Let Spending Continue!

By: Ron DeLegge – January 23, 2013

The House of Representatives voted to extend the nation's borrowing limit an additional four months, through May 18.

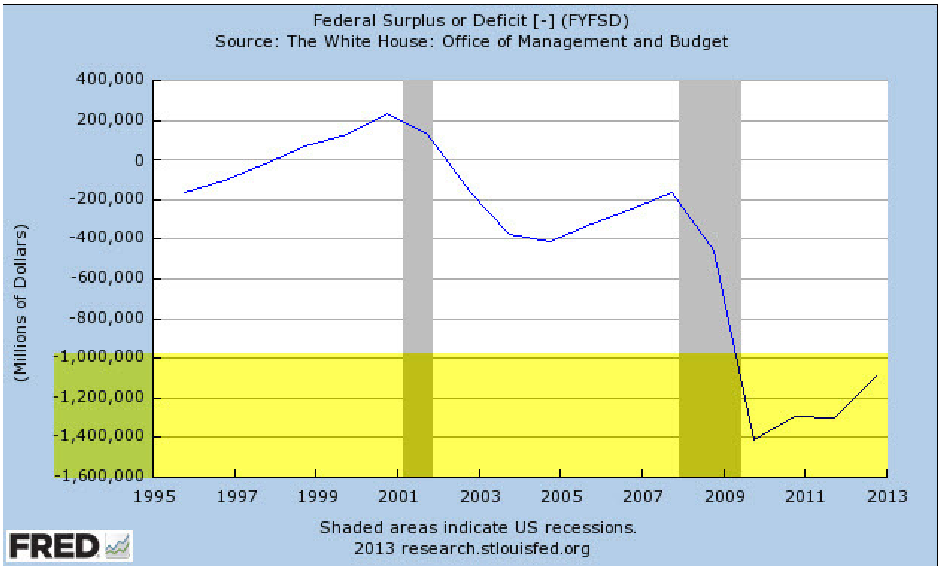
The "No Budget, No Pay Act" now buys Congress more time to find a longer term agreement on the $16.4 trillion debt ceiling, which was breached on Dec.31, 2012.

"If the debt ceiling isn't raised, the consequences would be catastrophic," is what spendthrift Keynesians argue. Ironically, increasing or even eliminating the debt ceiling also leads to catastrophic consequences, but with a delayed reckoning day.

In an outstanding piece by Chris Edwards, the director of Tax Policy Studies at the Cato Institute he correctly observed this. In "America's Spending Crisis" he wrote:

"Even if the economy recovers in the next couple of years and federal revenues rise, policymakers will likely find new reasons to spend more money and keep deficits high. Another economic downturn would bring forth demands for more Keynesian spending stimulus. A new military conflict would push up the already bloated defense budget. And as we've seen in the wake of Hurricane Sandy, every unexpected natural disaster is an excuse to open the spending floodgates for infrastructure and aid payments. The fiscal reality is that policymakers have no choice but to sharply reduce spending if the US is to head off the looming fiscal train wreck. Unfortunately, it does not appear that they are prepared to make the necessary spending cuts at this time. Unfortunately, the longer they wait, the more difficult will be the reforms."

Deficit spending by the U.S. government has exceeded $1 trillion for four consecutive years and in 2012 it was $1.1 trillion. (See chart below) Although deficit spending does not stimulate economic demand, it can stoke inflation. (See 1960s and 70s when the Vietnam War era deficits led to inflation.)



Annual budget deficits occur when spending exceeds revenues, forcing the government to borrow to cover the shortfall.

Federal debt held by the public is the total value of outstanding Treasury bills, notes, bonds, and other debt instruments (including Treasury securities held by the Federal Reserve) that have accumulated over time to finance the government's activities.

The yield on 10-year U.S. Treasuries (NYSEARCA:IEF) is at 1.84% and its 52-week high is 2.40%. ETFs tracking 7-10 year Treasuries have gained 2.83% over the past year while 20+ year long-dated Treasuries (NYSEARCA:TLT) have edged up 3.47%. The total U.S. stock market (NYSEARCA:SCHB) over that same time frame increased by 13.49%.