Up the creek without a compass

THE AGE OF DIMINISHED EXPECTATIONS
U.S. Economic Policy in the 1990s
Paul Krugman
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Jimmy Carter's declaration of an "age of limits" at the beginning of his presidential term was a dose of political realism that, for all its empirical validity, did nothing to further his political career. Branded a dreary pessimist, a Southern nabob of negativism, Carter was incapable of convincing the American public that the U.S. could no longer perform unilaterally in the economic, political, and military spheres as it had once done during the heyday of the "American century." Then, in 1981, Ronald Reagan unveiled morning in America. Obscurantism had momentarily vanquished realism.

Reagan's optimism has subsequently proven to be little more than a historic blip. The beginning of the 1990s have confirmed the drift of American policy: the savings and loan fiasco, the woefully expensive and questionably ethical war in the Persian Gulf, another recession, a ballooning budget deficit, political stagnation, endemic crime and urban blight, in short a decline in national health facilitated in all respects by hypertrophied military muscle. Morning in America had become morning sickness. Skillfully monitoring the vital signs, the Cassandras of the latter half of the 1980s had produced several sober, and sobering, reflections on the downward trajectory of American empire. Paul Kennedy (*The Rise and Fall of the Great Powers*) and Walter Russell Mead (*Mortal Splendor*) began the rollback of optimism. Economist Paul Krugman has brought that analysis into the 1990s, translated into dollars and cents.

Krugman's *The Age of Diminished Expectations* derives its impact as much from the clarity of its content as from the stature of its author. The *wunderkind* of M.I.T., Krugman is known for his arcane analyses of trade policies and his work with President Reagan's Council of Economic Advisors. He is not, in other words, the type to write a doomsday book. Of course, Krugman remains true to his profession, preferring an understated style and balanced presentations to irresponsible predictions. Though he suspects that the U.S. will most likely muddle through into the near future, he rates the chances of the bottom dropping out the economy at one in four. Not very reassuring after a decade of cowboy swagger.

Krugman's argument is simple. After a postwar period of unprecedented growth, the American economy settled in the 1970s into what seems to be chronic stagnation. The gap between rich and poor has widened, productivity has leveled out, inflation continues to infect our economy despite tight monetary policies, and huge deficits have opened up in the current trade accounts and government budget. Americans, Krugman argues, have come to treat this hobbled economy as acceptable, even normal.

Krugman doesn't offer an array of solutions. He is more interested in showing the complexity of problems, the built-in give-and-takes, the economic Gordian knots pulled all the tighter by political considerations. Along the way, he tackles some popular myths—the U.S. trade deficit is related to the rate of domestic savings not high tariffs abroad, bringing down inflation necessarily means accepting recession and higher unemployment, lowering the value of the dollar would have beneficial effects on U.S. trade. He even offers one or two unorthodox suggestions, for instance pointing out that a solution to the third-world debt problem could cost roughly one-twentieth of the S&L bailout (the trick is to look not at the actual amount of the aggregate debt but at its price on secondary markets).

The best aspect of *The Age of Diminished Expectations* is its accessibility. Krugman has the laudable ability, rare among economists, to condense pages of complex argumentation into one or two clear paragraphs (an act of rhetorical agility as useful to the layperson as it is probably infuriating to the expert). Krugman brings economics, which is after all a *social* science, from the level of number-crunching impenetrability down into the public domain. Mathematical economics, as Robert Heilbroner once pointed out, combines "rigor" with "mortis"; the airport bookstand variety is simultaneously digestible and disposable; the newspapers favor graphs and deceptively transparent description. Krugman, by contrast, has produced an economic primer, short and laconic in style, a book that an interested non-expert needs close by to check for the umpteenth time the relationship between a falling dollar and a trade deficit.

Despite all these merits, the book does have substantial blind spots. At many points, Krugman deliberately refrains from providing definitive conclusions. Should the government drive the dollar down? Should the government aim for greater employment? There are pros and cons and Krugman presents both sides. Yet despite adherence to traditional "value-free" economics and a desire to describe rather than prescribe, he cannot maintain distance: his opinions invariably bleed through. "American interests," Krugman writes at one point, "would probably best be served by a world of free trade, with the temptations of strategic trade policy kept out of reach by international treaty." Thus, free trade is championed for national as well as economic reasons (so much for "pure" cost-benefit analyses and policies based exclusively on efficiency and rationality).

Were it simply a matter of throw-away lines such as the one above and were he honest about his ideology like liberal Robert Lekachman or conservative Milton Friedman, Krugman's perspective would be tolerable (or at least assessable). Instead, his views covertly permeate his analysis, particularly at those times when he attempts to be most even-handed.

In a chapter on corporate finance, for instance, Krugman discusses two current explanations for the enormous growth in profits made in the field in the 1980s. One school maintains that the profits derive from the increased productivity of a replaced or reordered management after a corporate take-over. The other school suggests that the profits come from the pockets of workers forced to accept wage cuts or dismissed outright after one of the many industrial restructurings of the decade. Following liberal tradition, Krugman

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decides that the truth lies somewhere in the middle. But based on the evidence he himself presents in the book, the profits gained through improved productivity could not possibly compare to the profits earned through labor givebacks: the difference is of several orders of magnitude. Throw in the profits from government kickbacks, favorable tax policy, and outright criminality and the windfall earnings of the 1980s become even more suspect. Giving credence to the efficiency school allows Krugman to hide behind "normal" economic explanations instead of examining more closely the grossly inequitable aspects of corporate finance that permitted the spending spree of 1980s, a tab picked up thank-you-very-much by taxpayers now and for many decades into the future.

Irritating lapses aside, *The Age of Diminished Expectations* remains a helpful guide to today's economic conundrums and a necessary tonic for any residual Reagan optimism that appears, as one or more points of light, in the current presidency. We will, as Krugman suggests, be drifting for quite a while. Should the stretch of stagnation before eventual *perestroika* be a long one, we may as well read our Cassandras, heed their warnings, become informed and incensed, and be that much better prepared for the time when our leaders once again accept or are forced to accept the inevitability of an age of limits. □