

TW Notes on

Stephen D. King (2013) *When the Money Runs Out: The end of Western affluence* Yale Univ Press

He argues that we are in for much slower growth in the future and that both sides of the current debate about fiscal austerity miss this because of 'optimism bias'

We have taken economic projections for granted. Policies toward pensions etc have been based on this

Bob Gordon's (2012) six headwinds that will slow future US growth, perhaps ~~to~~ by one half or more of the 1.9% average from 1860 to 2007

demography, education
inequality, globalization
energy / environment, debt overhangs

①

4 yrs after peak end 07 US
GDP up 0.8%

Ave. for post war cycle 913.77
worst before 7.7% after 70s oil shock

Adam Smith need economic
growth to keep economy from
fragmenting
loss aversion
sense of entitlement

Can't meet pension projections
illuminary wealth used to
fuel consumption before crisis
assumption of high returns on pensions
to meet expected pay cuts

Budget deficits + over optimistic
growth rate projections

late 1990s US fiscal surplus
Quickly changed $T \downarrow + G \uparrow$

"Western economies were on fiscal
life support long before the
crisis happened" p 67

(2)

Fed forecast mid 2010	actual	growth
2010 2.9 - 3.8	3.0	
2011 2.9 - 4.5	1.7	

skeptical of QE

"Monetary policy works for the most part through its impact on people's expectations" p 77

The more a pension plan is underfunded the more \downarrow t_i \Rightarrow \uparrow in cost of provisioning pension short falls increase $S + CV$

When manipulate govt bond yields "the anchor for all asset values is slowly eroding" p 77

CB implicit guarantee of govt debt - its awash with liquidity while private economy starves. Few will respond to take risk \downarrow (except for stocks) because of bleak outlook

Form of financial repression

NY rate depreciation "borderline tax on domestic income" p 81

Zombie and regulatory traps

To stimulate the economy central banks need to convince that inflation will rise and they won't increase interest rates

The sensitivity to exchange rate changes has declined in UK falling share of manufacturing and exports

output gap estimates are unreliable

US 2000-07 +10 million jobs
but -2 in manufacturing
+ 2 in construction

Because of structural shifts macro stimulus can't generate a big increase in jobs

Krugman appears to suffer from a "Depression fetish" 118

Risk of Trust

Trust Confidence in Congress 31% in 1972 72%
81% dissatisfied with way US is governed

3 Schumi

1 Income Inequality

importance of why it's unequal

"the financial system gives beliefs - and beliefs about beliefs..." 169

2 Growing Old Disgracefully

"We are on the verge of an intergenerational cost war" 171

for fiscal 2010 est that state government pension gaps = \$1.38 Tr

3 Declining Trust Between Creditors and Debtors

"we are about to witness the politicization of global capital flows" 174

Greater potential political risk for int capital flows
Capital will stay at home

Ch 8 From economic disappointment to political instability

"Without economic pain, the urgency of reform is reduced but, without reform, the risk of continuing stagnation only rises" p 181

Macro policies designed to promote stability may produce instability

Panic of 1873 started with collapse of
Viennese stock mkt

65 mo of contraction Great Depression
only 43

Byran Law of Gold 1896

Same Parallel with today

"The twenty-first equivalents of a near-
universal gold standard or the global
dollar standard... and, within Europe,
the euro" p 190

[But there are important differences]

"The story of the late 1990s Asian crisis
can be simply summarized"
having been forced to recognize recession
they had lived beyond their means,
the nations involved took their pain
up front but were then able to
recover strongly" p 192

In 1998 the crisis countries GDP
fell from between 6 (K) + 13% (Indonesia)

Western reaction "a lazy imperial
assumption of economic and financial
superiority" 195

(6)

To regain previous level of GDP
took Korea 7Q's, Thailand, 19, and

Indonesia 22

10 years later they were 30 (Indonesia)
to 55% higher (Korea).

He misleadingly describes the
crisis as "a man panic on behalf
of Asia's foreign creditors in light
of evidence - however limited - that
the game was up. Someone
should fire, the creditors ran
to the exits" 196

There's no discussion of the
behavior of the borrowers

He puts all of the problem as being
dependent on foreign capital

Mahathir in Malaysia blamed
foreign firms while the Koreans
pulled together and worked hard

It would be believe Western public
would accept such a sudden
large fall in their standard of living
Wages cut

The Asian's need narrative
to explain what had gone wrong
and then varied across countries

The West doesn't yet have a narrative
(He must mean generally accepted) ⑦

[?]

Ch 9 Dystopia

The euro crisis narratives have the Germans and Greeks blaming each other

Protectionism is likely to be strongest in finance with greater home bias in banking

"A home bias would... surely be the death knell for the eurozone" p 218
[too strong]

The problem today is fundamentally different from the 1930s when there weren't so many entitlements

~~to~~ He thinks there's considerable risk the eurozone will breakup because of the lack of "political glue" 224

The Great Depression started with the failure of an Austrian bank due in part to the ending of French assistance to Austria because of political issues

"We are in danger of letting a culture of blame and mistrust develop" 227

The return of political extremism
(8)

"Global capital markets and autonomous nation states do not sit happily side by side" 226

"We may have reached the limits of what globalization can achieve" 228

Ch 10 Avoiding Dystopia

Surplus countries often display a 'moral inconsistency' since surpluses must match deficits 237

"drop the idea that creditors are somehow morally superior"

The Eurozone members need to recognize "that monetary union succeed only if they are accompanied by fiscal union" 237

"The great advantage of an independent monetary policy is the ability to delay until ~~tomorrow~~ tomorrow what otherwise might be necessary today" 239

"Dealing with time" - outpunching the future" 241

Constitutional social contract between generations

"inflation targeting is too narrow an ambition" 246

" [Inflation targeting] creates an illusion that monetary policy is somehow 'neutral' [while it's all the time] creating both winners and losers" 246

" Moreover, it suggests that monetary and fiscal policies are completely separate" 248

He favors nominal income targeting

" If capital cannot go to where labour is, let labour go to where capital is" 252

" The main lesson for policy-makers surely, is the need to recognize that the world is an inherently uncertain place which does not respond well to simple macroeconomic macroeconomic rules ... " 253

Major crisis can be associated with banks of all sizes" 255

" ... banks are faced with a series of potentially inconsistent objectives" 255

Before the crisis " banks were under huge pressure from shareholders to deliver higher returns" (255) so they took on more risk

"The dismal science has become a
dismal failure" 258 To much
reliance on math and not enough
on history