Funding the Future

MMT and exchange rates

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I was asked this question yesterday:

Can you please say a word about the effect MMT might have on the exchange rate – a potential "currency crisis" is a convenient bogeyman for opponents to raise.

This was my reply:

This is a common concern, often raised precisely because it sounds alarming and yet remains vague.

MMT does not deny that exchange rates matter. What it challenges is the idea that a government using its monetary and fiscal capacity responsibly is somehow inviting a currency crisis.

The exchange rate is influenced by many things: relative inflation, interest-rate differentials, trade balances, geopolitical risk, speculation, and confidence in institutions. Fiscal policy is only one part of that picture. There is no automatic link between government spending and currency collapse.

A genuine currency crisis usually arises when a country:

* Borrows heavily in a foreign currency it cannot issue.
* Runs persistent trade deficits without domestic productive capacity, or
* Pegs its exchange rate and then loses reserves trying to defend it.

MMT explicitly warns against all three.

In fact, MMT-style policy can strengthen currency resilience if spending is directed toward expanding domestic capacity: energy security, housing, food supply, transport, skills and productivity, as it suggests to be appropriate policy measures. That action reduces import dependence, which is one of the biggest sources of exchange-rate vulnerability.

What opponents often imply is that markets will “punish” governments for abandoning austerity. But markets react to inflation risk and external balance, not to whether a government understands its own monetary system. Countries like Japan show that high public debt does not automatically produce currency collapse when institutions are credible and policy is coherent.

So the real safeguard is not pretending we are financially constrained. It is:

* Spending well.
* Taxing appropriately.
* Managing inflation, and
* Investing in the real economy.

A currency crisis is not triggered by honesty about money; it is triggered by ignoring real resources and external constraints. MMT is unusual in making this clear. It does not create risk. It is explicit bout how to manage it.

Comments