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FISCAL AUSTERITY, DOLLAR APPRECIATION, AND HIGH INCOME INEQUALITY PUT U.S. ECONOMIC GROWTH ON FRAGILE PATH, NEW LEVY ECONOMICS INSTITUTE REPORT SAYS

ANNANDALE-ON-HUDSON, N.Y.— While the U.S. economy is about to enter the seventh year of its recovery, and unemployment has steadily decreased—from a peak of 10 percent at the height of the crisis in mid-2009 to 5.4 percent in April of this year—a new report from the Levy Economics Institute of Bard College argues that the current recovery is the weakest of the postwar era and is undermined by three structural obstacles: the weak performance of net exports, prevailing fiscal conservatism, and high income inequality. In their new Strategic Analysis, *Fiscal Austerity, Dollar Appreciation, and Maldistribution Will Derail the US Economy,* the Levy Institute's Macro Model Team—President Dimitri B. Papadimitriou and Research Scholars Greg Hannsgen, Michalis Nikiforos, and Gennaro Zezza—contend that these structural characteristics make the economy's future recovery once again dependent on an unsustainable rise in private borrowing that is bound to end in another serious crisis. The medium-term prospects for the U.S. economy are further threatened, they suggest, by the appreciation of the U.S. dollar and the fragile economies of many of the United States' trading partners.

"Our baseline scenario shows that for the (Congressional Budget Office) projections to materialize, the private sector, beginning in 2017, has to again become a net borrower—for the first time post crisis—and increase its debt and debt-to-income ratio," the Levy team writes, stressing that, with high levels of income inequality, this unsustainable increase in debt and the debt-to-income ratio will disproportionally fall on the households at the bottom of the distribution, which are bearing an ever-rising consumer-debt burden. This kind of unsustainability was the primary reason for the downturn of 2001 and the more recent Great Recession. As our simulation results show, the recovery of the US economy requires that the same unsustainable process be repeated once more."

The Levy scholars point out that, "on average, households of modest means, especially those in the bottom quintile, still carry very high levels of debt in relation to their incomes. The deleveraging of household balance sheets continues, and still has not progressed

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to a sufficient extent in the aftermath of the Great Recession of 2007–9. We continue to believe that the combination of anemic wage growth and rising household debt—of whatever kind—cannot sustain growth."

Further undermining a long-run, sustainable recovery, the authors maintain, is the appreciation of the U.S. dollar and the fragile economies of many of the United States' trading partners. Using the Levy Macro Model, they find that "a further depreciation and/or slowdown of growth in the economies of US trading partners will have very significant consequences: an increase in the foreign deficit, which will lead to a decrease in the projected growth rate and, at the same time, an increase in the need for private (and government) borrowing, thus rendering the US economy even more fragile," they write. "The stagnation, or weaker-than-expected performance, of the 'rest of the world' translates into weaker demand for US exports and has a negative impact on the rate of growth."

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Strategic Analysis: *Fiscal Austerity, Dollar Appreciation, and Maldistribution Will Derail the US Economy*

To read the full text of this policy paper or to learn more about the Levy Economics Institute of Bard College, please visit http://www.levyinstitute.org/publications/fiscal-austerity-dollar-appreciation-and-maldistribution-will-derail-the-us-economy.

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