

[Matt Yglesias](#)

Nov 4th, 2010 at 2:28 pm

[If QE2 Inspires Foreign Investment That, Too, Will Help Boost US GDP](#)



(cc photo by
LateNightTaskForce)

One of the reasons you can tell that though QE2 may be too modest to do much good, it's still a step in the right direction, is that its strongest critics have critiques that just don't add up. The Cato Institute's Mark Calabria, for example, says we [should be worried that QE2 will succeed in pushing the price level up](#) closer to its trend level. But there's no reason to worry about that—doing so would be a good thing. Similarly, Pete Davis [lays out a theory](#) whereby higher inflation expectations harm the economy:

Will it work? Yes and No. It should raise short-run growth, but only if this money is put to use by American businesses and consumers. **If they fear further weak growth and long-term inflation because the Fed may be unable to unwind these massive liquidity injections fast enough, it could**

easily end up being saved and invested overseas. So a lot depends upon market and consumer perceptions of whether the Fed picked a large enough liquidity injection to raise growth, but a small enough one to avoid fears of future inflation. The Japanese experience with quantitative easing a decade ago was that it didn't work very well.

I completely disagree with this. The Japanese experience with quantitative easing was that it didn't work very well *at raising inflation expectations*. But higher inflation expectations boost growth in a severely depressed economy (note that the "in a severely depressed economy" part is an important qualifier). Higher inflation expectations are likely to inspire cash-hoarding firms to unload their money and invest it in something. There are two choices here. One is that they might invest it in expanding their real economy activities here in the USA. That would boost growth. The other, as noted by Davis, is that they might invest it abroad. That would decrease the value of the dollar boosting import-competing and exporting US-based firms. That would boost growth.

As I [mentioned yesterday on BHTV](#) it's important to be clear about what "more inflation" would mean in this context. Relative to where we are today, the inflation rate of the Clinton and George W Bush administrations would be "more inflation." Relative to where we are today, the inflation rate of the "Morning in America" recovery of 1983-90 would be a *lot* more inflation. Saying "Yglesias wants inflation" sounds bad. Saying "Yglesias wants to return to Reagan-era levels of inflation" sounds much more reasonable.

3

Like

Showing 17 comments

Sort by [Subscribe by email](#) [Subscribe by RSS](#)