Faculty Address: Prof. Lawrence Krohn
Professor of Practice, International Economics

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[In brackets, the reader will find some comments that were omitted from the delivered address. The speaker felt that they were just too dry and wonkish for that warm, time-constrained and very festive Sunday afternoon!]

Thank you, Chris and thanks to the entire Fletcher Student Council.

I received news of this award by e-mail three weeks ago, and was surprised, stunned, very appreciative and extremely proud. Those reactions were enhanced when Dean Sheehan subsequently sent me the list of those illustrious colleagues who had preceded me in receiving it. My emotions are undiminished as I speak to you today.

Now, my allotted time is short and this is not an Academy award, so I will not thank each of my ancestors individually – nor my agent. But I do want to collectively acknowledge the individuals who stand behind those of us who teach. The deans, administration, staff, teaching assistants – they all toil to make us look good. So when we do succeed, no small measure of credit owes to them. Some of you are here with me on the podium, some in the audience; you have my profound gratitude.

My theme today is civility (and, alas, the lack of it). First, the Fletcher faculty, my extraordinary colleagues. They are so diverse, come from so many backgrounds, with differing ideologies, philosophical and pedagogical. Yes, there are disagreements among them; that is quite natural. What impresses is that compromises are worked out, decisions are reached, Fletcher progresses. This is a quality in my colleagues that I greatly appreciate, one that enhances my pride in being associated with the Fletcher School.
But you, the Fletcher student body, are even more diverse; you come from everywhere. And in and out of the classroom, your civility is remarkable. Even in seminar courses, where student participation is high and opinions can be freely expressed, there has never been in my experience a moment of friction, not to mention incivility. I want to express my admiration for these qualities in you. The point I will be making is that they are not only morally desirable traits, but constructive ones as well.

Now my tone must darken. In the world that I abandoned four years ago to come teach here at Fletcher – that of financial services – and the various worlds to which many of you are now destined, such civility is not always the norm. I would even go so far as to say that over the last two decades civility has waned dramatically – at great cost – and not just in the US.

The deterioration of economic culture played an important role in the crisis of 2007 – 08; some would say a predominant role. This might be perceived as old news and thus not of great current interest. But the cost of this economic incivility, which is virtually unmeasurable, is ongoing and the necessary repairs are far from complete. Many of us remain distrustful of our banks, our brokers, our regulators, our rating agencies. In matters financial, we are wary, skeptical, bruised.

On the political front, there has also been a huge decline in civility. Many of us do not trust our elected representatives and candidates to elective office. We certainly don’t believe the campaign promises we hear. You all read the papers. Political discourse is poisonous and is likely to become even more so as the current US campaign progresses.

You know, when I was a kid, my late parents were great admirers of Adlai Stevenson, a brainy senator from Illinois who had the temerity to run for president twice against World War II hero Dwight Eisenhower. I remember that he was characterized by his opponents as an ‘egghead’, a very slightly pejorative epithet for an intellectual. That's what passed for political invective in those days. How far we've come. In any case, the point to which I'll return in a moment is that on the political front too, the cost of present-day incivility is high.
How can we explain the deterioration of our economic and political culture? Some say our institutions are flawed. Our incentives are misaligned. True enough. But why? How did they get that way? This is a profoundly difficult question to answer and must remain the subject for another day.

With your indulgence I would like to wear my wonkish economist hat for just a few moments. You'll soon see where I'm going with this.

Fiscal austerity is the topic of the day. Discussions of it are inescapable, its importance transcending the business pages. It has become the stuff of page 1. How can one not favor fiscal austerity? Just compare the economic well-being of those countries whose governments have lived within their means and that of the countries whose governments have not. It is clear: fiscal austerity is imperative.

[Sustained fiscal irresponsibility will always end badly. That said, the US is in the unique position of being able, if it chooses, to engineer what amounts to a Ponzi scheme for far longer than any other nation.]

By implication, Angela Merkel, the German Chancellor, is right, David Cameron, the UK Prime Minister, is right. The so-called freshwater or Chicago school of economic thought in the US is then right as well.

But here is the critical qualifier: they are right only in an ultimate, longer run sense. In the short run, at least for the US and UK -- and quite likely for several other countries, like Germany, as well -- they are wrong. Dead wrong.

Instead, those who preach less, not more, near-term austerity, like Paul Krugman and Joseph Stiglitz, are right. More recently, the IMF [International Monetary Fund] is right as well on this issue. Because it is still too early for fiscal consolidation in many countries.

The UK is in recession. [It has suffered two consecutive quarters of falling output (real GDP), although the last data point – QI of this year – is still subject to revision.] Germany is not, but its neighbors and trading partners are. [Germany has long been supported, through exports, by the domestic demand
of its local trading partners and now has an opportunity to repay them in kind.]

The US is not technically in recession, but is operating well below its natural or potential level of output or, otherwise put, is operating well above its natural rate of unemployment.

[The declining US unemployment rate, currently at 8.1%, is deceiving because so many discouraged workers have dropped out of the labor force. If the labor force participation rate, currently at 63.6%, were at 66.0% where it sat in November 2007, on the eve of the recession, the current unemployment rate would be 11.5%, compared to 4.7% in November 2007. The economic – and human – cost of such extensive and durable joblessness has been underestimated.]

In several countries, low interest rates imply that the benefits of austerity are greatly outweighed by its costs.

[The strongest argument against fiscal policy has always been the ‘crowding-out’ effect, whereby (in the case of stimulus) the additional government borrowing pulls up interest rates, at the expense of investment and durables consumption, so that the net stimulus is greatly reduced. But this effect is not operative under the current circumstances of ‘liquidity trap’ whereby basic short-term interest rates stand effectively at zero and the public is holding more liquidity than it needs. Any additional government borrowing would merely absorb some of that excess, leaving interest rates largely unaffected. Moreover, for certain ‘safe-haven’ countries like the US, UK and Germany, even longer-term sovereign borrowing costs are nil or negative once adjusted for inflation. The burden on future generations of any borrowing today is diminished to that extent.]

But why are we even having this discussion 4 1/2 years after the onset of recession in the US and three years after the economy resumed growth? Yes, on July 1 we will be embarking on the fourth year of so-called recovery. The answer is that monetary policy is nearly exhausted and fiscal policy has been
woefully inadequate. I will focus on fiscal policy because that is by far the more politicized of the two.

Back to my main theme. We got too little fiscal stimulus in 2008 - 09 and what we did get was inefficiently designed. You heard yesterday's speaker Dr. Richard Haass lamenting the state of US infrastructure and education. Why didn't we support them given the desperate need we had for fiscal stimulus, which meant that we could spend at negligible opportunity cost?

Because the state of political incivility was such that in the face of a dire national emergency, ideology, political maneuvering and pandering trumped common sense. There was too little goodwill, too little cooperation.

[True, the inside (decision-making) and outside (implementation) lags involved in fiscal policy – especially public works spending – are notoriously long. But through planning ahead for such eventualities, reinforcement of the automatic stabilizers, and above all political harmony in responding quickly to the need for well conceived spending projects, the lags can be shortened. By September 2008, it was clear that the depth of the crisis implied that a longer than usual planning-cum-implementation horizon had presented itself. But the opportunity was squandered.]

Now the moral outrage of a single academic is not the point here; that is subjective to him and not of great interest. But incivility has an enormous objective cost, one that is now being borne (not just in the US) and will continue to be borne unless we change course soon.

Fletcher graduates, I implore you to take your civility with you when you leave -- as you will today -- our embrace. I realize that you can't impose it; the worlds you are about to inhabit may not be receptive. But you can inspire by example. For the reasons I have cited, the effort is worth making.

Thank you for your attention to my comments, thank you for the Paddock award and good luck to you in all of your endeavors.