Former Obama Official Calls for U.S.-Financed Keynesian Spending Binge in Europe

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There's an old saying that insanity is doing the same thing over and over again while expecting different results. This certainly is a good description of **Keynesians**, who relentlessly push more government spending as some sort of magic potion for the economy – **notwithstanding a record of failure**.

The latest example if Larry Summers, the former economist for the Obama White House, who says Europeans need to make government bigger.

Here is some of what he **writes for today's Washington Post**.

European efforts to contain crisis have fallen short. …Much of what is being urged on and in Europe is likely to be not just ineffective but counterproductive to maintaining the monetary union, restoring normal financial conditions and government access to markets, and reestablishing economic growth. The premise of European policymaking is that countries are overindebted and so unable to access markets on reasonable terms, and that the high interest rates associated with excessive debt hurt the financial system and inhibit growth. The strategy is to provide financing while insisting on austerity, in hopes that countries can rein in their excessive spending enough to restore credibility, bring down interest rates and restart economic growth.

The good news is that Summers recognizes that there has been "excessive spending." The bad news is that he uses the wrong definition of austerity.

Many European nations seem to think higher taxes are a sign of fiscal conservatism (see **this post** by Veronique de Rugy for a good discussion of this confusion). Summers accepts that approach, and says that policy makers should choose a Keynesian policy instead.

Unfortunately, Europe has misdiagnosed its problems in important respects and set the wrong strategic course. …Europe's problem countries are in trouble because the financial crisis underway since 2008 has damaged their financial systems and led to a collapse in growth. High deficits are much more a symptom than a cause of their problems. And treating *symptoms rather than underlying causes is usually a good way to make a patient worse. …The right focus for Europe is on growth; in this dimension, increased austerity is a step in the wrong direction.*

There's more good news. Summers is right in stating that Europe suffers from low growth. And I agree with him that the European version of austerity – higher taxes – is not a solution.

But, as always, there is a catch. Summers has the wrong approach on how to encourage growth. He wants Keynesian spending, and here is his defense.

Skeptics will rightly wonder how a prescription for more spending by countries that already have trouble borrowing can be correct. The answer lies in the difference between borrowing by individuals and countries. Normally, an individual helps his creditors by borrowing less; but a person who stops borrowing to finance commuting to his job does his creditors no favor. A country's income is determined by spending, so a country that pursues austerity to the point where its economy is driven into a downward spiral does its creditors no favor.

Sounds semi-reasonable. After all, everyone understands that it is important to get to their place of employment. Sometimes you spend money to make money.

But here's the problem. Can anyone name anything in so-called stimulus schemes that actually increase a nation's productive capacity? As we saw with Obama's failed stimulus, lots of money gets distributed, but the main purpose seems to be buying votes and creating dependency.

What about jobs? A **miserable failure**.

Adding insult to injury, you probably won't be surprised to learn that American taxpayers are supposed to pick up the lion's share of the tab for the new spending in Europe since Summers wants the IMF to be the sugar daddy.

Going forward, the IMF and international community should condition further support not merely on individual countries' actions but on a common European commitment to growth.

This approach is illogical, as explained in this video.

[Video]

And let's consider the historical record. Nations that have tried this type of "stimulus" have not fared well. **Big spending increase under Hoover and Roosevelt failed in the 1930s**. Japan tried several Keynesian packages and failed in the 1990s. Bush failed in 2008 and Obama failed in 2009.

Germany did not go with a big program of government spending, and they did better than the United States. The **same is true about Canada**. But the real success story is the

Baltic nations. They**imposed real spending restraint**, not the **fake austerity found in places such as the United Kingdom**.

And even though it caused some short-term pain since there's a short-term cost when labor and capital get redeployed to more productive uses, the **Baltic nations are now in much better shape** that the European nations that have floundered because they limited themselves to the **no-win choice of Keynesianism and tax hikes**.