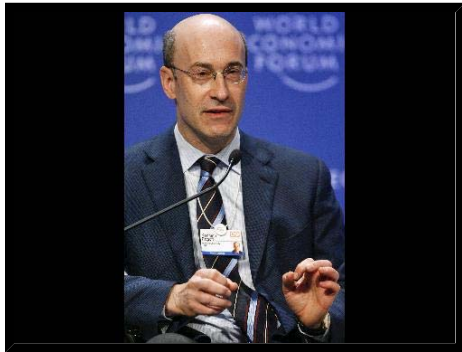





Rogoff Slams Four Toxic Words, 'This Time Is Different': Books

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Review by James Pressley



Oct. 12 (Bloomberg) -- Wouldn't it be nice to have \$1,000 for every time a pundit proclaims an era of endless prosperity, consigning booms and busts to the dumpster of history?

The next time you hear that canard (and you will) pour yourself a single malt and dip into [Carmen M. Reinhart](#) and [Kenneth S. Rogoff's](#) landmark study, "This Time Is Different." Wherever you open the book, you'll find proof that debt-fueled expansions have ended in financial ruin for hundreds of years.

Rogoff is a Harvard University professor and former chief economist for the International Monetary Fund. He and [Reinhart](#)

of the University of Maryland have pieced together an exotic array of data from 66 countries to produce what they call "a quantitative history of financial crises."

Deploying charts, tables and appendixes, they survey eight centuries of meltdowns, be they sovereign debt defaults during the Napoleonic Wars or [hyperinflation in Zimbabwe](#) this decade.

Then they suggest ways to establish an "early warning system" to anticipate the next crisis.

The authors have previously made some of [their findings](#) public in papers tracking the busts following booms in real [housing prices](#). Their conclusions make grim reading for anyone trying to fathom how bad the fallout might be from the current crisis, which they call the Second Great Contraction.

Prolonged Slumps

Slumps like this are prolonged and deep, according to their data. Real housing prices, from peak to trough, drop a cumulative 36 percent over an average of some six years. Real gross domestic product per capita slumps an average 9.3 percent. Unemployment rises for almost five years, with the rate increasing about 7 percentage points.

More unsettling still, government debt surges an average of 86 percent, driven mainly by plunging tax revenue, the authors say. In other words, \$100 billion in debt swells to \$186 billion after three years, adjusted for inflation.

Why do meltdowns recur time after time? That's the question Reinhart and Rogoff seek to answer in this engrossing volume. Their main answer is summed up the words of a trader who inspired the book's title.

"More money has been lost because of four words than at the point of a gun," they quote the trader as saying around the time hedge fund Long-Term Capital Management LP collapsed. "Those words are 'This time is different.'"

You know the song. Boom times breed talk of a Permanently High Plateau, New Economy or Great Moderation. The longer the good times roll, the bigger [debts grow](#), and the more people believe that "financial crises are things that happen to other people in other countries at other times," as the authors

say.

'We Are Smarter'

"We are doing things better," they summarize. "We are smarter, we have learned from past mistakes. The old rules of valuation no longer apply."

History teaches that debt-fed prosperity doesn't last forever. Sooner or later, something triggers a crisis of confidence -- whether it's Edward III of England defaulting on his loans from Florentine financiers in 1340 or a mountain of subprime mortgages. Bank runs, fire sales and other unpleasantness follow.

If you're looking for a narrative history of financial crises a la Charles Kindleberger, this isn't it. You'll find only passing references to how Henry VIII clipped coins or how French monarchs executed their creditors -- "an early and decisive form of 'debt restructuring.'"

What you get instead is a systematic and brisk tour of data culled from sources stretching back as far as 12th-century China. The result is a visual history laid out in beguilingly simple graphs and tables, making the book both definitive -- a must read for professors and investors -- and accessible to a wider audience.

Serial Defaulters

One table, for example, lists the repeated external defaults by European countries between 1300 and 1799. (France and Spain led the pack.) Other graphics show how domestic government debt often surges in the run-up to a crisis, flashing a signal: Danger ahead.

Data on domestic debt, it turns out, are hard to come by. This, even though (or perhaps because) debt accounted on average for between 40 percent and 80 percent of total government debt between 1900 and 2007. To piece together the trend, the authors dug into the archives of the League of Nations. It was "an exercise in archeology," they say.

Reinhart and Rogoff would like to see governments disclose this data, noting that "increasing public debt has been a nearly universal precursor of other postwar crises." They also recognize the greatest drawback to monitoring such flashing red lights: Come the next boom, many people will dismiss the signals "as irrelevant archaic residuals of an outdated framework."

Then they'll utter those four words.

"This Time Is Different: Eight Centuries of Financial Folly" is from [Princeton](#) (463 pages, \$35, 19.95 pounds). To buy this book in North America, click [here](#).

([James Pressley](#) writes for Bloomberg News. The opinions expressed are his own.)

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