Krugman and Keynes to Obama and Lagarde: Get Real!

By Steve Weissman, Reader Supported News

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" I read the New York Times, it's where I get the news. Paul Krugman's on the op-ed page, that's where I get the blues."

The Krugman Blues

Loudon Wainwright III

Some people call him a sage or super-guru, others compare him to hemorrhoids. But, love him or loathe him, Paul Krugman has become a pivotal figure in our economic conversation, both in the United States and in Europe.

Having a platform at the New York Times helps, though it has hardly kept his stable-mates Tom Friedman and David Brooks from regularly spouting nonsense, especially about the economy. Having a Nobel Prize in Economics adds credibility, though the Swedes gave the same award to Margaret Thatcher's Austrian guru, Friedrich Hayek, whom Krugman correctly called "a Zombie" and "not an important figure in the history of macroeconomics."

Krugman's place in the debate comes more from his ability to explain complex issues with clarity and wit, and from a way with words that many of his fellow economists - and journalists - envy in unseemly ways. More than most of his peers, he has also shown a moral sensibility that echoes the outrage of anti-austerity protesters on the streets of Athens and Madrid. Almost a year ago to the day, in Spain's "El Pais" as well as the NYT, he castigated the International Monetary Fund (IMF) and policy-makers of the European Union (EU) and the European Central Bank (ECB) for imposing "economic suicide" on so much of Europe. He called their actions "Eurodämmerung."

On British television last spring, he chided the country's coalition government for applying the same deadly poison to their own economy. "None of this is about fiscal responsibility," he told leading Tories. "It's not really the budget deficit that concerns you. You're looking for a way to exploit the deficit situation to pursue an [ideological] agenda."

In America, Krugman has repeatedly explained why the federal debt and deficits do not currently pose a pressing problem, especially not at a time when inflation is low, growth is weak, and interest rates are close to zero. His logic reached back to the British economist John Maynard Keynes, whose observations on how macro-economies work still have relevance for times like the present. But, before we consider his ideas, we need to clear away some mental cobwebs.

Contrary to the rumblings of the undead, Lord Keynes was never a raving lefty. He dismissed Karl Marx, had no time for the "labor theory of value," left plenty of room for "the market," and found the bourgeoisie far more enticing than the working class. Nor do his ideas necessarily lean to either right or left. Deficit financing, the major tool of Keynesian economics, has been used in the United States less to fund welfare programs than to pay for World War II, the military-industrial complex, and the wars in Vietnam and Iraq, while Hitler did not need Keynes to use deficits in Germany to grow the Third Reich out of the Great Depression. On its own, the approach does not solve structural problems in the economy, whether caused by business, labor, or misplaced regulators, and does not tell us how to create self-sustaining growth that will preserve the planet. All that said, Keynes and Krugman do point us toward the beginning of a rational economic policy. The rule of thumb is simple. When times are tough and the private sector pulls back, borrow or print money to stimulate demand. When growth returns, pay down the borrowing, an essential follow-through for both Keynes and Krugman. Timing is crucial, and now is the time to spend to promote growth, not to cut back in the name of austerity.

In a way, Krugman has already won the argument. Berkeley's Brad deLong and Harvard's Larry Summers, who was Obama's chief economic advisor, used mathematics to explain "Fiscal Policy in a Depressed Economy." Top economists at the IMF performed their own math exercise, which led managing director Christine Lagarde and European officials to begin moving to loosen fiscal targets for troubled economies and to give Portugal and Italy an additional seven years to pay back their bailout loans. The IMF has also warned British Chancellor George Osborne that he is "playing with fire" by pursuing austerity too aggressively. As for Obama, he has always understood the need for federal spending to stimulate the economy, even if he is now agreeing to cut Social Security and increase Medicare payments as part of "a grand bargain" to trim the deficit - or as Professor Bill Black calls it, "the grand betrayal."

And just this week, one of the leading arguments for austerity and against stimulus - Carmen Reinhart and Kenneth Rogoff's "Growth in a Time of Debt" - was found to have a major spreadsheet error and some questionable statistical techniques.

Intellectually, this is where the great debate now stands, especially in Europe. As London's "Financial Times" editorialized last week, "It is increasingly clear to the Eurozone core that there is only so much left to squeeze from the periphery." But politically, no one with any power - not even French President François Hollande, who taught economics at his country's top graduate schools - has stepped forward to carry Krugman's winning argument to its obvious conclusion. Why not join together in all of the troubled economies to throw off the suicidal austerity and move stimulus into high gear? Why not indeed?

I can think of at least a dozen answers, from Obama caving in to deficit hawks, many of them on Wall Street, to the influence in Europe of German Chancellor Angela Merkel and the die-hards at the Bundesbank. But, if Obama, Lagarde, and Company fail to use available Keynesian tools to promote growth, the Krugman Blues could change radically. As economic conditions continue to worsen in Europe and disintegration becomes more likely, new forces from the right or left will try to take matters into their own hands. And as Obama continues to betray the New Deal traditions of the Democratic Party, who knows how the Congressional elections of 2014 will impact Keynesian prospects, be they civilian or military?