Austerity has been the defining issue of the post-recession world in advanced economies. The merits of public deficit reduction divided opinion in 2010 and still do.

It is too much to expect a consensus on fiscal management to emerge in 2014, but the issue will probably not have the power to polarise of the past four years. Optimism that the debate over public finances might lose some of its venom comes from a global stalemate last year.

Supporters of austerity took a severe knock in April when a core prop to their arguments was shown to be error-strewn. Whether the mistakes were sufficient to invalidate the conclusions was irrelevant to the fact that the advice from professors Carmen Reinhart and Kenneth Rogoff, that economic growth rates fell once public debt rose above 90 per cent of national income, could no longer be used to convince policy makers or the public of the need for deficit reduction.

Being confounded by events was far from limited to austerians. Last year started with widespread predictions of coming woes in the US economy stemming from a massive fiscal tightening. The budgetary consolidation resulted from partisan political fighting, but far from tanking, the US recovery continued and it ended the year as the fastest-growing economy in the G7.

There is broad consensus on four issues. First, most advanced economies need to cut public spending or raise taxes to bring down public borrowing. Economists agree that the crisis has made most rich countries poorer, making budget deficits persistent, rather than temporary nuisances that will disappear with recovery. Second, efforts to reduce deficits generally cut growth, although the degree is widely disputed. Third, the negative effects of austerity are larger when monetary policy has less scope to offset demand weakness. And fourth, some countries with fiscal crises, such as Greece, had no option but to cut hard at a difficult time.

The most bitter arguments arise over countries that arguably did have a choice. Should fiscal consolidation have been gentler, or was this not a credible option for the governments of the US, UK, core eurozone and Japan? No clear answer came from the performance of these countries in 2013.

While the US surprised most with the recovery’s resilience to tax increases and the “sequestration” that cut public spending indiscriminately, Ben Bernanke, Federal Reserve chairman, said performance could have been better. In one of his last acts in charge of the Fed he said, “excessively tight near-term fiscal policies have likely been counterproductive”.

He added: “With fiscal and monetary policy working in opposite directions, the recovery is weaker than it otherwise would be. But the
current policy mix is particularly problematic when interest rates are very low, as is the case today.”

In the UK, the opposite was seen. No sooner had the International Monetary Fund accused the British government of “playing with fire” over its excessive austerity, which Olivier Blanchard, its chief economist, said was damaging private spending, than households opened their wallets. Britain is now more worried about excessive and unbalanced consumer-led growth than stagnation. George Osborne, chancellor, feels vindicated for having imposed a multiyear plan of deficit reduction and stuck to it.

In the eurozone, the insistence of prominent figures, such as Jens Weidmann, president of the Bundesbank, that other countries must “stick to what is undoubtedly an arduous adjustment path to the very end” has not obviously helped foster recovery, with the zone merely limping out of an 18-month second recession last summer. And in Japan, the “second arrow” of Abenomics, which initially involved a fiscal stimulus, appeared to contribute to the country’s recovery.

This year, the development likely to damp disputes over austerity is that the advanced world is aiming to do less. The IMF believes “fiscal tightening is expected to moderate ... as a large part of the consolidation has already taken place”. Apart from Japan, it estimates that advanced economies have already implemented two-thirds of the necessary austerity.

The question is whether political institutions are capable of long-term prudence. A new study from the OECD, which noted the large number of democracies that had kicked out of power the parties that were in charge during a fiscal crisis, said there was no magic solution to deficit reduction.

It said the optimal moment to impose austerity was just when the economy was turning up, but that it is almost impossible to time correctly.

It warned that crisis slashing of budgets often has nasty longer-term side effects and more successful governments manage to reduce long-term spending pressures. It urged countries to manage finances prudently rather than waiting for a crisis before acting.

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