

# Coyote Economist

News from the Department of Economics, CSUSB

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## Panel Discussion on The Recession

The Economics Department hosted a panel discussion on Wednesday, October 27, exploring the current recession, the stimulus program and the tipid nature of the current expansion.

The panel, chaired by Mayo Toruño, consisted of Professors Parviz Asheghian, Jim Charkins, Eric Nilsson, and Thomas Pierce.

All agreed that the most recent recession, from December of 2007 until June of 2009, was the most severe since the Great Depression of the 1930s. It was also agreed that the American Recovery and Reinvestment Act of 2009 (the official

name of the Federal Government stimulus package) was not as stimulative as it should have been, and that the Fed's expansionary monetary policy, while appropriate and necessary, has run up against the classic liquidity trap problem.

The first panelist, Dr. Parviz Asheghian, offered the audience a brief history of the 1930s Great Depression, reminding us of the fact that it wasn't until the U.S. entered World War II that the economy rebounded. The unprecedented fiscal stimulus provided by the Federal Government's war-related deficit spending dramatically reduced the unemployment rate while setting the stage

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Economics Panel, from left to right: Mayo Toruño, Parviz Asheghian, Eric Nilsson, Jim Charkins, Thomas Pierce.

## Econ Radicals!!

The new president of the Econ Radicals, the Economics Student Club, is Adam Elway.

The Econ Radicals take their name from a desire to go to the root of injustice and explore ways to improve the human condition. The purpose and aims of the Econ Radicals are: (1) to promote interest in economics within academia and on a societal level; (2) to provide students an environment in which to explore past, present and future economic issues, beyond the confines of academia; (3) to inform students of career options and upcoming events that may be useful in career planning; (4) to design products, plan guest speaker seminars, and organize field trips; and (5), contribute to the community through volunteerism.

The Econ Radicals are on Facebook. If you would like to join the Econ Radicals, please email "econradicals@gmail.com"

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for the prosperity of the post-war era, the Golden Age of American capitalism from the end of World War II until the early 1970s.

Professor Asheghian noted that there are interesting parallels between the era of the Great Depression and the current time period. For example, in both eras income and wealth inequality grew dramatically in the decades leading up to the economic contraction, contributing to the speculative bubbles that preceded both contractions.

Dr. Jim Charkins laid out the economic facts of the current recession, highlighting the fact that this is easily the most severe recession the U.S. has experienced since the Great Depression.

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Gross domestic product (GDP) declined more dramatically than at any point in the post-World War II era. In addition, not only has this been the longest recession since World War II (lasting 18 months) it brought about the greatest decline in employment – approximately 8 million jobs– while increasing the average duration of unemployment to 35 months (the net highest average duration of unemploy-

ment was a little over 20 months in early 1983).

Finally, home prices (as measured by the Case-Shiller home price index) have fallen more dramatically in the current cycle than at any point since the early 1980s (when the Case-Shiller index was first developed). Similar

*...as macroeconomic students know, the tax multiplier is smaller than the government spending multiplier.*

housing data going back to the 1970s is consistent with this observation.

While the National Bureau of Economic Analysis has declared the recession formally over, the evidence suggests that unemployment will remain high for a few more years.

Dr. Eric Nilsson summarized the impact of the American Recovery and Reinvestment Act by noting that despite its price tag, \$787 billion, the effect was not as strong as it could have been.

The reason is simple: 40% of the stimulus spending consisted of tax cuts rather than direct government spending; and as macroeconomic students know, the tax multiplier is smaller than the government spending multiplier.

Although it was weaker than it could have been, the stimulus program did save approximately 2.4 million jobs and, so, was a good thing.

Dr. Thomas Pierce, closed out the discussion by explaining the actions of the Federal Reserve System (the Fed) during the most recession.

He noted that the Fed carried out an unprecedented volume and variety of stimulative monetary policies with the intention of not only stabilizing the financial sector but, at the same time, providing the context for the increased spending which lower interest rates are supposed to prompt.

As a result of the Fed's policies short-term interest rates are at historic lows (essentially zero for the Federal Funds rate and in the 4.5% range for 30-year, fixed, mortgages). Yet, in a context of extremely weak aggregate demand (due to the enormous number of unemployed people), motivating people and businesses to spend – even when interest rates are low – is very difficult.

## We're on Facebook !!

Don't forget to check us out on Facebook and say that you like us!

You can find the economics department at The CSUSB Department of Economics Facebook page. Joining us on Facebook is an important way of keeping up with departmental news and events as well as getting information on political economy.

## Staying Informed about CSUSB Department of Economics Events and News

If you're receiving the *Coyote Economist*, then you're on our mailing list and everything is as it should be. But, if you know of an Economics Major, or an Econ Fellow Traveler, who is not receiving the *Coyote Economist* through email, then please have him/her inform our Administrative Support Coordinator, Ms. Jacqueline Carrillo, or the Chair of the Economics Department, Professor Mayo Toruño. Our phone number is 909-537-5511.

You can stay informed by consulting:

**Our Website** - <http://economics.csusb.edu/>

**Our Facebook Page** - <http://www.facebook.com/pages/CSUSB-Department-of-Economics/109500729082841>

**Chair of the Economics Department** – [mtoruno@csusb.edu](mailto:mtoruno@csusb.edu)

# Deficit Spending and Belt Tightening

The last ten months have witnessed increased concern over deficit spending and the growing public debt.

While these concerns are most frequently voiced by right-wing politicians, they're now being expressed by political centrists and the mainstream media.

Thus, this past February, President Obama signed an executive order establishing the National Commission on Fiscal Responsibility and Reform, whose mission is to balance the Federal Government's budget, excluding interest payments on the debt, by 2015. The commission's report is due December 1, and will more than likely be used by President Obama to propose belt tightening measures at his upcoming 2011 State of the Union message.

This is unfortunate because this is exactly the opposite of what the government should be doing at this time. Rather than *reducing* the size of the deficit, the government should be *increasing* it through direct government spending to reduce the suffering and economic waste brought on by unemployment.

But the problem is that pleas for government belt tightening resonate with an electorate that's experiencing economic hardship.

*...government borrowing will take up the slack left by the decline in private borrowing.*

A common refrain is that government should learn to live within its means; governments, so it's believed, should not be spend more than they collect in taxes, especially at a time when the average household is being forced to live with less.

While these sentiments have an air of common-sense fairness, accounting for their populist appeal, they're riddled with contradictions and logical fallacies.

Here we'll focus on only one version of this belt-tightening argument; the claim that deficit spending has little to no stimulative impact because it leads to a reduction in private spending.

At least two versions of this argument exist, but the one that's most common among conservative economists is that deficit spending causes interest rates to rise (as a result of the increased public borrowing) which in turn causes investment spending, consumption spending and net exports to fall.

*...it's important to remember that in the current recession interest rates are at a historic low*

In the extreme, this argument claims that the reduction in private spending will counterbalance the increase in public spending, negating thereby the stimulative impact of the deficit.

The only time such an argument might have merit would be in the context of full employment, in which case deficit spending is unnecessary anyway. But, in a context of considerable unemployment, government borrowing will be financed by the excess saving that's not being absorbed by the private sector.

Rather than displacing private borrowing, government borrowing will take up the slack left by the decline in private borrowing. The impact on interest rates will be slight. In addition, the increased economic activity brought on by the government's deficit spending will have the effect of inducing firms to add to their productive capacity by increasing investment spending.

This can occur even if interest rates were to rise (since investment spending depends on the difference between the expected rate of profit and the

interest rate, it will increase if expected profitability rates grow faster than interest rates).

Thus, deficit spending, rather than crowding out private investment through rising interest rates, will actually induce investment spending through the rising profit expectations made possible by the growth in aggregate demand brought on by government deficit spending. What's more, as the economy grows and incomes begin to expand, so too will the flow of saving which will put further downward pressure on interest rates.

But, in addition to the above, it's important to remember that in the current recession interest rates are at a historic low as a result of the Fed's aggressive monetary policy.

*...it's exactly the opposite of what the government should be doing at this time.*

Thus, government can borrow at much lower rates than was possible at the beginning of the recession. The private saving that is not being channeled into productive activity can be borrowed by the government for deficit spending, without putting upward pressure on interest rates.

This will stimulate the economy and induce investment spending (as well as consumption spending and net exports), causing GDP and employment to grow.

Once the economy comes back to full employment, the deficit, as a proportion of GDP, will decline of its own accord. The growing level of income and employment, made possible by aggressive fiscal and monetary policy, will have the effect of increasing the flow of tax revenues which, with a given level of government spending, will cause the deficit to shrink over time.

# Econ 390: Origins of Political Economy

In *Winter 2011* the Economics Department will be teaching a special topics course: Economics 390, Origins of Political Economy. This course will consider in detail the economic and social theories of Karl Marx and the intellectual, political, and economic environment that caused these theories to appear.

In the future, the material appearing in this special topics course will be taught in a new course, Economics 443 (Origins of Political Economy). The already-existing Economics 445 (Political Economy) will be transformed to focus on 20<sup>th</sup> and 21<sup>st</sup> century developments in Marxian economic and social theory.

## Tentative *Spring* 2011 Schedule of Classes

#	SEC	TITLE	HOURS		DAYS	INSTRUCTOR
200	02	PRIN MICROECON	0400-0550	PM	MW	PEREZ-MARES
372	01	BUSINESS CYCLES	0400-0550	PM	MW	HARRIS
202	02	PRIN MACROECON	0600-0750	PM	MW	JORGENSEN
200	01	PRIN MICROECON	0920-1030	AM	MWF	HARRIS
202	01	PRIN MACROECON	1040-1150	AM	MWF	HARRIS
200	03	PRIN MICROECON	1000-1150	AM	TR	PEREZ-MARES
202	03	PRIN MACROECON	1000-1150	AM	TR	NILSSON
450	01	GLOBAL ECONOMY	1000-1150	AM	TR	ASHEGHIAN
200	04	PRIN MICROECON	0200-0350	PM	TR	ASHEGHIAN
202	04	PRIN MACROECON	0200-0350	PM	TR	PIERCE
490	01	ECONOMETRICS	0200-0350	PM	TR	KONYAR
500	01	HIST ECON IDEAS	0400-0550	PM	TR	TORUNO
410	01	MONEY & BANKING	0600-0750	PM	TR	PIERCE
200	05	PRIN MICROECON	0600-0750	PM	TR	KONYAR
360	01	ENVIRO ECON	0800-0750	PM	TR	DULGEROFF
311	01	ECON K-8	1200-0150	PM	TR	CHARKINS
445	01	POLITICAL ECON	1200-0150	PM	TR	NILSSON

## Tentative *2011-2012* Schedule of Classes

Fall	Winter	Spring
Econ 200	Econ 104	Econ 200
Econ 202	Econ 200	Econ 202
Econ 302	Econ 202	Econ 311
Econ 311	Econ 300	Econ 360
Econ 335	Econ 311	Econ 372
Econ 410	Econ 311	Econ 410
Econ 435	Econ 322	Econ 450
Econ 443	Econ 333	Econ 490
Econ 480	Econ 357	Econ 500
Econ 503	Econ 430	
Econ 530	Econ 445	
Econ 600	Econ 475	
Ssci 320	Econ 540	
	Econ 573	