

# Contents

LIST OF FIGURES	xi
LIST OF TABLES	xiii
ACKNOWLEDGEMENTS	xv
PREFACE TO THE THIRD EDITION	xvii
PREFACE TO THE SECOND EDITION	xix
PREFACE TO THE FIRST EDITION	xxi
1. RATIONAL EXPECTATIONS AND THE RECONSTRUCTION OF MACROECONOMICS	1
Behavior Changes with the Rules of the Game	1
The Investment Decision — Are Government Deficits Inflationary?	
General Implications of the Examples	10
New Econometric Methods	11
Historical and Cross-Country Analysis	13
Implications for Policymakers	15
2. REAGANOMICS AND CREDIBILITY	17
Dynamic Games	19
An Economy as a Dynamic Game	21
Are Government Deficits Inflationary?	26
Reaganomics and Credibility	33
Conclusion	36
3. THE ENDS OF FOUR BIG INFLATIONS	38
Introduction	38
The Gold Standard	42
Austria	47

Hungary	53
Poland	58
Germany	60
Czechoslovakia	64
Conclusion	66
Appendix	67
4. STOPPING MODERATE INFLATIONS: THE METHODS OF POINCARÉ AND THATCHER	111
Introduction	111
The "Poincaré Miracle"	116
The British Experience	123
Mrs. Thatcher's Plan	124
The Outcome of the Plan So Far	129
Overshooting the £M3 Target	130
The Government Deficit	132
North Sea Oil and the Pound Sterling	136
Conclusion	142
Second Thoughts	143
Poincaré and Moreau	
Methods of Thatcher and Reagan	145
Where to Play Chicken	146
5. SOME UNPLEASANT MONETARIST ARITHMETIC	162
<i>with Neil Wallace</i>	
Introduction	162
A Simple Monetarist Model	166
The Cagan-Bresciani-Turrone Effect	171
Conclusions and Qualifications	173
Appendix 1	177
Appendix 2	180
Appendix 3 by Danny Quah	193
6. INTERPRETING THE REAGAN DEFICITS	197
Government Budget Balance	197
Barro Tax Smoothing	199
Wallace's Game of Chicken	204
Conclusion	207

Appendix	208
Hall's Model — Barro's Model	
7. SPECULATIONS ABOUT THE SPECULATION AGAINST THE HONG KONG DOLLAR	211
<i>with David T. Beers and Neil Wallace</i>	
A Look at Hong Kong's Monetary System	212
The Official Float Policy	214
An Indeterminate Exchange Rate?	215
A Timely Depreciation	218
Hong Kong's Other Options	222
Epilogue	223
8. SIX ESSAYS IN PERSUASION	228
Back to Basics on Budgets	228
Confrontations over Deficits	231
An Open Letter to the Brazilian Finance Minister	233
Letter to Another Brazilian Finance Minister	237
The Economics Are Simple — Credibility — A Delicate Institutional Issue — Advice	
Reasonable Doubt about the Real Plan	241
An American History Lesson for Europe	245
9. MACROECONOMIC FEATURES OF THE FRENCH REVO- LUTION	248
<i>with François R. Velde</i>	
Introduction	248
Chronology of Events — Macroeconomic Theories Coloring Our Observations	
Before the Revolution	251
Even Absolute Monarchies Have Budget Constraints — The British Experience — Across the Channel — French Fiscal Backwardness or Optimality? — Snapshot of the Old Regime Laws — Offices — Taxes — Apology for the Old Regime — Fiscal Pressures to Reform — Sentiment for Copying Britain — A Temptation Resisted — Sustainability or Bad Choices? — The Last Fiscal Crisis of the Old Regime	

The Search for a New Order	267
Annus Mirabilis (1789) — Some Adverse and Persistent Revenue Shocks — Designing a New Tax System — Birth of a Currency	
Rise and Fall of the <i>Assignat</i>	274
A Real-Bills Regime (1790–92) — War — Terror (1793–94) — Legal Restrictions — Hyperinflation (1795–96) — The Government's Response — Default	
The Legacy	292
Unintended Consequences for England through Specie Flows	
Appendix: The Auction Mechanism	294
10. UNITED STATES THEN, EUROPE NOW	297
Introduction	297
The Math	300
Need for More Economic Theory? — A Humbling Message? — Modeling Reforms	
The United States	307
Victorious but in Default — Trade Policies — Crisis and a Second Revolution	
Restructuring Fiscal Institutions	310
The Order of Fiscal and Monetary Reorganizations — Fiscal Policy — Discrimination and Liquidity — Federal Bailout of States — Why Pay? — Monetary Arrangements — A National Bank? — A Mint — Outcomes	
Following Through?	319
Federal and State Paper Monies? — What Kind of Currency Union?	
What Kind of Fiscal Union?	323
Another Federal Bailout of the States?	
Lessons for Now?	328
Appendix: Outcomes in Graphs	331
Data Sources	
REFERENCES	339
AUTHOR INDEX	357
SUBJECT INDEX	361