BOOK REVIEW

PAUL KRUGMAN WANTS A QUICK END OF THE ECONOMIC DEPRESSION[1]

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1. Krugman's main considerations on crisis and economic recovery

In his book *End This Depression Now!* Paul Krugman tries to find some solutions to the lasting economic depression, mirrored by a low rate of growth and high level of unemployment. It is obvious that during the last three years (2010-2012) the economy of the most developed countries passed through a disappointing stagnation with a major contribution of austerity policies. But Keynes said that austerity had to be applied during the economic growth not when the economy was decreasing, and based on this idea Paul Krugman pleads for more government spending in order to support private sector and economic recovery.

Paul Krugman has resumed part of his assessments made in his previous book *The Return of Depression on Economics and The Crisis of 2008* referring to recent financial and economic crisis. He questions Ben Bernanke optimism about economic outlook expressed in an interview in March 15, 2009 and afterwards and also his view on so called *the economy of happiness*. From USA to China the most pressing matter is now the high level of unemployment, and Krugman refers to involuntary unemployment and combats with stupid ideas of some American right wing politicians and economists that many unemployed people do not want to find jobs. How many unemployed people exist now in USA? Nobody knows exactly, the official figure was over 13 million in December 2011, (12.2 million in December 2012), compared with 7 million in the fall of 2007, but many people have now part time jobs and this represents a kind of hidden unemployment. In June 2011 Democracy Corps made a survey and found that over 40% of total American families had been affected by the cuts in the number of worked hours, salaries level and non-wage benefits. Long term unemployment is a painful reality and its social effects are extremely negative, especially when it concerns many young and even graduated people. A protracted period of unemployment can badly affect for a long time the vocational career and even the life of many young people.

In 2008 and 2009 the contraction of economy, measured by GDP decrease, was quite impressive and the recovery was slow and limited. In USA the estimation of real potential of GDP made by the Congressional Budget Office at the beginning of 2012 indicated a deficit of 7% in the operating potential of American economy, which means a loss of 1000 billion $ per year and a total loss of at least 5000 billion $. This huge loss signifies goods, salaries, profits not achieved or materialized. For Krugman paying attention mainly to long term perspective is a mistake, because short term difficulties, economic and social, will badly impact on long term economic development. The loss of investor confidence, the decrease of funds assigned for education and health, postponing infrastructure projects will have very negative effects on the future economic development. European Union was also seriously disturbed by the crisis and now Southern Member States are facing a lot of difficulties caused by the deficits, public debts and high unemployment. We may see a certain revival of extremist and nationalist movements due to the dissolution of middle class, but their risk is not comparable with that of the totalitarian regimes from 20th century. For Krugman there is a huge human disaster caused

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by the crisis but there is no excuse for political leaders not to take appropriate measures because we have the necessary knowledge and action tools for solving the economic problems and to end the depression as soon as possible.

After *The Great Depression of 30's* Keynes noted that we had enough resources but not enough expertise in the field of economics, while nowadays we have even more resources and much more knowledge in economics but we have serious deficiencies or troubles in the organization and coordination of market economy. Krugman believes that economic morass is the result of decades of applying wrong policies and bad ideas, harmful to most people but useful for a small minority. Solving the crisis is not easy and also not very difficult because it requires intellectual clarification and political will. For Krugman everything revolves around demand, the decrease of consumer demand led to output and investment reduction, diminution of public expenditures, economic recession. He combats the stupid assertion that general lack of demand cannot affect the economy and gives a famous example with the babysitting association in order to draw the following conclusion: *your spent money is my income and my spent money is your income.* If this clear conclusion is ignored and citizens and governments spend less, deficits and troubles will occur sooner or later. Less demand means low capacity utilization and less income. Now economy is facing coordination failures more than the lack of output capacities. Due to the losses recorded during financial crisis many people have reduced their demand, they spent less revenue, buy less goods and save more money. The amount of credit has been drastically reduced due to the banks attitude and debtors difficult position, forced to cut their expenses, as a result incomes and employment collapsed and the only solution seemed to be the strong increase of money supply. Since 2008 Fed has tripled the money base without any visible effect, that is why a legitimate question looms: *can we revive the economy with more money?* The answer is very simple: we cannot now due the liquidity trap.

Before the financial crisis, US economy had two engines: housing construction and consumer expenses based on higher and higher prices of houses, but the breaking of housing bubble led to economic depression. Fed tried to increase money supply and reduced the reference interest to almost zero in 2008. We have a liquidity trap when there is enough money or liquidity but the demand remains at very low levels due to the fact that there are too many debts, less borrowed money, less consumer spending, less confidence of creditors and investors.

There are structural problems related to modern economy, produced by a rapid increase in labor productivity, but it is not retraining a part of labor force and moving it in other sectors the main problem of American economy but the strong demand contraction that induced a setback of private sector despite the increase of money supply. After 1937 depression, American economy revived during the Second World War when the administration had strongly increased its military expenses which fueled a powerful economic recovery. For Krugman governmental expenditures create consumer demand which is the engine of economic growth.

Do we have now a new economic thinking or have we returned to the ideas of famous past economists like John Maynard Keynes, Irving Fisher or Hyman Minsky? Why is a great economist like Minsky, long time marginalized, so important and useful now? Because he launched the financial instability hypothesis based on the increase of indebtedness for supporting investments during the economic stability periods. The accumulation of debts in relation to assets and income or the increase of indebtedness finally leads to financial and economic crisis. Krugman thinks that making financial debts for investments and growth is a good thing, but for a family or a company is not suitable to accumulate high debts which make you vulnerable to difficult situations like loss of assets value or sales volume.

It was the great American economist Irving Fisher who disclosed in 1933 that a sudden economic decline may lead to a debtor race or panic for hastily paying their debts and consequently to a deflation period mirrored by a general decrease of prices and an increase in currency purchasing power. More the debtors try to pay more they are indebted. For Krugman the difficult situation of world economy is revealed by the fact that the debtors cannot spend and the creditors do not want to spend. Within EU highly indebted countries, like Greece, Spain, Italy, cannot easily borrow money now due to their difficult financial situation, they are assisted by European Central Bank and other euro countries, like Germany, through European Stability Mechanism, but they were forced to apply tough austerity programs. But austerity measures were enforced also by other EU countries with a low public debt, like Romania, or with a relatively strong financial position, like Germany, which may badly affect global demand.

Borrowing money is not a risky activity when there is a boom of economy, although it may provoke a future crisis, especially when a break of a speculative bubble appears and the high risks of debts blow out. The Minsky moment or Wile E.Coyote moment is the truth moment when an economic collapse happens due to high debt risks assumed by the population and economic agents.

Between 1929 and 1955 the debt of population increased 4 times in US, but due to inflation and economic growth its share in GDP had marked decreased. The huge boost of private debts between 1929 and 1933, during the Great Depression, points to manifestation of deflation by debts when depression and deflation aggravate the debt burden. Krugman blames Republican Party policy after 1980 focused on deregulation, liberalization and accumulation of huge public debts starting with first Ronald Reagan Administration.

Is the austerity and prudent attitude based on cutting the expenses and costs and paying the debts the only solution for remedying the difficult financial situation of population? Krugman considers that *the combination of liquidity trap with prolonged effect of excessive debts pushed us to fail on the realm of paradoxes.* One of them is the saving paradox, when there is an economic depression saving much more money does not stimulate the investments and leads to income contraction and economy restrain. Other two paradoxes are: the de-indebtedness paradox revealed by Fisher and the flexibility paradox described by Gauti Eggertsson, referring to the effect of wage cutting on employment. For Krugman cutting the wages through labor flexibility is a mistake because it leads to income reduction while the debt level remains the same. Someone needs to spend more and borrow more money and this is the state, so Krugman embraces Keynes opinion favoring more government expenses for overcoming the economic depression and deems that a certain level of inflation will diminish the debt burden and have other positive effects.

Krugman blames Alan Greenspan for misinterpretation of the role of financial derivatives which led to the reckless lending, huge debts and high credit risks. Due to what happened with commercial banks during the Great Depression, new and important legislative regulations were adopted in the 30's, but starting with the 80's the deregulation process and the delay of regulation updating played an evil role in the massive increase of debts and the following crisis.

People who invest money have to choose between liquidity and earnings, but a bank provides liquidity for deposits and earnings by giving credits or loans. But a sudden loss of trust on behalf of depositors or a panic situation may cause massive withdrawals of deposits, strong devaluation of bank assets, bankruptcy of many banks. The ratio between equity and raised funds within bank assets had considerably decreased in more than a century, from 20-20% to around 5% and this explains banks vulnerability to panic situation and creating a lender of last resort(central banks). US Congress adopted in 1933 Glass-Steagall Act (abrogated in 1999) in order to protect the banks and economy against massive withdrawals, also by setting up a public agency to guarantee bank deposits-FDIC, by establishing a system of deposit insurance and by limiting banking activity to granting loans. The activity of commercial banks was clearly separated from the activity of investment banks and other savings and credit institutions. The deregulation activity which started in some service sectors in the 70's leading to an increased competition and efficiency had stimulated the deregulation of banking activity which attracted to taking high risks. A strong increase of loans and risks involved in lending activity created great difficulties in many banks. Clinton Administration supported the removal of prohibitions separating activities of commercial banks from those of investment banks which encouraged risky derivative operations. In 2007 non-regulating *parabanking sector* surpassed in size the traditional banking sector, but the risks amplified and the debts accumulated to a large extent and financial crisis finally erupted.

In Krugman's opinion *The Big Lie* of financial crisis is to blame the US Congress for market deregulation and liberalization and not the banks for disastrous lending policy. Poor people had benefited from legislative deregulation and from cheap lending but there were many assets and markets unrelated to lending to the poor. Most risky credit activities were carried out by deregulated private creditors and not by Fannie Mae and Freddie Mac, the two public agencies involved in the procurement of housing loans. Financial deregulation started in 1982 with Garn-St.Germain Act for supporting savings and loans of popular banks but this led to a classic case of moral hazard. A lot of credits were granted to real estate developers and finally taxpayers had to cover losses amounting to 130 billion $. In the 90's commercial banks were facing serious difficulties due to huge loans offered to the developers of commercial premises. In 1998, when the financial crises haunted in East Asia, the failure of an important hedging fund like Long Term Capital Management was avoided with the financial assistance of New York Federal Reserve. Financial leaders, like Alan Greenspan, praised deregulation excessively, on the ground that it would have led to improved economic performance. Financial deregulation had a small contribution to economic growth and household income, but a great contribution to the extraordinary income growth of some few people from financial sector.

The *second gold age* started after 1980 but only for very few people, like managers of hedging funds, investment banks, commercial banks, other financial agents and some few personalities close to them. It has been recorded an impressive income increase, but only for the top financial elite and their henchmen, representing 0.1% and 0.01% of US population. While financial leaders pathetic attempted to justify huge income differences and increasing social inequality on the base of higher education, Occupy Wall Street Movement claimed to defend the interests of 99% of population. Office for Budget of Congress (OBC) showed in a recent report that between 1979 and 2007 the share of the top 1% within the total net income increased from 7.7% to 17.1%. Based on Gini index in the same period half of total income growth was displaced for the top 1% of population. Very few among the top 0.1% have become enriched by creating valuable products or services, most of them are corporate managers who set their own salaries which are not tied to management performance. As for the managers of hedging funds, investment funds and banks the remuneration packages are extremely stimulating regardless of performance achieved, they may engage in very risky activities without any liability or penalty. Credulity of investors and depositors, lack of regulation and supervision by the authorities, large tax cuts for high incomes are the keys of their financial prosperity irrespective of their real contribution to the general welfare.

Paul Krugman considers the right wing orientation in politics may also explain the sudden and massive increase of high incomes, the financial deregulation, the proliferation of new financial institutions and financial derivatives. Increasing income inequality could have contributed to the accumulation of too many debts by the middle class and to a lower saving rate. A lot of money buys more political influence and this explains why politicians were blind to the risks of financial deregulation. Some important American authors, who have analysed the causes and implications of income inequality, are mentioned by Krugman. What it is very interesting and was noticed not only by Krugman is the fact that enough financial leaders had become important decision makers in public institutions, took important decisions in favor of financial sector and then returned to (other) financial corporations where they could effectively lobby politicians. Krugman has quoted Matthew Yglesias opinion on political leaders like those from EU countries who have lost the trust and respect of their own people but are valued by Davos Group, IMF, other supernational institutions, like Europeans ones, thus being able to get very good jobs in international institutions after leaving the office as a reward for their docility in applying austerity programs (maybe under the unspoken slogan: *I do not serve my country, I serve only the masters of universe)*. Krugman defines himself as a social liberal and severely criticizes the Republican Party for becoming the party of the rich in the last three decades.

One of the lessons and achievements of Great Depression is *macroeconomics,* which George Lucas jr. believed it could prevent new depressions, assertion that proved to be false, especially as many economists have frantically argued for financial deregulation. Krugman coined a suggestive expression: *a dark age of macroeconomics,* possible due to unfortunate combination between politics and theoretical sociology. Long time Keynes ideas were repudiated by right wing ideologists and their supporters from universities based on so-called similarities between state intervention in the economy and socialism of central planning and radical redistribution. In 1943 Michal Kalecki, a socialist thinker, spoke about the blackmail with the lack of confidence of economic agents or businessmen in government policy, today the same argument is used to fight against any regulation and state intervention. Very wealthy people do not accept Keynes ideas mainly on creating jobs by state. State intervention is strongly blamed, even monetary policy is rejected by keen conservatives as an effective tool to stabilize the economy. While Keynes did not like the idea of leaving financial markets at the mercy of speculators, nowadays liberal economists, like Eugene Fama, University of Chicago, blindly believe in efficient markets hypothesis, although large and rapid fluctuations and speculative excesses ought to raise serious doubts on markets rationality.

Krugman does not put a great value on econometric models that have been highly fashionable in recent decades. Theoretical model developed by finance economists, so-called *Capital Asset Pricing Model,* for determining capital value, was used for financial investments on Wall Street, for selecting securities portfolio, to value derivatives, to get Nobel prizes for its creators. Blind faith that modern science of finance economics keeps everything under control and markets recover quickly to normal operation after any depressive relapse is specific to notorious and influential persons like Greenspan and Fama. In the 60's and 70's the vision of monetarist school, led by Milton Friedman, was rather close to Keynes vision on recessions and markets, but meanwhile macroeconomics divided into two factions: *salty water economists* with a Keynesian vision and *fresh water economists* with an ultraliberal vision. Fresh water economists would be the purists of *laissez faire* philosophy, they consider ordinary people as rational human beings and markets as functional, they take for true one cannot have situations of general failure of demand and inflation is guilty of workers and firms confusion and implicitly of temporary recessions (as Robert Lucas jr. said in the 70's). Long time they questioned the value and utility of Keynesian theory, spreading a vision dominated by real business cycle theory which says recessions are a rational, even effective, reaction against adverse technological shocks. Neo-keynesian theory, opposed to Robert Lucas ultraliberal vision and questioning the perfect markets and their perfect rationality, was hosted by universities like MIT, Harvard, Princeton and by Fed and IMF. Neo-keynesian economists, like Christina Romer and Ben Bernanke, were able to advance useful response measures to recent crisis.

Although Paul Krugman is a great admirer of monetary policy he recognizes the limits of monetarist vision of Milton Friedman and the limits of monetary policy effectiveness in counteracting economic recessions. Tax incentives and government expenses, supported by neo-keynesians, have been rejected or hardly challenged by neoliberal or monetarist economists as potential effective tools in combating recessions.

Paul Krugman has investigated US Administration response to the recent crisis and thinks it was quick but not sufficient, if we take into account the high level of unemployment. In US and EU the governments and central banks intervened with cheap money policies and bank bailouts, but these actions could not create jobs and reduce unemployment significantly. Krugman disapproves Administration timidity on economic recovery measures and the rigid and inflexible position of right ideologists, economists, politicians on any state intervention. He analyzes the effects of real estate bubble bursting on housing and financial assets prices, the impact of Lehman Brother bankruptcy on banking sector, the generous and substantial financial assistance offered to banks by Fed and Administration (TARP), the absence of a solid recovery and stimulus plan for real economy(only 787 billion $) .Krugman and Stiglitz were not wrong criticizing Obama feeble plan because unemployment exceeded 10%, GDP growth rate was low, the increase of federal spending share accounted mainly emergency assistance given to citizens in need. It seems absurd for Krugman the attempt to save the economic system of 45 trillion $ (3 year GDP) with only 787 billion $. Achieving political compromise between Democrats and Republicans in US Congress was and still is extremely difficult and deterred Obama Administration to offer a greater financial assistance to real economy. Krugman advocates for a direct reduction of mortgage debts for more than 10 million Americans and shows the lamentable failure of Administration specific program. For him it is obvious that political games and intellectual confusion would have blocked economic recovery actions in USA.

The previous high public and private deficits became even higher during the crisis due to bailouts and other programs and led to public expense cuts and to a weak financial support for job creation. Krugman believes the lack of jobs is much worse than the burden of high deficits which are not an essential issue during an economic depression. The fear of budget deficits is enhanced by the fear of any attack from bond vigilantes, investors who sell a country's bonds when they have lost the confidence in its monetary and fiscal policies. But for US the costs for selling treasury bonds are very low so the Department of the Treasury may borrow more money and increase the public debt within a favorable market situation. The campaign for cutting the public expenses of debt hawks was based on a future and hypothetic raise of borrowing costs which has not materialized, the interest rates being at very low levels between 2008 and 2011 when US Administration borrowed more than 5000 billion $. At the end of 2011 and beginning of 2012 the borrowing costs were at the lowest level ever recorded.

The liquidity trap reveals the large amount of private sector savings, retention of firms to invest and the need for government borrowing and spending which expands the aggregate demand and consequently leads to absorption of excess of savings supply. The private sector savings provided the money for government borrowing in US due to 1000 billion surplus recorded per year (the difference between savings and investments). Krugman sees no competition for getting funds between budget deficits and private sector, as the government tries to use the savings surplus of private sector. The difference between short term interest rates (controlled by Fed) and long term interest rates (influenced by investors confidence) and their impact upon economic recovery explain why both remained very low in the last years. Albeit the deficits and debts are very high (as a share in GDP) US do not have any payment incapacity risk and it is in a better financial position than Japan and Great Britain. Euro countries like Italy, Spain, Portugal, Ireland and even Greece, with lower public debts, proved to be more vulnerable because they do not have their own currencies.

Krugman deems there is no problem with increasing the level of public debt when recording economic growth and inflation. As it was demonstrated the debt must not be paid but transferred to future generations, it has a high cost and it will burden the future but any fast payment may cause great economic difficulties. Krugman draws the attention upon the recklessness to concentrate on short term deficit. Due to liquidity trap a reduction of public expenses by 100 billion $ leads to a GDP decrease by at least 150 billion $ which involves a weaker economy, less revenues and a net debt cut of no more than 50 billion. When there is an economic recession any expense cut is not a good solution for strengthening the fiscal position and could harm the future economic recovery. To reduce the real debt value one may resort to partially debt canceling or to a higher inflation, or to replace a part of private debt with public debt. After Second World War the depression did not return in US because the robust economic growth and enhanced inflation had reduced the debt relative to GDP.

A good part of American right political spectrum, headed by Raul Paul, a proponent of Austrian School of Economics, is rather fearful of inflation caused by high deficits, huge bank reserves and dollar devaluation and blames Fed's hypothetic inflationary policies. But between 2009 and 2012 inflation rate did not exceed 2.0% on average and there is only one explanation: the liquidity trap. Fed has not printed money but bought financial assets, like treasury bonds, and gave loans to commercial banks against transfer of ownership of bonds. Fed acquisitions may lead to inflation by credit expansion in a period of economic boom, but now we have a prolonged recession. We do not have a stagflation period although energy and food prices have strongly increased due to the fact they haven't propagated to salaries. Consumer Price Index is used for calculating the inflation rate but Krugman brings into question *the core inflation,* without taking into account food and fuel prices, for measuring inflation inertia. Krugman is critical to those who challenge the official figures of US Bureau of Labor Statistics supported by MIT (Billion Prices Project) and advance aberrant figures on inflation. He thinks we need a higher inflation rate, around 4%, also considering the opinion of Olivier Blanchard, IMF chief economist. Firstly a higher inflation will stimulate borrowing money and will give more room for maneuvering monetary policy, secondly a higher inflation will help in reducing the real value of debts, thirdly the employees accept more easily a higher inflation than nominal wage diminution. The wages have not diminished in US, on the contrary they have increased to a certain extent and this explains why there was no deflation in US. But we cannot neglect the contribution of food and energy prices and of companies policy to cut the costs and not the prices.

Krugman makes a brief history of European integration and believes that European elites have overestimated the single currency gains. But for a country giving up to its own currency surely removes the devaluation policy as a means of adjustment to an economic shock. Instead one needs to cut the nominal wages to gain competitiveness and this is extremely difficult to accept by employees. Krugman insists on *optimal currency area,* concept introduced by Robert Mundell in 1961 which focused on labor mobility. Comparing EU with US one can notice the low labor mobility, lack of fiscal integration, poor economic governance. Cheap money policy, pursued by European Central Bank was a great mistake since it led to high indebtedness of Southern Member States and to huge housing bubbles. Large capital inflows fueled speculative bubbles and overgrowth of labor costs, and also recording of growing trade deficits within euro area. With the onset of the crisis production and employment have dramatically decreased, it swelled bank bailouts, debts burden and cost of financing them. For Krugman the *Great Illusion of Europe*, consists in the wrong belief that the sovereign debts crisis was caused in EU by fiscal irresponsibility, which may be true only for Greece. Until 2007 the public debt of GIPSI group as a share in GDP has decreased constantly, but once the crisis started it has sharply grown up. Although on overall the public debt and private debt are smaller than in US, inflation rate is quite low and current account is balanced, the situation differs depending on the considered country. For Germany dislikes the adjustment through inflation it remains only the solution of deflation for states with financial difficulties, hard to attain in the context of wages rigidity. In Iceland the strong devaluation of crown led to an important reduction of wages denominated in euro while in Ireland and Spain the wages have decreased only very slow and to a small extent with high long-term unemployment price. The heavy burden of high debts may be successfully tackled only through a combination of inflation and rapid economic growth. The single currency has still a drawback: some countries are extremely vulnerable to self-validated panic, they are not able to refinance their short and medium term debts due to the lack of interest of foreign investors or banks for their new issued bonds. EU Member States which have not adopted euro are doing better than the single currency countries while new recent members, like Slovenia, pass through great difficulties likewise. Saving the euro depends mainly on European Central Bank policy, the implementation of European Stability Mechanism, the fiscal and structural adjustment measures of Southern States, IMF financial assistance and access to private capital markets. Austerity measures focused on cutting the expenses and increasing the taxes could not have good results, on the contrary they emphasize the economic and social decay.

Much of bankers and financiers decided almost overnight to become the followers of austerity measures and in the spring of 2010 OECD recommended to US Administration a massive cut of budget deficit and to FED a high growth of short term interest rate, but the guidelines were not observed. Not the same thing did Great Britain and European Central Bank that had not taken into consideration the extent of unemployment and the consequences of austerity measures. Other institutions, like Bank for International Settlements, and influential economists and businessmen have argued in favor of austerity through tightening of monetary and fiscal policies. Krugman remarks lack of consistency of the arguments and frequent changing of explanations for *austeriens.* It is obvious that Greece bad example is used by the austerity adepts like a fright for imposing an urgent cutting of the deficits and debts based on ruined reaction of markets. One cannot deny the high cost of debts (public and private) but it is hard to believe or demonstrate with solid arguments that austerity could lead to economic expansion. Ireland and Canada are offered as good examples for reducing public deficits, but this was achieved during an economic boom as a result of a strong increase of fiscal revenues. Prime Minister of Great Britain David Cameron imposed an austerity program in the field of public expenses but the trust of companies and investors fell to a very low level and the economy has remained in a visible stagnation. On February 13, 2013 in a desperate attempt to revive the economy, Bank of England started a program for directly financing the corporations, including banks, by buying their bonds amounting to 50 billion £. When monetary policy is focused on targeting the inflation it is difficult to understand why OECD and ECB insisted on interest rate growth. Krugman does not agree with Raghuram Rajan from Chicago University who seems convinced that US must undertake deep structural reforms for improving supply side and not to revive former demand patterns. Schumpeter, Hayek and Rajan are included by Krugman in so-called *liquidatorist stream*, which considers one should not do anything to mitigate the consequences of a depression. John Maynard Keynes had explained why David Ricardo opinion on the fact that *an economy may not suffer from an inadequate demand*, although it is not truthful, has become a sort of axiom. All austerity policies are in favor of creditors (bankers), while central bankers and financial officials do not like excessive expenses and low interest rates.

Krugman proclaims his optimistic view on economic recovery, but recognizes that reducing income disparities is a difficult task and will take a long time. The optimistic official signals since 2009 proved to be soap bubbles as long as the employment rate of people between 25 and 54 year old remained around 75%. In Krugman’s opinion private sector in US does not want to spend enough money for full utilization of productive capacity and for offering enough jobs to millions of people. Krugman believes the government should take the initiative to spend more instead of private sector. More government spending means more GDP and more jobs, rising of consumers and companies confidence, funding from central and local level of enough projects with spillover effects. Krugman suggests a temporary and massive increase of public spending, especially for financial aid given to local and state authorities with the aim to create new jobs, to develop infrastructure projects, to increase unemployment benefits. Caught in a liquidity trap at the beginning of 90’s Japan had passed through a long stagnation period and in 2000 professor Ben Bernanke criticized Bank of Japan (central bank) for not taking appropriate measures, like those suitable for FED: increasing money supply for quantitative easing and offsetting the tax cuts, low interest rates (under 2.5%) for long term bonds, devaluation of dollar by means of central bank interventions, a higher target for inflation rate (3-4%) for a ten year period. As the Chairman of Fed, Ben Bernanke has adopted a passive position and not a resolute one, partly because of institutional conservatism within Fed and partly due to fierce Republican opposition. Refinancing or reducing mortgage loans proved not to be easy in US, although Obama Administration introduced Home Affordable Refinance Program, which was too cautious and too restrictive, while Federal Housing Finance Agency, charged with overseeing of Fannie Mae and Freddie Mac, had a totally inappropriately activity. Krugman also draws other action proposals, like a rougher attitude towards China in trade field, more severe environment regulations, policies for creating new jobs, promotion of sustainable development.

If US is a center-right country one could not accept major initiatives for new government spending, and electoral considerations usually limited any bolder actions in the field of economic and social policies. For Krugman the best strategy is the one not approved by target groups researchers or by prestigious newspapers, like Washington Post, but the strategy that brings good results. The quality and efficiency of economic policies depend on the color of US Administration, its control on Congress or what kind of majority exists, theoretical guidance of President’s counselors, internal process of decision within the Administration, lobby of interest groups. Krugman is deeply convinced that economic recovery is impeded by a lack of intellectual clarity and political will and that increased government spending would be critical for economic recovery, the evidence is offered by what happened during the wars and arms race. The level of taxes, on which depends the government spending, is in inverse proportion with the level of unemployment.

Krugman is firmly convinced that austerity impedes recovery, the only solution being a massive increase of government spending. IMF researchers identified 173 cases of fiscal austerity in the developed countries and discovered that after austerity policies there were recorded economic contraction and unemployment rise. Krugman cites Stiglitz and Romer as theoretical allies in supporting his ideas on fiscal policy role and importance of fiscal stimulus in creating new jobs and also on negative effects of budget deficit reduction on economic growth. Unfortunately according to IMF chief economist Olivier Blanchard and IMF economist Daniel Leigh, IMF used a mistaken calculation coefficient that led to underestimation of the negative effects of the crisis. The used multiplier is the coefficient linking the evolution of public spending or tax level to economic growth rate which may be in times of crisis 3 times higher than that used by IMF.

2. Some conclusions on Krugman's ideas

Definitely Paul Krugman is a demand-sider and also very fond of monetary policy, albeit he pretends to have a great admiration for Keynes and to be a social-liberal. Though one cannot deny the importance of monetary policy within macroeconomic policy one should mention that monetary policy is not able to solve any crisis or to prevent a new one when a speculative bubble will burst. He is absolutely right considering high unemployment as the main problem to be addressed to and to be resolved in US and other countries. The economic and social impact of the crisis was very high and was somewhat statistically measured, but Krugman talks about a huge human disaster and about the need to rapidly solve the economic difficulties and to resume a robust economic growth. It is true that consumer demand is the engine of economic growth and its contraction, due to high private debts, loss of revenues and jobs, led to economic depression. In US and EU increasing the money supply by the central banks could not revive the economy due to liquidity trap (demand is low due to high debts and lack of investors and consumers trust). Important past economist like Minsky, Fisher, Keynes are mentioned by Krugman for their valuable contributions to analysis of debts impact on crises, demand, public and private spending, while other famous economists, like Schumpeter and Hayek, are considered advocates of non interventionism during the economic depressions.

IMF is excessively and repeatedly praised by Krugman for its interventionist position of Keynesian inspiration. Maybe Krugman has not forgotten it was IMF that had imposed austerity policies in many emerging and transition economies which had benefited from its financial assistance, and the evil results of such policies were remarked even by IMF economists. Perhaps Krugman was disappointed when IMF economists have recently shown that IMF overall policy was wrong because it underestimated the negative effects of the crisis by using an incorrect fiscal multiplier. I was quite puzzled when I found out there was a study entitled "Growth in a time of debt" published in 2010 by two reputable economists from Harvard University, Carmen Reinhart and Kenneth Rogoff, former employees of the IMF, that was used to justify the austerity policies from USA and EU, which proved to be wrong, because it showed that in the countries with a debt of more than 90% of GDP the economic growth is negative, when in reality it turned out, three years later, that these countries may achieve a growth up to 2.2% per year. I think Kenneth Rogoff is right when he says that the huge public debt of USA may affect the whole planet and anyhow represents a real threat for the country's capacity to face future shocks. Another contradictory position of IMF economists is related to the correlation between fiscal deficit and current account deficit, the business cycle model GEM points to no short term effects and very reduced medium term effects of fiscal deficit on current account deficit, while the model developed later on by Michael Kumhof and Douglas Laxton indicates an instant impact of fiscal deficit.

In the past decades US and EU economies had three engines: housing sector, foreign trade sector and finance sector, the first and the third one facing enormous speculative bubbles caused by inflation targeting policy (cheap money), bankers greed and their risky activities (derivatives), financial deregulation and weak public supervision. After three decades of economic growth the main beneficiary of impressive income growth was the financial elite, representing only 0.1% of population but having a strong political influence. Krugman blames huge income differences and increasing social inequality because they were not based on true economic performance and a real and consistent contribution to general welfare. On the other hand many national political leaders have become the accomplices of financial oligarchy and a sort of mercenaries of international and supernational institutions. I could also mention the radical opinions of John Perkins who believes that political leaders from USA and probably from many other countries and people working within important national and international institutions (like World Bank) have become promoters of the interests of large corporations, which treat the citizens of developing states as slaves and are only interested in getting huge profits derived from the exploitation of their natural resources and cheap labor. For all less developed countries entered in the sphere of globalization and to the attention of international corporations, prosperity is a distant dream and only accessible by small and privileged categories that are very obedient and respond quickly to any foreign demands.

Krugman speaks about dark age of macroeconomics due to strong politics and ideology interference into field of economics. Keynes, the father of macroeconomics, was contested by right ideologists and ultraliberal economists, like Robert Lucas jr., and proliferation of econometric models induced the wrong idea that markets and economy are under an effective control. For Krugman salty water economists have a Keynesian vision while fresh water economists have an ultraliberal vision, although one can find ultraliberal economists also in universities like Harvard and MIT.

Krugman blames small financial assistance offered by Obama Administration under different programs, also its focusing policies on deficits reduction and the excessive anxiety of inflation. In EU cheap money policy of ECB and national central banks, speculative housing bubble, speculative capital inflows, persistent trade deficits explain the troubles from Euro Zone. Krugman criticizes the austerity measures and reveals the strong vulnerabilities of less competitive countries which adopted the single currency and recommends a higher inflation rate and stimulating economic growth. To exit from liquidity trap Krugman still envisages some monetary measures and to encourage economic growth he proposes a massive increase of public spending, opinion which is contrary to that of the libertarians challenging the efficiency of fiscal stimuli over time as generating a crowding out effect: the government spends funds that would be allocated more effectively by the private sector, and governmental investments focus too much on GDP quantitative component detrimental to qualitative one and to medium/long term productivity of investment programs. But on short term any quick economic recovery needs strong stimuli from the government given the reluctance of private sector to invest or to increase the output in the context of reduced consumer demand. One may discuss on the nature or specificity of these stimuli but I do not think about their necessity. Paul Krugman opposes to supply side policies, like those suggested by Raghuram Rajan, although he accepts the importance of financing targeted projects in the field of infrastructure or green energies. As regards the confrontation between demand-siders and supply-siders one cannot deny that the implementation of demand side policies, through accelerated expansion of credit, led to the financial crisis and there is an acute need for a reindustrialization process and also for sectoral policies in sensitive fields, such as energy, environment, competition, innovation, which requires significant changes on supply side. Maybe Raghuram Rajan is right when he says: "the worst thing the governments can do now is to oppose the adjustment, by supporting non-viable companies or by supporting through cheap credit the demand for the products of non-viable industries".

It is not clear that Krugman wants a tax increase because it seems to me that he does not like the classic tax reduction (on profits) proposed by supply-siders like Mundell and Lucas. It is obvious that due to the high burden of public debts and its financing costs, the public deficits must be reduced to a large extent and the growth of government spending cannot be achieved otherwise than through tax increases and/or large domestic and external loans. It is easy to criticize the austerity policy but it is difficult to find a viable alternative, any fiscal expansion may lead to a deterioration of fiscal deficit and current account deficit, to more borrowing and to worsening of public and private debt burden. On the other hand the government capability to influence the size of private deficits and debts, and their proper solution, remains very limited in the near future.

Another important source of revenues is represented by the funds raised through a complex policy, both at national/European level and at international level, against tax evasion, estimated at about 2000 billion euro for EU and at 2000 billion $ for USA . But the main tax dodgers are multinational companies and OECD intends to prepare an ambitious action plan in the first semester of 2013 to reorganize the international norms, poorly adapted to globalization and digital economy, that too often allow international corporations to escape entirely from paying taxes, particularly through transfer pricing policy. In February 2013 during G 20 meeting from Moscow, Angel Gurria, Secretary General of the OECD, said that during these difficult times of budgetary austerity the tax burden is likely to fall on the shoulders of SMEs and on the middle class if multinational companies pay small or no taxes at all due to legal subterfuges. Much of the money obtained from tax evasion could be found in offshore fiscal heavens where quite recently have been identified a lot of hidden funds, amounting to about 32,000 billion $. Another phenomenon is threatening the fragile situation of the middle class. At the end of 2012, in USA, corporate profit margins hit an all-time high (exceeding 11% of GDP as against 3% in 1985) while wages were at an all-time low (descending to 43.5% of GDP as against 53.5% in 1970). The corporate race after short term profits at the expense of paying more to the employees badly affects the consumer demand and implicitly the future economic growth. A legitimate question arises: if the middle class is heavily eroded by the crisis and budgetary austerity, will capitalism remain a truly democratic society?

I may agree with Paul Krugman when he considers the liberalization of capital flows may create financial vulnerabilities through sudden exit or entry of capital into a country, but I have serious doubts that a large public debt does not have harmful effects on the economy. USA may print and use their currency, dollar, to pay or cover any external deficit, and also may sell bonds for covering internal deficit to many other countries in the world, it is not the case with the other countries. It is obvious we are the witnesses of a fierce confrontation between the followers of Keynes and those of the Austrian school of economics. While the first ones are in favor of increasing the government expenditures for stimulating the economy, the second ones are accepting the essence of business cycle theory developed by Ludwig von Mises and Friedrich Hayek: the cheap money policy of central and commercial banks leads to unsustainable growth of money supply and to wrong investment decisions of private actors, financial crises appearing when supplying money can no longer be supported, recessions representing the necessary corrections for a more effective reallocation of resources.

One cannot deny that Paul Krugman and Joseph Stiglitz are right when they conclude that austerity policies have led to economic contraction in Southern Europe and to economic stagnation within the EU, but is fiscal expansion a viable alternative for euro countries when deficits and debts are very high? Any form of fiscal expansion, external or internal financed, may aggravate the public deficit and public debt and is practically impossible under the present financial circumstances when banks, markets, investors and consumers lost their confidence in the success of economic reform measures. In my opinion the debates and confrontations on economic policies may continue a long time but it is hard to find quickly any realistic solutions for getting out of the current economic situation and resuming a robust and sustainable economic growth. Do we face now with a crisis of capitalist system or a crisis of growth? Here's a tricky dilemma to be solved in the near future by the great specialists in economics, like Paul Krugman.