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How to Kill a Recovery

By PAUL KRUGMAN

The economic news has been better lately. New claims for unemployment insurance are down; business and consumer surveys suggest solid growth. We're still near the bottom of a very deep hole, but at least we're climbing.

It's too bad that so many people, mainly on the political right, want to send us sliding right back down again.

Before we get to that, let's talk about why economic recovery has been so long in coming.

Some economists expected a rapid bounce-back once we were past the acute phase of the financial crisis — what I think of as the oh-God-we're-all-gonna-die period — which lasted roughly from September 2008 to March 2009. But that was never in the cards. The bubble economy of the Bush years left many Americans with too much debt; once the bubble burst, consumers were forced to cut back, and it was inevitably going to take them time to repair their finances. And business investment was bound to be depressed, too. Why add to capacity when consumer demand is weak and you aren't using the factories and office buildings you have?

The only way we could have avoided a prolonged slump would have been for government spending to take up the slack. But that didn't happen: growth in total government spending actually slowed after

the recession hit, as an underpowered federal stimulus was swamped by cuts at the state and local level.

So we've gone through years of high unemployment and inadequate growth. Despite the pain, however, American families have gradually improved their financial position. And in the past few months there have been signs of an emerging virtuous circle. As families have repaired their finances, they have increased their spending; as consumer demand has started to revive, businesses have become more willing to invest; and all this has led to an expanding economy, which further improves families' financial situation.

But it's still a fragile process, especially given the effects of rising oil and food prices. These price rises have little to do with U.S. policy; they're mainly because of growing demand from China and other emerging markets, on one side, and disruption of supply from political turmoil and terrible weather on the other. But they're a hit to purchasing power at an especially awkward time. And things will be much worse if the Federal Reserve and other central banks mistakenly respond to higher headline inflation by raising interest rates.

The clear and present danger to recovery, however, comes from politics — specifically, the demand from House Republicans that the government immediately slash spending on infant nutrition, disease control, clean water and more. Quite aside from their negative long-run consequences, these cuts would lead, directly and indirectly, to the elimination of hundreds of thousands of jobs — and this could short-circuit the virtuous circle of rising incomes and improving finances.

Of course, Republicans believe, or at least pretend to believe, that the direct job-destroying effects of their proposals would be more than offset by a rise in business confidence. As I like to put it, they believe that the Confidence Fairy will make everything all right.

But there's no reason for the rest of us to share that belief. For one thing, it's hard to see how such an obviously irresponsible plan — since when does starving the I.R.S. for funds help reduce the deficit? — can improve confidence.

Beyond that, we have a lot of evidence from other countries about the prospects for “expansionary austerity” — and that evidence is all negative. Last October, a comprehensive study by the International Monetary Fund concluded that “the idea that fiscal austerity stimulates economic activity in the short term finds little support in the data.”

And do you remember the lavish praise heaped on Britain’s conservative government, which announced harsh austerity measures after it took office last May? How’s that going? Well, business confidence did not, in fact, rise when the plan was announced; it plunged, and has yet to recover. And recent surveys suggest that confidence has fallen even further among both businesses and consumers, indicating, as one report put it, that the private sector is “unprepared to fill the hole left by public sector cuts.”

Which brings us back to the U.S. budget debate.

Over the next few weeks, House Republicans will try to blackmail the Obama administration into accepting their proposed spending cuts, using the threat of a government shutdown. They’ll claim that those cuts would be good for America in both the short term and the long term.

But the truth is exactly the reverse: Republicans have managed to come up with spending cuts that would do double duty, both undermining America’s future and threatening to abort a nascent economic recovery.



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