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The Crisis Is Over: Welcome to the New Crisis

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ECONOMY

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Illustration by Adam McCauley

Robert J. Gordon, **The Rise and Fall of American Growth: The U.S. Standard of Living since the Civil War** (Princeton University Press, 2016)

Adair Turner, **Between Debt and the Devil: Money, Credit, and Fixing Global Finance** (Princeton University Press, 2015)

Jacob S. Hacker and Paul Pierson, **American Amnesia: How the War on Government Led Us to Forget What Made America Prosper** (Simon & Schuster, 2016)

A TOP SHELF PICK

It's been quite a decade for the global economy. The popping of the American housing bubble in 2006, the subprime mortgage financial crisis and its spread to Wall Street in 2007–08, the collapse of the world economy into the first global recession in decades in 2008–09, the knock-on eurozone financial crisis that began in 2010, and a slow, often faltering recovery — it's been a tumultuous 10 years. And the period has produced a bumper crop of excellent economics books by academics, journalists, and practitioners who have attempted to grapple with the extraordinary macroeconomic disaster. They have examined why it happened, how to fix it, what it means, and how to avoid a recurrence of anything even remotely as hellish.

But we may have arrived at a crossroads. Recently, Martin Wolf's *The Shifts and the Shocks: What We've*

Learned — and Have Still to Learn — from the Financial Crisis (one of *s+b*'s top economics books of 2015) and Barry Eichengreen's *Hall of Mirrors: The Great Depression, the Great Recession, and the Uses — and Misuses — of History* (which received a highly favorable review in *s+b*) put a capstone on the intellectual structure of analysis on the crisis. And this year, in my view at least, the most compelling books on economics are widening the lens. Only one of the three, Adair Turner's *Between Debt and the Devil: Money, Credit, and Fixing Global Finance,* deals with the 2006–10 period. The others take a broader view. Robert J. Gordon's *The Rise and Fall of American Growth: The U.S. Standard of Living since the Civil War* tries to make sense of the economy not in a five-year period in the recent past but over the entire 150-year sweep starting in 1865. Jacob S. Hacker and Paul Pierson's *American Amnesia: How the War on Government Led Us to Forget What Made America Prosper* argues powerfully that the voluntary donning of ideological blinders has made U.S. economic policy lousy and the country's political economy so badly dysfunctional.

In *The Rise and Fall of American Growth*, Robert J. Gordon, a professor of economics at Northwestern University and one of our greatest economic historians, paints a pessimistic picture. It's unappreciated that for much of history, growth in economic frontiers — what we would call development markets — was actually quite low. The era of modern economic growth got started only in 1870, with the simultaneous advent of the iron-hulled screw-propelled oceangoing steamship, the submarine telegraph cable, and the industrial research lab. It was then that the pace of growth kicked up a notch to a steady, long-term per capita economic growth rate of 2 percent per year. That may not sound like much. But it meant that in an average year, the share of the average household's resources that was needed to acquire what that household had acquired the previous year shrank by one-fiftieth. With a 2 percent growth rate, well-being rises faster, because the resources released by that growth for other purposes can be spent acquiring not just more of the same but all of the new goods and services that are the fruits of ongoing invention and innovation. Over time, as this growth compounds, it leads to enormous increases in economic output and standard of living.

But Gordon, whose pessimism is driven by data, believes this era of growth has come to an end: In the coming decades, frontier economies will see a measured pace of growth of only 1 percent per year. Why? Between 1850 and 1950, we saw the invention of life-changing technologies such as jet aircraft, telephones, indoor plumbing, gas cooking and heating, electric refrigerators, streetcars, automobiles, radio and television, antibiotics, and steel-and-concrete construction. Between 1950 and 2015, we saw the widespread diffusion of those technologies — and the coming of computers, mobile phones, and the Internet. But what comes next? Gordon says: less. You can only industrialize your society once, after all. And that slows down the pace of innovation. In addition, economies today face significant headwinds that they didn't face in the past: an aging population, an average education level that has hit a ceiling, rising income inequality and wealth inequality, and struggles to continue to run pay-as-you-go social insurance. Add it up, Gordon says, and for the first time, an American generation faces the possibility of not living better than its parents did.

Now there still are techno-optimists, those who point to the immense value creation emanating from Silicon Valley as proof that we may be in the second inning of the ball game rather than the ninth. I certainly want to be a techno-optimist. But Gordon's exhaustive research program — this highly readable book checks in at 784 pages — has knocked me back on my intellectual heels. After one plows through this volume, the boulder one must roll uphill to make the case for techno-optimism is considerably heavier.

The Devil We Sort of Know

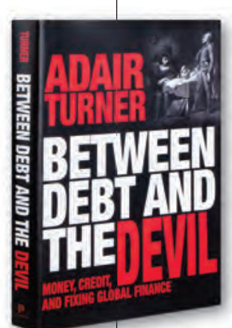
Over the last several years, it has often seemed as if the financial world has been turned upside down, what with negative interest rates, bailouts of huge banks, and a widespread shift from optimism to pessimism. Just as Robert Gordon wants to upend the conventional wisdom about growth, Adair Turner wants us to shift our thinking about debt 180 degrees. As head of the U.K. Financial Services Authority, Turner had a front-row seat at the first great global financial crisis of the 21st century. And *Between Debt and the Devil* has, at its core, an argument that I trace to an economist who had a front-row seat at the greatest global financial crisis of the 20th century. Taking a page from John Maynard

Keynes, Turner in effect argues that we are approaching the age of the "euthanasia of the *rentier*."

What does this mean? In the past, the world was poor enough, economic growth was fast enough, and the capital requirements of enterprise were high enough that the world was genuinely short of savings. As a result, society found that the promotion of enterprise required more than those who brought to the table labor, skills, knowledge, drive, technology, and a willingness to experiment and bear risk. But to get the capital that would turn these ingredients into growth, society also needed to induce those who would otherwise consume resources to delay consumption and deploy their capital. Thus the simple commitment of one's current purchasing power to an enterprise could command a healthy return, and one could live well as a rentier off the coupons from bonds and debt that were safe stores of value. On the plus side, this form of economic organization did induce people to mobilize savings and resources for the enormous capital investments needed for economic growth. On the minus side, this form of economic organization would inevitably lead to episodes in which debt securities that had been widely believed to be safe turned out not to be so — and there would then follow one hell of a mess.

In Turner's view, debt no longer has a productive role to play.... It's time to treat debt as a form of economic pollution and tax it.

Now, however, we are in an age of what Larry Summers, the former Treasury secretary and Harvard University president, calls secular stagnation, in which low growth, low interest rates, and low prospects for innovation make it unattractive for people to deploy capital. Because too much cash is chasing too few opportunities, the mere willingness to postpone consumption no longer commands a real return, as anyone who has tried to augment wealth without taking on risk since 2008 knows very well. Indeed, there appears little prospect that the mere willingness to postpone consumption will command a real return as far out into the future as financial markets forecast. As of July 2016, some US$13 trillion in bonds around the world were carrying *negative* interest rates. This state of affairs is metaphorically killing off the rentiers.

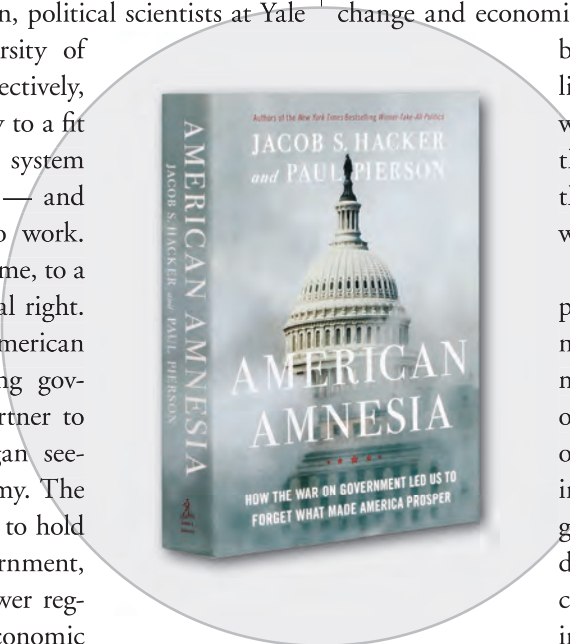


Turner's insight is that in such an environment, debt no longer has a productive role to play. And yet it still carries its dangers. And so it's time, Turner argues, to treat debt as a form of economic pollution and tax it. Labor and skills and knowledge should be recompensed with wages and salaries. Technology should be recompensed with royalties and licensing fees. Drive and willingness to experiment should be recompensed with profits and options. And a willingness to bear risk should be recompensed with equity returns. But, in Turner's view, the era in which debt is good and we can look benignly on high or increasing leverage is over — if it ever truly existed.

Turner concludes that we need to revise economic policy and economic policymaking in two important directions. First, we must recognize that we will never be able to attain the perfected economic system. We will always face a choice of institutional imperfections. So we need much higher capital requirements and much stronger lending standards, and we need to build a political economy that can resist the howls of those who want to leverage up. Second, we need to abandon the belief that public policy can be reduced to simple and stable rules. The idea that it can be is, Turner argues, as much a fatal conceit as the now outdated belief that central planning could do the job.

The Decline of Pragmatism

The low yields on government bonds reflect a high level of faith in the functioning of the governments whose credit backs them. And yet, as political scientists Jacob S. Hacker and Paul Pierson write in *American Amnesia*, that faith may be misplaced. *American Amnesia* is the best business book of the year on the economy. In part it is my favorite because its thesis runs exactly parallel to the thesis of my own book, co-written with Stephen S. Cohen, *Concrete Economics: The Hamilton Approach to Economic Growth and Policy.* Our thesis, and theirs, is that up until 1980 it was taken for granted in the United States that the public and private sectors were partners in a project of equitable growth. It was never the case that the government needed to take control. And it was never the case that what the U.S. needed was to drown government in the bathtub and let laissez-faire rip. Rather, the government needed to do its proper job of clearing the ground, opening up the space, setting up the playing field and keeping it level, building the institutions, and providing whatever support it could that would greatly add value to private enterprise. While government does the blocking, private enterprise takes the ball and carries it forward at great speed. This is how the U.S. developed from a group of poor, disconnected, agrarian colonies into a powerful, industrialized, integrated nation.



But Hacker and Pierson, political scientists at Yale University and the University of California at Berkeley, respectively, argue that the U.S. fell prey to a fit of amnesia. Our political system forgot how things worked — and how they are supposed to work. And the authors pin the blame, to a large degree, on the political right. Sometime around 1980, American conservatism stopped seeing government as primarily a partner to private enterprise and began seeing it exclusively as an enemy. The conventional wisdom came to hold that the smaller the government, featuring low taxes and fewer regulations, the faster the economic growth. This was, moreover, not a practical judgment but an ideological imperative. The deregulated low-tax laissez-faire market could not fail: It could only *be* failed. Policies that failed to deliver results could do so only because the policies were not extreme enough.

Hacker and Pierson tell a compelling story of the descent of first American conservatism and then the Republican Party from pragmatic engagement to ideological echo chamber. The story that struck me as most worrisome was the last one they told, which concerned the response to the 2014 Ebola virus outbreak. The U.S. government began to organize what seemed to all specialists and all those knowledgeable about infectious disease to be prudent and effective but not alarmist infection-control policies. And yet, the authors note, many influential commentators from various points of the center-right spectrum rushed to conclude that the response couldn't be trusted and would fail — simply because it was being conducted by the government. "What scares me is the fact that we can't trust the institutions that deal with such threats, and we can't trust the people who run them," said Ron Fournier, avowed centrist columnist at the *National Journal*. Talk-show host Glenn Beck said he believed the Obama administration had somehow targeted Dallas for infection because the city leaned Republican.

I do, however, think that Hacker and Pierson miss an important sociological cause and concomitant of the shift. They miss the Republican Party's transformation from a group of forward-looking enterprisers who think they can take advantage of the creative destruction that change and economic growth will bring to a group of backward-looking owners who believe that they are as rich as they will ever be, and who are under threat from the creative destruction that change and economic growth will bring.

These three books together paint a picture of the business, economic, and political future that is much more pessimistic than the one we were looking forward to only one short decade ago. Business in an age of slowed growth and greater headwinds, as Robert Gordon projects, must proceed more cautiously than business plunging into a third industrial revolution led by information and biotechnology. Yet, as Adair Turner convincingly argues, seeking to avoid risk and pull in one's horns is unlikely to produce wealth in an era in which debt is transforming from a means of mobilizing resources into a form of economic pollution. The ideologically fettered political economy Hacker and Pierson warn against is unlikely to enact and implement the proper policies to cushion the blows and take advantage of whatever opportunities remain.

That may not be the most uplifting possible set of messages to start us off in this postcrisis era. But, as Walter Cronkite used to say: That's the way it is. +

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