

Four Nations, Four Lessons

By N. GREGORY MANKIW

AS the economy languishes, politicians and pundits are debating what to do next. When we look around the world, it's hard to find positive role models. But as we search for answers, it is useful to keep in mind those fates that we would like to avoid.

The recent economic histories of four nations are noteworthy: France, Greece, Japan and Zimbabwe. Each illustrates a kind of policy mistake that could, if we are not careful, presage the future of the United States economy. Think of them as the four horsemen of the economic apocalypse.

Let's start with Zimbabwe. If there were an award for the world's worst economic policy, it might well have won it several times over the past decade. In particular, in 2008 and 2009, it experienced truly spectacular hyperinflation. Prices rose so fast that the central bank eventually printed 100 trillion-dollar notes for people to carry. The nation has since abandoned using its own currency, but you can still buy one of those notes as a novelty item for about \$5 (American, that is).

Some may find it hard to imagine that the United States would ever go down this route. But reckless money creation is apparently a concern of Gov. Rick Perry of Texas, who is seeking the Republican nomination for president. He suggested in August that it would be "almost treasonous" if Ben S. Bernanke, chairman of the Federal Reserve, were to print too much money before the election. Mr. Perry is not alone in his concerns. Many on the right fear that the Fed's recent policies aimed at fighting high unemployment will mainly serve to ignite excessive inflation.

Mr. Bernanke, however, is less worried about the United States turning into Zimbabwe than he is about it turning into Japan.

Those old enough to remember the 1980s will recall that Japan used to be an up-and-coming economic superpower. Many people then worried

(too much, in my view) that Japan's rapid growth was a threat to prosperity in the United States, in much the same way that many people worry today (too much, in my view) about rapid growth in China.

The concerns about Japanese hegemony came to a quick end after bubbles in the real estate and stock markets burst in the early 1990s. Since then, Japan has struggled to regain its footing. Critics of the Bank of Japan say it has been too focused on quelling phantom inflationary threats and insufficiently concerned about restoring robust economic growth.

One of those critics was Mr. Bernanke, before he became Fed chairman. Watching Japanese timidity and failures has surely made him more willing to experiment with unconventional forms of monetary policy in the aftermath of our own financial crisis.

The economists in the Obama administration are also well aware of the Japanese experience. That is one reason they are pushing for more stimulus spending to prop up the aggregate demand for goods and services.

Yet this fiscal policy comes with its own risks. The more we rely on deficit spending to keep the economy afloat, the more we risk the kind of sovereign debt crisis we have witnessed in Greece over the past year. The Standard & Poor's downgrade of United States debt over the summer is a portent of what could lie ahead. In the long run, we have to pay our debts — or face dire consequences.

To be sure, the bond market doesn't seem particularly worried about the solvency of the federal government. It is still willing to lend to the United States at low rates of interest. But the same thing was true of Greece four years ago. Once the bond market starts changing its mind, the verdict can be swift, and can lead to a vicious circle of rising interest rates, increasing debt service and budget deficits, and falling confidence.

Bond markets are now giving the United States the benefit of the doubt, partly because other nations look even riskier, and partly in the belief that we will, in time, get our fiscal house in order. The big political question is how.

The nation faces a fundamental decision about priorities. To maintain current levels of taxation, we will need to substantially reduce spending on the social safety net, including Social Security, Medicare, Medicaid and the new health care program sometimes called Obamacare. Alternatively, we can preserve the current social safety net and raise taxes substantially to pay for it. Or we may choose a combination of spending cuts and tax increases. This brings us to the last of our cautionary tales: France.

Here are two facts about the French economy. First, gross domestic product per capita in France is 29 percent less than it is in the United States, in large part because the French work many fewer hours over their lifetimes than Americans do. Second, the French are taxed more than Americans. In 2009, taxes were 24 percent of G.D.P. in the United States but 42 percent in France.

Economists debate whether higher taxation in France and other European nations is the cause of the reduced work effort and incomes there. Perhaps it is something else entirely — a certain *joie de vivre* that escapes the nose-to-the-grindstone American culture.

We may soon be running a natural experiment to find out. If American policy makers don't rein in entitlement spending over the next several decades, they will have little choice but to raise taxes close to European levels. We can then see whether the next generation of Americans spends less time at work earning a living and more time sipping espresso in outdoor cafes.