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Obama Chooses Badly: Recovery Thwarted

By Jon N. Hall

President Obama's defenders and detractors look at the same economic data but come to entirely different conclusions. Obama defenders say things would have been worse; Obama detractors say things should have gotten better by now.

Obama defenders contend that but for his heroic measures in combating the economic meltdown, America would have been plunged into another Great Depression.

Obama detractors contend that those same measures are thwarting a sustainable recovery and setting America up for an even more painful Day of Reckoning.

Other nations have had more reason to fear inflation than has America. Germany, for example, had hyperinflation in the 1920s, which made their money virtually worthless and brought the nation to its knees. With the Continental currency, America experienced hyperinflation during the Revolutionary War. But since the 1930s, the big economic fear in America is depression. Americans think depressions must be avoided at all costs because our experience with the Great Depression teaches us that a depression can be intractable.

Nevertheless, Obama takes his cue for dealing with the meltdown from FDR. It's the Keynesian template for how to handle a down economy: massive government intervention. The Keynesian cure includes deficit spending, jobs programs, and expanded government aid to the unemployed. Hence our trillion-dollar deficits, shovel-ready stimulus jobs, and "99ers," folks who have received unemployment benefits for 99 weeks and are soon to be bumped off the program. Obama's program is FDR's on steroids. Obama assures us that "only government" can cure what ails the American economy. Otherwise, we risk sinking into depression.

We shouldn't be so spooked. After all, we think of recessions as being necessary, even cleansing. They're part of the business cycle. They're corrections. We need them to get the economy back on an even keel. Perhaps if government dealt with them differently, sharp downturns that threaten depression could also be cleansing and corrective.

There *are* alternative methods for grappling with nasty recessions. The most recent case came in 1981 with Reagan. Reagan's methods are in sharp contrast with Obama's. Reagan cut marginal income tax rates, and Fed Chairman Volcker killed inflation with high interest rates. At about this point in Reagan's first term, the economy was on its way to a quarter-century expansion. Another example is that of Pres. Warren Harding in the Depression of 1920, the "forgotten depression."

Historian Jim Powell of the Cato Institute outlines how Harding's methods contrast with those of FDR. Harding slashed federal spending, cut taxes, and relaxed regulations. These actions got the nation out of depression in just a year and a half and ushered in the Roaring Twenties. It also led to eleven years of back-to-back budget surpluses from 1920 through 1930 (see Table 1.1). Powell's article appeared at National Review Online right before Obama's inauguration, and in it, Powell suggested that "President-Elect Obama ought to consider the model of Warren G. Harding, whose policies raised Americans' standard of living, and lifted the nation itself out of a depression."

After it became clear that Obama wasn't going to heed Powell's advice, Thomas Woods of the Mises Institute wrote a longer, footnoted article on Harding for the Fall 2009 issue of The Intercollegiate Review, now available here (and here if you haven't updated your browser). Woods writes (footnotes removed):

> Instead of "fiscal stimulus," Harding cut the government's budget nearly in half between 1920 and 1922. The rest of Harding's approach was equally laissez-faire. Tax rates were slashed for all income groups. The national debt was reduced by one-third. The Federal Reserve's activity, moreover, was hardly noticeable. As one economic historian puts it, "Despite the severity of the contraction, the Fed did not move to use its powers to turn the money supply around and fight the contraction." By the late summer of 1921, signs of recovery were

> already visible. The following year, unemployment was back down to 6.7 percent and it was only 2.4 percent by 1923.

(Woods also touches on Harding's place in the presidential firmament. Because he quickly ended a depression, Harding is the anti-FDR. So left-wing academics and pundits have for years marginalized Harding while inflating FDR, arguing that FDR "saved capitalism." Democratic strategist Bob Beckel of Fox News repeatedly touts Obama as "the greatest economic president since Roosevelt." Who knew?)

So we have two models for how to handle a bad economy -- one where government is downsized and one where government hypertrophies; one led by the private sector and one led by government. And we have two historical outcomes to judge -- one of quick success and one of protracted failure. The choice between the two would seem obvious. But Obama knows best.

Although America voted for change, the change we're getting is all going in the wrong direction. Where we should be going is back -- back to what's tried and true.

But to get back to that fabled economy of yesteryear, America must not only endure but must embrace a period of pain. We must take our medicine. Government cannot shield us from our ordeal of pain -- government caused it. That's why government is so intent on deflecting blame for the crisis onto the private sector, rather than on the Federal Reserve, Fannie and Freddie, a dreadful Congress, and a clueless administration.

Some in D.C. flatter themselves that by turning a few dials, they can manage the American economy. They think they can skate near the edge of the abyss, and while others have failed abysmally, their brilliance and mastery will keep them from falling in. When we have proven models for handling recessions, we allow unelected bureaucrats to experiment on the American economy in an attempt to vindicate their pet theories about the causes and cures of the Great Depression.

When Pres. Harding died in August 1923, he hadn't even completed two and a half years in office. But in that short time, Harding dramatically turned around America's economy. By rejecting Harding's proven methods, Obama has chosen badly. America is not seeing a "return to normalcy." Our economy is facing four lost years.

America's unemployment rate has risen to 9.8 percent.

How's that "Summer of Recovery" working out for you?

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