The Problem with Federal Debt

My friend County Executive Mark Harris is a deficit hawk fanatic. If you're ever in an elevator with Mark, and mention the Federal Government's level of debt, Mark will go into tremendous detail about how big it has gotten and how fast it is growing. My advice is, if you're ever in an elevator with Mark, don't mention the Federal debt!

I mostly agree with Mark on this issue. So, why am I not upset with President Obama, who's proposing to add nearly a trillion dollars to that debt in the next year? Because there are deficits, and then there are deficits. Mostly, as Mark will tell you, deficits are a bad thing. But not right now.

This is my third column on the evils of borrowing. Too much debt is a problem for families; and too much debt is a problem for investment bankers. Well guess what – too much debt can be a problem for governments as well. Just as businesses that rely too heavily on debt, and households who live beyond their means, usually end up in hot water [google "Asian Financial Crisis"], governments who live beyond their means end up in trouble as well [google "Latin American Debt Crisis"].

Those troubles can involve hyperinflation, when the government tries to bail itself out by printing lots of money. Or they can involve essentially giving up sovereignty, and having one's budgetary decisions dictated to you by foreigners [google "IMF bailout conditions"]. Both can wreck your economy, taking a decade or more to recover from. The US economy is large enough, and the US government stable enough, that it can probably borrow for a long time before either trouble arises. But a long time is not forever. Even the most wayward of chickens will eventually come home to roost.

So why are deficits OK right now? Because we're in a recession, and it's the government's job to pump up the economy. In normal times, banks supply loans to businesses, to help finance investments in plant and equipment, that create jobs, that generate income, that create consumer demand, that create more jobs, that generate more income, etc. But in a financial panic those loans dry up, as does that investment, those jobs, and all the other jobs as well.

So Obama wants the government to borrow money, to invest in roads and schools and other public projects, to create the jobs, etc. It's the classic Keynesian prescription, and it works.

Bush did something similar, in his "Economic Growth and Tax Relief Reconciliation Act of 2001." The Bush tax cuts during the 2001 recession were designed to put more money in our pockets by cutting our taxes, so we'd increase our spending, and so similarly create jobs. The problem was that after the recession ended, the tax cuts didn't. A deficit, created either by a tax cut or a spending increase, is an appropriate fiscal policy when the economy is weak. But a $200 to $300 billion deficit in times of strong economic growth is inexcusable, right, Mark?

So Mark, these deficits right now, during these times, no problem. But let's not put our deficit-hawk hats away entirely. A year from now, those Bush tax cuts will finally expire – the ones that supposedly pulled us out of the last recession but didn't prevent our sliding into this one. When they do, and Obama's "middle class tax cuts" replace them, let's demand that the resulting package is designed to move us quickly towards a fiscal surplus. Because for the most part, even for governments, too much borrowing is a bad idea.