

**The monetary situation in the
Eurozone and implications on the
international monetary system**

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**Some theoretical issues
raised by this situation**

- I

The inflation risk and internal devaluation

- **1. The monetary nature of inflation and the deflation risk.**
- **a. Is inflation purely a monetary phenomenon?**
 - The “Hume-Ricardo-Fisher” legacy. How do we arrive to the Fisher’s equation
 $MV = PQ$ (static)
 - $M = \text{CPI} + \text{GDP}$ (dynamic)
 - The modern concept of monetary inflation.
 - Rational expectations en R. Lucas.
 - The difference between “Hyper-inflation” and inflation.
- **b. The “Structural inflation” concept.**
 - The Cantillon-Hayek legacy. A microeconomic approach of inflation.
 - The “structural” school (Myrdal, Timbergen, Lance Taylor).
 - Imperfect information and applied psychology. How “mainstream” economists are re-discovering “structural” inflation.

– **c. The deflation risk.**

- » Keynes analysis and the 1930' s. Why deflation is far worse than inflation?
- » Minsky and the Debt-deflation mechanism.
- » The differential prices flexibility (Akerloff)

- **2 Devaluation, internal devaluation and the fiscal multiplier: what precisely is at stake?**
 - **a. What is an “internal devaluation”**
 - » Devaluation and deflation.
 - » The 1930’ horror story.
 - » Differences in adjustment speed.
 - **b. A comparison of both processes.**
 - » Why a normal devaluation is better than an “internal devaluation”.
 - » The cost of an internal devaluation.
 - **c. The time-lag factor.**
 - » What is the reaction time for a devaluation.
 - » What is the reaction time for an “internal devaluation”.
 - » Spill over effects.

- **d. Mistakes and illusion about the fiscal multiplier.**
 - » What is the “fiscal multiplier”.
 - » The IMF mistake and its correction.
 - » The difference of the current situation.
 - » What is the impact of the fiscal multiplier now
- **e. The debt ratio and growth comparison.**
 - » Is it a good indicator?
 - » The « Controversy » of 2013.
 - » What assumptions are.
 - » Is there a « good » level of government debt?

- II

**A lack of theoretical tools or
an ideological issue?**

- **1 The failure of DSGE model.**
 - **a. What DSGE models are.**
 - » The origins of the DSGE model.
 - » R. Lucas and his legacy.
 - » A tool commonly used.
 - **b. Are DSGE models useless?**
 - » What are the main failures of DSGE models.
 - » Why these failures are important now.
 - » Goodhart and the issue of using “non-realist” models.
 - **c. Theoretical problems raised by DSGE models.**
 - » Back to the drawing board.
 - » A mistaken view of what are now microeconomics.
 - » Post-Keynesians and the controversy.
 - » What is to be the “next fashion”.

- **2. What theoretical tools are available for European leaders?**
 - **a. Why the EU still sticks to discredited models?**
 - » The “Troika” and the ECB/EU vs IMF feud.
 - » The OECD and the IMF.
 - » The position of the ECB
 - » What’s next?
 - **b. How policies are estimated?**
 - » The use and misuse of statistics.
 - » When policy use economics.
 - » A lack of objective estimation tools.
 - » Is the issue one of a lack of theoretical tools or one of ideological bias?

- **To be read**

- **On deflation**

- Minsky H.P., “The Essential Characteristics of Post-Keynesian Economics”, The Jerome Levy Institute of Economics, Bard College, 1993. (pdf)
 - Eggertsson Gauti B., and Paul Krugman, DEBT, DELEVERAGING, AND THE LIQUIDITY TRAP: A FISHER-MINSKY-KOO APPROACH, The Quarterly Journal of Economics, 2012, n-6. (pdf)

- **On fiscal multiplier**

- Blanchard O., et D. Leigh, *Growth Forecast Errors and Fiscal Multipliers*, IMF Working paper, WP 13/1, January 2013, (pdf).
 - Baum A., Marcos Poplawski-Ribeiro, and Anke Weber, *Fiscal Multipliers and the State of the Economy*, IMF Working Paper, WP 12/286, December 2012. (pdf)

- **On DSGE models:**
- Galbraith, J.K., “The collapse of Monetarism and the Irrelevance of the New Monetary Consensus”, *Public Policy Note 2008/1*, Annadale-on-Hudson, N.Y., The Levy Economics Institute of Bard College, 2008.
- Goodhart, C.A.E., “The Continuing Muddles of Monetary Theory: A Steadfast Refusal to Face facts”, paper presented to the 12 th Conference of the Research Network *Macroeconomics and Macroeconomic Policy* , Berlin, Germany, October 31 st – November 1 st , 2008.