



The Morning Line

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Politics Team

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Krugman: Second Great Depression Unlikely, But a 'Lesser Depression' Is

SUMMARY

Stocks plummeted on Wall Street and around the world Monday as President Obama tried to reassure investors that the United States economy is still worthy of a A Judy Woodruff discusses the historic market drop with Princeton University's Paul Krugman, Harvard University's Ken Rogoff and Terry Belton of JPMorgan Chase.

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Transcript

JUDY WOODRUFF: We take a closer look now at today's historic drop in the stock market and the economic winds that are swirling here a abroad.

Paul Krugman is a Nobel Prize- winning economist from Princeton University. He's also a columnist for The New York Times. **Ken Rogoff is a former chief economist for the International Monetary Fund. He's co-author of a book about financial crises called "This Time Is Different." And he's a professor of economics at Harvard.** And Terry Belton is head of fixed income strategy for **J.P. Chase.**

We thank you, all three, for being with us.

Terry Belton, I want to start with you since you're closest to the markets. What was behind today's massive sell-off?

TERRY BELTON, J.P. Morgan Chase: Well, the -- Judy, the downgrade was a catalyst for, but it's a lot more -- it's about a lot more than that. I think what the downgrade is highlighting to investors is that, on the fiscal policy side, the U.S. has run out of bullets. We -- what we really need near-term monetary stimulus and longer-term fiscal austerity. And I think what the market is concluding now is that near-term stimulus coming. We have run out of bullets on the monetary policy side for some time now. And we have been at zero interest rates. It now looks like we as well on the fiscal policy side. U.S. economic growth is very weak. And it's not clear to the markets how it's going to be revived.

JUDY WOODRUFF: And so you're saying the -- the S&P downgrade was the catalyst, but in addition to that, you mentioned U.S. -- the U.S. economy. And what about the global economy?

TERRY BELTON: Well, in the global economy, we have a global debt issue. And in a way, the European situation is a bigger worry to global macroeconomic growth than even the weak growth in the U.S.

They have a liquidity crisis. European governments are behind the curve there. It began as a problem in the much smaller, peripheral governments it's now spread to Italy and Spain. Italy is the third largest bond market in the world. And there are funding pressures showing up there. That's negative for the global growth. The market is very worried about that.

JUDY WOODRUFF: Paul Krugman, I want to get to that S&P downgrade in just a moment. But, first, while we're talking about the worries strength of the U.S. economy, worries internationally, how do you size up how much that is weighing down the U.S. market?

PAUL KRUGMAN, The New York Times: Oh, I mean, this is a -- everyone is looking and seeing a strong possibility of a global recession right

But I just want to follow up on what Terry said. What really -- I think -- let me translate it into my terms. The reason that the S&P downgrade if it did at all, is not that it made people think that U.S. debt was unsafe. In fact, people have piled into U.S. debt, right? Interest rates on U.S. government debt are at their lowest point since January 2009.

What the downgrade did is, it made people think that the U.S. government is now going to be hamstrung, not able to take action to prop up the economy, not because it can't actually finance the debt -- the spending, not because it's in real fiscal trouble, but because some guys at S&P by that downgrade have bullied the U.S. economy, have bullied the U.S. government into taking actions that are going to be the wrong thing to do

So, this is not -- you know, the narrative which says that we have a fiscal problem and that's the source of the difficulties is not at all right. What actually happening is that the same people who have been urging us to take the wrong policies, to not focus on jobs first and deficits later, have upped the ante. And that's making the economy look worse. And that's leading to this global crash.

Similar things are happening in Europe, and so we have a global downturn based not on -- again, not on real fiscal constraints, but on bad ideas enforced by bad agencies like S&P.

JUDY WOODRUFF: Ken Rogoff, is that how you read -- as long as we're going to go ahead and talk about this downgrade, let's talk about it how you read the downgrade and its effect and how it's the interplay with what's going on in the rest of the world?

KENNETH ROGOFF, Harvard University: Well, I think the downgrade has had a big effect, although I beg to disagree with Paul. I think the spade a spade.

You look at the acrimony, the debt/deficit debacle, and it really hurt our institutions. And I don't see how they could have called it any other way. Certainly, markets are looking and seeing nobody home. And monetary policy has actually been getting tighter. And as Paul and Terry noted, the policy looks like it's getting tighter.

But, more broadly, I think people see that they have continuously misdiagnosed this as a normal recession, when it's not. It's a long-term contraction. And they have tried conventional tools. And they need to do things to bring down this debt overhang of private debt, not just public debt.

JUDY WOODRUFF: Paul Krugman, how do you respond?

PAUL KRUGMAN: No, I -- I think Ken and I, in many ways, have got the same model of what is going on.

But part of what you need to do while you do this -- I think Ken and I both think that the Fed needs to be doing more, that we actually need more inflation, not to be all worried about inflation, the way the policy-makers have been. But we also need some support while this is happening from the federal government, from federal spending.

And what we're actually doing is moving in the wrong direction. As for that downgrade, there was no new information. There was nothing. S&P had to have done some arithmetic. And then it turned out the arithmetic was wrong. And so they ended up just doing -- you know, saying, oh, the U.S. political system is a mess.

Well, any guy at the bar can tell you that. There's nothing new there. This wasn't appropriate for them to act in the way they did. I would say a lot of failing institutions. And I'm afraid the rating agencies are among those failing institutions.

JUDY WOODRUFF: Ken Rogoff?

TERRY BELTON: Well, I would say -- if I can jump in, Judy, I would say that...

JUDY WOODRUFF: Sure.

TERRY BELTON: ... if you look at the U.S. fiscal metrics today, we look a lot more like a AAA sovereign than a AA. Our debt-to-GDP is lower than France, lower than Great Britain.

But where I would disagree with Paul is that our trajectory is much worse. And without a change in policy, it's only a matter of a few years when the metrics will absolutely look like a AA. Our debt-to-GDP ratio now is in the mid-70s. It's headed up to the mid-80s, even after last week's decision by Congress on the budget control act.

JUDY WOODRUFF: Ken Rogoff, whether one believes this downgrade was justified or not, what are the consequences in the short term and long term?

KENNETH ROGOFF: Well, I think in the short term, the consequences are hard to predict because it's a very volatile and emotional market. People are scared about growth slowing, but they're looking for direction. They're looking for leadership. And the credibility is just shot in Europe. They have had one plan after another which has fallen short. And I think the United States is indeed in a much stronger position.

But it was very ugly, what happened. I think it really cut into our institutions. We shouldn't have this debt ceiling. They should have raised it unconditionally. I think President Obama shouldn't have given in so much to the Tea Party. And that I think weakened his long-term hand in the presidency.

JUDY WOODRUFF: Paul...

PAUL KRUGMAN: Judy, can I just weigh in?

It -- all of this is -- there's a lot of truth in all of this, but what actually happened in the markets today did not look like a solvency panic. It looked like a growth panic. It looked like the markets, investors are afraid that this global economy is going back into the ditch, and nobody is prepared to do anything. And in a way, what the markets were telling us was, you guys have been obsessing on the wrong things. Sure, we have a long-run fiscal problem.

right now we need to be getting this economy moving. And that's the thing that nobody has been talking about.

JUDY WOODRUFF: Well, if that's the case, Terry Belton, what -- what can be done to stop this? Or is there just no stopping it in the near te

TERRY BELTON: Right.

Well, as I said, we're almost out of bullets. It's like, you know, those Superman episodes. The only thing left is to throw the gun. I think we will Fed do that tomorrow when it...

JUDY WOODRUFF: What do you mean? What do you mean throw...

TERRY BELTON: Well, I think -- well, throw the gun, I mean, you're out of bullets. The only thing left to try to deal with it is whatever you c

And tomorrow, I think what we're going to see from the Fed is not a QE3 announcement, but, in all likelihood, it's going to change its reinvest program to really extend and lengthen the purchases out the curve in the treasury market. That will keep rates lower.

I think, on the fiscal side, what we need -- and we have sort of missed the boat here -- a little bit of the opposite of what we got. We need long-t reform. We need to deal with entitlements reform and tax reform. That lowers the deficit in the long run. But we actually need stimulus now.

We're almost getting the opposite. Coming in to next year, we're going to have quite a fiscal drag kick in as the 2011 tax cuts run off. That's goi growth a lot next year.

JUDY WOODRUFF: Ken Rogoff, how do you see what needs to happen in the short term to turn this around, or do we just fasten our seat b

KENNETH ROGOFF: Well, I think, definitely, we need to see higher inflation. We don't need to see the Fed just talk about QE3, more bond but QE3 for -- they should announce that they're trying to hit significantly higher inflation.

They really have to move decisively. It was really half-baked and timid the first time they did it. I don't think they're out of bullets at all. I think effective. But they need to do something. They need to do something about the mortgage debts. We have to find a plan. There are plans out the writing down the mortgage debts.

And then finally, of course, there are lots of areas we could have so-called structural reforms. But let's start with getting rid of the debt ceiling pretty depressing for global markets, thinking about that year after year.

JUDY WOODRUFF: Paul Krugman, for ordinary Americans, what do they think about? How worried should they be as they go to sleep ton

PAUL KRUGMAN: Well, OK, I don't think we're about to see Great Depression two. But I do think we are really looking at a long period of v performance.

There's a pretty good chance of a second leg to the recession, a double-dip. There's a very good chance that unemployment is still going to be r percent or higher a year from now, two years from now. So what we're seeing now is the -- you know, is -- I have been calling it the lesser depr really long period of really poor performance.

If you're unemployed now, I really feel for you because your chance of getting reemployed is very low. And so this is -- this is depressing. And v somebody to stand up -- in a way that the president didn't, by the way, this afternoon -- and say, we are on the wrong track. We are not -- we a dealing with the problem at hand and at least to call out the people who are standing in the way of doing the right things.

JUDY WOODRUFF: Terry Belton, just quickly, what should Americans, ordinary Americans, be thinking at this point about the future?

TERRY BELTON: Well, I think -- I mean, it's not all doom and gloom. I think there are some good signs. We're seeing a little bit of signs of r in the labor market. The unemployment rate is still obviously very high, at -- above nine percent.

But we are seeing for the first time this summer labor market gains. We have -- jobless claims is down at the lowest level since April. Last mor payroll number was double what we had been getting the previous three months. Corporate profits are still good.

So we actually think we're -- we're through the worst. We had abysmal growth in the first half. It will be a little bit better in the second half. Bu just not enough.

JUDY WOODRUFF: And, very quickly, Ken Rogoff, a word on, what should people think tonight?

KENNETH ROGOFF: Well, there's no two ways about it. It's a scary moment. And I think again this absence of credibility, no one to stand t take charge, I would like to see it start with the central banks both in Europe and the United States moving decisively to make monetary condit easier.

That may sound like heresy, but I really think it's a time for outside-the-box thinking.

JUDY WOODRUFF: All right.

Ken Rogoff, Paul Krugman, Terry Belton, gentlemen, we thank you, all three, for joining us.

TERRY BELTON: Thank you.

KENNETH ROGOFF: Thank you.

PAUL KRUGMAN: Thanks.



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Don_B1 • a year ago

Good segment; but the real takeaway should be the paragraph from Paul Krugman:

"... but what actually happened in the markets today did not look like a SOLVENCY [what S&P's downgrade implies] panic. It looked like a GROWTH [what needs more fiscal support/stimulus to avoid] panic. It looked like the markets, investors are afraid this global economy is going back into the ditch, and NOBODY is going to act." [Emphasis mine.]

If all the VSPs (even this program from time to time) emphasize the wrong part (e.g., "Second Great Depression Unlikely, But a 'Lesser Depression' Is") which is the likely RESULT but not the CAUSE, which is that our "leaders" from the Tea Party to President Obama and advice from incompetent VSPs, whether that incompetence comes from real ignorance or hidden motives ("make Obama a one-term president") it will cause great and unnecessary pain throughout the middle and lower classes and eventually the upper classes when the denouement hits.

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Rudy Haugeneder • a year ago

Britain's AAA rating is probably going up in flames as riots spread from neighborhood to neighborhood and city to city.

Once it starts -- rioting -- and the population itself doesn't take immediate action to halt it, chaos accomplishes a critical mass which is difficult to control, especially if a country is caught in the midst of high unemployment and growing economic recession fears.

America should be alarmed it could erupt in the USA just as quickly.

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Don_B1 • a year ago

How do you title this section with Krugman's comment that a "Second Great Depression Unlikely but a Lesser Depression is." The thrust of his comments come in the paragraph where he says,

"what actually happened in the markets today did not look like a solvency [the S & P diagnosis] panic. It looked like a growth [the lack of support/stimulus] panic. It looked like the markets, investors are afraid that this global economy is going back into the ditch, and not prepared to act."

This part of his comments relate to his diagnosis of the cause of the problem, the understanding of which is necessary to the formulation of an effective solution. That leads to the understanding of why our "leaders" [from the Tea Party guerrillas on up to Obama] are choosing a path that will not solve the problem and the result will be a "Lesser Depression."

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Kire Rentiem • a year ago

In the clip preceding this discussion Obama calls S&P an agency. Then Krugman calls it the same. Folks, S&P is a for-profit corporation. Stop trying to elevate it to the pseudo-governmental status the same as people do with the Federal Reserve.

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