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## The Reinhart/Rogoff brawl

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An insistent question of our time is, how much government debt is too much. Is there some debt level that becomes crushing as opposed to merely costly? The controversy over research by economists Carmen Reinhart and Kenneth Rogoff shows how explosive the issue is. They suggested that debt exceeding 90 percent of a country's economy (gross domestic product, or GDP) corresponds to a sharp drop in economic growth. But their work is being challenged by three other economists, who say that Reinhart and Rogoff made basic errors that invalidate their results.

This dispute, which would normally be confined to obscure scholarly journals, has assumed greater visibility because it involves the debate over deficit spending. One group of economists and policymakers argues that annual deficits must be cut because they're creating — or have already created — dangerous debt levels. Another group contends that large deficits are needed to propel stronger recoveries and reduce huge unemployment.

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It's "austerity" versus "stimulus." If debt exceeding 90 percent of GDP is hazardous, then the case for austerity seems stronger. (Already many countries exceed or are approaching the 90 percent mark.) If not, deficit spending remains a possible temporary spur. Which is it? Although the newly discovered errors in Reinhart and Rogoff's 2010 paper ("Growth in a Time of Debt") are embarrassing, they do not alter one of its main conclusions: High debt and low economic growth often go together.

Glance at the table below. It compares the annual economic growth rates of 20 advanced countries from 1945 to 2009 at various debt levels. The debt-to-GDP levels are given in the left-hand column. The next two columns show the annual economic growth rates estimated by Reinhart and Rogoff and then by the challenging economists from the University of

Massachusetts. (They are Thomas Herndon, Michael Ash and Robert Pollin; Reinhart and Rogoff are both at Harvard.)

Debt/GDP	Annual economic growth, 1945-2009	
	Reinhart/Rogoff	UMass economists
0-30%	4.1%	4.2%
30-60	2.8	3.1
60-90	2.8	3.2
90+	-0.1	2.2

After recalculating the Reinhart/Rogoff data, the UMass economists confirm that high debt implies lower economic growth. At the highest debt levels, growth is half what it is at the lowest debt levels. Whether debt causes low growth or merely reflects economic weakness is undetermined. But the UMass economists debunk the notion that growth collapses when debt hits 90 percent of GDP. One problem with the Reinhart/Rogoff study: A coding error excluded five countries — Australia, Austria, Belgium, Canada and Denmark — from the calculations.

Still, these modest mistakes have inspired outlandish allegations. “Did an Excel coding error destroy the economies of the Western world?” asked economist Paul Krugman in his New York Times column. Well, no. The Reinhart/Rogoff paper was published in January 2010, more than a year after Lehman Brothers’ failure and the onset of the financial crisis. At that point, all the ingredients of Europe’s debt crisis (housing bubbles in Spain and Ireland, huge budget deficits in Greece, weak banks throughout the continent) were also in place.

“How much unemployment was caused by Reinhart and Rogoff’s arithmetic mistake? That’s the question millions will be asking,” suggests Dean Baker of the Center for Economic and Policy Research, a left-leaning think tank. Actually, millions won’t ask, and the answer is: probably none. History may or may not judge Europe’s austerity a mistake, but German Chancellor Angela Merkel — its chief advocate — was not taking her cues from Reinhart and Rogoff. Her policies reflect strongly held German beliefs and values.

Something similar can be said of British Prime Minister David Cameron. He took office in May 2010 when the Reinhart/Rogoff paper still enjoyed standard academic obscurity. Cameron’s decision to make deep cuts in Britain’s budget deficits, then running about 10 percent of GDP, was controversial. At most, Reinhart/Rogoff provided some intellectual cover for policies that would have occurred anyway.

The charge that Reinhart and Rogoff cooked their numbers to support a preconceived policy position is contradicted by their 2012 paper (“Public Debt Overhangs: Advanced-Economy Episodes Since 1800”). It showed that results varied by country and that the slowdown at the 90 percent debt/GDP level was generally more gradual. As for American “austerity,” there hasn’t

been much. Though declining, budget deficits remain large and the Federal Reserve's monetary policy remains loose.

What's sobering about this brawl is that it settles nothing. With some exceptions, most advanced countries, including the United States, seem caught in a similar trap. Their debt/GDP ratios are high and rising, so it's hard to embrace massive deficit-financed stimulus programs. But austerity programs of spending cuts and tax increases may dampen growth and raise debt/GDP ratios. There is no obvious exit from this dilemma except a burst of spontaneous growth, which is conspicuous by its absence.

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