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Why Government Spending Is Bad For Our Economy

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Though President Barack Obama has spent trillions of dollars, the U.S. economy is stagnant, fewer people are employed than when he became president, the percentage of people unemployed for over a year has doubled since then, the poverty rate is the worst in two decades, and more than 40 million Americans — a record — are on food stamps.

More government spending has been widely-touted as a cure for unemployment, but support for that view seems to be eroding – not least because Obama has little to show for his spending spree except about $4 trillion of additional debt. America needed more than 200 years to hit that number, but Obama did it in only three years. The experience offers a reminder that there isn't any net gain from government spending since it's offset by the taxes needed to pay for it, taxes that reduce private sector spending.

When Obama was sworn in, his top priority ought to have been reviving the private sector, since the private sector pays all the bills. Government basically doesn't have any money other than what it extracts from the private sector. Yet Obama decided to indulge his progressive whims and make government bigger.

His administration drained resources out of the private sector via taxes, then he signed his $825 billion "stimulus" bill, the American Recovery and Reinvestment Act of 2009 (ARRA), so that money could be redistributed among government bureaucracies. For instance, Obama authorized spending money to repair U.S. Department of Agriculture buildings, maintain the Farm Service Agency's computers and inform the electronically disadvantaged about digital TV.

Obama essentially acknowledged that he didn't know or care about how to stimulate the private sector, since he provided hardly any specific guidance for spending the money. For instance, ARRA awarded $600 million to the National Oceanic and Atmospheric Administration, saying only that the money was "for procurement, acquisition and construction" — which could have meant almost anything.

If the aim was really to stimulate recovery of the private sector, the most effective way of doing that would have been to leave the money in the private sector. After all, people tend to be more careful with their own money than they are with other people's money. Undoubtedly people would have spent their money on all sorts of things to help themselves, things worth stimulating like food, clothing, gasoline, downloads, cell phones and household repairs.

Because of the federal government's taxing power, it commands vast resources, and politicians can be counted on to start new spending programs they can brag about during re-election campaigns. Unfortunately, spending programs often have unintended consequences that can make it harder for the private sector to grow and create productive jobs. Nonetheless, interest groups that benefit from the spending lobby aggressively to keep the money flowing, which is why, since the modern era of big government began in 1930, spending has gone up 88% of the time. If we exclude the demobilization periods following the end of World War II (three years) and the Korean War (two years) when spending declined, it has gone up 95% of the time.

Economists James Gwartney, Randall Holcombe and Robert Lawson reported: "Evidence illustrates that there is a persistent robust negative relationship between the level (and expansion of) government expenditures and the growth of GDP. Our findings indicate that a 10% increase in government expenditures as a percent of GDP results in approximately a 1 percentage point reduction in GDP growth." Similarly, Harvard economist Robert J. Barro found that "growth and the size of government are negatively related when the government is already very large."

For example, every year the federal government funds tens of billions of dollars worth of student loans for college. Altogether, the federal government has provided money for some 60 million students. In 2010, for the first time, student-loan debt surpassed credit card debt. There are about a trillion dollars of student loans outstanding.

By enabling more and more people to bid for a college education, the government has promoted inflation of college costs — some 440% during the past quarter-century, quadruple the overall rate of inflation. Vance H. Fried, author of *Better/Cheaper College*, reported that nonprofit colleges make huge profits on undergraduate education, and they're spent on "some combination of research, graduate education, low-demand majors, low faculty teaching loads, excess compensation, and featherbedding." Meanwhile, an increasing number of families have difficulty paying for college without financial aid.

Federal farm subsidies range between $10 billion and $30 billion annually. Subsidies are paid on the basis of output or acreage, which means big farmers get more money than small farmers. Subsidies are limited to the "program" crops like corn, cotton, rice, soybeans and wheat, that account for about a third of farm production. Aside from enriching big farmers, the main impact of the subsidies is to encourage over-production and inflate the value of land suitable for program crops. One study, by economists at North Carolina State University, analyzed the different types of subsidies and concluded that each $1 of farm subsidies per acre inflates the value of an acre of farmland between $6.38 and $27.37, depending on applicable subsidies.

Since the mid-1960s, federal, state and local governments have spent hundreds of billions of dollars subsidizing government-run urban transit systems. Economist Randal O'Toole explained, "The number of transit trips per operating employee have fallen more than 50%, and the inflation-adjusted cost per trip has nearly tripled during the past four decades. Today urban transit is the most expensive way of moving people in the United States, and it's no better than cars in terms of energy consumption or pollution." Despite the endless subsidies, urban transit systems tend to be inadequately maintained, and they're loaded with debt. New York City's transit system alone has $30 billion of debt plus $15 billion of unfunded pension liabilities for its unionized employees.

The federal government gathers tax revenue from the general population and then channels about $2 trillion each year into the health care sector. The big entitlements Medicare and Medicaid account for 46% of health care spending, according to the Kaiser Family Foundation. Moreover, by establishing government as a third party payer for health care services, the entitlements eliminate incentives for individuals to be concerned about health care costs. Employer-provided health insurance has a similar effect. No surprise, then, that health care inflation is currently going up 9% a year, more than double the Consumer Price Index.

In the name of "affordable housing," Congress passed the Community Reinvestment Act (1977) that required bankers to provide more sub-prime mortgages for people who would have difficulty making the payments. Moreover, the government-sponsored enterprises Fannie Mae and Freddie Mac spent several trillion dollars buying securities that were bundles of sub-prime mortgages. This spurred Wall Street firms to churn out those securities. Result: more and more people put all their money into a single asset – their house. They bid up housing prices until there weren't any more buyers, and the housing market collapsed in 2008. As we know, the federal government subsequently spent trillions of dollars on housing-related bailouts. The Pew Research Center reported that black households lost more than half of their money. Hispanic households lost two-thirds. These were people supposedly helped by government spending.

Ever higher taxes are required to pay for all this and other government spending, which means draining more resources out of the private sector – making it harder to create growth and jobs. As these examples suggest, government spending often makes things more expensive, causes chronic inefficiencies, leads to more debt and disruptive financial bubbles. Far from being an economic stimulus and a cure for unemployment, government spending increasingly turns out to be bad for our economy.