Intellectual Dishonesty (Gasp!) from a Conservative Economist

I've referred you guys to Greg Mankiw on a couple of different occasions. He is a highly-respected economist at Harvard University who was the head of the outgoing President Bush's Council of Economic Advisers. Mankiw is a pretty good benchmark for "smart" conservative economic thought -- which, being a University of Chicago economics grad, I have a healthy degree of respect for. If Mankiw's article in today's New York Times is any indication, however, the conservatives are out of good reasons for opposing Barack Obama's stimulus.

The main problem with Mankiw's article is this:

MIGHT TAX CUTS BE MORE POTENT? Textbook Keynesian theory says that tax cuts are less potent than spending increases for stimulating an economy. When the government spends a dollar, the dollar is spent. When the government gives a household a dollar back in taxes, the dollar might be saved, which does not add to aggregate demand.

The evidence, however, is hard to square with the theory. A recent study by Christina D. Romer and David H. Romer, then economists at the University of California, Berkeley, finds that a dollar of tax cuts raises the G.D.P. by about $3. According to the Romers, the multiplier for tax cuts is more than twice what Professor Ramey finds for spending increases.

Why this is so remains a puzzle. One can easily conjecture about what the textbook theory leaves out, but it will take more research to sort things out. And whether these results based on historical data apply to our current extraordinary circumstances is open to debate.

Christina Romer, incidentally, has been chosen as the chairwoman of the Council of Economic Advisers in the new administration. Perhaps this fact helps explain why, according to recent reports, tax cuts will be a larger piece of the Obama recovery plan than was previously expected. The paper Mankiw refers to, written by Berkley Economists Christina and David Romer, is the sort of thing that will make your head spin. But the gist of it is that (i) It is very important to differentiate the motivation for different types of tax cuts or tax increases, and (ii) a certain type of tax cut or tax increase may have a much larger effect on growth than is generally acknowledged.

The type of tax cut that Romer and Romer think falls into this category is what they call an "exogenous" tax cut -- one designed not to counter business cycles, but rather a "spontaneous" tax cut under relatively healthy economic circumstances.

This is very much not the type of tax cut that we are contemplating right now. Instead, what is being contemplated is a countercyclical action in an unhealthy economy designed to return the economy to normal growth. Romer and Romer are not all that keen on this
type of tax cut; in fact, they argue that such "countercyclical fiscal policy is not achieving its intended purpose," and that "policymakers’ efforts to adjust taxes to offset anticipated changes in private economic activity have been largely unsuccessful". You might also have inferred this from the fact that Christina Romer, who is the chair of Barack Obama's incoming Council of Economic Advisers, released an impact assessment (.pdf) yesterday positing a much lower multiplier on a "stimulative"/countercyclical tax cut.

This is not a trivial detail. It's as if Mankiw had said...

"A new study has shown that cholesterol can actually reduce your risk of a heart attack! So stop for a Triple Whopper Value Meal on your way home -- and don't forget to supersize it!"

...but omitted the fact that the study was referring only to HDL ("good") cholesterol -- not the LDL ("bad") cholesterol likely to be found in abundance in your Value Meal.

The thing is that's really irksome is that Mankiw should know a lot better. This is not some random blogger at Townhall trying to parse a difficult economics paper and overlooking an important point of context -- this is one of the premier economists in the world. He knows very well what the Romer and Romer paper says -- and he's made a deliberate choice to misrepresent it.

In poker terms, this is what we'd call a "tell". Mankiw doesn't have anything. He's bluffing. Out of ideas. Taking one for the team, and touting the party line for shits and giggles. Except, this isn't exactly fun and games, and Mankiw should leave the discussions to people who are serious about getting our economy moving again.

-- Nate Silver at 7:58 AM