

Iraq: The Three Trillion Dollar War

INTERVIEW WITH JOSEPH STIGLITZ

*On April 20, 2008 Joseph Stiglitz, a professor at Columbia University and recipient of the Nobel Memorial Prize in Economic Sciences in 2001, met with YJIA Editors Alexander Besant and William Ko to discuss some of the themes raised in his most recent book, *The Three Trillion Dollar War*, co-authored with Harvard Kennedy School of Government Professor Linda J. Bilmes.*

What inspired you to write your new book (with Linda J. Bilmes), *The Three Trillion Dollar War*?

There are a couple of reasons why we wrote this book. First of all, our decision to write this book was academically motivated. One of the main concerns in public sector economics pertains to the disparities between budget costs and costs to society. The war provides a very dramatic case study on these differences. Linda and I were involved in both, the issues of government transparency, and the accounting aspects of the economics of information—a lack of information in either leads to bad decisions. The example of the Iraq War enables us to scrutinize what went wrong in the budgeting and accounting procedures, as well as to examine the subsequent consequences. The second and much more compelling reason was that we suspected a disparity between the advertised cost of the war and the true cost on the economy. We did not anticipate it to be as large as it would be.

You mentioned that the low estimates of the costs of the Iraq War range from a loss of \$200 billion to a positive gain. How did so many individuals miscalculate the aggregate costs of the Iraq War? Did you make your own estimates prior to the war?

Actually, the best estimate of the costs before the war was done by Professor William Nordhaus at Yale University. His work is an example of what I call "good analysis". Obviously, he did not have the time to work on the estimates

as much as we did, and there were items that he could not fully take into account like we did in our book, but what was remarkable was the accuracy of the range. In fact, he anticipated that if the war extended for as long as it did, the costs would exceed one trillion dollars.

Anybody who conducted the analysis carefully would have come to the same conclusion that Nordhaus did. It is difficult to look retrospectively at these numbers and comprehend how even smaller figures could be obtained. There were some things that could have been factored, but were not. An example would be serious injuries versus fatalities or the advances in modern medicine, which would consequently lead to an increase in costs. Nevertheless, had these analysts remained honest to what they were doing, they would have conducted a study similar to Nordhaus's study, and they would have reached the same conclusions—but there was an obvious combination of incompetence and a deliberate attempt at concealing the costs. We see this most visibly in the reaction of individuals like Donald Rumsfeld. After Lawrence Lindsey said the war might cost \$100-200 billion, this figure was dismissed in favor of a \$50-60 billion estimate. It was clear that they had an agenda to keep the actual numbers away from the people.

On January 29, 2008, Paul Krugman wrote an opinion piece for the New York Times, stating that the wars in Afghanistan and Iraq provided short-term expansionary growth for the economy. He says, with slight qualifications, that Iraq is not responsible for the current economic troubles in the United States, but rather that the greatest challenge to the American economy is the bursting of the housing bubble. Do you agree with this statement?

Well, I think he is looking at it in too partial a way. What he misses—and it is surprising considering how good an economist Paul is—is two points. The first is that the war is at least partially responsible for the increase in the price of oil. The futures markets expected that the price of oil would remain at twenty-three to twenty-five dollars per barrel for at least a decade after 2003—the year we went to war. He knew about the expansionary demands on the part of China and other emerging markets. He also knew or believed in an increase in the supply of oil from the Middle East. You can't find one responsible energy analyst that doesn't think the war had something to do with the increase in the price of oil. Now, how much the increased demand has to do with the increase in price is a matter of dispute, but we were very conservative in our estimates. We talked about a five to ten dollar per barrel increase for seven to eight years; the futures markets now expect prices to remain at an elevated level—over a hundred dollars a barrel now—for the

next ten years. The fact of the matter is that the war is related to the high price of oil, and the high price of oil in turn has had a depressing effect on the economy. We are spending money on importing oil from Saudi Arabia, Kuwait, and other countries—money that we could have spent in the United States. This has a depressing effect on the economy.

Economists often do a differential incidence analysis, which involves asking: what is the appropriate thought experiment if we had done this instead of that? In our book, we did this extensively, and each time, we came to the same conclusion. But let me provide a simple example. If we take the amount of money that we are using to hire a Nepalese worker in Iraq and we spend that money on constructing highways, developing schools, or funding research in the United States, the American economy would have been that much stronger, and by a significant magnitude. It depends on what your comparison is. Deficit spending of the magnitude that we have engaged in can't help but have a negative effect on our economy. At the very least, it has led to a weakening of the dollar, which has led to inflationary pressures—which itself is bad for the economy.

There are a number of these channels and Krugman looked at them in the old fashioned way of: "if we can spend this money and nothing else happens, then the economy is more stimulated." But you cannot do that. You either have to borrow that money or substitute that money for other things you would have spent—there is no experiment that allows for increasing spending without adjusting other factors. He made a fundamental mistake. If you agree with the analysis that I have just provided—that this type of spending is not as stimulative as other forms of spending due to the high oil prices—this means that the federal government had to do something to maintain the economy at an even keel. They (those within the federal government) took this task seriously, but myopically. In turn, they let loose more liquidity and kept more lax regulations than there otherwise would have been because they thought they needed to keep the economy going. The more lax the regulation, the more the liquidity, the bigger the housing bubble. The bigger the housing bubble, the greater the bust. The housing bubble is what led to savings going down to zero, so Krugman is right in saying that it has to do with the debacle in the financial markets, but he has not done enough analysis to explain why we have allowed this to happen in the first place. If we had been stimulating the U.S. economy, we would not have needed to do this. They would have had to increase interest rates, and the downturn would not have been as severe.

It is often cited that United States is fighting on borrowed funds, particularly from China. To what extent is this true?

The fundamental essence of this claim is true. The point is that the United States had a very large deficit in 2003 but we lowered the taxes just as we went to war without cutting back on expenditures. Consequently, every dollar and every dime has been borrowed. Since America's savings is down to zero, we have had to borrow from abroad. So although you cannot say that the money that China is lending is going to Iraq *per se*, we are nevertheless borrowing from abroad, and that money is going to war. This is the first war since the Revolution that we have had to rely on foreign debt.

What are the problems with funding a war through emergency supplementals as opposed to normal budgetary appropriations?

There are two problems. The first is that it leads to a set of funding by thrifts and graphs so that no one has a sense of just how much the war is costing.

It was remarkable how many congressmen did not keep a tally of how much the war was costing. I think we are going through twenty-five or twenty-six separate bills for the war. The more fundamental point, however, is that the regular appropriation process is designed to have the numbers looked over carefully by Congress, the CBO (Congressional Budget Office), and the OMB (Office of Management and Budget) to make sure that there isn't corruption and that the money is well-spent. But emergency appropriations have been, for a long time, the vehicle through which a lot of corruption occurs because corporate welfare is hidden. A lot of backspending emerges in these appropriations and contributes to the rising costs of the war.

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There is also a fundamental philosophical point that we emphasize in the book. We can say, in the beginning, that we did not anticipate going to war. But we are now in our sixth year of the war and cannot claim that it is still a 'surprise'. If you are claiming that there is a surprise and that is why you need more money, what you are saying in effect is that things are not going as well as you thought. And if things are not going as well as you thought, it is incumbent upon you to explain to the American people and to Congress why things have not gone as well as you had expected, and why you thought you didn't need the money but now you do. This serves to highlight what is going wrong and forces them to do better planning ahead of time. It just

results in better accountability and better spending.

Can you comment on some of the mechanisms and enforcement measures for increasing the accountability of the Department of Defense, the Secretary of Defense, and the Chief Financial Officer?

Well, in general, Congress does tie its own hands. It is done in a way that more money will not be appropriated unless taxes are raised or cutbacks in other expenditures are made. To override this agreement, sixty percent of favorable votes are required. It requires estimates of what the costs are going to be, and they have tried to improve the quality of decision-making and accountability. What we need now is the same process to be adopted. As the book states, we hold the private sector to higher standards than public servants. We require CFOs to sign the books, but we do not require the same financial statements at the Department of Defense. What is interesting is that almost every other department has such restrictions, and it is only the Department of Defense that does not. I think what Congress ought to do is simple—if you can't do that then you have to offer a remediation plan or resign. The caveat, of course, is that the remediation plan must be sent to Congress in such a way that it can be remediated. In a democracy, one way that you force yourself to do it is to call public attention to your failures.

Why has the United States used private contractors to the degree that it has for the Iraq War? Do you predict an increase in the privatization of war in the future?

This war is the most privatized that we have ever had. I think it is a combination of several factors. This war has been marked by a higher level of corruption than other wars and has been a way of providing higher payoffs to people at Halliburton and Blackwater—individuals who are clearly related to the administration in one way or another and reap significant rewards. Second, the administration has been committed from the beginning to convincing the American people that they could have a war for free without feeling the effects of the costs. This is why we have borrowed every cent.

What you can do is hide from public light. They did not want the American people to know that this war would require 250,000 to 300,000 troops. This would be bordering on Vietnam-War size commitments—not exactly of that magnitude, but pretty close. So what you do is use 150,000 American troops and fill the remaining 100,000-150,000 personnel with contractors. You never let people know for certain how many contractors or people are working in Iraq, let alone the people back at home supporting the war effort. This

method is a way of disguising the magnitude of the war effort.

Contractors are much more expensive service-for-service than using the Department of Defense. Furthermore, they create competition for the armed services, so we have to spend more to recruit. When a guy's tour of duty is over, he can just join a private contractor to double his pay. The only way we can keep him is to create high enlistment bonuses and to drive up the wage, but what we have done is create competition to drive up our own competition. It does not stop there—it is worse than that. Contractors are simply bad for morale. Just imagine how it is for two people to be doing the same job, but one is paid two to three times more than the other. Finally, it undermines the mission because the contractors are focused on minimizing costs and maximizing profits, and not on achieving a stable peace. So as we point out in the book, it is very important to win the hearts and minds of the people and to lower the unemployment rate in Iraq, which currently sits at around sixty percent. But, for example, the contractors often decide that it is better instead to hire a Filipino contractor. Not to mention, the Filipino contractor is working against Filipino law, but we would rather violate Filipino law just to make the war effort seem like it cost less than it actually did.

The institution here has a free-market ideology, but the extent to which such an ideology is relevant...it really has been intended to cloak this

giveaway to corporations—payoffs to their friends. Anybody who understands market economics would understand that the way they have done it and the circumstances of war are not circumstances in which private sectors work well. What makes markets work are voluntary exchanges in competitive frameworks. They outsourced to Haliburton—this is not competition. Exchanges between Blackwater and the Iraqi people are not voluntary exchanges. These areas have a long understanding that the private sector does not work well. Our history of these failures has been further validated by the debacle in Iraq. The only way to understand this phenomenon is to assert that this war was a combination of a corporate giveaway and a cover up.

You mentioned that veterans' healthcare should be viewed as an entitlement rather than as discretionary funds. Why do you think veterans' benefits have been subject to discretionary funds in the first place and what would the benefits of such a move towards an entitlement program be?

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We should be held to the same standards as in the private sector: if promises are being made out to workers, then funds should be set aside. The reason is that funds do not get put aside, and workers get short-cheated. We force them to do that, but we have not been living up to those standards ourselves. There is a real risk, and it is a risk that has already been evident in the Bush Administration because they have under-funded the VA (U.S. Department of Veterans Affairs). In effect, they are breaking the contract.

Anybody with a long-run concern about the strength of our military has to say that the worst thing we can do is to convey the impression that we do not treat our troops well and that is what the Bush Administration has been doing. We need to give future veterans the assurance that they're going to get what we promised them. Considering the damage in the past five years where we have broken our promise over and over again, it is really critical to say that we are going to live up to our promise and that we are going to put aside the money.

The other reason why entitlement programs are important is because they ensure good accounting. When you take an action, you want to know the full costs. These are part of the true costs when we go to war—which includes knowing the disability costs and the fact that we have to fund them. Having said that, we certainly have to record these costs in our account, but we have to follow through with the provisions as well.

Do you believe we should cut our losses and begin redeployment of the troops from Iraq?

That is a very big question, and Chapter 7 of our book presents the right framework for thinking about that. The framework for thinking about this, at the very least, is then to ask the question: “what would happen if we leave now?” versus “what would happen if we stay?” No one has made a convincing case that the likelihood of significant improvement in the situation is going to occur anytime soon.

We may have reduced the level of violence—though this claim is highly debatable—but there is absolutely no debate over the fact that there has not been a political settlement. In fact, consider the experience in Basra. Funding separate militias has led to an explosion of conflict. This is precisely the strategy of what we have been doing in the Sunni area. The likelihood is that the same effects will occur. Unless someone can make a more compelling case than anybody has so far, the costs of staying outweigh any benefits, and we should be beginning an orderly withdrawal from Iraq. ■