

The Possibilities and Limits of Macro Policy in the U.S.

Robert Pollin

University of Massachusetts-Amherst

For conference on: *Transatlantic Agenda for Shared Prosperity,*

Berlin

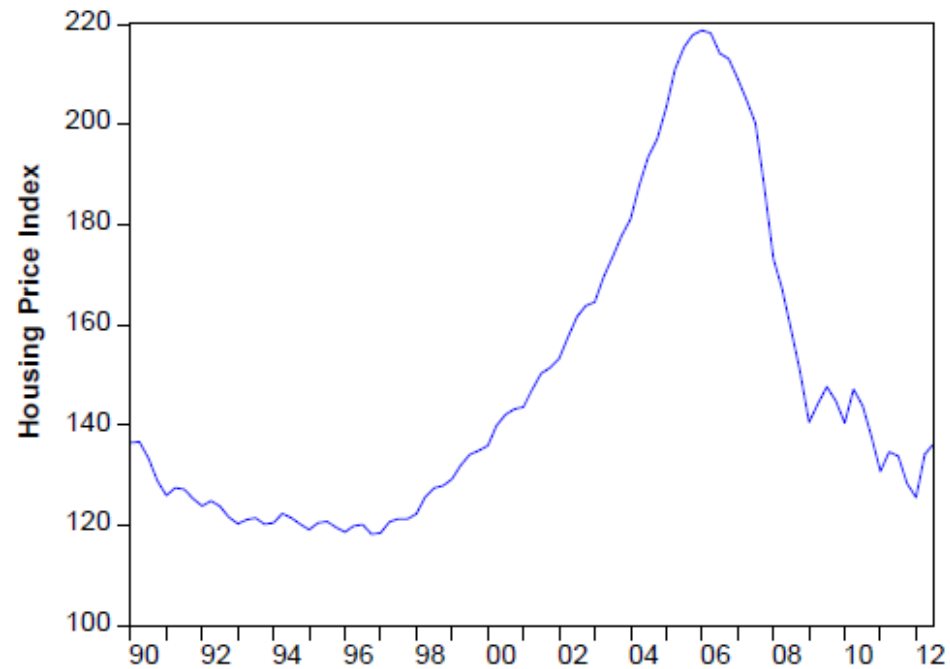
March 11, 2013

An Economic Crisis of Neoliberal Capitalism

- **Wall Street Crash and Great Recession**
 - Deregulation of financial markets produced hyper-speculation and overleveraging
 - This has been pattern with unregulated financial markets throughout history
 - Kindleberger, *Manias, Panics and Crashes*

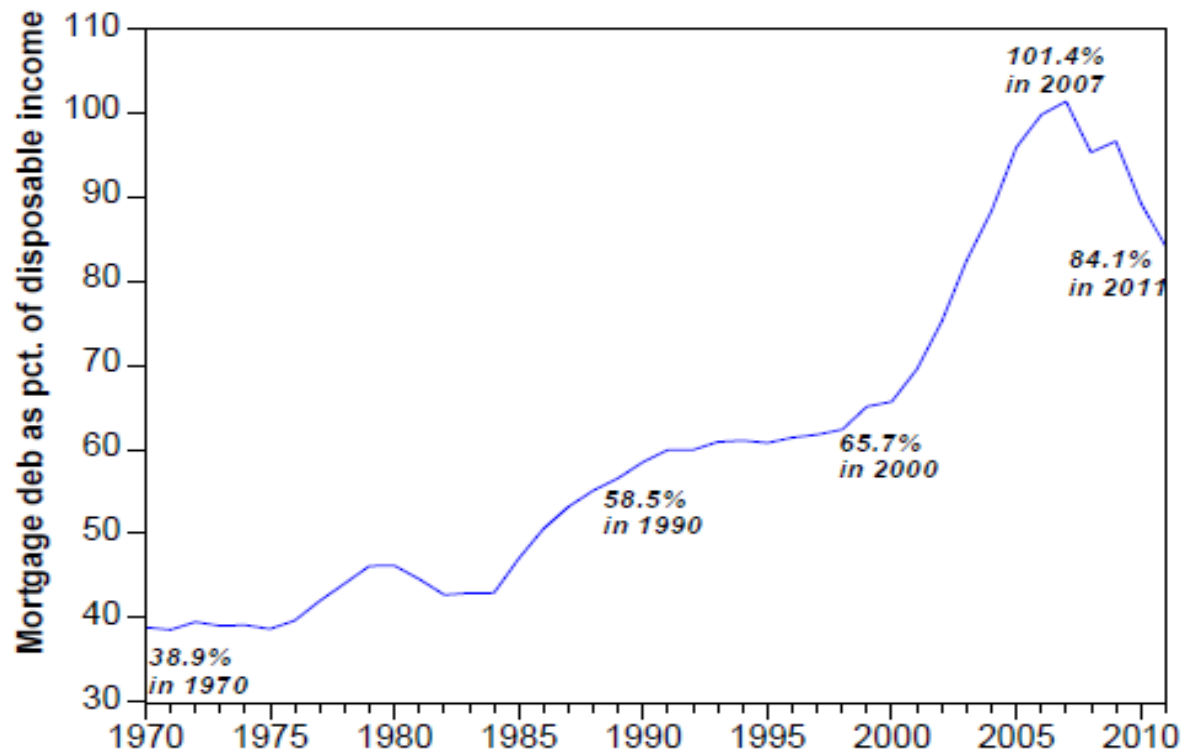
From Financial Bubble To Crash

Figure 16.1
Real Quarterly Housing Prices in the U.S., 1990.1 - 2012.3



Source: Case-Shiller Housing Price Index
Note: Case-Shiller Index deflated by CPI-U price index

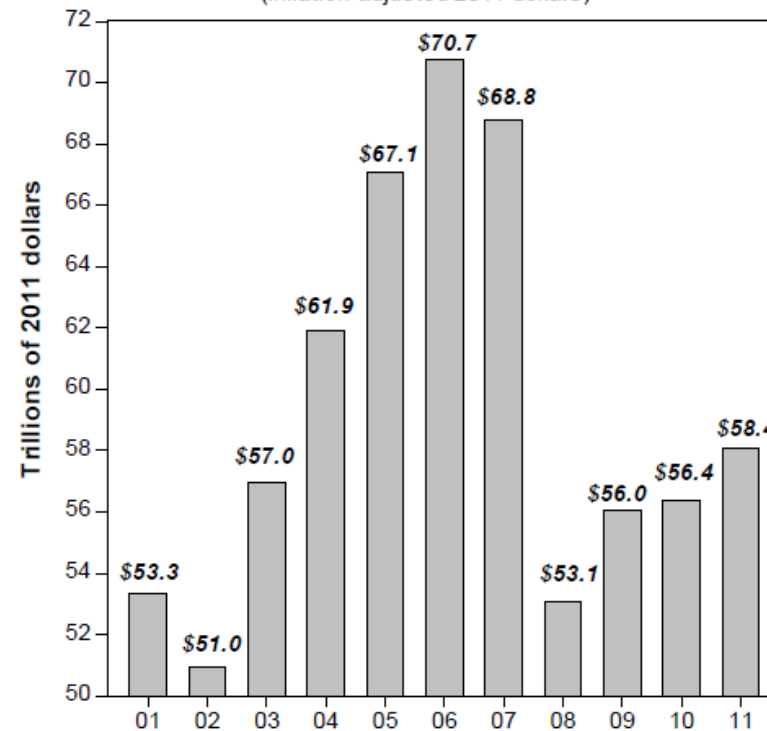
Figure 16.3
U.S. Household Mortgage Debt as percentage of Household Disposable Income, 1970 - 2011



Source: U.S. Flow of Funds Accounts

Evaporation of \$17 Trillion in Household Wealth

Figure 16.2. U.S. Household Net Worth, 2001--2011
In Trillions
(inflation-adjusted 2011 dollars)



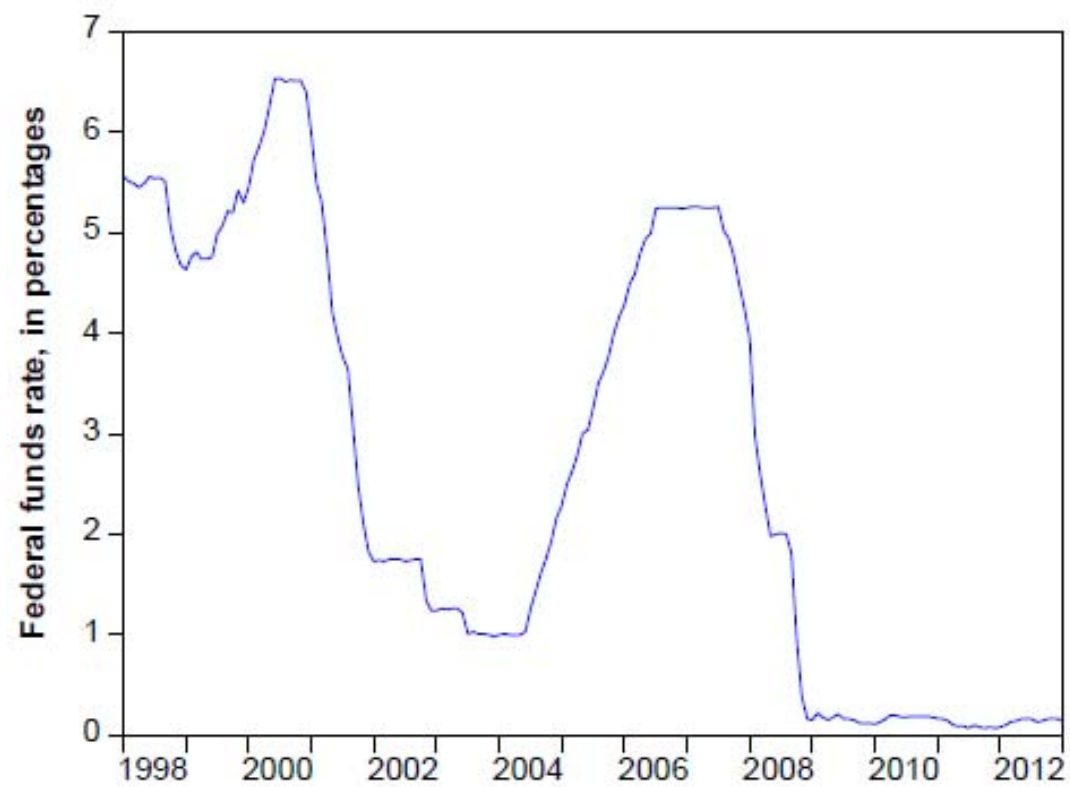
Source: Balance Sheets of U.S. Economy

Note: Inflation adjustment with CPI-U.

Policy Responses to Crisis

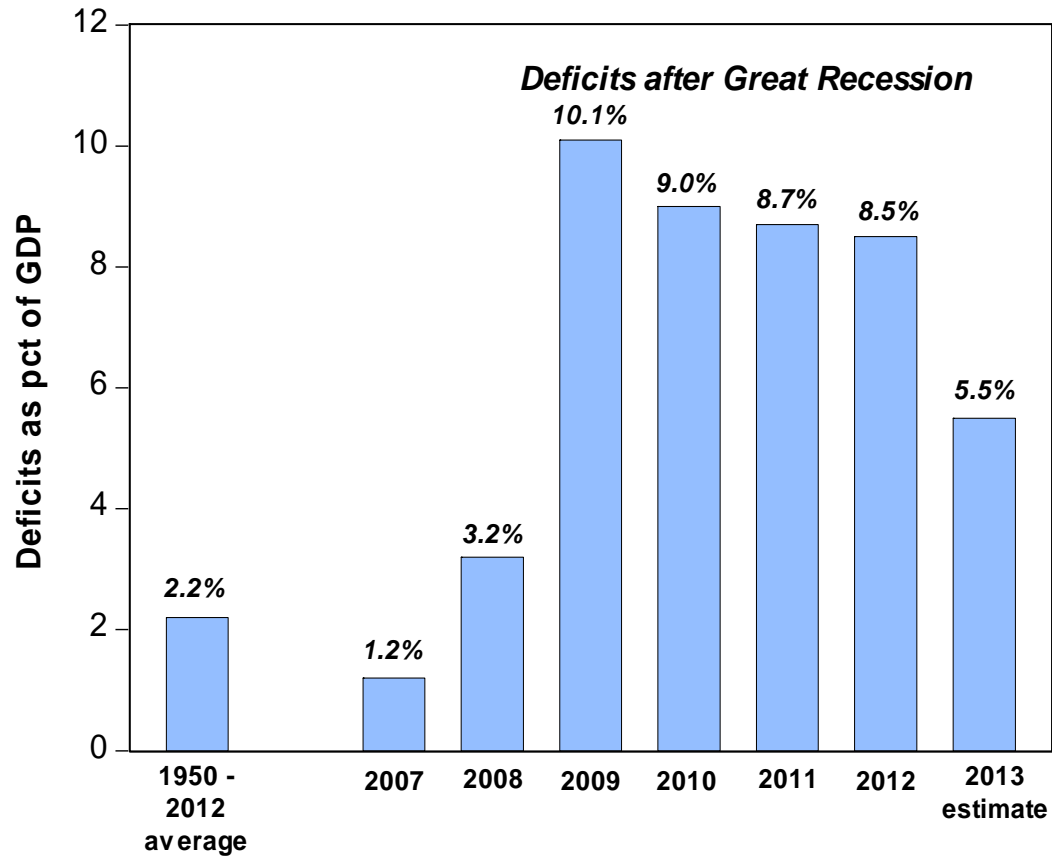
- **Bailouts for financial institutions and markets, and auto industry**
 - Via both U.S. Treasury and Federal Reserve
- **Near-zero interest rate for Fed policy rate—
federal funds rate**
- **\$787 billion fiscal stimulus**
 - American Recovery and Reinvestment Act (ARRA) of 2009

Figure 17.3
U.S. Federal Funds Rate, 1998.01 - 2013.01



Source: Economagic

Figure 1. U.S. Federal Deficits as Share of GDP

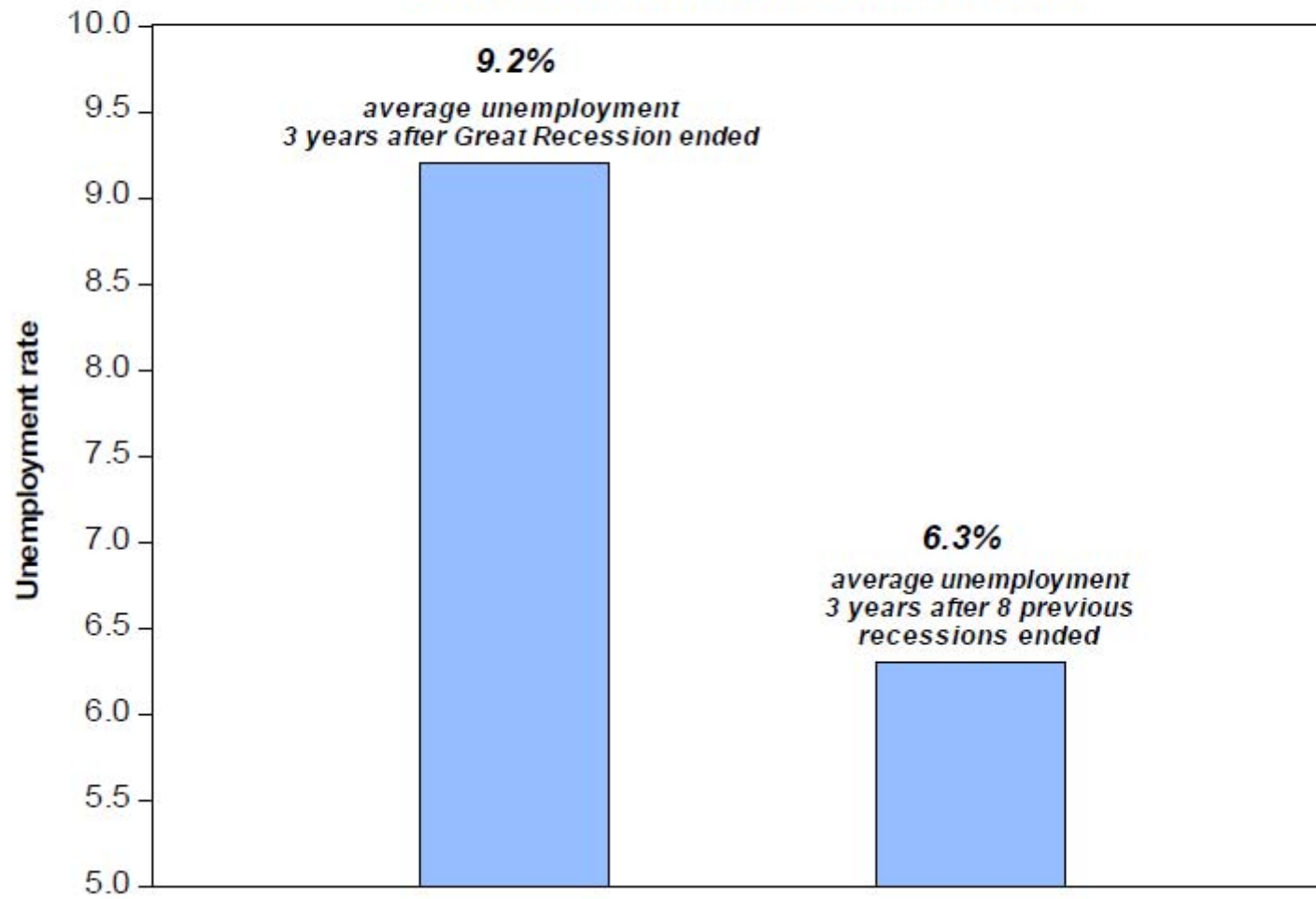


Source: U.S. Office of Management and Budget

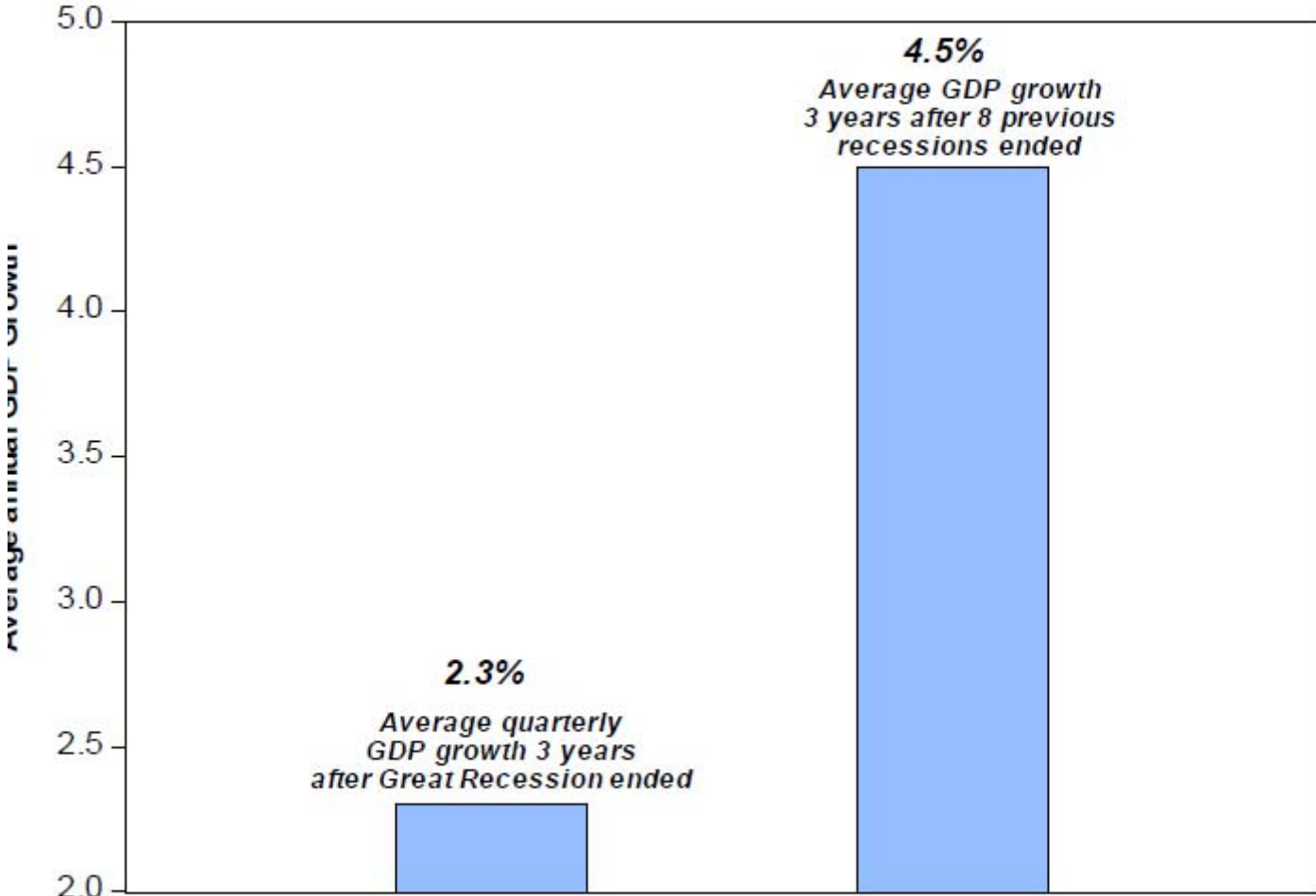
"Recovery" from Great Recession versus 8 Previous Recessions/Recoveries

Where is the Economy 3 Years After Recession Ended?

Unemployment remains much higher



GDP Growth is Much Slower



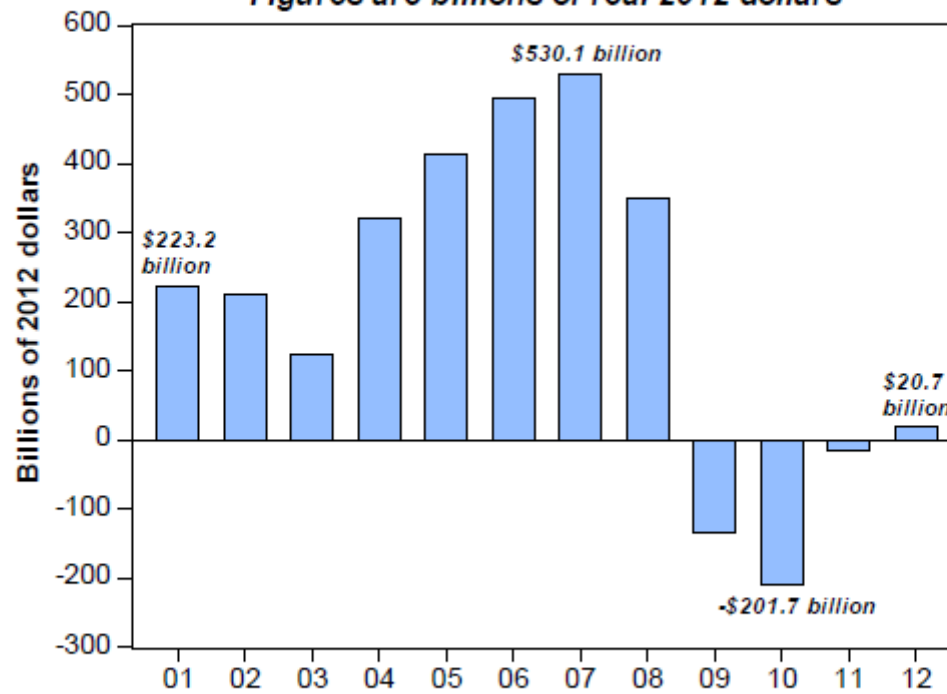
Source: Economagic

Why Weak Recovery?

- **Wealth evaporation**
 - Wealth effect ~ 3 – 5%
 - \$17 trillion in lost wealth = ~ \$500 billion in aggregate demand loss
- **Stimulus too dependent on tax cuts**
 - Congressional Budget Office:
 - Multipliers for direct govt. spending 4 times higher than for tax cuts for high-income people
 - Tax cuts 24% of stimulus
- **Collapse of Credit for Small Businesses**
 - Banks hoarding cash instead

Figure 10.1
Borrowing by U.S. Non-Corporate Businesses, 2001 - 2012

Figures are billions of real 2012 dollars

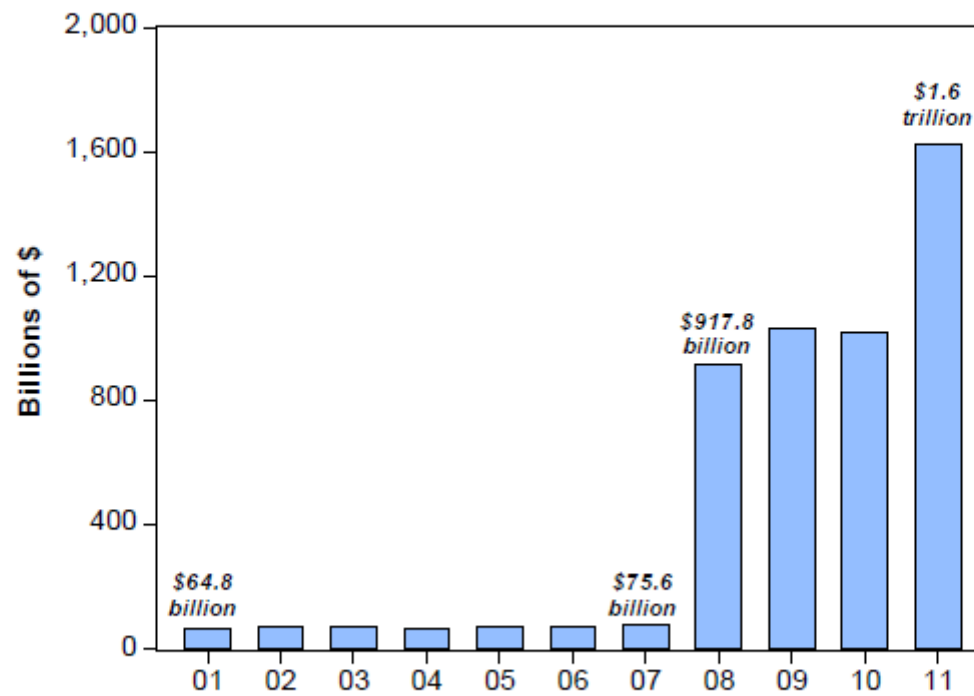


Notes: Inflation adjustment is with producer price index; 2012 figure is through 2012.3

Source: U.S. Flow of Funds Accounts

Figure 17.6
U.S. Depository Institutions Vault Cash and Reserves, 2001 - 2011

Billions of Dollars



Source: U.S. Flow of Funds Accounts

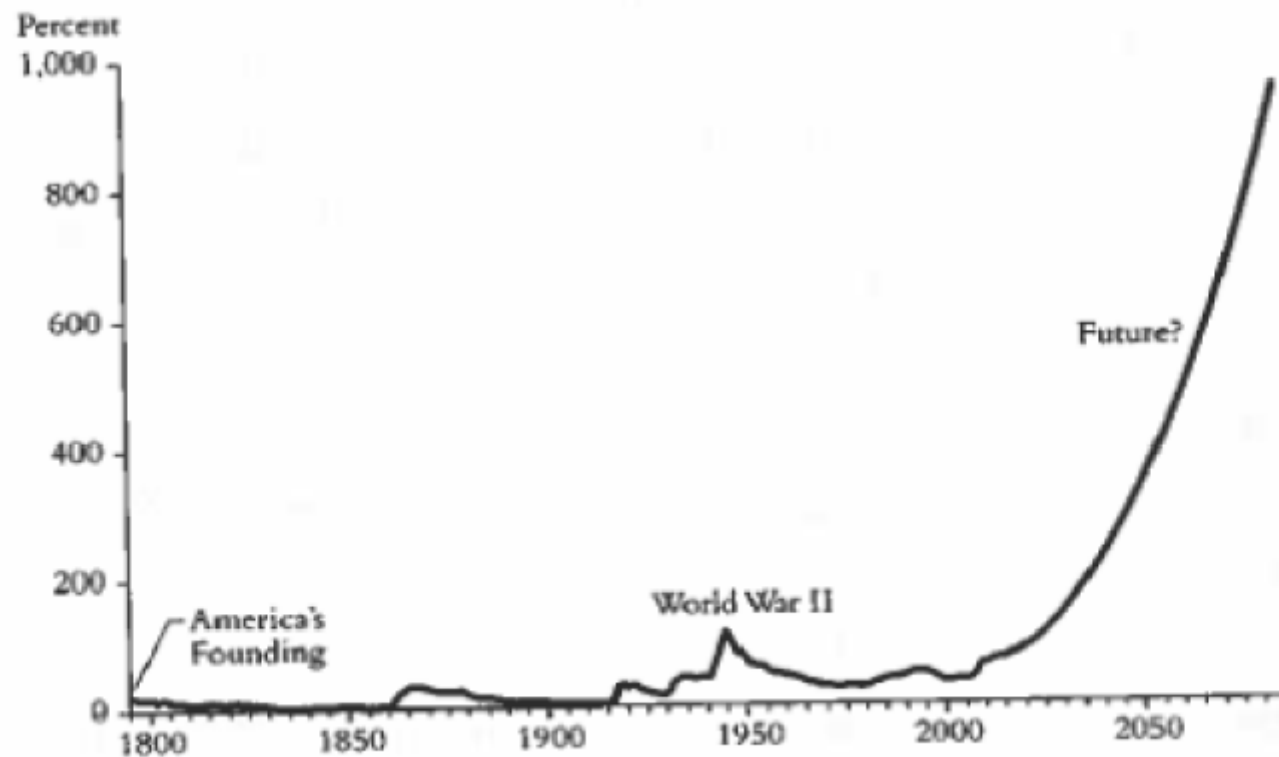
Arguments of Austerity Hawks

- **Most fundamental problem with economy is fiscal deficits/debt**
 - Not mass unemployment/weak growth recovery
- **Increases in fiscal deficits will produce**
 - Inflation
 - High interest rates
 - Overwhelming government debt burden
- **Arguments for “sequestration”**
 - \$110 billion/year in automatic cuts relative to previous allocations

U.S. Federal Debt/Income Ratio from 1800 – 2050 Projection

*Projection by U.S. Congressional Budget Office, with Annotation by John Taylor
As Cited in Taylor (2012)*

From America's Founding to Its Ending? Federal Debt Relative to the Size of the Economy

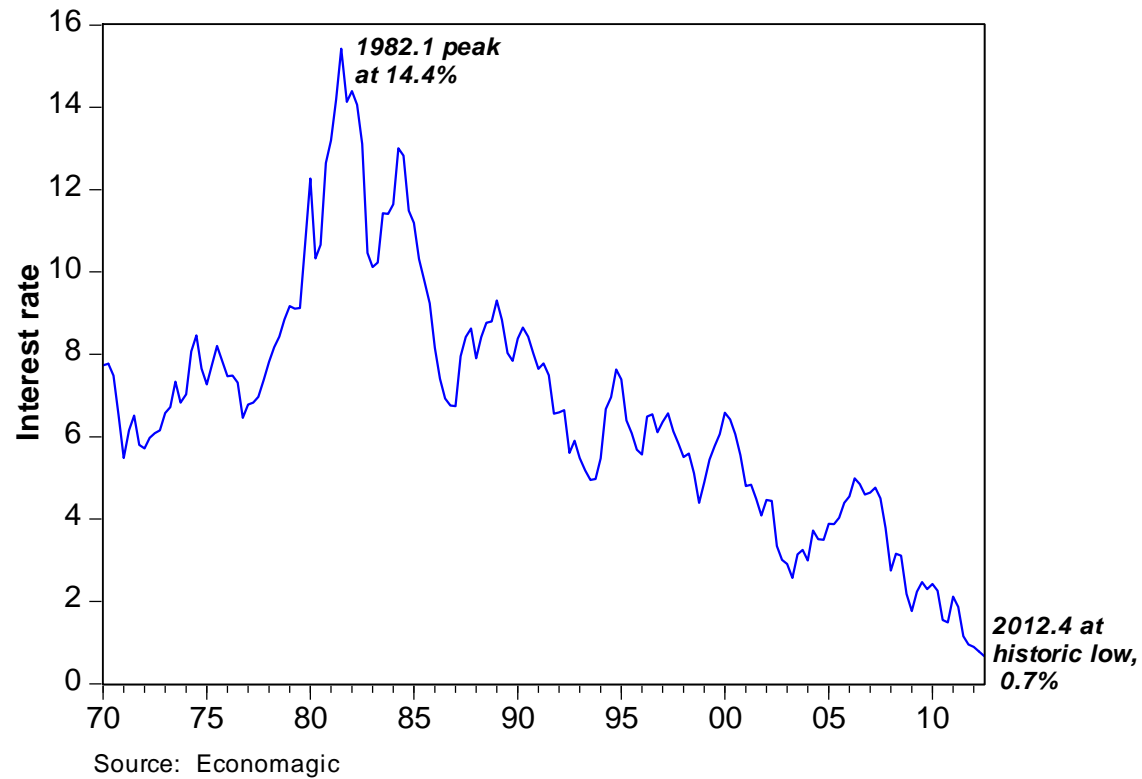


Prof. John Taylor on Rising Debt/GDP Ratio

- *“Its soaring upward climb resembles the fireworks on America’s Independence Day. But rather than remind us of America’s founding, it portends America’s ending. I carry a version of the chart in my wallet and show it to my students, and to my children and grandchildren, because it’s their future on the line,” (p. 101).*

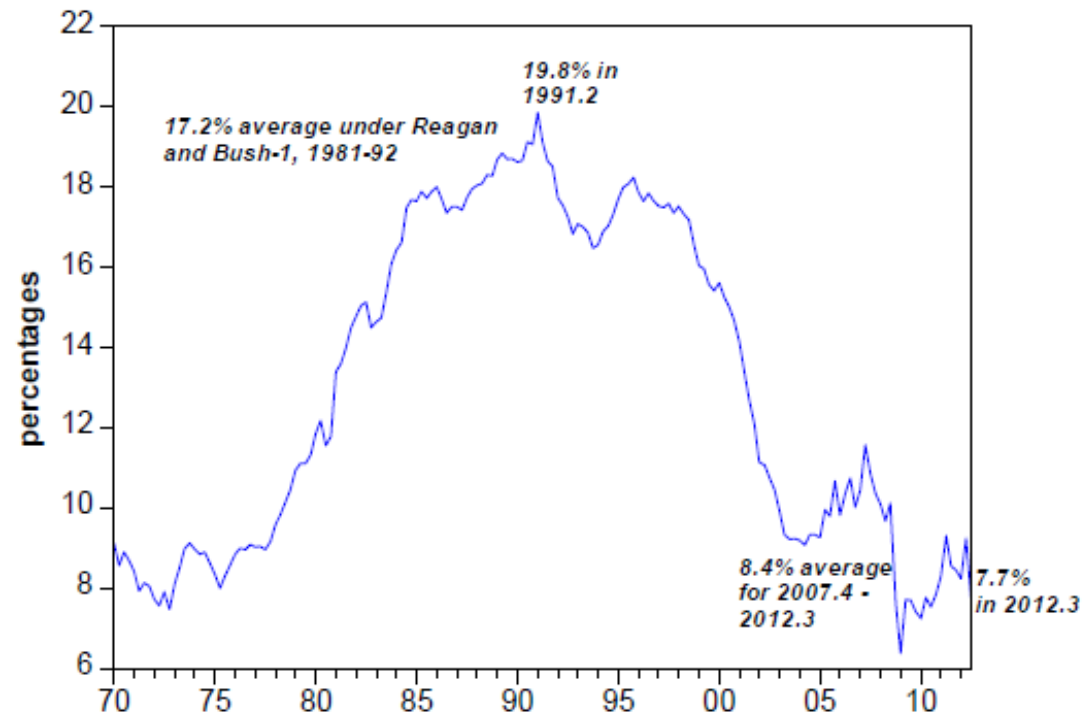
Interest Rates?

Figure 2. Interest Rate on 5-Year U.S. Treasury Bonds



Debt Burden?

Figure 16.8
U.S. Federal Government Interest Payments
as pct. of Federal Expenditures



Source: U.S. National Income and Product Accounts

Macro Policy Imperatives for Now

- **Fiscal Policy: *New Round of Fiscal Stimulus***
 - Focused on direct government spending
 - State & Local Governments
 - Education, Health Care, Public Infrastructure
 - Green Economy
- **Monetary Policy: *Carrot and Stick with Bank Cash Hoards***
 - Maximum reserve requirement/excess reserve tax
 - Expand loan guarantees for small businesses
 - Measures will have almost no fiscal impact