The Fairy Tale on Spending Cuts

By: Michael Tanner - February 26, 2013

"The sequester is coming, the sequester is coming," cries Chicken Little, speaking of the across-the-board spending reductions set to kick in next Friday. As a result, much of the Washington establishment, politicians of both parties, and the media are bracing for the apocalypse.

Henny Penny worries about poisoned meat going uninspected, the air traffic control system shutting down, and schools being forced to close. Meanwhile Turkey Lurkey is afraid that national security is threatened because our military will be gutted. And Foxy Loxy is concerned there will be massive job losses and our economy will crash.

Some think the sequester imposes savage spending cuts, but that's not true."
The reality, though, is that most of what we are being told about the sequester is just a fairy tale. Here's why:

The sequester imposes savage spending cuts

Actually, the sequester doesn't cut federal spending at all, or rather it cuts it only in the Washington sense of any reduction from projected baseline increases is a cut. In reality, even if the sequester goes through, the federal government will spend more every single year. In fact, in 2023 it will be spending $2.39 trillion more than it does today.

OK, but at least the reductions in projected spending are big, right?

Hardly. This year, the sequester would slow the growth in federal spending by just $85 billion, from an expected, pre-sequester budget of $3.64 trillion — less than a 2.3% reduction. To put that in perspective, the federal government borrows $85 billion every 28 days . In fact, this actually overstates the size of this year's cuts. Because of ongoing contracts and the Byzantine labyrinth of federal budgeting, only $44 billion of that $85 billion will actually be cut from this year's budget. The rest will be cut in future years, but attributed to this year's budget. So, the real reduction in federal spending this year is just 1.2%. If the federal government can't reduce spending by less than a penny-and-a-half on the dollar without throwing us into the dark ages, something is truly wrong.

But aren't the cuts larger for domestic discretionary spending?

It is true that the cuts are not spread equally across all types of federal spending. Entitlement programs, such as Medicare, Medicaid and Social Security are generally exempt — Grandma's Social Security check won't be cut — meaning that discretionary spending takes a disproportionately larger hit. Still, we are talking about a reduction of less than 9%. That would leave domestic discretionary spending, after adjusting for inflation, at roughly the same level as 2009. You recall 2009, don't you? The starvation, the mass closure of our schools, the shutdown of the transportation system, the burning cities?

What about defense? Surely, the sequester guts defense

Defense does take the biggest cut under sequester, nearly 13% of planned spending. In fact, defense spending would really be cut, in the sense of actually spending less, over the next two years. Still, it would never fall below the level of spending we had as recently as 2007, a year we managed to survive without al Qaeda wading ashore in Long Beach. Beginning in 2015, defense spending would start rising again, in real terms, and would exceed current levels by 2019. Keeping all this in perspective, over the entire 10-year period covered by the sequester, defense spending would average roughly $100 billion more each year (after adjusting for inflation) than we spent at the height of the cold war.

I'm still worried about the impact on the economy. Some economists believe that the sequester will cost thousands of jobs and throw us into another recession. True or not?

The proposed spending reductions amount to less than 0.03% of our gross domestic product. If our economy can't survive spending cuts of that size, we truly are Greece. Of course, in the short term, there will be some layoffs and furloughs. This will be hard on some communities that depend heavily on government spending, and even harder on those workers directly affected. However, most of the numbers cited about the numbers of jobs at risk come from industry groups with a vested interest in making the cuts look as bad as possible.

This entire argument buys into the Keynesian conceit that government spending creates jobs over the long term. But the resources necessary to create those jobs have to be extracted from the private economy either through taxes or borrowing. That means the private sector then has fewer resources to invest in job creation. Given that the private sector generally puts those resources to a more productive use, it is likely that government spending destroys more jobs over the long run than it creates.

We can and should have a legitimate debate about the best way to cut spending. But let's not be distracted by fairy tales about how the sky is falling.