OBAMA AND U.S. DOMESTIC ECONOMIC POLICY

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As the world watched from afar and 2 million did so in person, a new era began when Barack Hussein Obama became the U.S. president. In his person, he exemplified how far the country had advanced from its sorriest history. He announced that the country was returning to its principles in its foreign and domestic behavior, to the probable discomfort of his predecessor who listened from only feet away. The spirit with which he and his announcement were received is exemplified by the fact that not a single arrest was made among those in the unprecedented throng.

He knew, and those distant and present had to know, that he was taking office in the worst economic circumstance that most of those living had ever experienced. He was expected to ameliorate it. To help him, he assembled a team of experienced practitioners. Almost all had held positions of responsibility in the past. Their experience would help him decide what needed to be done now.

There is no secret about the available tools – primarily monetary and fiscal policies. Some innovative aspects of them were and are being devised but their fundamental virtues and frailties for rectifying the present distress remain.

In these circumstances, the aim of monetary policy is to so reduce the cost of borrowing and to so increase the supply of lendable funds that borrowers are willing to borrow and lenders are willing to lend. Achievement of these laudable aims is limited. Two commonly used phrases explain why: "You can lead a horse to water but you can't make him drink" and "You can pull on a string but you can't push on it." They mean: first that increasing the capital of lenders may not induce lenders to lend and secondly that though increasing the cost of borrowing may restrain it, lowering its costs can't induce borrowing in the absence of adequate demand for output. In light of this, it is not a surprise that frustration has led to growing talk about nationalizing some banks, as has already been done with some other financial organizations.

In these circumstances, the aim of fiscal policy is to restore the level of spending because deficiencies in income are the same as deficiencies in spending. Two means are available – reduce government's tax revenues and increase government spending. Either way, the government's outstanding debt rises. The practical question is which approach, lowering taxes or increasing spending, will be more restorative of total spending and therefore income.

Recent experience is that a dollar decrease in individual taxes does not lead to a dollar in new spending. Some is used for saving and personal debt reduction. A dollar decrease in business taxes would only increase private investment if there were prospective needs for more and cheaper output, that is, if there was prospective demand. It is hard to realistically expect what many in and out of Congress espouse – that cutting business taxes will reflate the economy. Moreover, businesses in severe distress already pay little, if any, taxes just as this is true for individuals.

The alternative, government spending, provides the assurance that each dollar of deficit will be spent and generate income. Real issues exist about the speed with which it can occur and the utility of the fruits of the expenditure. Unfortunately, discussion in and out of Congress treats other matters as though they were as important as these issues.

Another real issue is the implications of the rising national debt. As long as the debt is held internally, its effect on income distribution can be offset in a variety of ways, if that is desired. When foreigners hold much of the debt, there are national and international implications that are presently unremarked. That is regrettable, particularly because the presently discussed level of prospective government deficit is probably substantially too small to do what is expected, restore income levels through spending and re-spending.

At least in public, Obama has behaved in the name of bipartisanship as though all policy positions might have some validity and that we’ve learned nothing from the recent experiences of giving money to both individuals and financial institutions. Hopefully he and his advisers know that direct spending is the most effective and efficient route and that the presently discussed amounts of increased debt are only a fraction of what may be needed. At the time of this writing, his bipartisanship has won him zero Republican votes in the House of Representatives.