Is the Deficit a Friendly Giant After All?

Allan H. Meltzer
Carnegie Mellon University, am05@andrew.cmu.edu

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Published In
debt. Better management of public resources is a more productive direction than ever-larger deficits.

Allan H. Meltzer
University Professor of Political Economy
Carnegie-Mellon University
Pittsburgh, Pennsylvania
Visiting Scholar
American Enterprise Institute for Public Policy Research
Washington, D.C.

Much of the postwar fiscal history of the federal government can be written in three sentences: receipts have remained between 16% and 20% of GDP, spending as a share of GDP has increased persistently, a growing budget deficit is the result.

What matters most about budget deficits is how fast they grow, what they pay for, and how they are financed. Government, like everyone else, can finance its deficit by borrowing, but unlike the rest of us, can tax and print money. Inflation results when money grows faster than output does. Many countries have experienced high inflation because of budget deficits and excessive money growth.

Borrowing to finance budget deficits can be useful if we use the borrowed resources productively. If the large deficits of the 1980s and 1990s had financed productive investment, we would be richer now or in some way better off. To the extent that the Reagan deficits financed a military buildup that the Soviets would not and could not match, the world is now more peaceful, and we are better off. Of course, we could have paid for the buildup with current taxes, but doing so would have concentrated the costs at a point in time instead of spreading them over present and future beneficiaries.

A common argument against recent deficits is that they financed a consumption binge. It is true that reported investment grew relatively slowly in the 1980s, but published data are misleading. A larger issue is whether or not increased consumption is bad or should be avoided. It is not a cause for alarm if the public willingly chooses to consume more today than tomorrow. Most of us do just that when we buy a house and take out a mortgage. As a society, however, we should be concerned about biases in the tax system, in laws, in regulations, and in government spending that tilt spending toward consumption and against investment or that encourage borrowing and indebtedness. If there are such biases, we should correct them in the interests of efficiency.

What matters most about budget deficits is that they financed a military buildup that the Soviets would not and could not afford, that the Reagan deficits financed a military buildup that the Soviets would not and could not match, and the world is now more peaceful. The Reagan deficits deserves more rational and less emotional responses by our government. Many of the points he raises in support of this argument are difficult to refute and reflect the sound analysis of an experienced economist who has been examining this subject with a professional, open mind for many years.

I want to comment on a few points that deserve closer attention and suggest that his premise might be modified to something more palatable: deficits may not be harmful if they are directly associated with specific, high-priority, economic restructuring activities. Indeed, this statement can accommodate Eisner's argument, as long as stimulating "purchasing power for the products of American business" has some merit, particularly as it serves to point out that the subject of deficits deserves more rational and less emotional responses by our government. Many of the points he raises in support of this argument are difficult to refute and reflect the sound analysis of an experienced economist who has been examining this subject with a professional, open mind for many years.

Eisner misleads when he writes that government debt gives our children "a nice cushion of accumulated savings." The only way we can enrich future generations is by having more knowledge or more capital assets, things such as plants, equipment, schools, and airports. For society, government deficits, no less than private borrowing, reduce total saving.

Eisner's appeal for increased government spending takes us to the heart of the issue. Most of the fuss and noise about the budget deficit is not about deficits. It is about spending and redistribution. Many of the critics of recent deficits want to spend more, not less, and to tax the "rich." One needs only to look at the current Clinton budget and the coming health care proposals to see that tax rates and government spending will rise without reducing the deficit much below the levels projected without the additional taxes. But many of those who railed against "deficits" will fall silent.

William Reinfeld
President
William Reinfeld & Associates
Taipei, Taiwan

Eisner's premise that deficits can be good "if they generate otherwise lacking purchasing power for the products of American business" has some merit, particularly as it serves to point out that the subject of deficits deserves more rational and less emotional responses by our government. Many of the points he raises in support of this argument are difficult to refute and reflect the sound analysis of an experienced economist who has been examining this subject with a professional, open mind for many years.

I want to comment on a few points that deserve closer attention and suggest that his premise might be modified to something more palatable: deficits may not be harmful if they are directly associated with specific, high-priority, economic restructuring activities. Indeed, this statement can accommodate Eisner's argument, as long as stimulating "purchasing power for the products of American business" is seen as a high-priority, near-term, restructuring goal.

I am in agreement with Eisner that the definition of the federal budget deficit needs to be standardized and made relevant to what it addresses. It certainly should, as a minimum, distinguish between current or oper-