Foundation to Aid Industrial Recovery- Macroeconomic Analysis & Policy Studies.

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Source: [datalab.usaspending.gov](https://datalab.usaspending.gov)

Biden's Covid relief plan for \$1.9 trillion is being criticized that it would lead to huge public debt, however if measures/spending are not taken by the government the effect of the pandemic will hit even more than anticipated. What MMT states is that this \$1.9 trillion is essential to inject in the economy to alleviate any recession/depression risk. And this injection is done by the government by printing excess money.

### Essence of Modern Money

MMT is a heterodox macroeconomic theory that emphasizes that a government issuing its own fiat currency can never run out of it. The central authority holds the supreme monopoly of being the issuer of their country's currency. They are not financially constrained like households and businesses are. A country where the government owes to the lenders in the country's own currency, in that case it can repay the public debt by issuing new debt. - that is the central idea of modern money theory regarding repayment of debt.

The Government does not depend on the tax collected; taxes are not a source of revenue for the government authorities and they especially do not fund government spending. This leads us to the question, "Why are we taxed then?"

## Role of Taxes

Taxes are a mandatory payment made by the citizens of a country to the government. The citizens of the United States of America have to pay their taxes in dollars, just like Indian citizens pay it in rupees, Japanese citizens in their Yen and so on.

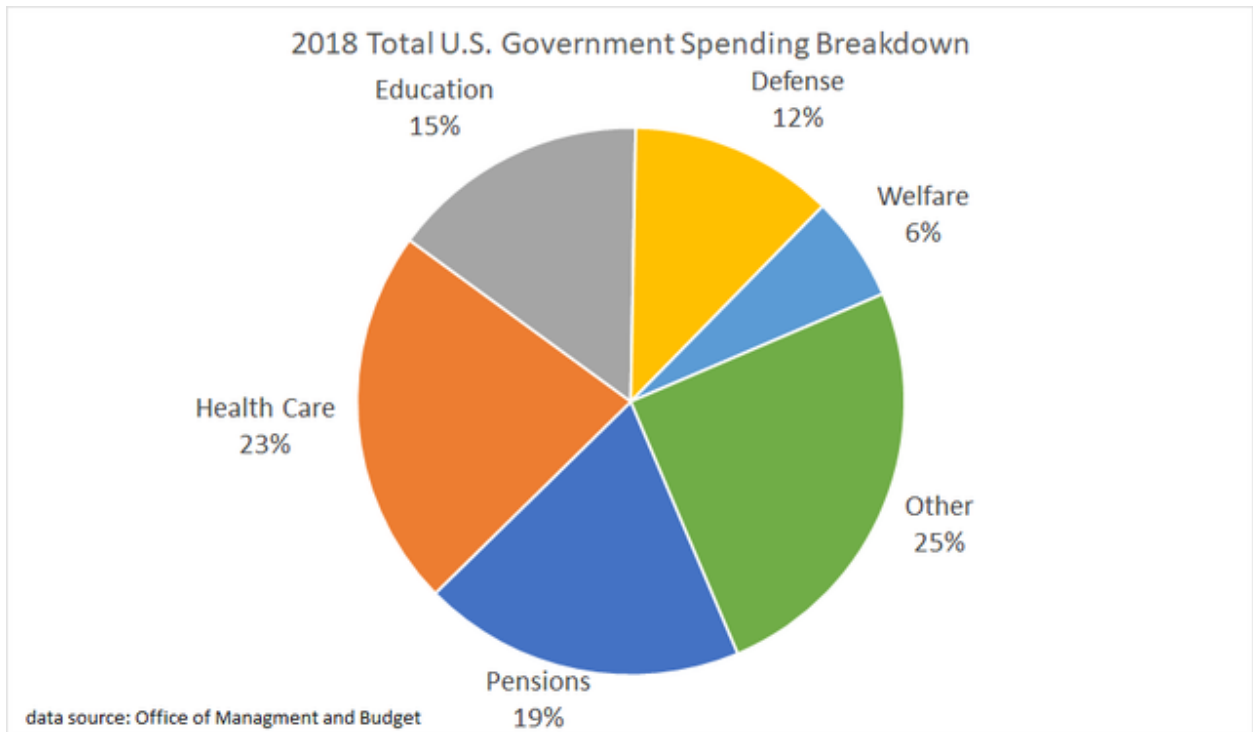
The national debt clock ticking (increasing every second) in Manhattan, New York City shows the amount that each individual has to contribute in repaying the USA's national debt. This wrong interpretation of the public debt clock often becomes the cause of worry among the taxpayers. The clock indicates that the taxpayers and their future generations will be taxed more and they would have to bear the burden of debt repayment. This is called Ricardian equivalence and this theory is what is normalized by the mainstreamers. MMT economists reject this theory and suggest that taxes are levied on us mainly to keep up the demand for cash and as a means of controlling inflation or draining out of cash. And presents a more straightforward way of repaying internal debt in a nation.

## Important Factors to Consider in the Repayment of Public Debt

**Monetizing Debt:** Here we bring back the central idea of modern money. To deal with debt, money is created out of thin air. It is also called helicopter money. This is a practice of the government borrowing money from the central bank by selling them bonds and then spending it on the public. It is a way to finance the government's spending needs. However, merely labelling it as a 'printing money' is wrong as we need to look at it from a broader perspective:

**GDP Growth:** The most important aspect is that as long as the GDP of the country grows along with the public debt, how large is that PD amount doesn't matter. The ability of the country to sustain that debt is what's important. As the debt trend on the above figure showed the increase in debt over the years, along those years our GDP grew too and hence accumulation of PD is not an issue here.

We should also consider the liability of the government (i.e. the debt) as an asset of the households and businesses (non-bank private sector), as monetizing the debt leads to the **addition of reserves** of the NBPS. Government's debt is nothing but the public's savings. Moreover, government spending on public enterprises by building schools and hospitals, constructing roads and other necessary sectors leads to social welfare. According to a source -The US Government spends most on Social Security (\$1,050 billion), Medicare (\$2,736) and other mandatory spending. The figure below illustrates this.



[https://en.m.wikipedia.org/wiki/Government\\_spending\\_in\\_the\\_United\\_States#:~:text=As%20Figure%20A%20suggests%2C%20Social,Veterans%20Benefits%2C%20and%20other%20programs](https://en.m.wikipedia.org/wiki/Government_spending_in_the_United_States#:~:text=As%20Figure%20A%20suggests%2C%20Social,Veterans%20Benefits%2C%20and%20other%20programs)

These are some unavoidable spending the state has to incur for the welfare, security and growth of the economy and in doing so it does spend more than it is taxed, which will lead to public debt and that is okay. The government in a sovereign nation having the power to settle this debt by creating money should be able to do so.

### Conclusion

To conclude, we can say that debts and deficits don't really matter and in fact restricts the economy's growth. A country's central government with currency sovereignty can afford any spending that is entitled in its own currency.