

THECURRENTMOMENT

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INTERVIEW WITH JEFF FRIEDEN

~~This website publishes an interview with Jeff Frieden~~ (<http://www.people.fas.harvard.edu/~jfrieden/>), a professor of international monetary and financial relations at Harvard University. Along with co-author [Menzie Chinn](http://www.ssc.wisc.edu/~mchinn/) (<http://www.ssc.wisc.edu/~mchinn/>), of Econbrowser (<http://www.econbrowser.com/>), Frieden recently published *Lost Decades: The Making of America's Debt Crisis and the Long Recovery* (<http://www.people.fas.harvard.edu/~jfrieden/Lost%20Decades/index.html>), an important account of the sources of the 2007-08 US debt crisis. Frieden is also author of *Global Capitalism: Its Fall and Rise in the Twentieth Century* (<http://www.people.fas.harvard.edu/~jfrieden/Selected%20Articles/Books/GlobalCapitalism/index.html>), as well as numerous articles on global political economy.

What are the stories right now that you think people either aren't paying enough attention to, or about which we have the wrong view?

Too many to list! Inadequate analysis of the causes and implications of the crisis. Too much focus on short-term fiscal issues when the real problem is long-term. And a myriad of others....

Let's turn to the Eurozone debt problem. The dominant view is that Greeks and Italians are corrupt, inefficient and lazy, and that is why they find themselves in this mess. What is your view of what is going on?

The Eurozone debt crisis is a microcosm of America's debt crisis. After 1999 Northern European investors lent very heavily to peripheral European countries – both to their governments and to their households. This lending/borrowing boom took place in part because these were rapidly growing countries, in part because EZ-wide common interest rates meant that real interest rates were largely negative in the fast-growing peripheral countries, in part because there were expectations that in the event of debt problems the ECB would bail out the creditors and the debtors. Eventually there *were* problems, and the bailout expectations were realized.

Sources of the debt differ from country to country. In the case of Greece, it was almost entirely due to huge fiscal deficits. In the cases of Ireland and Spain, the borrowing was entirely private, largely to finance housing bubbles – although when the crisis hit their governments were forced to spend heavily (and borrow heavily) to bail out their financial sectors.

It should be stressed that responsibility for the debt crisis lies both with irresponsible borrowers, in peripheral Europe, and irresponsible lenders, in Northern Europe. And if the crisis is not resolved, it is both the creditor and the debtor countries that will suffer.

The standard recipe for the recovery from the Eurozone crisis is austerity and structural reforms in the peripheries, plus some recapitalization of banks. Do you think this is the right way to go?

Certainly there is a need for austerity and reform in the debtor nations – they will have to cut back on consumption to service their debts. And a recapitalization of the banks will be necessary to avoid a financial catastrophe. But there will also have to be a major restructuring of existing debts. These debts cannot be serviced as written. Creditors will, and should, have to take major losses that both reflect their poor judgment and make the debts more realistically serviceable.

What do you think would address the trade and debt imbalances between Northern and Southern Europe? Do you think it can be done within the European monetary order?

Yes, but it will require changes in policy. The Northern European countries cannot continue to rely on exports to the South as the engine of their economic growth; and the Southern European countries cannot continue to rely on borrowing. At the level of the Eurozone, the ECB should explicitly declare its willingness to serve as a lender of last resort; and the member states should outline explicit and very clear ways in which they will make credible a commitment *not* to bail out errant debtors.

The hegemony of the demand for austerity is striking. It is offered as the solution to the Eurozone crisis, as well as to the American situation – the US Congress even created a supercommittee to find savings. Yet it seems odd to have such agreement around austerity in the midst of a potential double dip recession. What is wrong with the demand for austerity? How do you account for the strength of this common sense?

What is wrong is timing. We need fiscal and monetary stimulus now and for the next couple of years, until the economies are recovering. But over the next 15-20 years there is a real need for fiscal reforms to avoid an inability to cover the costs of major social programs. A reform of the tax code to make it more efficient – and to remove indefensible loopholes and deductions – would also be helpful.

The demand for fiscal retrenchment now, in the middle of a recession, is largely due to the very uneven impact of the crisis. Those in the upper income registers are not suffering so much – and they would be the ones mainly paying for a stimulus, now or in the future. Those in the lower half of the income distribution are in deep trouble, and are much more supportive of fiscal and monetary activism. What gets lost is the fact that as a country (or a union, in the case of the EU) there are national issues at stake: if long-term unemployment persists, it will drag down the rate of economic growth for everyone.

In the US, there is an influential view that we need to have continued expansionary monetary policy but contractionary fiscal policy. That seems to be the recipe of the moment, with the Fed even contemplating another round of quantitative easing. What do you think of this approach to inadequate demand and balance sheet problems?

It is the best option given the political constraints on fiscal policy. But it is second best. Fiscal and monetary expansion would be better, but at this point it seems impossible.

Debt, especially mortgages and student loans, have become a major issue over the past few years. What if anything do you think should be done about it? How should we understand the growing debt of American households in the past decades?

Why did Americans accumulate so much debt? Households responded to incentives. With real interest rates near or below zero, and housing prices rising continually, there were tremendous

incentives to borrow – reinforced by financial institutions' development of innovative instruments that made them ever more eager to lend.

What needs to be done? Households need to retrench: increase savings, reduce consumption. And many of these debts need to be restructured to reduce the real debt burden, either by negotiation or by inflation.

One thing that seems to tie the American and European situation together is the considerable growth of financial activity. Is there anything to the view that the last decades can be understood as a period of financialization? If so, what does it mean to say the economy has become financialized?

No idea. Certainly the financial sector has grown, and certainly some of that growth is pure rents. But it's also the case that a more efficient financial system is good for the economy as a whole. How to separate the former from the latter is very tough. Mostly I find the complaints about "financialization" to be simple-minded and ill-informed.

Related to that question, what do you think accounts for the 'bubbliness' of the US and Europe economies, and especially the scale of these bubbles? We have seen a number of different bubbles and credit crises – housing bubbles in the US, UK, Ireland, and Spain; sovereign debt events in Greece, Portugal, and Italy, perhaps even France. While there was the dot com bubble in the late 90s, and the East Asian financial crisis, those don't seem to have had the magnitude and systemic character as the latest period. What is, or isn't, different about what we're experiencing now?

As has always been the case, finance can make the good times better, and the bad times worse. There is no question that modern, efficient, financial markets can exacerbate asset bubbles (and busts). This is, in some sense, a price society pays – because the greater availability of credit is on net a good thing. I believe that the principal responsibility for assessing and managing the tradeoff lies with macroeconomic policymakers and regulators. Monetary policy should take asset prices into account; and regulatory policy should take the systemic implications of financial-institution decisions into account.

How optimistic/pessimistic are you about the ability of national democratic procedures to provide solutions to the current economic crises in Europe and in the US? What do you think of the recent proliferation of technocratic governments in Greece and Italy? Does the current crisis expose some basic tensions between capitalism and democracy? If so, how exactly?

It's all politics, and unless there has been a military coup I didn't notice, all these measures have been taken by democratic political systems – including the coming of technocratic governments. Capitalism and democracy are perfectly compatible, although (as in marriage) compatibility does not mean the absence of tension.

What are your views of the nascent protests (Occupy Wall Street, Indignados) developing in response to the introduction of austerity packages in Europe and the US? Are these movements a continuation of or a break with the anti-globalization movements of the past? Are they likely to fundamentally change public perceptions and government policy or will they have only a very small lasting impact?

I think of them more as a response to continuing trends in the deterioration of income distribution than related directly to globalization. It's too soon to tell if they will have a lasting impact.

What, finally, do you think the appropriate political response is to both these crises and their aftermath?

You mean by the populace, or by policymakers, or by me? No idea.

In general: I'd like to see fiscal and monetary policies that are both responsible and responsive to social needs; regulatory policies that are prudent without being prohibitive; and social policies that help equalize opportunity without squelching innovation. And let's not forget pie in the sky.

- <http://bit.ly/12KIK2u>

- ...
- **COMMENTS** *3 Comments*
- **CATEGORIES** *Uncategorized*

3 Responses to "INTERVIEW WITH JEFF FRIEDEN"

George Finch December 14, 2011 at 6:12 am #

It was a short post, but wished he was pressed a little more on his beliefs, namely:

He should have been forced to explain why he finds "the complaints about "financialization" to be simple-minded and ill-informed." Also wage deflation does not seem to bother him, as people are drawn to credit cards and refinancing homes primarily through the enticements, which suggest they are driven by superficial consumption, not stagnant incomes and increasing cost of necessities, including their kids education. His explanation is somewhat a leap, perhaps based on his lack of knowledge and experience with the lives of working people. Hard to believe the financialization idea is simple and ill informed.

He also suggest deficits need to be curtailed through entitlement reforms, primarily in health care cost (according to another book). Yet he does not even touch on the defense and war budgets. Why?

He may be on target, and he is more informed than moi, but would be nice to see someone ask him to answer these questions in another piece.

REPLY

from Italy December 15, 2011 at 8:33 pm #

Well, personally I think democracy in Europe is at risk, even if the threat at present is very well masked and in some way it's something new. Even if it is not Nazism or Communism or Putinism or whatever we already know, there is a degeneration in the democratic process of shaping European policies, and I think this became evident in the agreement reached few days ago, both in what was "agreed" and how it was "agreed".

REPLY

Armani Exchange Watch December 31, 2012 at 8:44 am #

With a little bit of care, your fine timepiece can last a lifetime.

Like any other piece of machinery, a watch must be cleaned, oiled and serviced on a regular basis. Still some online stores and sites are providing men watches of this brand in reasonable and affordable prices, but before buying, make sure that you are not being cheated.

REPLY

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