Personal Reflections on Robert Mundell

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When Robert A. Mundell passed away on April 4, 2021 in Siena, Italy, economics lost one of its all-time giants. Having been a colleague of Bob's at Columbia, I was invited to speak at a memorial service taking place at this moment in St. Paul's Chapel on the Morningside Heights campus. Given this conference, I obviously could not be in New York this afternoon. But it felt wrong not somehow to acknowledge in public Bob's immense contributions, to our craft and to me personally, directly and indirectly. Besides, as Yogi Berra said, and I'm sure Bob would agree, "If you don't go to people's funerals, they won't come to yours."

Upon reflection, it seemed appropriate to say something at this conference – to recall Mundell's brief but important tenure in the Research Department of the Fund and the centrality of his modeling to much of what we international economists do. Both are memorialized in the name of the Mundell-Fleming lecture. The organizers of this conference and of the Columbia event were enthusiastic, and they went beyond my request in arranging for these recollections to be livestreamed to St. Paul's, where many old friends of mine are in attendance. For that, I am very grateful.

I first encountered Mundell's work at MIT in the wonderful international finance course taught by Bob's student, Rudi Dornbusch, and known to MIT students as 14.582. For many young economists of the day, from Harvard as well as from MIT, that course would play a pivotal role in their

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*Remarks at the 23rd IMF Jacques Polak Annual Research Conference, livestreamed to the memorial service for Robert A. Mundell at St. Paul's chapel, Columbia University, November 11, 2022.

bildungsroman. According to the Fund's former historian, Jim Boughton, Rudi is likely responsible for christening the Mundell-Fleming model, and it was presented as such in the course. Mundell's two great books on international economics were on the reading list (along with several of Mundell's papers). The newer book, Monetary Theory, published in 1971, was available at the MIT bookstore for $15.95. The older book, International Economics, published by Macmillan in 1968, was harder to find. One day Rudi learned that 50 or so copies were being remaindered at a downtown Boston Barnes & Noble for $1.95 each. He sent his research assistant at the time, Bob Cumby, with a fistful of dollars to buy them all, and from then on, each of his graduating PhD students would receive a copy. Which is how I got mine. I think of these two books as Mundell's "Old Testament" and "New Testament."

Among other virtues, these works show Mundell as a pioneer of the "MIT style" of simple and intuitive models that cut to the core of a complex issue and clarify policy tradeoffs. All of we aspiring macroeconomists in my MIT cohort learned this approach from Dornbusch and Stanley Fischer, but Mundell was the innovator in applying it to short-run macroeconomic analysis. Mundell's analytical skills display the influence of Samuelson and probably Solow during his own MIT years, and of James Meade from his time at LSE, but I have no doubt that the broad historical and practical sweep of Mundell's sensibility, which is very evident in the testaments, owed to another MIT teacher not known primarily as a modeler, Charles Kindleberger.

I became Bob's colleague when I accepted an assistant professor position at Columbia, fresh from finishing at MIT. I was lucky enough to have three first-rate job offers coming out of grad school, from Columbia, from the (then) Woodrow Wilson school at Princeton, and from Chicago Business School (now Booth). Having grown up in New York, I was drawn by familiarity and family ties – my parents lived on

the upper West side of Manhattan when I was born, not far from Tom's diner of Seinfeld fame -- but I still found the choice difficult. Some characters who would later play important roles in this building advised me. Stan Fischer, later the First Deputy Managing Director here, thought Chicago would make a man out of me. Jacob Frenkel, future head of Research here, wouldn't entertain the possibility that I would do anything <u>other</u> than come to Chicago. One day as I sat in my Cambridge apartment the phone rang. Unexpectedly, it was Mike Mussa, Jacob's successor as economic counselor, calling from Chicago. The conversation was vintage Mussa. He said, "If you go to Columbia, you're making a small mistake. If you go to Princeton, you're making a big mistake." Rudi, my main adviser, gave me the advice that I wanted. "Do what feels right. And if you go to Columbia, you'll be with Mundell."

As I list these names, I must observe that alongside the impact of his own work, Mundell had a huge multiplier effect though his students and their academic progeny. Rudi, Jacob, and Mike are the most prominent students from his Chicago days, although they are not the only ones who went on to distinguished careers. Of his Columbia students, Carmen Reinhart stands out. In addition to their academic achievements, Jacob, Mike, and Carmen of course all played prominent policy roles here, across the street, and elsewhere. Rudi's brilliance was not suited to the constraints of bureaucratic responsibilities.

As a colleague, Mundell was supportive and inspirational, but in a sporadic and somewhat Delphic way. My experience on several occasions was that he would make an observation that seemed outlandish on its face, but that after reflection turned out correct under the right assumptions. For example, he once told me that "devaluation has no real effects," with no further explanation. One can indeed write a model in which this is true, and while the needed assumptions are not

realistic, working through what they are turns out to be instructive. I am reminded of something that Rudi wrote about Mundell in 2001: “He never, never in the time I saw him in Chicago answered any question other than with another question.” That was Bob.

Bob could be quite a presence in seminars. Several times I saw him reduce even the most eloquent and accomplished economists to exasperated speechlessness. Peter Neary, whom the *Irish Times* called “the most talented and committed Irish economist of his generation,” passed away at a much younger age only a few weeks after Bob. One time in the early 1980s he was at Columbia’s trade seminar with a paper on sectoral shocks and the real exchange rate. His coauthor was Doug Purvis, a revered Canadian student of Bob’s who died in a tragic accident at the age of 45. Bob insisted that the term “real exchange rate” was nonsensical – by definition, exchange rates are nominal. Flustered by Bob’s persistence, Peter tried to end the conversation by declaring, “Well, if Homer didn’t write the *Odyssey*, it was almost certainly written by someone else of the same name.” Mundell’s response: “Homer didn’t write the *Odyssey.*”

At a personal level, Mundell was clearly pleased with his role as my “academic grandfather” and showed it through grandfatherly solicitousness and advice, including on the proper way to wear a tie. In 1984, I was privileged to be at a conference on “Europe and the Dollar” in Torino organized by Rudi and another of his students, my much-missed Columbia colleague and friend Albert Giovannini. Mundell invited me to come after the conference to his beloved palazzo near Siena. Built in the early 16th century and five stories high, with a huge entry staircase big enough for a visitor’s horse to ascend, the palazzo has been lovingly restored by Bob and his wife Valerie over the years. “Bring as many friends as you like,” he said, “I have an infinitely elastic supply of beds.” I duly set out with Bob Cumby, Rick Mishkin, Jeff

Frankel and wives for a tour of the Liguriuan coast and a final stop at Bob's place in Santa Colomba. Santa Colomba is tiny and we soon came upon a huge Renaissance structure looming up out of very tall grass, easily taller than a man. After a few moments, the grass parted and Mundell emerged. "I apologize for the state of the garden. The gardener died several months ago, but I was not informed," he explained. Mundell invited us to have dinner, but there was no food in the pantry or fridge and indeed the electricity appeared to have been shut off. But the gas was still on and after we secured groceries and cooked, we were able to dine by candle light. A conversational highlight was Bob's disappointment with Marty Feldstein, who was then President Reagan's CEA chair but had criticized the Reagan tax cuts due to their effects on the US deficit. The next morning we deposited Bob in Florence at the Santa Maria Novella station for his next adventure.

Bob was always engaged in and motivated by policy, like most international economists of his cohort, but with the advantage of analytical gifts of an exquisite caliber. In the fall of 1961, still age 29, Mundell joined the IMF Research Department, where he worked for a couple of years before moving on to Geneva and Chicago in 1965. His division chief, later deputy director of the department, was Marcus Fleming. The department director was Jacques Polak, after whom this conference is named. Bob immediately set out to grapple with the United States' policy dilemma as the central link to gold in the Bretton Woods system: how to get growth going while safeguarding the U.S. balance of payments. His solution was the celebrated Mundellian policy mix: tight money to draw in capital flows, easy fiscal policy to further promote capital inflows while supporting demand. This policy mix was a Keynesian solution in Keynesian conditions. Mundell has recounted that in June 1963 he was part of the Fund's surveillance mission to the

United States, led by Polak. The degree to which Mundell's ideas inspired the Kennedy-Johnson tax cuts I will leave to historians.

By the end of the decade, U.S. conditions had changed, with inflation a major problem, much like today. Bob's solution came toward the end of his Chicago period in his Princeton Essay, *The Dollar and the Policy Mix: 1971*. This remarkable pamphlet can rightly claim to contain the origin of supply-side economics – which Bob presented not as a substitute for other macro policies, a kind of all-purpose panacea, but as a complement. Mundell diagnosed the U.S. inflation problem as coming in part from deficiency on the supply side – again much like today. He argued that tax cuts would have positive supply-side effects that amplified demand effects on growth, but also mitigated any resulting inflationary pressures, especially in the medium term. Supply-side economics has had its excesses and continues to have them, as seen in the recent market havoc in the United Kingdom. But Mundell's core point was important and economists of all stripes now acknowledge it. Fiscal policies are diverse and should be evaluated, not only in terms of Keynesian aggregate demand effects, but also in terms of how they change the economy's underlying productive potential.

Then there was the euro. In March 1970, more than a half year before the Werner Report appeared in October 1970, Bob circulated his "Plan for a European Currency." For Mundell, money represented much more than a technical lever for attaining economic efficiency. A stable monetary system was a key institution that represented a shared commitment by its participants, whether individuals or states, to markets and the rule of law. The same was true of an international monetary system. Mundell saw the potential for the euro to promote favorable political as well as economic evolution in Europe, and in the world at large.

Mundell's support of the euro flowed in part from skepticism about the arguments for flexible exchange rates advanced by his great Chicago colleague Milton Friedman and many other economists. As early as his "Optimum Currency Areas" paper, Mundell observed that the argument for floating exchange rates as a buffer – Friedman's celebrated "Daylight Savings Time" analogy – rested on some degree of money illusion, and would have little relevance if people adjusted wages and prices quickly to protect their <u>real</u> incomes. Somewhat ironic but little-noticed, Friedman's celebrated natural rate hypothesis, put forward in his 1967 AEA presidential address, likewise rested on the assertion that workers and firms could not be fooled for long by nominal price changes. Two other giants of international economics who have passed away in the past year shared Mundell's skepticism of pure floating to some degree. Richard Cooper viewed exchange rates as potential shock amplifiers and famously advocated the virtues of a world currency. John Williamson studied more limited exchange rate flexibility through a crawling peg regime or target zones.

Economists continue to debate how countries should manage their exchange rates. Mundell believed that only "hard" pegs provided a true contrast with other regimes, however, and he lauded the euro in its early years precisely because he thought it had banished speculation. However, the euro crisis and further crises that may lie ahead show how hard it is politically to maintain a truly hard peg among sovereign countries even with the benefit extensive institutional engineering.

In more recent years Mundell was a voice for economic reform in China, where he traveled frequently.

After Bob was awarded the Nobel Prize in 1999, Rudi Dornbusch and Andy Rose wrote excellent appreciations of his work for the *Scandinavian Journal of Economics.* As usual, Rudi put the case for Mundell memorably: his work brought about a "stunning break in open

economy macroeconomics" and "delegates to the upper bookshelves" the work of nearly all his distinguished predecessors. More than two decades later, Mundell's models retain relevance – while policy analysts may rely on more complex DSGE models for final detailed answers, most of them, whether they admit it or not, will make their first mental pass at a question using Mundell-Fleming.

But I would like to argue that Mundell's contribution is richer even than this – it cuts across doctrinal lines in a way that synthesizes multiple approaches into a greater whole. In 1986, Mundell told the *New York Times*, "In the very short run, I'm a Keynesian. In the intermediate run, I'm a supply-sider, and in the long run I'm a monetarist." It is a remarkable experience to re-read Mundell's two testaments today and appreciate how this macroeconomic perspective yields insights in a global setting. As Rudi's Nobel summary observed, few read Meade, Haberler, or Viner any longer, as important as their contributions to international economics were in their days. I truly agree that Mundell stands with Keynes and very few others as one whose works in the field should and will be read long into the future.