Financial crisis and stimulus: Could this time be different?

By Ezra Klein, Published: October 8. The Washington Post.

Christina Romer had been asked to scare her new boss. It was six weeks after the 2008 election, and the incoming administration had gathered in Chicago. David Axelrod, Barack Obama's top political adviser, couldn't have been more clear in his instructions to Romer: The president-elect needed to know how bad the economy was going to get. No pulling punches, no softening the news.

So Romer, the preternaturally cheerful economist whose expertise on the Great Depression made her a natural choice to head the incoming president's Council of Economic Advisers, worked up some numbers to show how quickly the economy was deteriorating and what would happen if the federal government wasn't able to mount an effective response.

It was not a pleasant presentation to sit through. The situation was grim. Afterward, Austan Goolsbee, Obama's friend from Chicago and Romer's successor, remarked that "that must be the worst briefing any president-elect has ever had."

But Romer wasn't trying to be alarmist. Her numbers were based, at least in part, on everybody else's numbers: There were models from forecasting firms such as Macroeconomic Advisers and Moody's Analytics. There were preliminary data pouring in from the Bureau of Labor Statistics, the Bureau of Economic Analysis and the Federal Reserve. Romer's predictions were more pessimistic than the consensus, but not by much.

By that point, the shape of the crisis was clear: The housing bubble had burst, and it was taking the banks that held the loans, and the households that did the borrowing, down with it. Romer estimated that the damage would be about $2 trillion over the next two years and recommended a $1.2 trillion stimulus plan. The political team balked at that price tag, but with the support of Larry Summers, the former Treasury secretary who would soon lead the National Economic Council, she persuaded the administration to support an $800 billion plan.

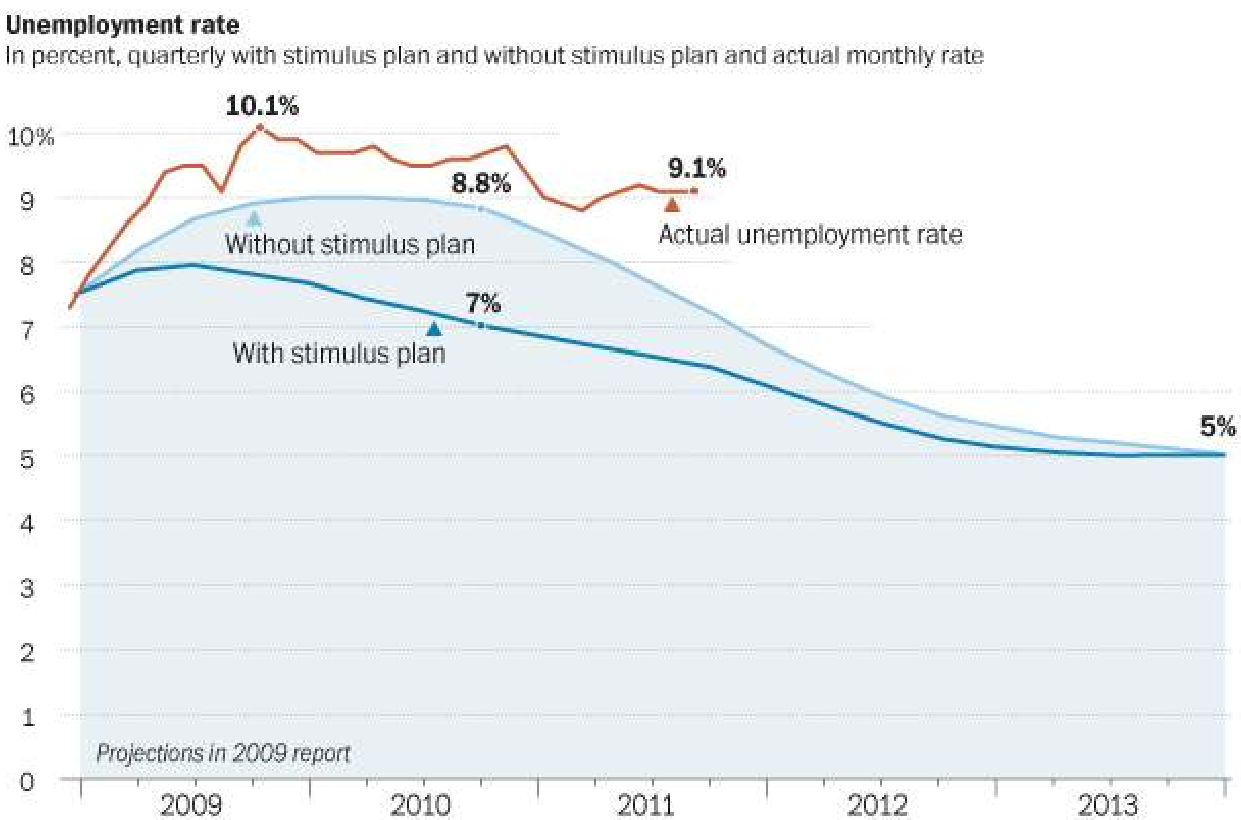
The next challenge was to persuade Congress. There had never been a stimulus that big, and there hadn't been many financial crises this severe. So how to estimate precisely what a dollar of infrastructure spending or small-business relief would do when let loose into the economy under these unusual conditions? Romer was asked to calculate how many jobs a stimulus might create. Jared Bernstein, a labor economist who would be working out of Vice President Biden's office, was assigned to join the effort.

Romer and Bernstein gathered data from the Federal Reserve, from Mark Zandi at Moody's, from anywhere they could think of. The incoming administration loved their report and wanted to release it publicly. Romer took it home over Christmas to double-check, rewrite and pick over. At 6 a.m. Jan. 10, just days before Obama would be sworn in as president, his transition team lifted the embargo on "The Job Impact of the American Recovery and Reinvestment Act." It was a smash hit.

"It will be a joy to argue policy with an administration that provides comprehensible, honest reports," enthused columnist Paul Krugman in the New York Times.

There was only one problem: It was wrong.

The issue is the graph on Page 1. It shows two blue lines sloping gently upward and then drifting back down. The darker line — "With recovery plan" — forecasts unemployment peaking at 8 percent in 2009 and falling back below 7 percent in late 2010.



Three years later, with the economy still in tatters, that line has formed the core of the case against the Obama administration's economic policies. That line lets Republicans talk about "the failed stimulus." That line that has discredited the White House's economic policy.

But the other line — "Without recovery plan" — is more instructive. It shows unemployment peaking at 9 percent in 2010 and falling below 7 percent by the end of this year. That's the line the administration used to scare Congress into passing the single largest economic recovery package in American history. That line is the nightmare scenario.

And yet this is the cold, hard fact of the past three years: The reality has been worse than the administration's nightmare scenario. Even with the stimulus, unemployment shot past 10 percent in 2009.

To understand how the administration got it so wrong, we need to look at the data it was looking at.

The Bureau of Economic Analysis, the agency charged with measuring the size and growth of the U.S. economy, initially projected that the economy shrank at an annual rate of 3.8 percent in the last quarter of 2008. Months later, the bureau almost doubled that estimate, saying the number was 6.2 percent. Then it was revised to 6.3 percent. But it wasn't until this year that the actual number was revealed: 8.9 percent. That makes it one of the worst quarters in American history. Bernstein and Romer knew in 2008 that the economy had sustained a tough blow; t hey didn't know that it had been run over by a truck.

There were certainly economists who argued that the recession was going to be worse than the forecasts. Nobel laureates Krugman and Joe Stiglitz were among the most vocal, but they were by no means alone. In December 2008, Bernstein, who had been named Biden's chief economist, told the Times, "We'll be lucky if the unemployment rate is below double digits by the end of next year."

The Cassandras who look, in retrospect, the most prophetic are Carmen Reinhart and Ken Rogoff. In 2008, the two economists were about to publish "This Time Is Different," their fantastically well-timed study of nine centuries of financial crises. In their view, the administration wasn't being just a bit optimistic. It was being wildly, tragically optimistic.

That was the dark joke of the book's title. Everyone always thinks this time will be different: The bubble won't burst because this time, tulips won't lose their value, or housing is a unique asset, or sophisticated derivatives really do eliminate risk. Once it bursts, they think their economy will quickly clamber out of the ditch because their workers are smarter and tougher, and their policymakers are wiser and more experienced. But it almost never does.

In March 2009, Reinhart and Rogoff took to Newsweek to critique the “chirpy forecasts coming from policymakers around the globe.” The historical record, they said, showed that “the recessions that follow in the wake of big financial crises tend to last far longer than normal downturns, and to cause considerably more damage. If the United States follows the norm of recent crises, as it has until now, output may take four years to return to its pre-crisis level. Unemployment will continue to rise for three more years, reaching 11 to 12 percent in 2011.”

It seems unlikely that unemployment will return to 11 percent this year, but if the global economy tips back into recession, anything is possible. Either way, Rogoff and Reinhart were a lot closer to the mark than most forecasters.

But the administration insisted on optimism. There was talk of “green shoots” and the “recovery summer.” Events in Greece and in oil markets were chalked up to bad luck rather than the predictable aftershocks of a financial crisis. The promised recovery was always just around the corner, but it never quite came. Eventually, the American people stopped listening. A September poll showed that 50 percent of Americans thought Obama’s policies had hurt the economy.

“I don’t think it’s too much of an exaggeration to say that everything follows from missing the call on Reinhart-Rogoff, and I include myself in that category,” says Peter Orszag, who led the Office of Management and Budget before leaving the administration to work at Citigroup. “I didn’t realize we were in a Reinhart-Rogoff situation until 2010.”

This time, it turned out, wasn’t different. But could it have been?

The boot and the slog

The basic thesis of “This Time Is Different” is that financial crises are not like normal recessions. Typically, a recession results from high interest rates or fluctuations in the business cycle, and it corrects itself relatively quickly: Either the Federal Reserve lowers rates, or consumers get back to spending, or both.

But financial crises tend to include a substantial amount of private debt. When the market turns, this “overhang” of debt acts as a boot on the throat of the recovery. People don’t take advantage of low interest rates to buy a new house because their first order of business is paying down credit cards and keeping up on the mortgage.

In subsequent research with her husband, Vincent Reinhart, Carmen Reinhart looked at the recoveries following 15 post-World War II financial crises. The results were ugly. Forget the catch-up growth of 4 or 5 percent that so many anticipated. Average growth rates were a full percentage point lower in the decade after the crisis than in the one before.

Perhaps as a result, in 10 of the 15 crises studied, unemployment simply never — and the Reinharts don't mean "never in the years we studied," they mean never ever — returned to its pre-crisis lows. In 90 percent of the cases in which housing-price data were available, prices were lower 10 years after the crash than they were the year before it.

There is no doubt that the post-crisis trajectory looks more like the slog Reinhart and Rogoff described than the relatively rapid rebound predicted by the administration and many forecasters. Yet even among economists who admire Reinhart and Rogoff's work, there is skepticism.

One source comes in how Reinhart and Rogoff find the economic phenomena they're trying to study. "There's an identification problem," Stiglitz says. "When you have underlying problems that are deep, they will cause a financial crisis, and the crisis itself is a symptom of underlying problems."

Another is in their fatalism. "I don't buy their critique in the sense that this was an inevitability," says Dean Baker, director of the Center for Economic and Policy Research and one of the economists who spotted the housing crisis early.

The Obama administration didn't buy the idea of inevitability, either. The team crafted a multi-pronged approach of stimulus spending, programs to address the housing market, and policy coordinated with an activist Federal Reserve. It firmly believed that it was better to do too much than too little. Its credo was well expressed by Romer at that December meeting, when she told the president, "We have to hit this with everything we've got." But in reality, the administration could only hit it with everything it could persuade Congress to give. And that wasn't enough.

Finding fault with the stimulus

Some partisans offer a simple explanation for the depth and severity of the recession: It's the stimulus's fault. If we had done nothing, they say, unemployment would never have reached 10 percent.

That notion doesn't find much support even among Republican economists. Doug Holtz-Eakin is president of the right-leaning American Action Forum and served as Sen. John McCain's top economic adviser during the 2008 presidential campaign. He's no fan of the stimulus, but he has no patience with the idea that it made matters worse.

"The argument that the stimulus had zero impact and we shouldn't have done it is intellectually dishonest or wrong," he says. "If you throw a trillion dollars at the economy, it has an impact. I would have preferred to do it differently, but they needed to do something."

A fairer assessment of the stimulus is that it did much more than its detractors admit, but much less than its advocates promised.

"The thing that people who want to argue that the stimulus failed have to deal with," Bernstein says, "is that if you look at the trajectory of job losses, you will find that right on the heels of the Recovery Act, the rate of job losses began to diminish and then the jobs numbers turned positive. The Recovery Act worked. The problem is we didn't keep our foot on the accelerator."

That's not the sort of success the president had promised, though. He said the stimulus would "jolt our economy back to life." In Denver, the site of the 2008 Democratic National Convention, he said that although "this was not the end of our economic problems," it was "the beginning of the end."

It wasn't.

Critics and defenders on the left make the same point: The stimulus was too small. The administration underestimated the size of the recession, so it follows that any policy to combat it would be too small. On top of that, it had to get that policy through Congress. So it went with $800 billion — what Romer thought the economy could get away with — rather than $1.2 trillion — what she thought it needed. Then the Senate watered the policy down to about $700 billion. Compare that with the $2.5 trillion hole we now know we needed to fill.

But it is hard to credit the argument that the stimulus could have been much larger at the outset. This was already the biggest stimulus in U.S. history, and congressional leaders had been quite clear with the White House: Don't send over anything that passes the trillion--dollar mark. To try and double the bill's size based on a suspicion that the recession was much worse than the early data indicated would have been a hard sell, to say the least.

Even if Congress had been more accommodating, there was a challenge to vastly increasing the size of the initial stimulus: The more you spend, the less effective each new dollar would become.

“We were trying to spend 10 times what had ever been spent in a year,” says Goolsbee, who chaired the Council of Economic Advisers until this year. “The tension was that the biggest bang for the buck comes from direct spending like infrastructure, but once you use up the big-ticket items, you eventually come to a point where the tax cuts are better bang for the buck than the 300 billionth infrastructure dollar.” And tax cuts, frankly, aren’t a very good bang for the buck.

But although the administration’s team hoped the initial stimulus would work, it figured that if it didn’t, it could go back to Congress for more.

“If you’re at the barber and they don’t cut your hair short enough, you can always ask them to go a little further,” Bernstein says. “That’s sort of how I thought about stimulus policy. I don’t think we could have done more in February of 2009 based on political and implementation constraints. But I probably didn’t recognize how hard it would be to go back to the barbershop.”

The theory was that success would beget success. Passing the stimulus would stabilize the economy, prove the White House’s political mettle and deliver immediate relief to millions of Americans. That would help the administration build the political capital to pass more stimulus, if necessary. But when the economy failed to respond as predicted, the political theory fell apart, too.

“The biggest problem we had in terms of the loss of political capital is we came in and did a bunch of stuff, and things got worse,” says Ron Klain, who served as chief of staff to Biden. “And some of that was just bad luck. If we didn’t have the 22nd Amendment and Barack Obama became president in late March rather than in late January, things would have been much worse when we came in than they were. And then the Recovery Act would have come not in February, but in May. We would already have hit bottom, and it would seem like things were getting better.”

This has led to a what-if that torments the White House’s political team: What if it hadn’t taken on so much? The administration rushed from the second bucket of bailout funds to the stimulus to the auto-industry rescue to health care to climate change legislation to financial regulation. In a world where the economy was steadily recovering, Obama might have amassed a record comparable to Franklin Roosevelt's. But as the situation slowly deteriorated, the American people turned against the administration's crush of initiatives. The frenetic pace made the White House seem inattentive and unfocused amid a mounting crisis.

But the alternative is similarly difficult to imagine. No one believes that significantly reining in the agenda would have led to much more stimulus. Perhaps the president would have benefited politically from speaking more about jobs and less about health care, but then again, he had historic majorities in both houses of Congress and had come into office promising dramatic change.

A more accurate understanding of the recession could, however, have led to a somewhat different stimulus — and perhaps a more durable political strategy. The policy was constructed at breakneck speed, with the emphasis on getting money spent fast. That led to more tax cuts, as they could happen quickly, and less infrastructure, as projects — particularly anything more complex than road repair — can take years to begin, by which point a typical recession has ended of its own volition.

Another cost of moving quickly was that it put a premium on policies already floating around that could be easily dropped into the legislation. That, according to Holtz-Eakin, solidified Republican opposition.

"If you're a staffer and you have been watching business in the House and Senate for a long time," he says, "what you saw them doing was pulling old ideas off the shelf — old ideas you had fought and that Democrats had abandoned. So Republicans in Congress just hated it."

A stimulus conducted with the Rogoff-Reinhart lessons in mind might have been broken into pieces and spread over a longer time frame. The administration could have pushed to tie key components such as unemployment benefits, state and local aid, and tax cuts to the unemployment rate rather than setting them to expire after two years. With the knowledge that it had years of low growth to combat, there could have been a short-term infrastructure component — potholes, school repairs and the like — followed, in separate legislation that Congress would have had more time to consider, by a long-term infrastructure component for big investments such as high-speed rail and health-information technology.

But there's little reason to believe that would have turned unemployment numbers around. In fact, we have seen fairly regular extensions of unemployment benefits and tax cuts over the past year. A bill with a longer time frame perhaps would have saved the administration from political headaches down the road, but it could have even made it harder to ask Congress for more, as the initial policy would not have finished spending out yet.

‘Politics on housing are hideous’

The stimulus was a bet that we could get out of this recession through the one path everyone can agree on: growth. The bet was pretty much all-in, and it failed. Reinhart and Rogoff are not particularly surprised. It’s hard to get through a debt-driven crisis without doing anything about, well, debt.

In our crisis, the “debt” in question is housing debt. Home prices have fallen almost 33 percent since the beginning of the crisis. All together, the nation’s housing stock is worth $8 trillion less than it was in 2006. And we’re not done. Morgan Stanley estimates there are more than 2.2 million homes sitting vacant, and 7.5 million more facing foreclosure. It is housing debt that has weakened the banks, and mortgage debt that is keeping consumers from spending.

In late 2008, when the economy was cratering, Holtz-Eakin convinced McCain that the way out of a housing crisis was to tackle housing debt directly. “What we proposed at the time was to buy up the troubled mortgages, pay them off and let people refinance at the lower rates,” he recalls. “That would have filled up the negative equity and healed bank balance sheets.”

To this day, Holtz-Eakin thinks the proposal made sense. There was one problem. “No one liked that plan,” he says. “In fact, they hated it. The politics on housing are hideous.”

The Obama administration, perhaps cognizant of the politics, was not nearly so bold. It focused on stimulus rather than housing debt. The idea was that if people could keep their jobs and pay their bills, they could pay their mortgages. But today, few on the Obama team will mount much of a defense of its housing policy.

Its efforts to heal the troubled market at the core of the financial crisis are widely considered weak and ineffective. The Home Affordable Modification Program, which proposed to pay mortgage servicers to renegotiate with financially stressed homeowners, couldn’t persuade the servicers to play ball and so has left most of its $75 billion unspent. The Home Affordable Refinance Program was projected to help 5 million underwater homeowners. It has reached fewer than 1 million.

Even so, the administration rejects the more radical solutions that are occasionally floated. The problem, it says, is that the choices are mostly between timid and unworkable.

One problem was that mortgage finance giants Fannie Mae and Freddie Mac were ultimately controlled by the independent Federal Housing Finance Agency. Created by Congress in 2008, the agency was initially led by a Bush administration appointee, James B. Lockhart III, and when he stepped down, by another Bush administration appointee, Edward DeMarco. The Obama administration's November 2010 effort to nominate its own director was foiled by Senate Republicans.

By that time, the administration had been in office for almost two years and seen the Democrats' 60-vote majority in the Senate come and go. If it had moved more quickly to appoint a director when it had firmer control of the Senate, it could perhaps have used Fannie and Freddie to kick off a giant wave of refinancing for underwater homeowners. That alone would have done something to ease the pressure on stressed households.

But when talking about what might have worked on a massive, economy-wide scale — that is to say, what might have made this time different — you're talking about something more drastic. You're talking about getting rid of the debt. To do that, somebody has to pay it, or somebody has to take the loss on it.

The most politically appealing plans are the ones that force the banks to eat the debt, or at least appear to do so. "Cramdown," in which judges simply reduce the principal owed by underwater homeowners, works this way. But any plan that leads to massive debt forgiveness would blow a massive hole in the banks. The worry would move from "What do we do about all this housing debt?" to "What do we do about all these failing banks?" And we know what we do about failing banks amid a recession: We bail them out to keep the credit markets from freezing up. There was no appetite for a second Lehman Brothers in late 2009.

Which means that the ultimate question was how much housing debt the American taxpayer was willing to shoulder. Whether that debt came in the form of nationalizing the banks and taking the bad assets off their books — a policy the administration estimated could cost taxpayers a trillion dollars — or simply paying off the debt directly was more of a political question than an economic one. And it wasn't a political question anyone really knew how to answer.

On first blush, there are few groups more sympathetic than underwater homeowners or foreclosed families. They remain so until about two seconds after their neighbors are asked to pay their mortgages. Recall that Rick Santelli's famous CNBC rant wasn't about big government or high taxes or creeping socialism. It was about a modest program the White House was proposing to help certain homeowners restructure their mortgages. It had Santelli screaming bloody murder.

“This is America!” he shouted from the trading floor at the Chicago Board of Trade. “How many of you people want to pay for your neighbor’s mortgage that has an extra bathroom and can’t pay their bills? Raise their hand.” The traders around him began booing loudly. “President Obama, are you listening?”

If you believe Santelli’s rant kicked off the tea party, then that’s what the tea party was originally about: forgiving housing debt.

Ultimately, concerns about the politics and policy questions behind widespread debt forgiveness were sufficient to scare the administration off of the policy. It’s a decision some ex-members of the White House regret.

“If we had thought harder about Rogoff and Reinhart, we might have made some different trade-offs regarding debt reduction,” Bernstein says. “Moral hazard is a big problem when you’re making policy regarding write-offs and principal cramdowns. It was always in the room when you were trying to help one underwater homeowner write off some debt while the person next door was playing by the rules and paying their mortgage every month. But with hindsight, I might have argued more rigorously against the risk of it.”

The Fed’s inflation option

There was, however, one institution that some think could have reduced the debt overhang crushing the economy and that didn’t face such political obstacles: the Federal Reserve.

The central bank manages the nation’s money supply and credit and sits at the center of its financial system. Usually, it spends its time guarding against the threat of inflation. But in December 2008, Rogoff argued that the moment called for the reverse strategy.

“It is time for the world’s major central banks to acknowledge that a sudden burst of moderate inflation would be extremely helpful in unwinding today’s epic debt morass,” he wrote.

Inflation — the rate at which prices for goods go up and buying power goes down — makes any amount of money worth less over time. It can help a depressed economy in three ways: It erodes the real value of debt. It gives people an incentive to spend and invest now, as their money will not go as far later. And it tends to drive down the value of the dollar against other currencies, making U.S. exporters more competitive.

At the Federal Reserve, inflation is a four-letter word. It has spent the past few decades convincing the market that it can and will “anchor” inflation at about 2 percent. Lifting that anchor could cause problems down the road, without doing much good in the present. After all, Federal Reserve Board Chairman Ben S. Bernanke doesn’t have a red inflation button beneath a glass case on his desk. Creating inflation is difficult when demand for goods is low, and it’s not even clear that the Fed can do it.

Rogoff scoffs at this. “Creating inflation is not rocket science,” he wrote. “All central banks need to do is to keep printing money to buy up government debt. The main risk is that inflation could overshoot, landing at 20 or 30 percent instead of 5 or 6 percent. Indeed, fear of overshooting paralyzed the Bank of Japan for a decade. But this problem is easily negotiated. With good communication policy, inflation expectations can be contained, and inflation can be brought down as quickly as necessary.”

But the policymakers who would have needed to create that inflation aren’t so sure. “It’s difficult, if not impossible, to create persistent inflation without demand exceeding potential supply over an extended period,” says Donald L. Kohn, who served as vice chairman of the Federal Reserve Board until 2010. “Yes, changing expectations might push inflation higher, but why would expectations change materially and persistently under current circumstances?”

Bernanke seems to agree. So, it seems, does the administration, at least judging by the economists it considered nominating to the Fed.

Summers, who had the inside track to chair the central bank if the Obama administration decided against renominating Bernanke, echoes Kohn’s skepticism. “In the model I understand,” he says, “inflation is mostly driven by demand, and when you increase demand, you increase inflation. And if you don’t increase demand, you don’t increase inflation. But if you’ve solved demand, you’ve solved your problem.”

Nobel laureate Peter Diamond, whom the Obama administration nominated to fill a vacant seat on the Fed’s board, puts it this way: “If the Fed says we are determined to keep going till we have, say, 4 percent inflation, would that really turn around expectations in a way that would stimulate the economy and create higher inflation? I doubt it.”

And, of course, the Fed might be insulated from politics, but it’s not immune to it. In recent years, Rep. Ron Paul (R-Tex.) has gained national prominence in part on an “End the Fed” platform. Texas Gov. Rick Perry, a Republican presidential contender, has threatened to do something “ugly” to Bernanke. Congress passed legislation to audit the Fed. Even noted monetary economist Sarah Palin weighed in, saying, “It’s time for Ben Bernanke to cease and desist.”

To the Fed, the nightmare scenario is that it tries to create inflation now and fails. It would have given up its hard-won credibility as an inflation fighter and invited political backlash, all without helping the economy.

Labor market’s long period of pain

Growth-focused and debt-focused strategies are attempts to end the recession. They’re policy on the offensive. But perhaps the real lesson from Rogoff and Reinhart is that these recessions rarely end quickly, and so officials must manage a long period of pain — defensive policy, so to speak. America doesn’t do defense very well.

“We’re trying right now to keep our lifestyles going,” says Michael Spence, a Nobel Prize-winning economist at New York University. “It’s not really working, but the way we’re doing it is putting all the burden on the unemployed while trying to leave the employed untouched. Eventually, this is going to require a redistribution of that burden.”

In other countries, he says, the burden is more widely shared. The employed work less — and get paid less — so there are more jobs to go around. That leads to a little pain for a lot of people, rather than a lot of pain for fewer people. It also keeps more workers on the job, which means their skills don’t deteriorate and the economy isn’t left with people who became unemployed and then found themselves unemployable.

That’s what we’ve seen here: Employers have become so leery of hiring the unemployed that the Obama administration has proposed to make it illegal to discriminate against them. Such a policy is easier said than done, but it speaks to the downside of letting workers fall out of the labor force for long periods of time.

Germany’s response to the recession included a work-sharing program that subsidized salaries when employers trimmed the hours of individual workers to keep more people on the job. If workers attended job training, the government gave a more generous subsidy.

The program worked. Even though Germany’s economy was devastated by the recession —

declining by almost 7 percent — the jobless rate fell slightly, from 7.9 percent at the start of the recession to 7 percent in May 2010.

There are reasons to question whether work-sharing programs would have been as effective here as they were in Germany. For one thing, they work best in sectors where jobs are bound to return after a recession — such as Germany's export sector — rather than sectors that need to be downsized after being inflated by a credit boom.

Germany also has a different labor market. Employers, unions and the government work together with an unusual level of cooperation. The culture is much more hostile toward layoffs than the United States' is, which has caused Germany problems in the past but has been a boon throughout this recession.

But paying the private sector to save jobs was not the administration's only option. There was also the possibility of simply paying workers to work.

For one thing, the government could have refused to fire anyone. Says Baker, of the Center for Economic and Policy Research: "We've lost 500,000 state and local jobs, and before that, we were creating 160,000 a year. If we hadn't had those losses and had done more to keep creation at that pace, we would have almost another million jobs."

It also could have started hiring. Romer, for instance, proposed to add 100,000 teacher's aides. Imagine similar proposals: Every park ranger could have had an assistant park ranger. Every firefighter station could have added three trainees. Every city could have expanded its police force by 5 percent. Everyone between ages 18 and 26 could have signed up for two years of paid national service.

In a relatively quick recovery, these programs wouldn't have made sense. Better to support the economy more generally and let workers migrate from unproductive sectors to productive ones. Employing workers directly is, at best, a stopgap, and at worst, a waste of the government's resources and the worker's time. The government doesn't know where workers are best used. That's better left to the market.

But in a long slog of a recession, that logic falls apart. Workers don't move into more productive sectors of the economy. They lose their jobs, and then they lose their paychecks, homes and, eventually, skills. That sucks demand out of the economy, further depresses home prices and makes it harder for the labor market to recover.

Call-and-response conundrum

So could this time have been different? There's little doubt that it could have been better. From the outset, the policies were too small for the recession the administration and economists thought we faced. They were much too small for the recession we actually faced. More and better stimulus, more aggressive interventions in the housing market, more aggressive policy from the Fed, and more attention to preventing layoffs and hiring the unemployed could have led to millions more jobs. At least in theory.

Of course, ideas always sound better than policies. Policies must be implemented, and they have unintended consequences and unforeseen flaws. In the best of circumstances, the policymaking process is imperfect. But January 2009 had the worst of circumstances — a once-in-a-lifetime economic emergency during a presidential transition.

Reinhart, for one, thinks the Bush and Obama administrations don't get sufficient credit for all they did.

"The initial policy of monetary and fiscal stimulus really made a huge difference," she says. "I would tattoo that on my forehead. The output decline we had was peanuts compared to the output decline we would otherwise have had in a crisis like this. That isn't fully appreciated."

In that way, Reinhart says, this time really was different — at least from the Great Depression, when output shrank by 30 percent and a quarter of the workforce was unemployed. "If the choice was this or the '30s," she says, "I'd take this hands down."

Give policymakers some credit: They really have learned from the Depression. So did the Japanese. In the 1990s, they pumped monetary and fiscal stimulus into their economy, too, and they didn't suffer a depression. But they never found themselves in a recovery. They stagnated for a decade, and then for another.

What we're in looks more like Japan in the '90s than the United States in the '30s. Reinhart doesn't think that's an accident; she thinks it's a product of the initial successes. "The same policies that serve you well in limiting the output collapse do not serve you well in speeding the time it takes to get out," she says.

By saving the banking system, you end up with banks that are quietly holding on to toxic assets in the hope that one day they'll be worth something. By limiting the output gap, you keep the economy from getting so bad that truly radical solutions, such as wiping out hundreds of billions of dollars of housing debt, become thinkable. You limp along.

The question, of course, is why do governments limp out of recessions when the weight of history tells them to run?

“Now knowing how much worse the storm was, people look back and say, you guys undershot,” sighs Treasury Secretary Timothy F. Geithner. “But we didn’t think we were undershooting at the time. We thought that the dominant strategy had to be massive, overwhelming force. There were political limits to what we could do, but we thought we were operating to expand the scope of those limits. I used to say to people, ‘Which mistake is harder to correct: doing too much, or doing too little?’ ”

Yet the Obama administration did too little. Its team of interventionist Keynesians immersed in the lessons of the Depression and Japan did too little. Everyone does too little, even when they think they’re erring on the side of doing too much. That’s one reason “this time” is almost never different.

The tendency thus far has been to look at these crises in terms of the identifiable economic factors that make them different from typical recessions. But perhaps the better approach is to look at the political factors that make them turn out the same, that stop governments from doing enough even when they have sworn to err on the side of doing too much.

These crises have a sort of immune system. It is never possible for the political system to do enough to stop them at the outset, as it is never quite clear how bad they are. Even if it were, the system is ill-equipped to take action at that scale. The actors comfort themselves with the thought that if they need to do more, they can do it later. And, for now, the fact that this is the largest rescue package anyone has ever seen has to be worth something.

Perversely, the very size of the package is part of its problem. With something extraordinary that is nevertheless not enough, the economy deteriorates, and the government sees its solutions discredited and its political standing weakened by the worsening economic storm. That keeps it from doing more.

Meanwhile, the opposition’s capacity to do more is arguably even more limited, as it has turned against whatever policies were tried in the first place. Add in the almost inevitable run-up in government debt, which imposes constraints in the eyes of the voters and, in some cases, in the eyes of the markets, and an economy that started by not doing enough is never able to get in front of the crisis.

These sorts of economic crises are, in other words, inherently politically destabilizing, and that makes a sufficient response, at least in a democracy, nearly impossible.

There's some evidence for this internationally. Larry Bartels, a political scientist at Vanderbilt University, examined 31 elections that took place after the 2008 financial crisis and found that "voters consistently punished incumbent governments for bad economic conditions, with little apparent regard for the ideology of the government or global economic conditions at the time of the election." Just look to Europe, where the path to ending the debt crisis and saving the euro zone — the group of nations that use the currency — is clear to most economists but impossible for any European politician.

That isn't to say that this time couldn't have been different or that next time won't be. But it is no accident that these crises so often turn out the same, in so many countries, with so many types of governments, who have tried so many kinds of responses.

In general, the policies that are vastly better than whatever you are doing are not politically achievable, and the policies that are politically achievable are not vastly better. There were many paths that could have been taken in January 2009, and any one would have made this time a bit different. But not different enough. Not as different as we wish.

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