

Economists See Deficit Emphasis as Impeding Recovery

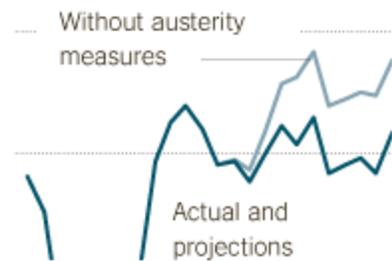


President Obama said last week that the only way to fix the economy was for both parties to sit down and say, “How are we going to make sure that we’re reducing our deficit sensibly?”

By JACKIE CALMES and JONATHAN WEISMAN

WASHINGTON — The nation’s unemployment rate would probably be nearly a point lower, roughly 6.5 percent, and economic growth almost two points higher this year if Washington had not cut spending and raised taxes as it has since 2011, according to private-sector and government economists.

After two years in which President Obama and Republicans in Congress have fought to a draw over their clashing approaches to job creation and budget deficits, the consensus about the result is clear: Immediate deficit reduction is a drag on full economic recovery.



Hardly a day goes by when either government analysts or the macroeconomists and financial forecasters who advise investors and businesses do not report on the latest signs of economic growth — in housing, consumer spending, business investment. And then they add that things would be better but for the fiscal policy out of Washington. Tax increases and especially spending

cuts, these critics say, take money from an economy that still needs some stimulus now, and is getting it only through the expansionary monetary policy of the Federal Reserve.

“Fiscal tightening is hurting,” Ian Shepherdson, chief economist of Pantheon Macroeconomic Advisors, wrote to clients recently. The investment bank Jefferies wrote of “ongoing fiscal mismanagement” in its midyear report on Tuesday, and noted that while the recovery and expansion would be four years old next month, reduced government spending “has detracted from growth in five of past seven quarters.”

That period roughly coincides with the time that Mr. Obama and Congressional Republicans have shared governance since Republicans took control of the House in 2011, promising an immediate \$100 billion in spending cuts. Republicans did not get that much then, but the series of budget compromises with the president since — while not so great as they wanted — will soon reduce annual discretionary spending for domestic and military programs to the lowest level in half a century.

As for revenues, Mr. Obama forced Republicans to acquiesce in January to higher taxes from wealthy Americans. But worse, in the macroeconomists’ view, both parties agreed not to extend a two-year-old cut in Americans’ payroll taxes for Social Security, reducing their spending money.

In all this time, the president has fought unsuccessfully to combine deficit reduction, including spending cuts and tax increases, with spending increases and targeted tax cuts for job-creation initiatives in areas like infrastructure, manufacturing, research and education. That is a formula closer to what the economists propose. But Republicans have insisted on spending cuts alone and smaller government as the key to economic growth.

The results, Mr. Obama has taken to saying, despite his complicity, are “self-inflicted wounds.”

“The only way the problem does get fixed is if both parties sit down and they say, ‘How are we going to make sure that we’re reducing our deficit sensibly?’ ” he said last week at a news conference. “How are we making sure that we’re investing in things like rebuilding our airports and our roads and our bridges, and investing in early childhood education, basic research — all the things that are going to help us grow?”

Mr. Obama added, “I cannot force Republicans to embrace those common-sense solutions.”

Speaker John A. Boehner stood by the Republicans' policies during a session Tuesday with reporters. "After four years of mediocre job creation, it's obvious that we don't need more tax hikes and more government spending," he said. "We need smarter policies to make America more competitive and expand opportunities for everyone in our country."

"We're the ones pushing this town to do the right thing when it comes to the economy and jobs," Mr. Boehner added.

The Federal Open Market Committee, which sets policy for the central bank, noted signs of improvement in the private sector last week in a statement. "But fiscal policy is restraining economic growth," it added, echoing public comments that Ben S. Bernanke, the Fed chairman, has made for months. In April, the International Monetary Fund said the United States would achieve further growth "in the face of a very strong, indeed overly strong, fiscal consolidation."

Thursday will capture as plainly as any day lately the differing approaches of Mr. Obama and Republicans toward the economy and government's role.

Mr. Obama plans to travel to Austin, Tex., to visit technology students, workers and entrepreneurs and promote his ideas to support efforts like theirs — the kind of initiatives that Republicans have blocked.

House Republicans expect to pass a measure that would allow the Treasury to "prioritize" debt payments if Congress and Mr. Obama cannot agree this year to increase the nation's debt ceiling so the Treasury can keep borrowing money to pay all creditors. Under the bill, as tax receipts came in, the first priority would be paying creditors — like China, Democratic opponents argue — and second would be Social Security checks. But the measure would likely die in the Democratic-controlled Senate.

The "prioritization" proposal first arose in 2011 from among the most conservative House Republicans, those who were driving hardest against the White House on raising the debt ceiling and expressing unconcern about default, but it has now become mainstream in the House ranks.

Economists and financial analysts generally dismiss the idea as unworkable if not dangerous, and count on Democrats to block it. Gregory Daco, a senior principal economist at IHS Global Insight, said the Republicans' proposal was the kind that caused his clients to ignore the fiscal policy out of Washington, and rely instead on the Fed to buttress the recovery.

"Whenever I talk to our customers or clients, they sort of brush off everything that's related to fiscal policy," Mr. Daco said. "The view is, 'Oh, it doesn't matter.' That's what I hear a lot."

"What we try to convey is that it does matter," he said. "It is important in terms of growth. It's also important in terms of confidence."

He noted that the economy was much stronger than Europe's largely because the United States initially opted for stimulus measures and allowed deficits to increase when the recession and financial crisis hit five years ago. European governments pursued austerity policies to cut their debts, further stalling economic activity and in turn inflating deficits.

The more recent austerity policies here are helping to bring annual deficits down, as a new report of the Congressional Budget Office shows, after four years of trillion-dollar shortfalls. Yet many analysts would prefer that the measures had been timed for when the economy is strong and unemployment below 7 percent.

"While I agree that the U.S. must get its fiscal house in order," Jerry Webman, chief economist at OppenheimerFunds, wrote, "I join the likes of the I.M.F. in cautioning that too much austerity, too soon, is likely counterproductive."
