

Comments on “The endogeneity of the natural rate of growth: an alternative approach”

This paper identifies a purported problem with previous studies that have investigated the endogeneity of the natural rate of growth to the actual rate. A solution to this problem is proposed that involves using the balance-of-payments-constrained growth (BPCG) rate rather than the actual rate of growth in the process for estimating the natural rate proposed by Thirlwall (1969). Subsequent empirical results corroborate the finding reported in previous literature, that the natural rate of growth is, indeed, endogenous to the actual rate.

I don't think that the premise of the paper is particularly well explained and, in fact, I'm not convinced that the way the authors address the problem they claim to identify is correct. For example, the introduction of the paper begins with the question of whether we should be focusing on the proximity of the actual rate of growth to the natural rate or the warranted rate when studying the endogeneity of the natural rate. But it then drifts into discussion of “balance of payments difficulties” and using the balance of payments constrained growth rate when testing for endogeneity of the natural rate, without it being clear how (if at all) this is related to the question with which the discussion began. In the terse discussion of Thirlwall (2001) on p.4, meanwhile, it is asserted that inflationary pressure will result when the warranted rate is less than the natural rate. But why? Are we supposed to assume that the actual rate is equal to warranted rate at this point? And even then, if the actual rate is equal to the warranted rate which is less than the natural rate, then the labor market will slacken over time (the employment rate will be falling). How is this supposed to result in inflationary pressure?

The main problem, however, arises on p.5, where the claim that γ in equation (1') is the natural rate is, in my view, simply wrong. Hence note that by definition, γ in equation (1) is the natural rate of growth. Put simply, γ in equation (1') is not the same thing and is not, therefore, the natural rate of growth. In fact it is not clear to me what (conceptually) is being measured by γ in equation (1'), but given that this term (erroneously identified as the natural rate) enters into everything that follows, I can only conclude that the paper does not succeed in testing for the endogeneity of the natural rate as claimed.

I would suggest that the authors need to fundamentally rethink what they are doing in this paper.