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End This Depression Now!
Paul Krugman, Published by W.W. Norton & Company, Inc., 2012
259 pages, $24.95

In the fifth year of the global economic crisis, Paul Krugman gives a prescription for a full recovery in his book End This Depression Now! His preferred remedy is increasing government spending to cure the United States' unemployment problem. The book is a sustained argument to shift public opinion in favor of government stimulus in order to reduce the damaging consequences of sustained high unemployment and underemployment. Throughout the book, Krugman is accompanied by, his intellectual mentors, John Maynard Keynes, Irving Fisher and Hyman Minsky.

The costs of the crisis

Krugman starts with an analysis of the damaging effects of long-term unemployment on people's lives and the economy. After this analysis, he makes clear that urgent actions need to be taken to solve this serious problem. His central argument is "unemployment is all about insufficient demand." Since heavily indebted people and businesses are not eager to make investments, the government is the only actor who can spend to create demand. Contrary to those pushing for immediate fiscal consolidation, he repeats Keynes' central dictum: "The boom, not the slump, is the time for austerity."

Krugman argues we are still under the influence of the crisis, but we are not using all the tools and knowledge which we have to solve this depression. What is required is political will to take the measures needed for a quick and complete recovery. This raises an intriguing question: if the problem and solution are not too complex, why do politicians not fix it? His answer is that bad policies which give unfair advantages to wealthy and influential people have a powerful hold over our political culture.

This book is an attempt to make the lessons of macroeconomics textbook and make them relevant to the current reality. And it is going to be tough reading, especially for conservatives. Krugman explicitly presents his analysis in direct rebuttal to ideas advocated by well-known economic conservatives. His style is engaging and, as ever, he makes an effort to describe, sophisticated economic concepts in a comprehensible and fun way, utilizing stories and parables. There are several lessons from the book which the author insists must be learned. Firstly: "it is the fact that your spending is my income, and my spending is your income." Secondly, an economy can be depressed due to failures of coordination rather than lack of productive capacity. Thirdly, the solution of significant economic problems may not be as hard as it seems.

Krugman states that in this crisis monetary policy has not been able to increase demand because of the liquidity trap in which people hoard cash despite low interest rates. The liquidity trap, together with excessive debt, creates some paradoxes for the economy. Among these, the most controversial is the paradox of flexibility, which lies at the center of an intense debate on the minimum wage increase. One view is that the mass unemployment problem can be solved by cutting wages. However, Krugman alleges that more flexibility in wages and prices would worsen the economy by reducing everyone's income. On the basis of this idea, he argues that rising wages and prices are desirable.

Krugman is not without his critics. In contrast with his prescription for the unemployment problem, Richard Posner (2011) points out that reducing the minimum wage in order to decrease unemployment is the simplest measure in the short and long run. Doing so would reduce labor costs and create demand for more labor. Even if a lower minimum wage has negative effects on some people's income, the final effect on employment would be positive due to the production increase. Posner also states that longer term and higher unemployment benefits and other subsidy programs discourage unemployed people from job-seeking.

Gary Becker (2012) builds on this argument. He suggests that the Fed should aim for full employment instead of a low unemployment rate since a reduction in the unemployment rate can be result of a reduced labor force. He states that "means tested welfare programs, such as food stamps, subsidies on mortgage payments, and Medicaid benefits … greatly expanded during the past four years." They and the extension of unemployment benefits cause individuals' to leave the labor force or accept part-time jobs. As long as these policies keep being implemented, the Fed's low interest rate policy to achieve full employment will not work. This situation also carries a risk of excessive inflation.

Ending the depression

Krugman's main criticism of the Obama administration is the inadequate scale of its response. The biggest job-creation program in U.S. history, the American Recovery and Reinvestment Act, has not been sufficient to end this crisis. Additionally, mortgage relief failed to reach its aim.

In order to achieve full recovery, Krugman proposes policy changes in three areas. Firstly, the government should spend where the private sector is not willing to make use of its full productive capacity. Additionally, he emphasizes that consumer and business confidence will rise with the economic recovery, and, therefore, there is no need to be afraid of deficits. One spending method the government can use is providing aid to states to compensate for their budget cuts. This approach will serve to decrease unemployment and restart projects which could not be realized earlier. Another method is more aid to distressed individuals in various forms, such as a temporary increase in unemployment insurance and other safety net programs.

Secondly, the Fed should adopt a more aggressive quantitative easing approach and should allow moderately higher inflation. Higher inflation can be helpful by making borrowing more attractive and by reducing the real value of debt. Since the debt of home buyers was influential in this crisis, a third area of action should be reducing the burden of repayment by means of debt relief for housing. Moreover, softening the mortgage refinancing rules would be helpful in letting homeowners take advantage of the fall in interest rates. In order to reduce the burden of debt, policies such as allowing moderate inflation and providing mortgage relief could be a part of the strategy which will end this depression. The most important thing is the determination to pursue policies for job creation until the goal of full employment has been achieved.

As a conclusion

While Krugman makes important points about the need for stimulus packages to reduce unemployment, a crucial consideration is how this money is spent. Expenditures which do not have high multiplier effects in the economy may result in only weak or temporary demand increases and, therefore, waste money. Similarly, while Krugman recommends moderately higher inflation, he does not mention the effects of higher inflation on reducing real purchasing power and total demand, which are the flip side of these policies. Despite these oversights, this book is an important contribution. In an environment where calls to "austerity" are being regularly made, Krugman offers an alternative set of ideas for solving the United States' unemployment problem. Along the way, this book provides readers without an economics background a "complimentary" introduction to macro-economic theory that is clear and comprehensible.

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