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Reinhart and Rogoff are wrong about austerity

Robert Pollin and Michael Ash

In 2010, two Harvard economists published an academic paper that spoke to the world's biggest policy question: should we cut public spending to control the deficit or use the state to rekindle economic growth? [Growth in a Time of Debt](#) by Carmen Reinhart and Kenneth Rogoff has served as an important intellectual bulwark in support of austerity policies in the US and Europe. It has been cited by politicians ranging from Paul Ryan, the US congressman, to George Osborne, the UK chancellor. But [we have shown that several critical findings advanced in this paper are wrong](#). So do we need to rethink austerity economics more broadly?

Their research is best known for its result that, across a broad range of countries and periods, economic growth declines dramatically when a country's level of public debt exceeds 90 per cent of gross domestic product. In their work with a sample of 20 advanced economies in the postwar period, they report that average annual GDP growth ranges between about 3 per cent and 4 per cent when the ratio of public debt to GDP is below 90 per cent. But it collapses to -0.1 per cent when the ratio rises above a 90 per cent threshold.

In [a new working paper](#), co-authored with Thomas Herndon, we found that these results were based on data errors and unsupported statistical techniques. For example, because of miscalculation and unconventional methods of averaging data, a one-year experience in New Zealand in 1951, during which economic growth was -7.6 per cent and the public debt level was high, ends up exerting a big influence on their overall findings.

When we performed accurate recalculations, we found that, when countries' debt-to-GDP ratio exceeds 90 per cent, average growth is 2.2 per cent, not -0.1 per cent. We also found that the relationship between growth and public debt varies widely over time and between countries.

So what does this mean? Consider a situation in which a country is approaching the threshold of a 90 per cent public debt to GDP ratio. It is not accurate to assume that these countries are reaching a danger point where growth is likely to decline precipitously.

Rather, our evidence shows that a country's growth may be somewhat slower once it moves past the 90 per cent public level. But we cannot count on this being true under all, or even most, circumstances. Are

we considering the US demobilisation after the second world war or New Zealand during a severe one-year recession? One needs to ask these and similar questions, including whether slow growth was the cause or consequence of higher public debt.

What of our present circumstances? Using the Reinhart/Rogoff data, we found that the average GDP growth rate for countries carrying public debt levels greater than 90 per cent of GDP was either comparable to or higher than those for countries whose debt ratios ranged between 30 per cent and 90 per cent.

Of course, one could say that these were special circumstances due to the 2007-2009 financial collapse and Great Recession. Yet that is exactly the point. When the US and Europe were hit by the financial crisis, and subsequent collapse of private wealth and spending, deficit-financed government spending was the most effective tool for injecting demand back into the economy. The increases in deficits and debt were indeed large in these years. But this was a consequence of the crisis and a policy tool for moving economies out of the recession. The debt was not the cause of the growth collapse.

The case for austerity has never relied entirely on Prof Reinhart and Prof Rogoff. But the other major claims made recently by austerity hawks have also not held up well. Austerity supporters circa 2009-2010 consistently argued, frequently in this newspaper, that the large US deficits would lead to dangerously high inflation and interest rates. Neither prediction came true. In fact, both inflation and interest rates on treasuries were at historic lows in the four years, 2009-2012, during which deficits were at their peak.

It is also untrue to say that the large deficits have created an unsustainable burden on the US public finances. In fact, since 2009, the US government's interest payments on debt have been at historically low levels, not historic highs, despite the government's rising level of indebtedness. This is precisely because the US Treasury has been able to borrow at low rates throughout these high deficit years.

We are not suggesting that governments should borrow and spend profligately. But judicious deficit spending remains the single most effective tool we have to fight against mass unemployment caused by severe recessions. Recent research by Prof Reinhart and Prof Rogoff, along with all related arguments by austerity proponents, does nothing to contradict this fundamental point.

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