Recession, Depression and Expansion

Economics invests common words with new meanings. As the economic slump is explained in innumerable newspaper columns, the terms ‘recession’ and ‘depression’ have acquired great significance. The dictionary defines ‘recession’ as ‘a mild but widespread slowdown in economic activity’. ‘Depression’ appears to be a more serious ailment being defined as ‘a period during which business and employment decline or remain at a low level of activity’. As global economic indicators lurch downwards many columnists remind us of the 1930s and the ‘Great Depression’, an economic downturn of a magnitude that has never since been experienced in the United States. Historians of economics and political analysts now revisit the turbulent years of the 1930s, a decade which must remain etched in history as one of the 20th century’s most critical periods. In today’s globally interconnected economy an American ‘slump’ necessarily influences distant countries; the virus of recession and economic instability is quickly transmitted. The ongoing recession has brought in its wake a new prominence to unfamiliar words; ‘deflation’, a term used only in the context of tyres, now describes a rare economic trend. The elections and the Indian Premier League seem to have successfully diverted attention in India from gloomy economic forecasts, providing a recess from discussions of economic indicators and their interpretations. Economics and political ideologies are sometimes closely linked, with the result that even the most eloquently argued analyses are viewed with suspicion by ideological opponents. Statistics are quoted, misquoted, interpreted and misinterpreted in a manner that seems to set economic analysis distinctly apart from the sciences. However, a consensus view has emerged that the global economy is ailing, in the grip of a recession whose duration is hard to predict. Will a recession deepen into a ‘depression’, a condition that appears more serious by dictionary definitions? In reading and listening to the current discussions of economic issues, as a lay outsider, I have been struck by the fact that the public perception of economics and economists must be better informed and that the role of public financial institutions, banks and insurance companies amongst others must be better understood. In India the relationship between the private sector and government has become increasingly onesided; corporate responsibility must be a well defined and clearly appreciated term if governments are to use public resources in times of distress, especially when complete freedom of action is demanded in more comfortable times.

In thinking about the present economic situation an analogy from the world of medicine is helpful. For clinicians, the understanding of the causative factors in a disease is often the key to treatment and, more importantly, the key to prevention. A simple minded extrapolation suggests that this must be true for the ills of economies. Where did the virus which has caused the present global economic recession originate? For virologists this will be a familiar question, reminding them of the rise and spread of AIDS, whose causative agent the human immunodeficiency virus (HIV) appeared rather suddenly on the scene in the 1980s. The origins of HIV, its evolutionary history and its future remain a fascinating subject of study. In a curious coincidence the discoverers of HIV, Luc Montagnier and Françoise Barre-Sinoussi received the Nobel Prize for Physiology or Medicine last year at the same time that Paul Krugman was awarded the Nobel Memorial Prize in Economic Sciences. Krugman, an economist at Princeton University is even more widely known and read as a columnist for The New York Times. Readers of The Hindustan Times will find Krugman’s essays on the Op-Ed pages, topical, provocative and entertaining. Krugman’s Nobel award recognises his contributions to ‘trade theory’ and his insights into the basic forces that shape economic activities across countries, giving rise to an ‘economic geography’. Krugman is also an engaging writer whose themes may have been somewhat distant from the concerns of lay readers in India, until the global economic crisis began to loom ominously. The term ‘meltdown’ now appearing with great frequency in columns by economists might remind scientists of nuclear reactors heading into an emergency. In a recent column, attractively titled ‘Making Banking Boring’ (The New York Times, 10 April 2009), Krugman argues that the ‘supersized financial sector’ which was touted as ‘the key to financial prosperity’ has ‘turned into the monster that ate the world economy’. In Krugman’s view the attractiveness of finance and investment banking as careers has made ‘wheeling and dealing’ in the banking sector a sure recipe for disaster. For years now, outsiders to the area of management edu-
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cation have watched with some disbelief the salaries drawn by engineers who by academic sleight of hand are converted into ‘investment bankers’, using risk analysis methods which may hardly be suitable to the real world. The traditional, conservative banker has been transformed over the years. Lending, and lending riskily has been the key to recent spurs of economic activity, even as uncovered debt has increased. Collapse of the frontline institutions is inevitable and a domino effect has already become visible. Krugman notes that the post-depression banking industry in America was ‘tightly regulated, far less colourful . . . and far less lucrative for those who ran it. Banking became boring, partly because bankers were so conservative about lending’.

The recession has already begun to be a matter of concern for universities in the United States. The large private universities, which manage corpus funds, larger than the economies of small nations, have begun to experience a shrinking of their base of flexible capital. The Harvard endowment, the largest in the world, is reported to have shrank by as much as $8 billion, forcing a rethink on expansion plans. Harvard is not alone, with several institutions considering salary and hiring freezes and increases in tuition fees for students, at a time when education loans are becoming tighter. Recessions also come with silver linings and some analysts expect that the demand for higher education will rise, as employment opportunities decline. Journals like Science and Nature have begun to carry reports on the effects of the recession on scientific research. Has India begun to worry about the recession or are we, as some would have us believe, ‘insulated’? Will we wake up, after the two month long recess for the general elections, to find that an economic crisis is upon us? Will the ambitious plans for expansion of the higher education sector and the area of scientific research find the financial resources needed to carry the plans to fruition? Or will we find that resources are limited and that suboptimal funding retards the new institutions at their birth? Indian institutions do not have large reservoirs of corpus funds and necessarily maintain themselves on annual government grants. As expenditures mount on salaries and essential services, development and expansion must take a back seat. As the government’s tax revenues show a downward trend it is hard to imagine that public funding of higher education and research will remain unaffected. It might be prudent to prepare for leaner days ahead, since belt tightening is an activity that is easier to do after an election.

When will the tides of the economic crisis recede? What is to be done? Krugman argues, in an essay in The New York Review of Books (2008, 55, Dec. 18) that ‘what the world needs right now is a rescue operation’. His prescription is one that is repeated almost daily by analysts: ‘get credit flowing and prop up spending’. The first is more difficult in Krugman’s view, but must be done. He argues for financial reform quoting John Maynard Keynes on the Great Depression: ‘We have involved ourselves in a colossal muddle, having blundered in the control of a delicate machine, the working of which we do not understand’. In emphasizing the power of ideas he again quotes Keynes: ‘Soon or later, it is ideas not vested interests, which are dangerous for good or evil’. Krugman argues against those who believe ‘that our economic problems are structural with no quick cure available’, by noting ‘that the only important structural obstacles to world prosperity are the obsolete doctrines that clutter the minds of men’. I suspect that both communism and unrestrained capitalism spurred on by under regulated free markets may well be described as ‘obsolete doctrines’. When will the recession end or has it already begun to retreat? In a recent column (The New York Times, 17 April 2009; The Hindu, 18 April 2009) entitled ‘Green Shoots and Glimmers’, Krugman borrows his title from two optimists, the Chairman of the US Federal Reserve (the equivalent of the Reserve Bank), who sees ‘green shoots’ and President Obama who ‘sees a glimmer of hope’. He is more cautious warning that ‘history shows that one of the greatest policy dangers, in the face of a severe economic slump, is premature optimism’.

In my idle reading of columns on economics I could not help wondering if monetary policy which involves central banks raising and lowering interest rates in response to economic indicators, was a conditioned response. There are other aspects of policy like tax cuts and tax breaks that are discussed leaving the ordinary reader mildly puzzled. In reflecting on issues that seem important but difficult to understand, I was reminded of a response to a scheme in the days of the US President Ronald Reagan which hoped that ‘top end tax cuts would trickle down to produce unparalleled growth’. The late Harvard economist and former US Ambassador to India during the 1960s, John Kenneth Galbraith is quoted (R. Parker, Boston Globe, 7 May 2006) as commenting on the scheme in characteristically acerbic fashion: ‘After feeding oats to the horses one should not gaze too closely on what trickles down to the sparrows’.

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