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War and famine. Peace and milk. — Somali proverb

Costs and Consequences of Austerity Issue

"There are no easy answers, no silver bullets. But... we have to amplify the menu beyond austerity and not keep praying for growth"

Carmen Reinhart
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ABOUT THIS ISSUE:

This issue is comprised of edited transcripts from the session "The Costs and Consequences of Austerity." presented by EPS at the AEA/ASSA meetings in Philedelphia on January 4, 2014

http://www.epsusa.org/events/aea.htm

Welcome Remarks

Allen Sinai

This session is motivated by the last three to four years' policies of Austerity with a capital 'A.' Austerity has been the generic policy used in the sovereign debt crises of a number of countries, principally Ireland, Greece, and Portugal, whose insolvency or near-insolvency led to requests for financial support from the Troika—the European Union, the ECB, and the IMF. Austerity in one form or another was part of the bargain, the conditionality in return for the help.

Other countries with sovereign debt and potential insolvency problems undertook programs of austerity as preventive measures.

Spain, Italy, the UK, and other Eurozone countries' ability to handle the crises was impeded by the single currency, single interest rate, and monetary policy of the Eurozone community. These factors immobilized two important mechanisms of equilibration for open-economy macroeconomics of countries: exchange and interest rates. Those countries where Austerity was applied also lost control of another potential mechanism for equilibration: fiscal policy.

The economic and financial crises gave us a really interesting laboratory experiment for the Eurozone arrangement. How would it all work out given the rigidity of the equilibrating mechanisms? The problems of the one-size-fits-all Eurozone economic and political arrangement; financial markets' reactions; interactions of the world economy with Europe through trade and finance; and the inevitable political instability made for an event in the global economy of monumental impact, negatively shocking.

The costs and consequences of Austerity, including potential benefits, is a question of major economic and policy significance. Is Austerity the way to go? What is the evidence pro and con? Is there a better way, or is Austerity the only way? What is the role of policymakers in these situations? How much attention should be given to political side-effects that inevitably have occurred throughout history? What about the interaction of policies and politics? What are the particulars of the recent use of Austerity in the Eurozone-UK context? In retrospect, has it failed? Or has it succeeded or been partially successful in its costs and consequences?

Most forecasts now are showing a recovery of some sort in the countries that have been impacted by austerity. It's taken a long time, and many of the signs continue to be tentative.

Thanks to a growing GDP and that GDP ratios should be coming down, in most forecasts it looks like the crises are abating.

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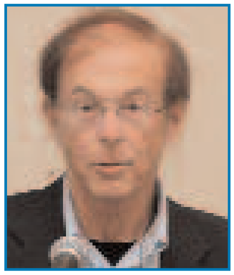

Allen Sinai is CEO, Co-Founder and Chief Global Economist and Strategist of Decision Economics. Prior to DE, he was Chief Economist at Lehman Brothers and The Boston Company (1983-96) and Chief Financial Economist at Data Resources, Inc. (1971-1983). Dr. Sinai has also been a non-partisan adviser and consultant to multiple facets of the U.S. Government including past Presidential Administrations, House and Senate Committees. He holds a Ph.D. in Economics from Northwestern University and an A.B. from the University of Michigan.

Olivier Blanchard A citizen of France, Olivier Blanchard has spent most of his professional life in Cambridge, U.S. After obtaining his Ph.D in economics at the Massachusetts Institute of Technology in 1977, he taught at Harvard University, returning to MIT in 1982, where he is now the Class of 1941 Professor of Economics. He was Chairman of Economics Department from 1998 to 2003. He is currently on leave at the International Monetary Fund in Washington, where he is the Economic Counsellor and the director of Research.

Carmen M. Reinhart is the Minos A. Zombanak is Professor of the International Financial System at Harvard Kennedy School. Previously, she was at the Peterson Institute for International Economics; Director of the Center for International Economics at the University of Maryland; Chief Economist at Bear Stearns; and the International Monetary Fund. Reinhart is a Research Associate at the National Bureau of Economic Research, and a member of the Congressional Budget Office Panel of Economic Advisers and Council on Foreign Relations.

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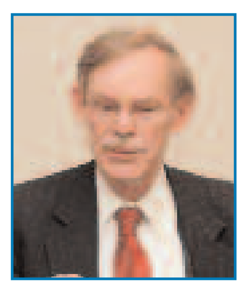
Robert Pollin is the co-director of PERI (The Political Economy Research Institute) and a Distinguished Professor of Economics at the University of Massachusetts Amherst. Professor Pollin has worked recently as a consultant for the U.S. Department of Energy, the International Labour Organization, the United Nations Industrial Development Organization, and the UN Development Program. He is presently a member of the Scientific Advisory Committee of the European Commission project on Financialization, Economy, Society, and Sustainable Development.



Robert Zoellick is the Chairman of Goldman Sachsí International Advisors. He serves on the boards of Temasek, Singaporeís Sovereign Wealth Fund, and Laureate International Universities, as well as on the international advisory board of Rolls Royce. Zoellick is also a Senior Fellow at the Belfer Center for Science and International Affairs at Harvard Universityís Kennedy School of Government. He is a member of the board of the Congressionally-created National Endowment for Democracy and the Peterson Institute for International Economics.

In Search of a Good Fiscal Rule

Oliver Blanchard

A good fiscal rule should be flexible. It should lead to countercyclical fiscal policy. It should be a credible commitment that debt will be honored.

Taking this as the goal, there are lessons from monetary policy that can be applied to fiscal policy. Central bankers have done crazy stuff over the last four years, yet they haven't lost credibility. Inflation expectations and whatever signals we have of credibility have remained anchored. I think the reason for this is that monetary policy has acted within a set of rules that people believe and that make them think that whatever is done today will in time be adjusted, that there is no reason to worry.

One example of the "craziness" is the increase in the size of the central bank's balance sheets. There have been increases of the order of 20 to 25 percent of GDP. Some countries' central banks have had rates of growth since 2008 of 300 to 400 percent, clearly completely out of the norm.

We can judge credibility of monetary policy by looking at the anchoring of inflation expectations.The central banks spent a large amount of time and capital to establish the two percent inflation target. In the UK, they systematically had higher inflation than what they had said they would. On the downside, Japan had less inflation than the central bank said it wanted, and yet inflation expectations remained around 1.5 or 2 percent. It's clear that the markets saw enormous movements in monetary policy, but did not worry very much about this.

My sense is that this lack of concern came from a fairly clear set of feedback rules. Until 2007, a lot of confidence was invested in interest rate rules. These rules convinced markets that if inflation picked up or activity became too strong, the central bank would do something. It's not as though people were sure that everything would be fine. There were discussions about what would happen if the US economy started heating up. Would the central bank be willing to increase rates? How would it be able to do this? There were some caveats but, in general, credibility and the feedback rules anchored expectations and gave them a lot of flexibility.

So the question is, can we think of a rule on the fiscal side, a feedback rule that would say, when things get worse, are we going to do more to counteract it? I want to push an old idea of Henning Bohn's from the 1990s. He showed that, if you have a rule in which the primary balance, excluding interest payment, reacts positively to the level of debt, that's basically enough. If you commit to saying, when debt goes up I will increase my primary balance by some amount--and it doesn't actually matter what the amount is, it just has to be a positive parameter--this actually will be enough to stabilize the debt.

If you commit to saying, when debt goes up I will increase my primary balance by some amount--and it doesn't actually matter what the amount is, it just has to be a positive parameter--this actually will be enough to stabilize the debt.

This rule says there is no magic debt or deficit ceiling. Debt could be very high, but as long as you stick to the rule, you will get it down. It shifts the focus from numbers like 60 percent, or 3 percent for deficit, to the primary deficit. Whenever debt is higher, you will increase your primary surplus a bit, or you will improve your primary balance, but you won't do it overnight.

Bohn showed that this rule was a very good description of what has happened in the US since the 1970s. In fact, we have shown at the IMF that it describes well what countries have done since the 1800s. Adjustment over the last four years has been very consistent with this rule. Obviously, in Greece, Portugal, and Spain, the adjustments went much, much faster than the rule would suggest as safe because these countries needed money and the lenders were not open to lending unless the adjustments went very fast.

This simple rule faces a number of challenges. First, there is no reason to think that the historical behavior is the optimal behavior. What has happened in the past has worked, but clearly we should sit down and ask ourselves what are the optimal values, rather than take them as given.

Another big issue is cyclical adjustment. If you want to avoid pro-cyclical fiscal policy-- namely, having fiscal contraction when there is a recession-- this rule has to apply to the cyclically adjusted primary balance. We have learned from this crisis that it's awfully hard to know whether a decrease in output is permanent or cyclical.

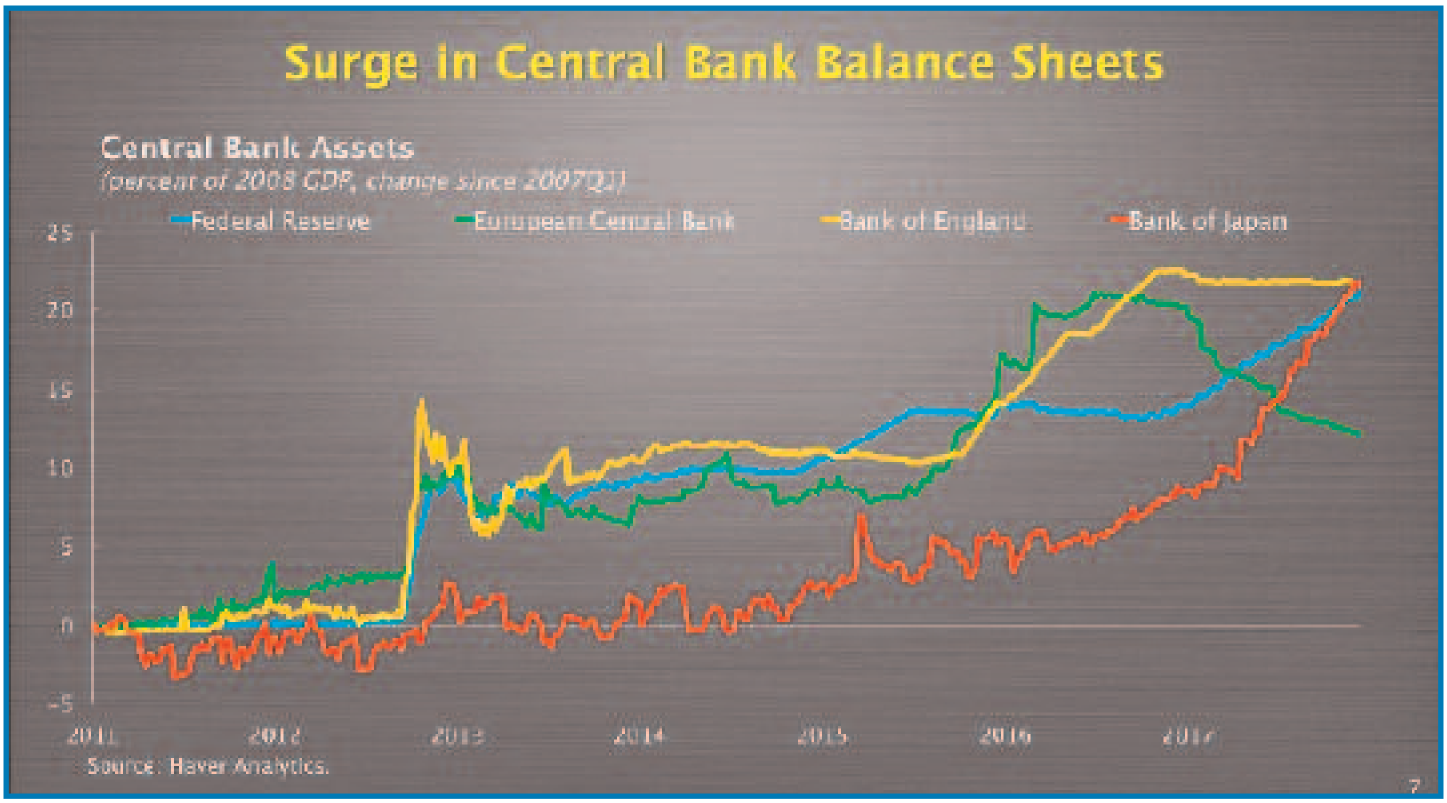
In Search of a Good Fiscal Rule (continued)

Historically there has been a lot of cheating, so the only way this works is through an institution that is apolitical, that tells the policymakers what the output gap or what the potential output is. You don't let the policymakers decide what the cyclical adjustment is, because if you do, they cheat.

Of course, you cannot run very large primary surpluses forever. A debt-to-GDP ratio of 600 percent, just to take a crazy number, would imply that you'd have to run a primary surplus that would be orders of magnitude bigger than realistic. Running a primary surplus of more than five percent for ten years hasn't happened very often. You have to assume that it will get you into political trouble; so that puts a limit on the level of debt in the end.

Could it be that when the level of debt is very high, the political strength to increase the primary balance is there? Looking at a large number of countries (25 emerging and 25 advanced), we see that with a debt-to-GDP ratio up to about 150 percent governments are able to increase the primary balance. At levels of debt above 150 percent, there's enormous uncertainty about what is happening and it goes the other way. There's just no way to generate the primary surplus you'll need, and then you're in trouble; and presumably there will be debt restructuring.

So it's clear that the argument is not that you can carry any level of debt, but up to very high levels of debt. It seems to me that a rule like this would actually dominate the way we're doing fiscal policy.



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Austerity in Context

Susan Collins

I think of austerity as a set of government policies intended to reduce the fiscal balance, particularly deficits, either through cuts in expenditure or increases in revenue. An austerity program is almost invariably implemented in the midst of adverse economic conditions. Sustainable, long-term, well-thought-through fiscal rules of the kind that Olivier was discussing typically are not labeled as austerity.

When countries make radical changes in policies it ís usually because there has been a failure to confront and tackle the longer-term challenges they're facing. The choices are difficult and highly charged; there are often very complicated contexts politically in terms of who should or is willing to bear the costs.

These factors make it all the more challenging to be considered credible when announcing that one is going to undertake fiscal rules. Credibility has often been squandered on exactly the opposite of the monetary policy situation in which central banks have accumulated a significant amount of credibility, providing them with the flexibility to undertake the crazy kinds of policies that they have, very successfully.

Recent empirical reassessments give strong evidence that fiscal policy can be a powerful countercyclical tool. Its effects are likely to be stronger in those contexts in which the economy is in a slump, with high rates of underused labor and physical capital. Under such conditions there are a couple of reasons that fiscal multipliers are likely to be particularly high. The type of crowding out that would come as interest rates are increased as a result of the fiscal expansion is unlikely to happen with the zero lower bound and the kind of monetary policy accommodation that we've seen. Also, to the extent that the private sector is constrained, it is likely to show more sensitivity of consumption investment to current income than to anticipated future income. Thirdly, risk premia are already low and unresponsive. The idea that fiscal consolidation by increasing credibility that debts will be lowered in the future will bring those risk premia down further, is unlikely to spur private sector growth. These are some of the key issues related to the added uncertainty that's often associated with radical types of consolidation programs.

> **It is also clear...that advanced economies...are vulunerable to fiscal risks..."**
> **Estimates suggest that Austerity policies in two economies with fiscal space have caused an accumulated reduction in GDP: 3 percent in the UK, and around 2 to 2.5 percent in the US.**

It ís also clear from the recent crisis that advanced economies, as well as emerging markets, are vulnerable to fiscal risks. It ís important that we take into consideration the broader implications of those very high debt levels that many countries accumulated and some of their associated challenges. The context really does matter. For countries able to borrow in their own currency, relationships between accumulation of debt and the various kinds of risks are different and more nuanced. However, not all countries have that fiscal space. Many of the countries that have taken those policy decisions did not have a lot of alternatives.

Estimates suggest that austerity policies in two economies with fiscal space have caused an accumulated reduction in GDP: 3 percent in the UK, and around 2 to 2.5 percent in the US.

These are clearly significant reductions and have implications for unemployment and distribution costs.

There are a number of broader, longer-run consequences that are also important to put on the table. In the United States and a number of other countries, there are longstanding concerns about the depreciation of both infrastructure and public capital; and there are significant concerns about the longer-term implications for potential GDP growth as a result of what's happened to both public investments and the fact that private investment has been much more sluggish. Although GDP growth has recovered to some degree, the recovery is much less than what many anticipated.

I've also mentioned the distribution costs. There is a recent paper that takes a comprehensive look at the different types of consolidations. Essentially it argues that there's a significant impact on inequality measured through the Gini indicator associated with fiscal consolidations; that association is much stronger with spending cuts than with tax revenue increases. At the same time, the paper highlights that a well-designed program

Austerity in Context (continued)

can offset and mitigate those distribution costs so that the burden of the adjustments does not fall so heavily on some of the most vulnerable populations. To the extent that the adjustments are viewed as being fair and equitable, the political dynamics that I mentioned at the start suggest that the
programs are much more likely to be sustained going forward.

Then, finally, while many of us have focused on austerity programs in the US and Europe, I think it's also important to highlight that there has been a much broader shift towards fiscal consolidation globally. A recent paper looked at 181 countries. In the initial phase, right
after the crisis, some 90 percent of the countries in that sample were, to varying degrees, in some type of expansion. In the second phase, about 40 percent of those countries began to retrench. The fiscal consolidations actually expanded, and they've expanded more extensively in developing countries than in industrial countries. There are a number of case studies that focused on fiscal consolidations associated with growth recoveries generated by increased exports. To the extent that this is a global phenomenon, I think the linkages and the externalities that are associated with reviving the global growth engines are also a great concern and suggest additional consequences to widespread austerity, especially in an environment with a zero lower bound, where it's much more difficult for an individual economy, through depreciations or other kinds of adjustments, to offset some of the lack of export opportunities when trading partners are undertaking austerity programs.

What I have done is to try to highlight some of the challenges and considerations that make me conclude that the kinds of fiscal rules that Olivier was talking about are much, much more sensible ways to adjust fiscal policies over time. Avoiding those adjustments, one can get into very very challenging situations; it's unfortunate to see such a large percentage of economies appearing to be in the midst of those austerity situations at the moment.

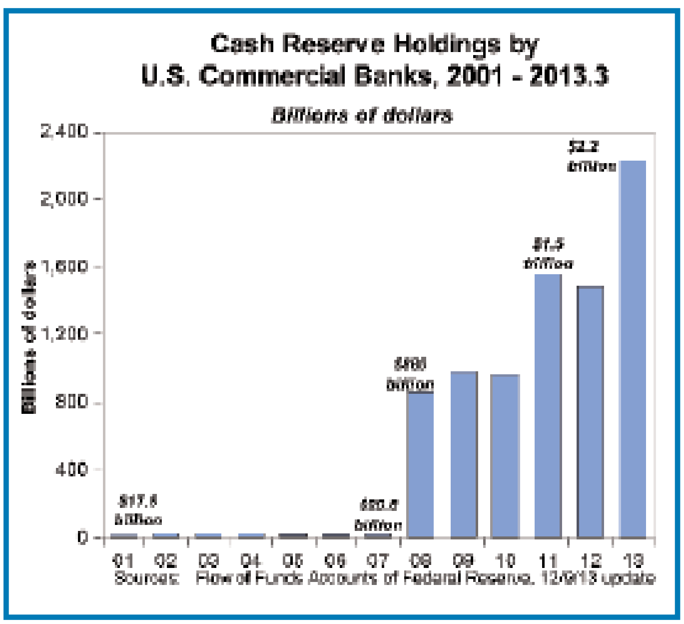


figure 1

Annual Revenue Potential for "Inclusive Prosperity Act"

Financial Instrument	2011 Trading Volume	Ellison Bill --FTT Tax Rate	FTT Revenues Assuming no trading reduction	FTT Revenues assuming 50% fall in trading
Stocks	$25 trillion	50 basis points	$125 billion	$62.5 billion
Bonds	$225 trillion	10 basis points	$225 billion	$112 billion
Derivatives	$480 trillion	0.5 basis points	$240 billion	$120 billion
TOTALS	---	---	$590 billion	$294.5 billion = 78% of CBO projected 2015 fiscal deficit

figure 2

Austerity and its Discontents

Robert Pollin

The US logic of austerity economics is still very ascendant. We can see that in the budget agreement that President Obama signed the day after Christmas [2013], which entailed cutting pensions for federal employees, including military personnel. It failed to extend unemployment insurance for 1.3 million long-term unemployed. It didn't address tax loopholes for the wealthy at all; it didn't provide for spending on priority programs for infrastructure or the green economy; and it cut food stamps for 47 million people, including 22 million children.

The most dramatic effect of the financial crisis and the Great Recession has been on mass unemployment. The broader measure of unemployment (U-6), including the official unemployment rates plus underemployed and marginally attached workers (as of January 4, 2014), is at 13.2 percent; that's 21 million people unemployed or underemployed by that measure. If you begin from the month that the NBER says the recession officially ended, and extrapolate the rate of reduction in unemployment until the unemployment rate reaches 5 percent, it would take until June 2017; to get to a 4 percent unemployment rate would take until March 2019.

The average fiscal deficit as a share of GDP from 1950 to 2012 was 2.2 percent. In 2007, before the crisis, it was 1.2 percent. It spiked to 10.1 percent in 2009 and stayed very high for three years. For 2012, the Congressional Budget Office is saying the fiscal deficit was 7 percent; 4.1 percent for 2013; and their prediction is 3.3 percent and 2.1 percent for 2014 and 2015, respectively.

As a consequence of the spike, austerity hawks concluded that the most serious problem was not mass unemployment, but the fiscal deficit itself; that the priority had to shift away from addressing unemployment to controlling the deficit. There were three basic arguments for this claim: that the large increase in the fiscal deficit would generate inflation, rising interest rates; and major declines in GDP growth. However, interest rates didn't go up, and the inflation effects didn't happen.

> **The most dramatic effect of the financial crisis and the Great Recession has been on mass employment...If you [follow the current trend]...to get to a 4 percent unemployment rate would take until March 2019.**

The government debt did of course grow as a consequence; but the interest burden on the debt actually is at an historic low. So if we define a fiscal crisis according to the capacity to cover your obligations over the next few months, the US is actually in better shape than it's been since the 1950s.

In this case the arguments of the deficit hawks don't hold. In the 2010 Reinhart & Rogoff papers, they showed that GDP growth declines significantly when the public debt-to-GDP ratio exceeds 90 percent. Reinhart and Rogoff reported robust evidence across countries and historical experiences. With my colleagues Thomas Herndon and Michael Ash, I produced a working paper saying that there are three basic problems with the Reinhart-Rogoff paper: one was a spreadsheet error, which they acknowledged; the second was the selective exclusion of available data; and the third was the weighting scheme that was used, which, without getting into details, seemed inappropriate. We replicated their work and found that GDP growth rate for the above-90 percent category was not -1.1, but 2.2 percent.

Reinhart and Rogoff contend that these are minor issues, but my coauthors and I conclude that they are actually quite relevant in understanding the capacity of governments to undertake fiscal stimulus to fight mass unemployment. The flexibility needs to be understood within a range of complementary policies for expansion and inclusive growth. The banking system now holds $2.2 trillion in reserves, 14 percent of GDP. (See figure 1, page 6)At the same time, lending to non-financial businesses since the recession has been zero. I agree with Alan Blinder that we should tax the excess reserves. I would also argue for imposing not just a stick, but also the carrot of expanded loan guarantees for small businesses.

And finally, I support a financial transaction tax. Representative Ellison is sponsoring the Inclusive Prosperity Act, based on the UK stamp tax, which taxes stocks at 50 basis points. This proposal also imposes lower tax rates on bonds and derivatives. A simple calculation using the 2011 level of trading shows this tax would generate $300 billion per year. Three hundred billion is 78 percent of the CBO's projected 2015 fiscal deficit. (See figure 2, page 6) Clearly, there are ways to address the long-term fiscal issues in an inclusive way.

A Menu of Policy Opptions

Carmen Reinhart

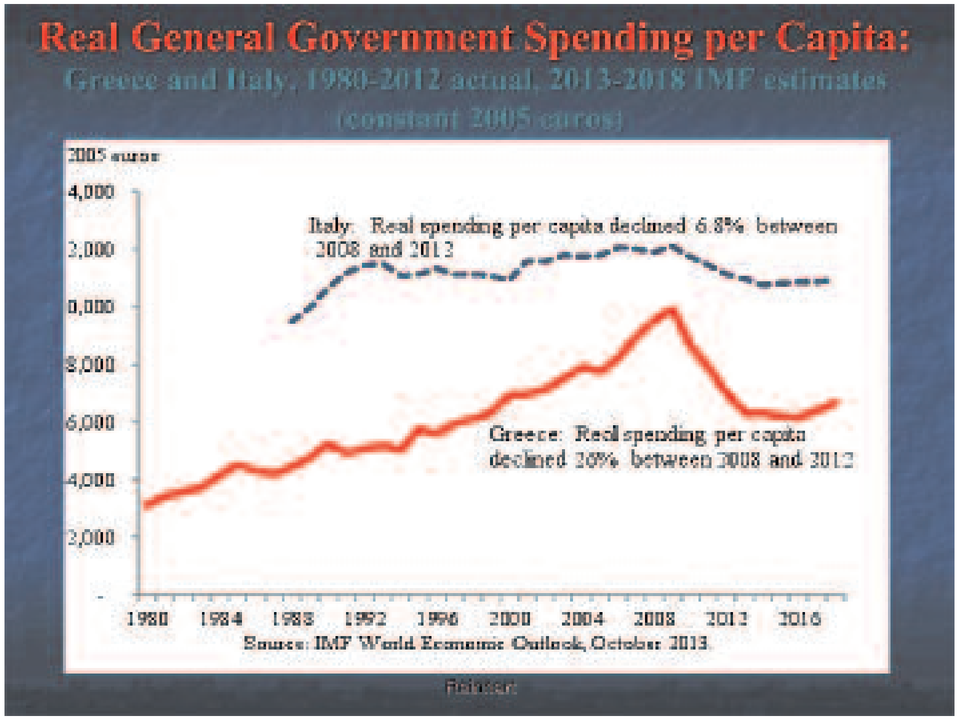
Austerity is a very broad term. Austerity in Greece is not the same as austerity in Italy, is not the same as austerity in the US. Austerity can be a way of reducing deficit. Growth is a great way of reducing deficit. But what about debt relief? Write-offs? Financial repression?

I am a firm believer that austerity has its roots in booms when everybody takes growth and income for granted and spends accordingly; and then, when things turn bad, the adjustment falls on the bad times.

In Greece, austerity has meant a decline of real spending per capita of 26 percent between the start of the crises in 2008, and 2012. That is austerity in its most extreme form. Greece has been in contraction all this time. The trough in economic activity in Greece, if we're lucky, was in 2013. In Italy, the decline has been about 7 percent.

In the US, we are still at levels of per capita government spending that are above what they were pre-crisis. This is not to belittle the fiscal drag we've had in the last few years, but that is in no way comparable to what happened in Greece, Italy, nor the rest of Europe. So austerity means different things for different countries. I think a lot of the debate that we're having is not so much whether or not high debt is a desirable thing. Countries aspire to high per capita income, high levels of education, high standards for health. I've never heard of a country that aspires to high debt. The question is how to bring the debt down.

I'd like to focus on the things we don't talk about. What are the things that we should have been doing that we haven't been doing or that are really part of the history lesson? Throughout history, growth was an important factor in reducing debt



levels. Fiscal adjustment and austerity sometimes played a critical role, but debt restructuring, outright defaults, or debt conversions have also been critical, and not just in emerging markets. When you look at the contraction in fiscal spending in much of periphery Europe, you have to ask yourself, from here on out, what is sustainable? What is advisable for Greece is not the same as for the UK or the US, where there is a lot of scope in monetary policy and the fiscal thresholds are different.

In the 1930s, the advanced economies on the whole defaulted on their debt. Part of the debt reduction involved the abrogation of the gold clause, which in the US meant a debt reduction of about 16 percent. Additionally, the UK and France did not repay their World War II debts to the US. These were about 22 and 24 percent of GDP for those countries, respectively. These are big debt reduction numbers.

In the US and the UK, an approach to debt restructuring a la Greece, Ireland, or Italy is not the issue. What are some other approaches? With financial repression basically you maintain negative real interest rates with heavy-handed regulation, and that liquidates your debt, or it's part of your debt liquidation. These are not run-of-the-mill policies that one goes out and advertises, but they have been an integral part of debt reduction in advanced economies. The concept that this is stuff that emerging markets do, but advanced economies have never done, is just not fact. When one gets into a high-debt, low-growth, high-unemployment environment, there are no easy ways out.

Let me say something about Robert's remarks: Ken Rogoff and I do not pretend to argue that growth will be normal at 89 percent, and sub-par (about one percent lower) at 91 percent, anymore than a car crash is unlikely at 54 miles an hour and near-certain at 56. What we're trying to do is map the theoretical notion of vulnerability

A Menu of Policy Opptions (continued)

Carmen Reinhart

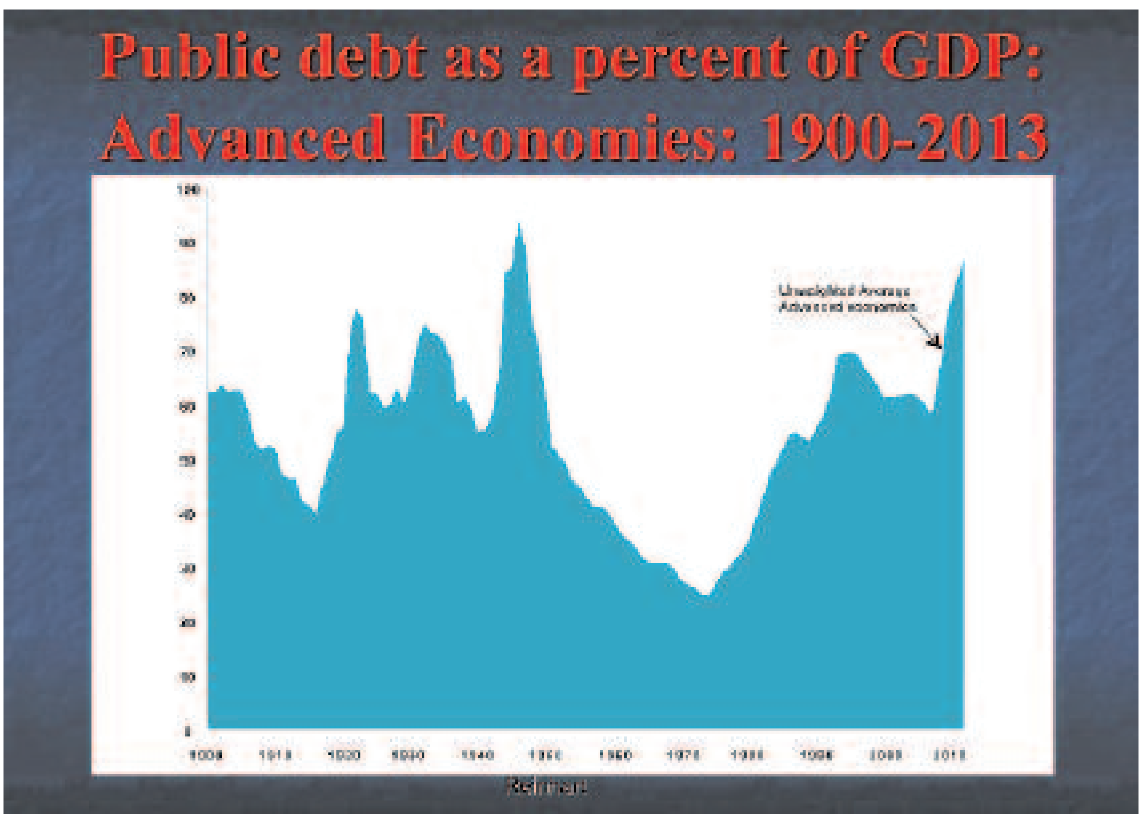
regions, which, of necessity, involves defining thresholds. US traffic signs don't say, "Just drive slower." They actually state a limit.

There is a burst of literature that we hope is dealing with all the deficiencies of our studies because our study was very preliminary, very first-pass. We put it out there without any policy prescriptions. As early as 1999, work I did with Graciela Kaminsky proposed that if real exchange rates get above a certain threshold, there's an overvaluation problem; you're less competitive. There's nothing special about debt per se, but the idea of identifying vulnerability regions is pretty fundamental.

One of the lessons that I take from history is that we've been straight-jacketed in how we have approached this crisis. We are in the sixth year of the crisis and of economic contraction in periphery Europe. The US and Germany are the only two countries that have regained their pre-crisis level of income. In a 2010 paper I did with Vincent Reinhart, in 10 of the 15 countries we looked at, unemployment didn't return to pre-crisis levels for 10 years. This is not to disregard unemployment, the absence of growth, nor the income distribution problems. But let's face it, high debt is an issue that is going to be with us for some time, especially in light of the fact that it's not just high public debt; it's high private debt, and private debt becomes public debt.

> **In the 1930s, the advanced economies on the whole defaulted on their debt. Part of the debt reduction involved the abrogation of the gold clause, which in the US meant a debt reduction of about 16 percent.**

I'm really delighted to have this opportunity to engage in a meaningful discussion of some of the issues at hand. Let me leave you with a message: I'm not an uplifting person. Even debt restructuring has costs and stigma issues, and creates uncertainty. There are no easy answers, no silver bullets. But I do think we have to amplify the menu beyond austerity and not keep praying for growth.



Beyond the Binary Debate

Robert Zoellick

In his invitation, Allen posed a very important question, which is, what have we learned from the recovery strategies after the Great Recession? I'd like to add to the mix today with some impressions of a policymaker.

I'm very skeptical of the austerity-versus-growth dichotomy. Of course, at the policy extremes, one can see the role of fiscal policy when demand collapses-although there are some very good questions to be asked about the effectiveness of the US fiscal stimulus. Monetary policy plays a role in terms of lessening tail risks and assisting deleveraging. The policy mix itself depends heavily on national, regional, and global circumstances. It also depends on the policy flexibility that policymakers have as they come into the situation. It depends very heavily on the type of the downturn.

My principal concern in the binary austerity debate is that it assumes that government and private spending and investment are the same. I would suggest it's perhaps time to start to think about a different framework. Policies also have to point to the need for a handoff to the private sector in employment, investment, and overall demand. It matters whether the public sector perceives itself as the ongoing driver of growth. In these discussions there's never any distinction as to where demand comes from. Part of the challenge is creating the conditions for this handoff, which affects psychology, behavior, and recovery.

It's very difficult to quantify the effects of government policy uncertainties on private sector expectations. We have seen that expectations of future public spending, debt, and taxes can cut the multipliers. The reality is that it's natural that policymakers focus on the short term; because if they don't get through the short term, they never get to the long term.

I am increasingly of the view that if one develops stimulus policies, they need to be accompanied by structural reforms that will create the environment for private sector investment, employment, innovation, and productivity growth. For example, in the United States we've seen very strong corporate cash flows and low costs of capital, yet, until very recently, very weak investment.

We have seen that expectations of future public spending, debt and taxes can cut the multipliers. The reality is that it's natural that policymakers focus on the short term; becuase if they don't get through the short term, they never get to the long term.

So how does a country point its economy back to stronger trend growth? What are the policy challenges? This is being debated in developing and middle-income countries, just as in developed countries. In the case of the United States, I would focus on the following six ideas to boost confidence, and growth: First, I think a broad-based tax reform with lower rates, equalizing tax treatment across all types of capital, eliminating distortions in tax subsidies, would go a long way toward building confidence.

Second, in cities and states around the world you can see the painful effects of the crises on benefits and pensions of the public employees. At some point we're not going to be able to continue the federal benefit programs if we don't at least start to think of modest steps. Frankly, as a policy official who's been doing this for a number of years, I think if you implemented just those first two steps, modest dealings with entitlement programs and a tax reform, you'd see a big takeoff in confidence and growth.

Third, human capital has to be given a lot more critical attention-private sector employment is still less than it was six years ago. The way you do this is with more flexible labor markets. The simple policy goal should be to get people into private sector jobs. I would suggest the government is not very good at setting the prices for labor. If we want more returns to labor, especially low-wage workers, why don't we consider a permanent reduction in the payroll tax? Why are we taxing labor in such a regressive fashion? Also, if you want to increase income for low-wage workers in a redistributive sense-it's a legitimate choice-why not do it through things like the earned income tax credit, as opposed to trying to have the government set a minimum wage?

There's much more that we can learn about helping people gain or regain skills, including making use of the private sector. I hope this becomes a field that the economics profession helps policymakers learn more about. Let me just give you a reference point: the United States government spends about $18 billion a year on worker and job training through about 50 separate programs run by nine agencies and they're almost never evaluated. That's a good place to start to figure out how we can better use our resources. If you think about it in the broader sense, our unemployment insurance program, our trade assistance program, our job retraining program are between 30 and 70 years old. What else in the

Beyond the Binary Debate (continued)

economy hasn't been reassessed and evaluated, given what's going on? We've got to be able to do that better.

Fourth, US immigration policy should focus on welcoming people that the American economy needs to boost growth and skill levels. Over 50 percent of the startups in Silicon Valley were created by immigrants.

Fifth, we've got a great opportunity with energy innovation if we don't choke it off.

And sixth, I continue to believe that an activist trade agenda with global competition would not only boost productivity, but it's a great way of forcing governments to face up to their failures.

In sum, even as we study the effectiveness of the macroeconomic tools, I would urge attention to policies that drive the microeconomic fundamentals, not out of some policy purism, but because those are the policies that will create the private sector opportunities and confidence that will enable the recovery to be handed off to the private sector.

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Michael D. Intriligator

1938 - 2014

Statement by James Galbraith, on behalf of the EPS Board.

We mourn the passing of Michael Intriligator, a wise and generous man, a great spirit in our lives and a driving force in the work of Economists for Peace and Security.

Mike Intriligator became known to me long years ago, when as a student I first read his lucid text on mathematical economics. We became friends when I joined the Board of Economists Allied for Arms Reduction " as it then was" about twenty years ago, and made the fortunate decision to ask him to serve as a Vice Chair.

From that point, we worked together closely. Everyone at EPS drew on his insights, on his contacts, on his reputation and above all on his inexhaustible energies and dedication. On internal matters we enjoyed his counsel, his constant encouragement and his unfailing support. He even came to meetings, hopping a red-eye to attend, and between meetings he gave his time on matters large and small. He would respond, almost at once, to pleas for help.

Mike's knowledge ranged over many fields, from pure theory, to armaments and strategic interaction, to the economics of health care, and to the practical difficulties of the Russian economy in the post-Soviet era. He was honored by membership in the Russian Academy of Sciences the only American economist with that distinction. He was a stalwart for us during the challenging moments of recent US political history, especially at the start of the Iraq war.

Kate Cell, a former EPS Director, writes for us all:

"Mike was a wonderful person--brilliant, humane, generous, cultured, curious, and kind. A great loss to the profession and especially to EPS whom he guided with wisdom, and supported by deploying his own peaceful
weapons: his vast network of colleagues, editors, publishers, former students, and other friends and admirers."

For everyone at EPS Mike Intriligator was a friend. And those who knew him best, loved him most.

Obituary from the Los Angeles Times

The Family was very generous in asking that in lieu of flowers, donations could be made to the Michael D. Intriligator Memeorial Fund of Economists for Peace and Security. If you would care to make a memorial donation in whatever amount, please click here.