Economists Tell Congress to Enact Spending Cuts

Northwood University Economics Professor Dr. Richard Ebeling told members of the subcommittee: "It is hard for Americans to think of their own country experiencing the same type of fiscal crisis that has periodically occurred in 'third world' countries. That type of government financial mismanagement is supposed to happen only in what used to be called 'banana republics.' But the fact is, the U.S. is following a course of fiscal irresponsibility that may lead to highly undesirable consequences."

The hearing coincided with a warning by U.S. Treasury Secretary Timothy Geithner that the U.S. government will reach its $14.294-trillion statutory debt limit within days and begin defaulting on its debts if the national credit card limit is not raised by August 2.

Nevertheless, a recent Gallup poll demonstrates wide popular opposition to raising the debt limit. According to the Gallup organization, "By a 47% to 19% margin, Americans say they would want their member of Congress to vote against raising the U.S. debt ceiling, while 34% don't know enough to say."

Dr. Matthew J. Slaughter, a Senior Fellow at the establishment organization Council on Foreign Relations and Associate Dean of the MBA program at Dartmouth College, told Congressmen that the financial fallout from a default would be impossible to predict precisely, but added, "Going in that direction carries great risk." Slaughter said that Congress was left with little choice other than to raise the federal statutory debt limit:

> Some might ask, couldn't a deficit-reduction plan be crafted and implemented that would create fiscal balance and thus prevent America from breaching its looming debt ceiling? Speaking practically, the answer is no. As of May 3 the total amount of federal debt outstanding was about $14.28 trillion. The debt limit is $14.294 trillion. Even if America wanted to do so, there simply is not enough calendar time for America to rewrite its spending and taxing laws to prevent reaching this limit. Speaking economically, the answer should also be no. There is no doubt that America must soon control its massive fiscal deficits. But doing so immediately would require such a massive combination of spending cuts and/or tax increases that it would almost surely throw America back into a deep recession.

Slaughter served as a member of the Bush administration's Council of Economic Advisers during the height of the housing bubble from 2005 to 2007. He expressed strong support for the current leadership of the Federal Reserve Bank, though he admitted Fed monetization of federal debt could become a serious national problem: "History does offer grim examples where central banks have excessively monetized runaway fiscal deficits when too few buyers of government debt materialized —

and thus spawned hyperinflation: Germany in the early 1920s or Zimbabwe in recent years. Thanks in large part to the ongoing sound leadership of Federal Reserve Chairman Ben S. Bernanke and his colleagues, such a catastrophe remains a near-impossibility in America today."

"I concede that is a problem and there will be some consequences," Representative Ron Paul (R-Texas), the chairman of the subcommittee, noted. "How bad is it if this debt limit isn't raised?... They are panicking us now and saying that anybody that would suggest this is equivalent to a 'terrorist.'"

"I don't think that it has the danger that has been suggested," Ebeling replied, adding that the alternative to raising the debt limit would be to cut spending to the level where the government is living within its means — that is, the taxes currently collected by the Treasury. "The U.S. government certainly takes in far and above the tax revenue necessary to meet interest and rollover costs of the existing debt." Ebeling stressed that the United States could make a serious dent in the deficit by cutting back on the military commitment to foreign wars and far-flung U.S. military bases abroad, a sentiment echoed by Massachusetts Democrat Barney Frank of the subcommittee, who said of NATO today: "We're defending wealthy nations against non-existent threats."

Ebeling, a former president of the libertarian Foundation for Economic Education and adherent of the Austrian school of economic theory, stressed that the Federal Reserve Bank's efforts to finance the federal deficit for the past few years has created an enormous "social cost of deficit spending" that has squeezed financing and savings from the market economy. "Every dollar borrowed by the United States government, and the real resources that dollar represents in the market place, is a dollar of real resources not available for use in private sector investment, capital formation, consumer spending, and therefore increases and improvements in the quality and standard of living of the American people. In this sense, the government’s deficit spending that cumulatively has been increasing the national debt has made the United States that much poorer than it otherwise could have and would have been."

In essence, Ebeling argues that deficit spending is cheating the nation out of economic growth: "Whether acquired by taxing or borrowing, the resulting total government expenditures represent the real resources and the private sector consumption or investment spending those resources could have financed that must be foregone. There are no 'free lunches,' as it has often been pointed out, and that applies to both what government borrows as much as what it more directly taxes to cover its outlays."