

The Ideas Deficit

Don't believe the hysteria about the debt

By: Idrees M. Kahloon – April 16, 2013

Washington is awash with apocalyptic prophecies of the national deficit as some sort of looming catastrophe. Casting themselves as clairvoyant Cassandras, politicians like Senate Majority Leader Mitch McConnell call debts and deficits “the transcendent issue of our era.”

Deficit hawks, bolstered by self-interested billionaires like Pete Peterson, campaign for severe entitlement reforms, including raising the age at which seniors receive Social Security benefits. The fiscally austere mistake the deficit as a result of runaway government spending instead of weak demand caused by the recession, where deficits actually improve overall demand.

Comparing the economic recoveries, or lack thereof, of countries from the most recent recession best illustrates this Keynesian point. Great Britain's austerity program, once applauded when ushered in by Conservative Prime Minister David Cameron, has driven the economy to a possible triple-dip recession.

Ireland's “admirable lesson in fiscal responsibility,” as hailed in 2010 by Alan Reynolds of the conservative Cato Institute think-tank, has instead provided disappointingly low growth and a severe, stubborn 14 percent unemployment rate. Contrary to philippics of the deficit hawks, deficit reduction is not a panacea that restores confidence — it destroys prosperity.

With a dysfunctional Congress consistently shooting the country in the foot, embracing fiscal austerity in America would shoot ourselves in the other foot to ensure the country couldn't even limp onward.

Organizations like Fix the Debt are fearmongerers, with warnings like “if we don't act now on our own terms, the markets will force action through a severe economic crisis,” crippling high interest rates, and generational injustice. The prognostications miss the basic economic point that deficits in depressed economies do not increase inflation or interest rates.

An undercurrent of xenophobia commonly runs through attacks that denounce borrowing from China as some sort of existential threat to the country's freedom.

The truth is that Chinese holdings of American debt are rapidly falling, and Japan may soon be the largest foreign owner of American debt. Moreover, China's dependence on American consumers for its exports puts the economic vitality of America squarely in its own self-interest. Any conspiracy to ruin America's economy would severely ruin its own.

In fact, medium-term budget concerns about the debt-to-GDP ratio have been mostly solved by the \$1.5-trillion cuts of 2011 and the \$600-billion tax increases in the fiscal cliff deal. The nonpartisan Center on Budget and Public Priorities has called for an additional \$1.4 trillion in cuts over the next ten years to stabilize the debt at 70 percent.

In the long-term, however, the demographic shift to an older population along with the increasing healthcare costs of higher quality medical technologies pose a significant challenge to the country's finance. And it is here that the deficit scolds may be right when it comes to urging entitlement reforms, albeit for the wrong reasons.

Congressional Democrats and liberals should, in fact, support Social Security reform for the simple reason that the program is no longer as progressive as initially intended. Middle- and upper-class workers have much higher life expectancies than their poorer counterparts—a gap that's expected to increase as income inequality expands and the cost of medical technology skyrockets. As a result, middle- and upper-class Americans tend to accrue much higher total lifetime benefits, leaving the system much less progressive.

And \$100 billion in benefits go to employer-sponsored retirement programs, flowing almost entirely to upper- or middle-class workers, since lower-class workers often have neither the opportunity or financial resources to participate in such programs. Congressional action to slow the growth of benefits to middle- and high-income earners could reduce two-thirds of the \$4.8 trillion long-term deficit of the program.

But Democrats are fearful of meaningful entitlement reform, while Republicans remain poisoned by the anti-tax ideological extremism of the Norquist flavor. The state of the deficit and entitlement debate, where the parties prefer simplistic mantras to reasoned and rational debate, points to the stunning inability of both sides to give up their sacred cows. With the more gerrymandered districts now in play, members of Congress appeal to constituents with increasingly absolutist stances that severely cripple the ability of our legislature to produce substantive bills, as evidenced by the 112th Congress, which earned the dubious distinction of being the least productive in history.

So while the deficit hawks targeting entitlement programs might spur a beneficial rethinking of entitlements, the crowd has warned of impending economic doom far too many times to be taken seriously.

As much as they may insist, the sky isn't falling.