
Report**June 2003**

Volume 13, Number 2

Conference:**13th Annual Hyman P. Minsky Conference
on the State of the U.S. and World Economies:
Economic Policy for Sustainable Growth**

Speakers and session participants at this year's Hyman P. Minsky Conference, which took place on April 15, assessed the state of the U.S. and world economies and speculated about what lay ahead. Opinions varied widely, and many participants expressed a high degree of uncertainty about their views. Among the issues discussed were the effects of low interest rates and the reemergence of budget deficits; the implications of large, ongoing current account deficits; and the potential for deflation in the U.S. economy in the near future.[continued](#)



Dimitri B. Papadimitriou speaks at the 13th Annual Minsky Conference

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The Levy Economics Institute of Bard College, founded in 1986, is a nonprofit, nonpartisan research organization devoted to public service. Through scholarship and economic research it generates viable, effective public policy responses to important economic problems that profoundly affect the quality of life in the United States and abroad.

Dimitri B. Papadimitriou, *President*

The *Report* is a quarterly publication of The Levy Economics Institute of Bard College.

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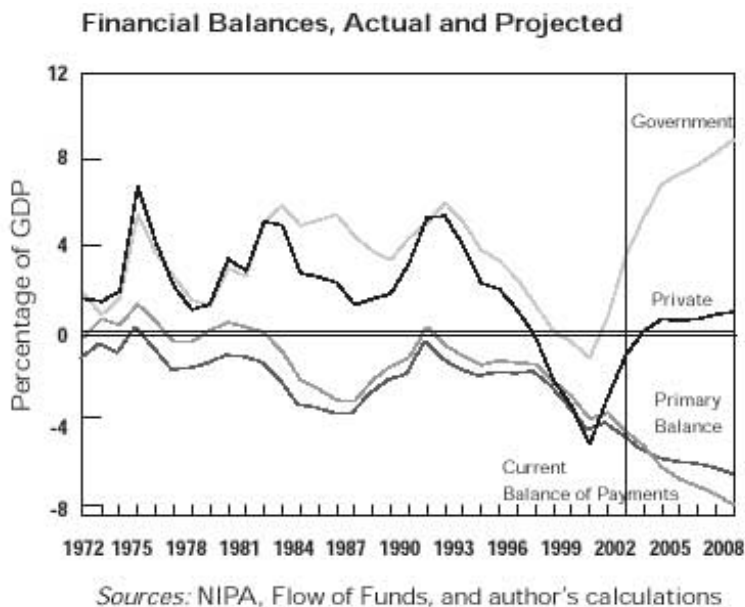
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Conference:

13th Annual Hyman P. Minsky Conference on the State of the U.S. and World Economies: Economic Policy for Sustainable Growth

Speaker: Dimitri B. Papadimitriou

Papadimitriou, president of the Levy Institute, began by reminding the audience of the Institute's previous warnings about the levels of household borrowing and current account (or current balance of payments) deficits. The rapid buildup of private debt, especially household debt, has tapered off, as we have long predicted. In the meantime, the United States is incurring huge current account deficits. These foreign deficits are the amounts by which imports exceed exports plus the net outflows of interest payments and some other related forms of income. Papadimitriou analyzed the implications of these developments, drawing on two recent Levy Institute Strategic Analyses.



The evolution of the two deficits--that of the private sector and that of the United States to the rest of the world--is shown in the chart at the top of the page. The chart shows that the current account deficit is at a historic high, of about 5 percent of GDP. The chart also shows that the private sector is rapidly reducing the rate at which it is going into debt, approaching a balance of approximately zero.

By definition, these two deficits are linked. The sum of the private sector deficit and the government deficit is equal to the current account deficit. Therefore, as the chart shows, a private sector balance of approximately zero implies that the government deficit is at rough parity with the current account balance. Furthermore, if the optimistic economic growth forecasts produced recently by the administration turn out to be correct, we project that the latter deficits will both reach approximately 8 percent of GDP, as shown to the right of the vertical line on the graph.

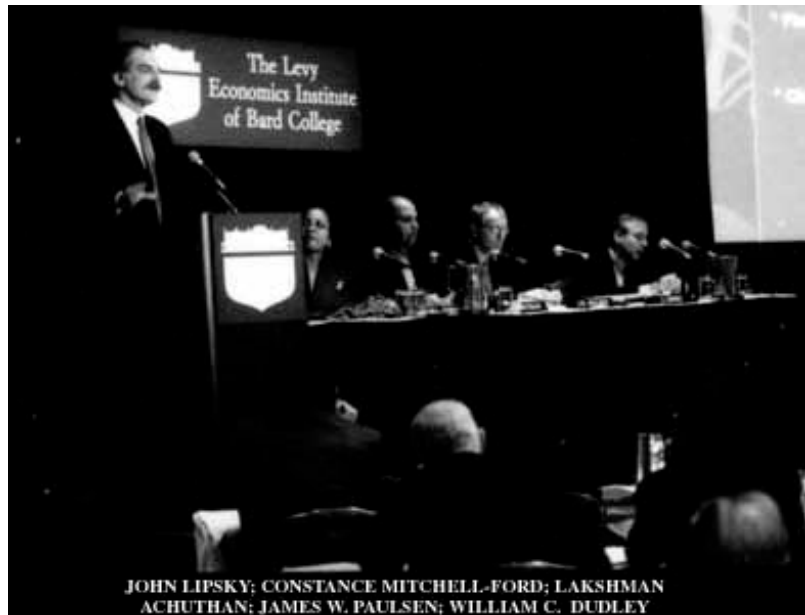
A current account deficit of this magnitude is clearly unsustainable over the long term, since it

implies that total foreign debt would rapidly rise to enormous levels. The conclusion one must draw is that the economy will not grow as fast as predicted by the administration. The only means available to avoid a "growth recession" is to dramatically reduce the current account deficit, perhaps by reducing the value of the dollar on foreign currency markets. Such a devaluation would narrow the deficit by increasing U.S. exports and raising the dollar price of imports to the United States.

A devaluation strategy suffers from some potential drawbacks. First, U.S. policymakers do not possess any fail-safe method of reducing the value of the currency. Second, a devaluation might create problems for our trading partners. A third possible pitfall, accelerating inflation, is only a remote possibility.

Session 1. The State of the U.S. and World Economies: A Wall Street Perspective

This session was moderated by CONSTANCE MITCHELL-FORD, economics editor of the *Wall Street Journal*. Participants were LAKSHMAN ACHUTHAN, managing director of the Economic Cycle Research Institute; JAMES W. PAULSEN, chief investment strategist at Wells Capital Management; JOHN LIPSKY, chief economist and global head of economic policy research at J.P. Morgan Investment Bank; and WILLIAM C. DUDLEY, managing director and director of U.S. economic research at Goldman, Sachs, and Co.



JOHN LIPSKY; CONSTANCE MITCHELL-FORD; LAKSHMAN ACHUTHAN; JAMES W. PAULSEN; WILLIAM C. DUDLEY

Achuthan cautioned his audience against viewing the recession of 2001 as a fluke occurrence against a backdrop of a nearly recession-proof "new economy." A long period of virtually noninflationary growth came to an end in that year as a result of the delayed impact of interest rate increases by the Federal Reserve Bank (Fed). The Fed had been forced to take action by a new "synchronization" of the business cycles of economies around the world. Seen in the light of the recent recession, the proclamations of the birth of a "new," more stable economy and a less volatile stock market seem overly optimistic. Recent events may herald a further decline in stock values, as investors demand compensation for incurring the risks of renewed volatility.

Paulsen asserted that recently released economic statistics support an optimistic view. Long-term interest rates are falling in response to the Federal Reserve's accommodative stance. The full effects of recent government deficits, yet to be realized, will become evident in the near future. The value of the dollar in foreign exchange markets has been declining, and an inexpensive dollar will allow foreigners to purchase U.S. goods and services more cheaply and stanch the flow of imports. While

the economy has not been creating new jobs, inflation-adjusted wages have been rising. A number of problems cloud the economic picture over the longer term, though, including the aging of the population, household debt, competition from emerging economies, and excess capacity.

Lipsky observed that the recession of 2001 was confined to the business sector; household spending has remained strong over the past few years. Some other aspects of the 2000-02 cycle bode well for the future: strong productivity growth, stimulative monetary and fiscal policy, and the increasing prevalence of bond finance, which puts pressure on firms to achieve results. Turning to specific problems, Lipsky pointed out that inventories have been the main soft spot in business spending; he expected that they will soon regain some ground relative to total sales. All types of business spending will receive a boost from more adequate inflows of cash. The magnitude of the current account deficit reflects the relative strength of the U.S. economy, rather than a lack of competitiveness, and is not a serious threat to growth.

Dudley described the economy's path since 2001 as a temporary uptick that will merely make up some of the ground lost during the recession, then give way to a shallower upward trend. The recent recession was driven largely by the collapse of the stock market. Businesses have adjusted to the loss of stock market wealth, and their cash inflows have increased--but not sufficiently to spark a boom in spending on equipment, software, and other capital goods. The end of the home refinancing boom will dampen the enthusiasm of consumers. Fiscal policy, which provided a boost to the economy last year, will be less of a factor in 2003; low interest rates are over-shadowed by a strong dollar and declining household wealth.

Speaker: Marc Faber

Faber, who heads a company that shares his name, argued that recent developments in the world economy are following established historical patterns. Major financial booms and waves of technological innovation have generally been accompanied by falling commodity prices and interest rates. Such a deflation followed the construction of the transcontinental railroad in the 19th century. Several current trends suggest a reemergence of this pattern: disinflation or deflation in many countries, generated partly by the opening of new markets; extremely low interest rates; and a dramatic run-up in property and stock market values. Does the decline of the stock market signal the turning point of these trends? If so, what lies ahead for the United States and its competitors?



Often, after markets crash, Faber observed, the affected economies do not regain their dominance. A

new economic center emerges, and the old one is permanently eclipsed. Current trends suggest that China may be the next leader. The strong dollar and low interest rates have enabled U.S. households to take advantage of low-cost Chinese imports. The resulting consumption boom has largely bypassed American producers and will last only until the recent surge in mortgage refinancing ends. The counterpart to the imbalance in the flow of goods and services is a vast transfer of American assets to foreign investors. If foreigners lose their appetite for U.S. securities, American financial markets may tumble again.

Meanwhile, as China and other emerging Asian economies expand, they will demand increasing supplies of oil, food, and other commodities, benefiting resource-rich countries such as Argentina, New Zealand, and Indonesia. If even a small fraction of the Chinese population joins the world's middle class, the center of gravity of the world economy will dramatically shift. Eastern Europe may also realize its great economic potential, as its industries take advantage of the expansion of the European Union. The United States, on the other hand, will suffer from both high inflation and poor growth, undermining the strength of its currency and financial markets.

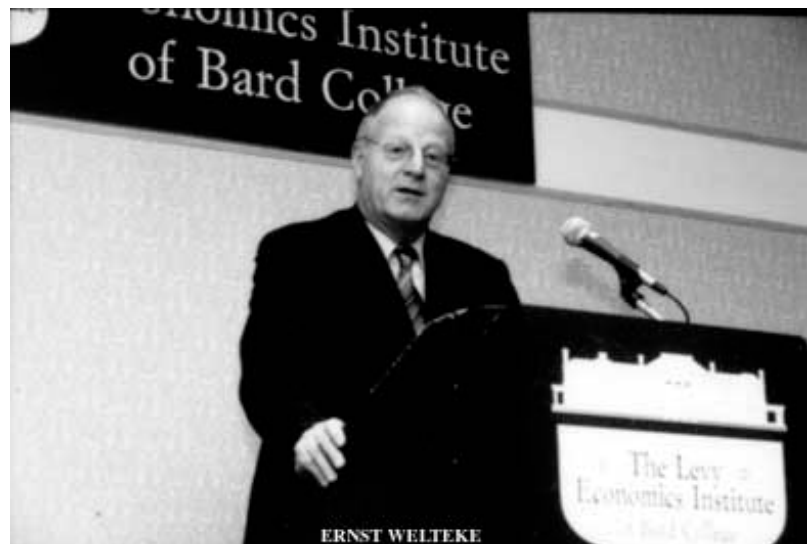
Speaker: Ernst Welteke

Welteke opened his speech by citing the "strain" in transatlantic relations. He declared that the U.S.-European dialogue "must not be interrupted." He went on to assess the strengths and weaknesses of the European economy and those of the world as a whole.

Welteke, the president of the Deutsche Bundesbank, Germany's central bank, expressed the opinion that several key imbalances, and not the war in Iraq, are the main contributors to economic uncertainty. The recent period of

"overinvestment," for example, has left a legacy of excess capacity. Also, growth has been strongest in North America and in the Asian economies other than Japan, which are vulnerable to imbalances of their own.

Fortunately, Welteke said, Europe possesses a number of strengths that will help it endure the present crisis. First, the monetary union has stimulated growth, in part by making capital markets more efficient. Second, despite the recent rise in the value of the euro, the export sector of Europe remains vibrant. Welteke strongly rejected the suggestion that Germany would "become another Japan," citing his country's well-developed infrastructure, strong productivity growth, and competitiveness on world markets. Moreover, German banks, unlike Japan's, are well capitalized, and German real estate is not overvalued.



Welteke stated that the main culprits in weak economic performance in Europe include "economic policy mistakes made during the unification process," such as excessive tax incentives for construction. A more long-standing problem is the inflexibility of labor markets. Welteke offered a policy agenda with three main elements. First, Europe must maintain its tough stance against inflation. The Stability and Growth Pact supports this objective and, notwithstanding its critics' complaints, does not impede growth. Second, as the European Central Bank concentrates on the goal of price stability, domestic policymakers must promote growth by lightening the burden on business of payroll taxes, the welfare state, and labor market regulation. Finally, financial regulators and supervisors should remain vigilant, but not overbearing. All in all, "each of the world's major economic zones has some homework to do."

Welteke concluded his speech by extolling the tradition of "transatlantic debate," and cautioning that we should not "let [foreign policy] differences spoil our long-term relationship."

Session 2. The Macroeconomic Prospects for the U.S. Economy

The moderator of this session was MICHAEL MANDEL, chief economist of *Business Week*. The other participants were J. ALFRED BROADDUS JR., president of the Federal Reserve Bank of Richmond; RANDALL S. KROSZNER, member of the President's Council of Economic Advisers; MARTIN MAYER, guest scholar at the Brookings Institution; and WILLIAM POOLE, president and chief executive officer of the Federal Reserve Bank of St. Louis.



Broaddus emphasized that the future holds many uncertainties, an observation that explains the recent decision by the Fed's policymaking committee not to announce a "bias" for the direction of interest rate policy in the near future. Broaddus deemed the recent Blue Chip forecast of moderate economic growth in the second half of this year and in 2004 a "plausible outcome." However, Fed policymakers must be "unusually vigilant" in this uncertain environment. They should continue their focus on permanent price stability and active stabilization in the short term, a strategy that partly accounts for the strength of the economy over the past 20 years. In light of considerable downside risks, the Fed should try to build credibility in responding to deflationary pressures, even as it maintains its hard-won reputation as an inflation fighter.

Kroszner discussed recent forecasts of moderate growth this year, also emphasizing the presence of many downside risks. Among the signs of potential weakness are slow or nonexistent job growth, a slow recovery of certain types of investment, and a lack of consumer confidence. Enactment of the president's tax-reduction plan, Kroszner said, would improve the situation. By ending the "double

taxation" of dividend payments to stockholders, the plan would enable firms to sell their stock more easily and at a higher price. Firms could use the proceeds to purchase technologically advanced software, factory equipment, and other items that make workers more productive. Other proposed changes would help displaced workers and small businesses.

Mayer analyzed exactly how Federal Reserve interest rate policy exerts its effects on the economy. The Fed is no longer able to affect the pace of economic activity by reducing bank loans, since banks do not rely on sales of government bonds as their sole source of funds, and because banks account for only a small fraction of total lending. For this reason, the impact of a change of policy by the Fed is more difficult to predict than in the past, and interest rate cuts can lead to a wide range of outcomes, including, for example, stock market rallies or increases in consumer spending. The current uncertain environment calls for humility on the part of regulators and those who set monetary policy.

Poole discussed the economy's resilience in the face of a number of recent "shocks," including the 9/11 attacks, the threat of new terrorist acts, war in Iraq, corporate governance scandals, SARS, and oil price hikes. He pointed out that the recovery from the recession of 2001 has been quite strong in spite of all of these developments. Poole cited several key factors, including Federal Reserve interest rate reductions, that in recent years have increased the ability of the economy to weather setbacks. But these actions have been possible only because the Fed has succeeded over the past two decades in taming the threat of inflation. Poole predicted the eventual return of rapid growth, though he emphasized, as had Kroszner and Broadbuss, the existence of economic uncertainty over the near term.

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New Working Papers

How Far Can U.S. Equity Prices Fall under Asset and Debt Deflation?

[Philip Arestis](#) and E. Karakitsos

[Working Paper No. 368](#)

The recovery from the recession of 2001 has been weak and has produced few new jobs. Will the country slip once again into recession? In a new working paper, Institute Professor Philip Arestis and E. Karakitsos of Trafalgar Asset Managers Ltd. assess the likelihood of such a "double dip" and its implications for the stock market.

Arestis and Karakitsos compare the current situation to three other periods when asset prices fell rapidly: the depressions of 1876-90 and 1929-1940, and the Japanese deflation of 1989 to the present. As they were in those times, asset prices are due for a correction, which will have an impact

on consumer spending. The ultimate result may be a second recession much more severe than the first.

The authors base their projections on a theory stating that consumers try to maintain a steady ratio between their net wealth and their incomes after taxes. In recent years, stock prices have fallen and debts have continued to rise, so that this ratio is at low levels, relative to its historical average. The theory states that in such a situation, consumers attempt to restore the ratio to a more normal level by saving a larger percentage of their incomes. Indeed the data show that this process of retrenchment, which has many precedents in U.S. economic history, has begun.

Once spending slows down, Arestis and Karakitsos say, the new recession will probably begin. The stock markets will likely fall dramatically, since current prices are based on unrealistically rosy forecasts. Eventually, the overheated property market will probably go the way of the NASDAQ, an event that has been only temporarily forestalled by the Fed's "easy money" policies and the movement of funds from stocks to real estate.

In their most pessimistic scenario, the authors estimate that the ratio of real estate wealth to disposable income would fall by 35 percentage points. Gross Domestic Product (GDP) would fall by 2.5 percent of its prerecession level. Profits would drop by 20 percent. Banks' balance sheets would deteriorate, forcing a reduction in lending that would further aggravate the recession. The S & P stock index would gravitate to a level of about 641. Thus, the authors conclude that the chance of a double-dip recession is not "remote, but under certain conditions highly probable."

On the Effectiveness of Monetary Policy and Fiscal Policy

[Philip Arestis](#) and [Malcolm Sawyer](#)
[Working Paper No. 369](#)

Many observers credit the Fed with the relatively good performance of the economy in most of the '90s. These economists, business journalists, and politicians have urged Congress to refrain from active fiscal policy and permit the Fed to do its work. In a new working paper, Philip Arestis and Malcolm Sawyer make a timely case for a rehabilitation of fiscal policy.

In the view of Arestis and Sawyer, although monetary policy has important effects on the economy, in some situations there is no substitute for fiscal policy. They document numerous ways in which monetary policy can fall short of its objectives, leaving masses of people jobless or aggravating problems such as anemic investment. The limitations of monetary policy stem from some inherent drawbacks in central banking. One is the monetary authorities' tenuous control of the long-term rates firms pay at banks and in the bond markets. Another is John Maynard Keynes's theoretical idea that there can be a "natural rate of interest" associated with any output level, not just full employment.

The authors dispel certain widely held misconceptions about the impotence of fiscal policy. One

such view is that public borrowing will "crowd out" private investment. In this scenario, government borrowing diverts funds from alternative uses, an unlikely outcome as long as the central bank maintains moderate interest rates. Another version has the government running up against the limits of the economy's production capacity. This barrier should not be of concern during a recession. One of the more imaginative theories holds that consumers' extra saving in anticipation of the future tax increases needed to repay government debt will completely offset the effects of deficits. According to Keynesian economics, though, government deficits sometimes allow households to increase their spending and the amount of their saving at the same time.

Testing for Financial Contagion between Developed and Emerging Markets during the 1997 East Asian Crisis

[Philip Arestis](#), Guglielmo Maria Caporale, and Andrea Cipollini
[Working Paper No. 370](#)

The Asian crisis of 1997 began with the collapse of the Thai baht. The ensuing collapse of markets, banking systems, and currencies throughout the region--which became known as the "Asian flu"--was an example of what economists refer to as financial contagion. Economists have developed several different theories to explain why crises tend to spread from one country to another.

Some explanations rest on the fact that when a nation's currency is devalued, its exports become less expensive to foreigners, while the local-currency prices of imported goods rise. While these adjustments can be beneficial to the country whose currency is depreciating, they come at the expense of that country's trading partners, pressuring them to respond with devaluations of their own. Since investors anticipate such competitive devaluations, they often sell financial assets of countries with close ties to already-troubled economies. Other theories of contagion rest on the "herd" mentality of investors. When one economy falters, a collective panic may develop in which market participants suddenly sour on the prospects of a group of countries.

In a new working paper, Institute Professor Philip Arestis, Guglielmo Maria Caporale of South Bank University, London, and Andrea Cipollini of the University of London use data on stock market returns for four victims of the "Asian flu" and for five advanced economies to test for the presence of contagion effects. Their study focuses on the 20 pairs of countries made up of one advanced and one emerging market. They define contagion as an increase in the tendency of the rate of return of stocks in two different countries to move in the same direction.

The authors find that problems in each of the Asian economies had only minor repercussions in markets in Japan, the United States, the United Kingdom, Germany, and France. The latter markets were resilient in part because loans to Asian countries made up only a small portion of the major banks' portfolios. Weakness in stock markets was in many cases transmitted, however, in the opposite direction--from the advanced to the emerging economies, especially in the case of Japan. This finding probably indicates that the Asian economies were adversely affected when the crisis caused the flow of funds from abroad to dwindle.

Credibility of Monetary Policy in Four Accession Countries: A Markov Regime-Switching Approach

[Philip Arestis](#) and Kostas Mouratidis
[Working Paper No. 371](#)

A new working paper by Institute Professor Philip Arestis and Kostas Mouratidis of the National Institute of Economic and Social Research in London examines patterns in the interest rate policies of four central banks in Eastern European countries that will join the European Union in May 2004. Of particular importance is whether monetary policy is credible, that is, whether consumers and firms believe that the monetary authorities are committed to fighting inflation. Central banks sometimes lack credibility, because they are tempted to sacrifice long-run price stability in order to achieve temporary spurts of economic growth. Most macroeconomists believe that a central bank that enjoys such confidence can contain inflation more effectively and with fewer disruptions of economic activity than a bank with low credibility. Credibility is important in the Eastern European case because the European Union expects new entrants to display a determination to harmonize their policies with those of current members.

Arestis and Mouratidis use a complex model of central bank policymaking to account for behavior of interest rates in the Czech Republic, Hungary, Poland, and Slovakia from 1992 to 2002. The credibility of each country's policy is gauged by the difference between its interest rates and those of 11 current European Union members. Arestis and Mouratidis posit that these countries switched from highly credible to low-credibility policy regimes from time to time throughout the period. The authors are able to show that their model fits the data well. They go on to compare the four countries, demonstrating that the central banks of the Czech Republic and Hungary are especially credible. Often, the policies of the four countries diverged significantly. The data present an intriguing, but somewhat ambiguous, picture of the prospects for a successful expansion of the European Union.

The Levy Institute Measure of Economic Well-Being

[Edward N. Wolff](#) and [Ajit Zacharias](#)
[Working Paper No. 372](#)

The nation's Gross Domestic Product (GDP) has climbed with only occasional interruptions since the end of World War II, increasing sixfold from 1946 to 2002. Would a measure of actual economic well-being register such rapid progress? Would it show that some demographic groups have improved their well-being more than others? And how would one construct such an index in the first place? These are some of the issues addressed in recent work by Senior Scholar Edward N. Wolff of New York University and Research Scholar Ajit Zacharias.

In this paper, Zacharias and Wolff, who were aided in their work by Research Assistant Melissa Mahoney, describe their Levy Institute Measure of Economic Well-Being (LIMEW). This index is designed to gauge the resources available to households for consumption or the acquisition of assets. The LIMEW includes such important items as work done without pay within the home; the value of government services; the net impact of taxes; and the benefits of holding various forms of wealth.

During the course of the project, the researchers confronted many difficult questions about the measurement of each of these components. For example, they were forced to choose between several methods of measuring the value of unpaid housework done by household members in their own homes. Two of the alternatives were to measure the cost of the time involved by using either the wage that could be earned by the household member in his or her regular line of (paid) work, or the wage earned by those who perform household work for cash. Zacharias and Wolff chose the latter.

The Levy Institute will monitor the level of the measure in the United States as it evolves from year to year. Eventually the economic well-being of different regions of the United States and even of other nations will be compared. The Levy index will show not only the aggregate level of well-being, but also how it is distributed among households, enabling researchers to gauge inequality in a comprehensive way and to measure how various government programs and taxes affect different demographic groups.

Does Trade Promote Gender Wage Equity? Evidence from East Asia

Günseli Berik, Yana van der Meulen Rodgers,
and Joseph E. Zveglich Jr.

[Working Paper No. 373](#)

Ever since the pioneering work of University of Chicago economist Gary Becker, the existence of discrimination in a competitive market system has been a matter of intense debate among economists. Becker argued that if white men were paid more than equally qualified minority workers or women in a particular industry, the firms engaging in such discrimination would produce at relatively high costs. Therefore, nondiscriminating firms could drive their discriminating rivals out of business by offering the same products at lower prices. In the long run, only fair employers would remain in the industry, and wages would be equal for all workers of equal skill and experience. The only remaining differences in pay would reflect the "preferences" of customers and workers to deal with members of their own groups--a deplorable form of prejudice, but one that arguably cannot be blamed on corporations.

In a new working paper, three scholars--Günseli Berik of the University of Utah, Yana van der Meulen Rodgers of the College of William and Mary, and Joseph E. Zveglich of the Asian Development Bank--marshal empirical evidence that casts doubt on Becker's hypothesis, as it applies to the effects of foreign competition. Partisans of Becker's theory might expect the recent

surge in foreign competition in many economies to put pressure on firms to reduce costs by abandoning discriminatory policies. Berik, van der Meulen Rodgers, and Zveglic, using data on a number of different industries in Taiwan and South Korea, examine how year-to-year changes in the proportion of each industry's output accounted for by imports and exports affect wage differences between the sexes. They only consider the portion of the wage differential that cannot be traced to differences in experience, education, and so on.

The authors link rising import penetration in Taiwan from 1981 to 1999 with a pattern of increasing wage inequality between male and female workers. In South Korea the proportion of output destined for export fell gradually and wages became more equal. Overall, the paper's findings strongly support the notion that foreign competition has an unfavorable effect on wage equity. Berik, van der Meulen Rodgers, and Zveglic ascribe this finding to the particular susceptibility of female workers in low-wage industries to job loss when market share is lost to foreign competitors and to women's disadvantages in competition for high-skill jobs in expanding industries. They suggest a remedy of strongly enforced antidiscrimination legislation.

The Nature and Role of Monetary Policy When Money Is Endogenous

[Philip Arestis](#) and [Malcolm Sawyer](#)
[Working Paper No. 374](#)

When economists say the stock of money is "endogenous," they usually mean that the amount in circulation is determined by the interaction of the demand for commercial bank loans with the willingness of banks to lend. Economists use the antonym "exogenous money" to refer to the idea that the central bank ultimately controls the supply of money. Many mainstream economists now believe that money is endogenous, a view long held by post-Keynesians and other heterodox economists.

In a new working paper, Institute Professor Philip Arestis and Senior Scholar Malcolm Sawyer of the University of Leeds discuss the implications of monetary endogeneity for the conduct of monetary policy. When money is endogenous, policy takes the form of central bank interest rate setting, since the central bank cannot fix the amount of money. In the view of the current mainstream consensus about the workings of the economy, interest rate policy is the most viable way of controlling inflation and stabilizing GDP growth.

One tenet of what is known as the "new consensus" of macroeconomists is that inflation is always the result of excessive demand for goods and services. The role of monetary policy is then to regulate the level of demand so as to keep inflation from accelerating. Arestis and Sawyer are not as optimistic as many mainstream economists about this picture of how monetary policy can be used.

The authors raise a number of objections to the consensus view. They cite empirical evidence showing that the economy does not respond strongly to changes in interest rates. Certainly, any anti-

inflation program that works by limiting demand will be ineffectual in stopping an inflation driven by increases in costs. The authors point out that tight monetary policy brings with it many potentially adverse consequences, such as a slowing of the introduction of productivity-enhancing capital goods, changes in exchange rates, and repercussions in various financial markets.

As an alternative to reliance on monetary policy, the authors suggest greater use of fiscal policy (taxes and expenditures), which they deem a more potent weapon. Once relieved of the burden of fighting inflation, the monetary authorities could concentrate their attention on encouraging investment and setting an appropriate nominal exchange rate, tasks to which interest rate policies are better suited. Perhaps if this approach to policy was implemented in the major advanced economies, worldwide growth could reach levels that have begun to seem unattainable.

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New Strategic Analysis

[The U.S. Economy: A Changing Strategic Predicament](#)

[Wynne Godley](#)

Most official economic forecasts for the second half of this year and 2004 indicate that the economy will grow at a moderate pace. However, as Distinguished Scholar Wynne Godley of Cambridge University points out in this new Strategic Analysis, U.S. households have reduced the rate at which they are piling up debt, a development that will continue to act as a drag on economic growth. Meanwhile, fourth-quarter data indicate that the U.S. current account deficit (the excess of imports over exports plus the net outflow of interest payments, dividends, and so on) has continued to widen, reaching a postwar record of five percent. This gap will also tend to hinder economic expansion, since money spent on imports "leaks" out of the flow of national income.

To demonstrate this point, Godley considers a hypothetical scenario, in which the economy grows at a moderate rate and no major actions are taken to balance international flows of products and property income. He calculates that in this case the current account and government deficits would grow to roughly 8.5 percent of GDP by 2008. Godley shows that this scenario is unlikely to materialize, because it implies that current account and public sector deficits would accumulate over time to implausible levels. He concludes that one premise of his calculations--moderate growth--is unrealistic, unless the government acts to reduce the current account deficit.

The results of this Strategic Analysis and an earlier one were discussed at the Levy Institute's 13th Annual Hyman P. Minsky Conference, held recently in New York City. Please see the front page for details.

Leon Levy: In Memoriam

Leon Levy, life trustee of Bard College and founder of The Levy Economics Institute, died on April 6, 2003, at his home in Manhattan. Mr. Levy was the leading donor to Bard College and the chairman of the Institute's board of governors. His philanthropy and leadership provided the means to promote programs associated with the study of the humanities and economics. He supported the Institute as a tribute to his father and contributed immeasurably to its development since its founding in 1986. He was a man of ideas, whose wise counsel and guidance will be sorely missed.

Mr. Levy was a hedge fund pioneer who joined the firm of Oppenheimer & Company in 1951 and founded Odyssey Partners with Jack Nash in 1982. He firmly believed that investing was as much a psychological as an economic act and that the stock market surge in the 1990s did not reflect a new economic reality, but only people's hopes. His autobiography, *The Mind of Wall Street* (with Eugene Linden), was published last year (Public Affairs, 2002). This semester, Mr. Levy taught a course at Bard College, Contemporary Developments of Finance, to which he brought peerless knowledge, delivered with characteristic enthusiasm and passion.



Mr. Levy was a trustee of the John Simon Guggenheim Memorial Foundation, Rockefeller University, and Institute of Fine Arts at New York University and was president of the Institute for Advanced Study at Princeton University.

The Bard community, including The Levy Economics Institute, extends its deepest condolences to his wife, Shelby White; his daughter, Tracy White; his brother, Jay; and the entire Levy family.

New Research Associate

Maria Sagrario Floro is an associate professor of economics at American University in Washington, D.C. Her recent research topics include gender dimensions of savings, time use, and overlapping activities and effects of financial crisis on gender relations. She was a coeditor of *Women's Work in the World Economy* (New York University Press, 1992) and has published articles such as "Economic Restructuring, Gender and the Allocation of Time," *World Development* (November 1995); "Women's Well-Being, Poverty and Work Intensity," *Feminist Economics* (Volume 1, Number 3, 1995); "Structural Adjustment, Gender and Labor Markets: The Philippines and Zambia," coauthored with Kendall Schaefer, *Journal of Developing Areas* (October 1999); and

"Financial Crisis, Gender, and Power: An Analytical Framework," coauthored with Gary Dymiski, *World Development* (July 2000). Floro received degrees from the University of the Philippines-Diliman and Monash University, Clayton, Australia, and a Ph.D. from Stanford University. Her dissertation on informal credit markets was published as a book, *Informal Rural Credit Markets and the New Institutional Economics: The Case of Philippine Agriculture*, coauthored with Pan Yotopoulos (Westview Press 1991).

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Publications and Presentations

Publications by Levy Institute Scholars

INSTITUTE PROFESSOR OF ECONOMICS PHILIP ARESTIS

Publications: "Causes of Euro Instability" (with I. Biefang-Frisancho Mariscal, A. Brown, and Malcolm Sawyer) and "Macroeconomics of Sterling and the Euro" (with Malcolm Sawyer), in A. M. Al-Agraa, ed., *The Euro and Britain: Implications of Moving into the EMU*, London: Pearson, 2002; "The Euro Area Deserves a New Economic Policy" (with Malcolm Sawyer), *Challenge*, March-April 2003; "The Importance of Capital Stock in Unemployment and Wage Determination," in H. Hagemann and S. Seiter, eds., *Growth Theory and Growth Policy*, New York: Routledge, 2003. Submitted written evidence to United Kingdom Treasury Select Committee on the Euro and Public Expenditure (with Malcolm Sawyer), February 18. Edited and contributed to special issue of *Eastern Economic Journal* on financial globalization, May 2003; contributions included introduction, "Financial Policies and the Average Productivity of Capital: Evidence from Developed and Developing Economies" (with P. Demetriades and B. Fattouh), and "Financial Globalization: Some Conceptual Problems" (with Santonu Basu).

Presentations: "On New Keynesian Economics," University of the Basque Country, Bilbao, Spain, February 4; "Critical Realism and the Political Economy of the Euro" (with A. Brown and Malcolm Sawyer) and "On Keynesian Monetary Policy" (with Malcolm Sawyer), Eastern Economic Association, New York, February 21-23; "The Nature and Role of Monetary Policy when Money Is Endogenous" (with Malcolm Sawyer), Post-Keynesian Study Group Seminar on Monetary Policy: Current "Consensus" and Future Alternatives, Downing College, University of Cambridge, March 28.

RESEARCH SCHOLAR ASENA CANER

Presentations: "Asset Poverty in the United States, 1984-1999: Evidence from the Panel Study of Income Dynamics" (with Edward N. Wolff) and "Savings of Entrepreneurs," Eastern Economic Association, New York, February 21-23.

SENIOR SCHOLAR

JAMES K. GALBRAITH

Publications: "The Brazilian Swindle and the Larger International Monetary Problem," *Brazilian Journal of Political Economy*, January 2003; "The Paramilitary Mind," *Texas Observer*, March 14, 2003; "What Price This War?" *Boston Globe*, March 24, 2003.

Presentations: "The Experience of Rising Inequality in Russia and China during the Transition" (with Ludmila Krytynskaia and Qifei Wang), Fifth International Meeting of Economists on Globalization and Development Problems, Havana, February 10-14.

SENIOR SCHOLAR**MALCOLM SAWYER**

Publications: "Causes of Euro Instability" (with Philip Arestis, I. Biefang-Frisancho Mariscal, and A. Brown) and "Macroeconomics of Sterling and the Euro" (with Philip Arestis), in A. M. Al-Agraa, ed., *The Euro and Britain: Implications of Moving into the EMU*, London: Pearson, 2002; "Investment, Capacity, and the Achievement of Full Employment," in E. Carlson and W. Mitchell, eds., *The Urgency of Full Employment*, Sydney, Australia: New South Wales Press, 2002; "The Euro Area Deserves a New Economic Policy" (with Philip Arestis), *Challenge*, March-April 2003. Submitted written evidence to United Kingdom Treasury Select Committee on the Euro and Public Expenditure (with Philip Arestis), February 18.

Presentations: "Fiscal and Monetary Policy in the Eurozone," University of the Basque Country, Bilbao, Spain, January 27; "The Ineffectiveness of Monetary Policy," Nottingham Trent University, United Kingdom, February 5; "Critical Realism and the Political Economy of the Euro" (with Philip Arestis and A. Brown) and "On Keynesian Monetary Policy" (with Philip Arestis), Eastern Economic Association, New York, February 21-23; "The Nature and Role of Monetary Policy when Money Is Endogenous" (with Philip Arestis), Post-Keynesian Study Group Seminar on Monetary Policy: Current "Consensus" and Future Alternatives, Downing College, University of Cambridge, March 28.

SENIOR SCHOLAR**EDWARD N. WOLFF**

Publications: "Skills and Changing Comparative Advantage," *Review of Economics and Statistics*, February 2003; "The Impact of Gifts and Bequests on the Distribution of Wealth," in Alicia H. Munnell and Annika Sundén, eds., *Death and Dollars*, Washington, D.C.: Brookings Institution.

Presentations: "Asset Poverty in the United States, 1984-1999: Evidence from the Panel Study of Income Dynamics" (with Asena Caner), and presidential address "The Devolution of the American Pension System," Eastern Economic Association, New York, February 21-23.

RESEARCH SCHOLAR**AJIT ZACHARIAS**

Presentation: "Accumulation, Gender Disparities in Paid Work, and Domestic Labor" (with Melissa Mahoney), Eastern Economic Association, New York, February 21-23.

RESEARCH SCHOLAR

GENNARO ZEZZA

Presentation: "Dynamic Properties of Stock-Flow Models with Stable Stock-Flow Norms," Eastern Economic Association, New York, February 21-23.

RESEARCH ASSOCIATE

RANIA ANTONOPOULOS

Presentations: "Ownership and Asset Building across Gender Lines: What Do We Know and Why Is It Important to Know?" Eastern Economic Association, New York, February 21-23; "Rethinking the Economy: The Hidden Household Sector," Business and Its Public Guest Speakers Series, New York University, March 3.

RESEARCH ASSISTANT

MELISSA MAHONEY

Presentation: "Accumulation, Gender Disparities in Paid Work, and Domestic Labor" (with Ajit Zacharias), Eastern Economic Association, New York, February 21-23.

HEAD OF INFORMATION SERVICES

GWYNETH H. CROWLEY

Publication: "User Perceptions of the 'Reliability' of Library Services at Texas A&M University," *Journal of Academic Librarianship*, February 2003.

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