

## Macro Roundup Article

**Headline:** [Fiscal Narratives for US Inflation](#)

**Article Link:** <https://www.grumpy-economist.com/p/fiscal-narratives-for-us-inflation>

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**Tweet:** [@JohnHCochrane revisits 2008-2020 and argues the Fiscal theory of the price level has been more consistent with inflation's behavior than Keynesians' warnings about deflation spirals or monetarist's predictions of hyperinflation.](#)

**Summary:** In 2008, with a huge recession, inflation went down, hitting -2%. Why did inflation decline? Once started, why didn't it keep going down? Many commenters, armed with standard models, predicted a "deflation spiral" at the zero bound. Deflation means high real interest rates, which causes more deflation. It didn't happen. Fiscal theory explains. Why was there deflation? Why, especially given the large deficits, which superficially look like they ought to cause inflation? In the recession, though deficits rose, the real interest rate fell. Real interest costs on the debt fell. This "discount rate" effect overwhelmed the deficits to make government debt more valuable. A decade of 2% lower real interest costs has, with 100% debt/GDP, exactly the same disinflationary force as a decade of 2% higher surplus to GDP ratio. Throughout the zero bound era, Keynesian economists warned of the incipient deflation spiral, Monetarists warned of hyperinflation from massive quantitative easing. None of these predictions happened. Fiscal theory is the only theory transparently consistent with steady quiet inflation at a pegged interest rate, including the zero bound, and in which immense open market operations have no effect on inflation. Related: Fiscal Influences on Inflation in OECD Countries, 2020-2022 and Fiscal Arithmetic and the Global Inflation Outlook and What We've Learned About Inflation

**Primary Topic:** Inflation

**Topics:** Database, GDP, Inflation, Monetary Policy, Op-Ed/Blog Post

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