The Washington Times
www.washingtontimes.com

Destructive Economic Myths

By Richard W. Rahn
Published February 8, 2011

Supposed 'truths' are toppling America's financial success

Wildly inaccurate statements from news commentators, financial analysts, politicians and even administration officials have most people believing that if Congress does not increase the debt limit in March, the U.S. government will default on its debt obligations, thus ending the government's ability to borrow. Nonsense.

If you make $5,000 per month, have a mortgage payment of $1,500 per month and then spend another $4,500 per month on food, utilities, gasoline, insurance and other expenses, including $2,000 per month traveling to sporting events and going to expensive restaurants, you will find yourself running a deficit of $1,000 per month. Your choice is to default on your mortgage and ruin your credit rating or cut back on sporting events and expensive restaurants.

The U.S. government is in exactly the same position. If the debt ceiling is not raised, government officials will have a choice to default on the interest payments (less than 10 percent of the government's total income) or cut spending. Sen. Pat Toomey, Pennsylvania Republican, has introduced the Full Faith and Credit Act (S.163), which would require the Treasury to make interest payments on U.S. government debt its first priority if the debt ceiling is not raised. This legislation would require the federal government to reduce spending on other activities and/or sell assets, as any business or family would need to do when faced with a similar problem.

The big-government crowd claims huge hardships would result from the mandatory spending reductions. Again, nonsense. Spending would only have to be reduced to roughly the 2006 level to avoid an ongoing deficit. The government receives a little more than $70 billion a day, or more than $2.5 trillion a year. Much of what the government spends is downright destructive and should be stopped. For instance, ethanol subsidies increase the price of food, decrease automobile mileage efficiency and increase - not decrease - the amount of carbon dioxide, which even Al Gore admits now. The U.S. government has roughly a trillion dollars in financial assets that are marketable and could be sold.

It could lease for hundreds of billions of dollars oil, gas and mineral assets that it has locked up to keep the environmental fringe happy. The U.S. government owns about one-third of the country's land - 654 million acres - worth several trillion dollars. Much of this land is poorly managed and, if sold, would bring in revenue, be better managed and be put on the tax rolls of state and local governments. A win, win, win.

Another widespread myth is that if the government reduces its spending, that will cost jobs. This myth is being promulgated by many Democrats and their allies in the media. The fact is that the percentage of adults in the labor force has fallen to its lowest level in three decades even as the government has grown by a quarter in relative size in the past three years. If government spending could bring about full employment, the socialist countries would have been great successes rather than basket cases. Remember, the money government spends on "creating" jobs comes from either taxing or borrowing - both of which take money and jobs out of the more productive private sector - thus reducing the total number of jobs.

The myth that the deficit problem can be solved only by some combination of tax increases and spending cuts is accepted as revealed wisdom by much of the political class, including some conservative commentators and economists. This myth is only true if you believe that the so-called entitlements - primarily Social Security, Medicare and Medicaid - must grow as a share of gross domestic product (GDP). The Cato Institute and other policy organizations have developed realistic and financially sound plans that both protect those who need to be protected and keep these programs from swallowing everything else. When you hear this myth, keep a simple fact in mind: If the government is growing faster than the economy (as it is now) no increase in taxes can reduce the deficit. If the government grows slower or at least no faster than the economy, as it did in the last Clinton and Reagan administrations, the deficit and federal debt will come down as a percentage of GDP without tax-rate increases.

Finally, the destructive myth persists that if only we could get the rich to cease engaging in tax avoidance, which is legal, and stop tax evasion, which is illegal, government would have adequate revenue. The fact is that rich people already pay most of the taxes. The top 5 percent pay almost 60 percent of the income tax, and trying to get more money out of them will just chase them away. One advantage rich people have is that if they feel too much tax oppression, they can leave for greener pastures - from New York to Texas, for instance. This past year, Congress passed measures to catch a few tax cheats that are having the unintended effect of making it almost impossible for many foreign financial institutions to invest in the United States, costing the U.S. tens of thousands of jobs and hundreds of billions of dollars in tax revenue.

The lack of jobs and economic growth in the United States easily can be traced back to policymakers who believe in destructive myths. Fortunately, on the centennial of his birth, more people understand a piece of wisdom from Ronald Reagan: “Government is the problem, not the solution.”

Richard W. Rahn is a senior fellow at the Cato Institute and chairman of the Institute for Global Economic Growth.

http://www.washingtontimes.com/news/2011/feb/7/destructive-economic-myths/