What is Helicopter Money?

"Helicopter Money" is in the news, and like many colloquial economic terms, those who use it rarely take the time to precisely define what they mean. Consequently, many popular discussions of helicopter money (HM) are difficult to follow.

Recent exceptions to that general statement are the exemplary HM discussions found in Ben Bernanke (2016)[1], Adair Turner (2015)[2] and Willem Buiter (2014)[3]. All three emphasize that HM involves a *fiscal expansion financed by a permanent increase in the monetary base*.

In this note I explain where I agree and disagree with the aforementioned authors regarding the essential ingredients of successful helicopter drops (HD)[4]. In short, I agree that they must comprise a permanent fiscal expansion but disagree that this expansion need be financed by a permanent increase in the monetary base. This point of disagreement is important. Much of the controversy surrounding HM is the potential impact on the independence of the monetary authority. If it can be shown that HD are efficacious without the monetary authority being involved…without the "M" so to speak, then their employment, when necessary, might become more widespread than otherwise would be the case.

This note serves as background for three notes that will be posted in succession that develop my position. The first of those notes discusses HM during the US Civil War—when there was no US central bank—and during the Great Depression when Congress gave the Treasury wide latitude to issue "greenbacks" directly to finance debt redemption and finance expenditures. The second note explains how permanent fiscal expansions may be financed without increasing the monetary base and argues that the effective economic impact of those HD are equivalent to HM. The third and last note simply discusses "helicopter bonds" as perhaps the least controversial of all the methods to finance a HD.

Of the consensus authors above, Bernanke's is the most concise treatment and I quote from him below:

"…a 'helicopter drop' of money is an expansionary *fiscal* policy—an increase in public spending or a tax cut—financed by a *permanent* increase in the *money stock*". [Emphasis Added}. He then goes on to substitute the term "Money-Financed Fiscal Program, or MFFP" for "helicopter money".

"…the Fed must pledge that it will not reverse the effects of the MFFP on the money supply…"

"A key presumption of MFFPs is that the financing of fiscal programs through money creation implies lower future tax burdens than financing through debt issuance".

"…the fiscal package is being financed by money creation rather than by new debt—a distinction that, again, the public must appreciate if the MFFP is to be fully effective".

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[1] *What tools does the Fed have left? Part 3: Helicopter Money*, Brookings Institution post April 2016.
[2] *The Case for Monetary Finance—An Essentially Political Issue*, paper presented at the 16th Jacques Polak Annual Research Conference, IMF, Washington, D.C., November 4-5.
[3] *The Simple Analytics of Helicopter Money: Why it Works—Always*. Economics Discussion Papers, No 2014-24, Kiel Institute for the World Economy.
[4] HD is broader than HM in that HD includes HM as well as fiscal expansions financed without money.

Bernanke adds that, in addition to the impact of the fiscal component of the MFFP, the monetary financing component would have an impact owing to "…a temporary increase in expected inflation, the result of the increase in the money supply…[and]…the fact that, unlike debt-financed fiscal programs, a money-financed program does not increase future tax burdens."

Although Bernanke does not explicitly define "money" in the quotations above, he is talking about the bank reserve component of the monetary base. In order to be precise, in what follows I will refer to "money financed" fiscal policy as "bank reserve financed" fiscal policy. Similarly, and true to the spirit of the original Friedman allegory, I will discuss expansionary fiscal policy as if it were an increase in transfer payments. A "transfer" is a provision of cash or commodities to a household without requiring the recipient to provide anything in return. It is essentially a gift from the state to the household.

Bernanke, Buiter, and Turner all stress that HM is fiscal policy. With that I am in complete agreement.

Essentially, a HD is an intra-societal transfer of wealth from a nebulous collective intergenerational structure of ownership and disposition to individual currently living households who are free to dispose of that wealth as they choose.

It almost goes without saying that in order for a HD to matter it is necessary that it be "permanent". It would be the height of folly for the US government to mail $1,000 in US notes to every household in America and include within the envelope a tax bill for an equivalent amount immediately due. Nor would it make the least sense to provide a bonus to every retired person receiving social security and immediately reduce the conventional social security payment by a corresponding amount. Indeed, the most efficacious use of HD is associated with a credible government commitment *never* to raise taxes (nor cut expenditures) to compensate for the wealth transfer.

Where I disagree with Bernanke, Buiter, and Turner is that I do not believe the permanent fiscal expansion must be financed with a permanent increase in bank reserves. In other words, HD may be HM but need not be. Informally, in the posts that follow I discuss various HD that are not financed with bank reserves including (i) transfers of real assets, i.e. transfers in-kind, (ii) provision of public services at reduced prices and (iii) financing the wealth transfer through the use of bonds. I also discuss the possibility of the government directly issuing money. Although this obviously is HM, it does not directly impact the authority of the monetary authority, that is, in such a case the monetary authority would be free to absorb the increase in bank reserves or paper money in circulation by selling bonds.

The most intuitive reason why I believe it is just as effective to finance a HD with bonds as with bank reserves (actually more so) has already been discussed in an earlier post called *Printed Money*[5]. Reiterating that argument—bonds are simply promises to pay money in the future, and in the case of short term bonds—treasury bills, they are virtually the same, with one important exception. Bank reserves can only be held by banks and thus can only be traded among banks. Beyond a rather low quantity necessary to effect payments through the nation's large value transfer system (in the US, "Fedwire"), reserves are useless to banks. Treasury bills, notes and bonds, however, may be traded

[5] http://**bit.ly**/1sh9gMm

among banks and nonbanks. Consequently, they are more utilitarian financial instruments than bank reserves which can be used only to settle interbank transactions. In financing the consolidated sovereign balance sheet, it is more efficient, and less costly to the sovereign, to rely on fungible instruments such as bills, notes, and bonds, than on excess bank reserves or paper money.

As I discussed in *Printed Money*, it seems that many persons believe that when a sovereign prints money it represents a permanent increase in the liabilities of the state that will never be reversed by increased taxes while when a sovereign prints bonds—which are nothing more than promises to pay printed money in the future—they always and everywhere intend to "redeem" those bonds with printed money obtained through *tax increases*. Although that characterization of the typical sovereign might have been valid in the years prior to the Second World War, it seems archaic, in its extreme form, today. Sovereign debt is today accepted without second thought as a permanent feature of the financial landscape. In contrast, the days of the "monetary base" appear numbered. Bank reserves in the US had fallen close to zero by 2006 and technological advances are beginning to engender—for the first time in history—declines in the nominal amount of paper money outstanding in some countries.

The key ingredient of helicopter drops is that the wealth transfer be permanent—neither reversed by future increases in taxes nor cuts in expenditure. The technical modalities of the transfer are not so important. In particular, it is not necessary, nor likely optimal, that they be financed by permanent increases in bank reserves. This latter point is the subject of the companion notes to follow.

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Companion Notes:

Helicopter Money without Helicopters and without Central Banks http://bit.ly/2b4FWr0

Helicopter Drops without Money http://bit.ly/2b8Wfaw

Helicopter Bonds http://bit.ly/2aKSMcF