Myths and Realities of Government Spending

BY GERALD FRIEDMAN

Conservatives claim that massive government spending threatens the economy. The corporate-funded Fix the Debt coalition, for example, warns that, under President Obama, wasteful government spending includes "unsustainable entitlement costs." Swelling government debt, Fix the Debt contends, will force the United States to pay ruinous interest rates that will drive down living standards. While these charges serve the political interests of those who oppose government social programs, they confuse the real fiscal issues in America: the effects of the Great Recession on government revenues and the inadequacy of current levels of government spending to deal with massive unemployment. D&S

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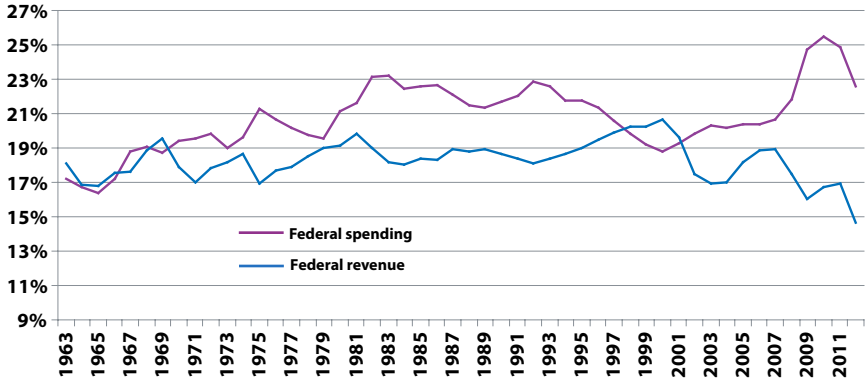
SOURCES: "Citizens' Petition," Fix the Debt (fixthedebt.org); *Economic Report of the President*, 2012; United States Treasury, "Joint Statement on Budget Results for Fiscal Year 2012," Feb. 12, 2012 (treasury.gov); Bureau of Labor Statistics, "Employment Situation, 2012" Feb. 1, 2013 (bls.gov); Bureau of Economic Activity, "Gross Domestic Product: Fourth Quarter and Annual 2012," Feb. 28, 2013 (bea.gov).

Figure 1: Federal Spending and Revenue as Share of GDP, 1963-2012



As a share of national income, federal spending peaked during the Reagan administration. There was a brief jump in spending as a share of Gross Domestic Product (GDP) in 2009 due to the fall in national income as well as the Obama stimulus program. Since then, however, spending has fallen sharply as a share of GDP. Large federal deficits since 2001 have been the result of declining revenues, first due to the Bush tax cuts and then due to falling incomes in the Great Recession.

Despite the stimulus program and demands for aid to the unemployed and to distressed local and state governments, inflation-adjusted spending has increased only half as fast under President Obama as under George W. Bush. Spending under Obama has risen at the slowest rate of any presidential administration since the 1960s, except Clinton's. In past administrations, spending increased with higher unemployment. Had federal spending increased with high unemployment as fast under Obama as in the past, spending would have risen two percentage points faster each year. This increase, over $70 billion dollars a year or nearly $300 billion by the end of four years, would be enough to enact another stimulus program leading to over 2.5 million additional jobs.

Figure 2: Federal Spending Growth

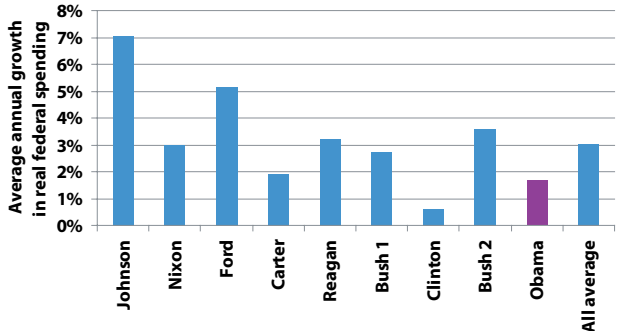
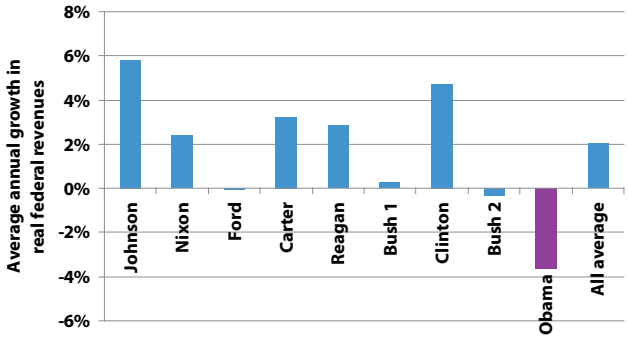


Figure 3: Annual Growth in Real Federal Revenue



Contrary to the conservative drumbeat about "out of control" spending, it is the decline in revenues, not rising spending, that accounts for the swelling federal deficit under Presidents Bush and Obama. Revenues have fallen dramatically due to the Great Recession because laid off workers and shuttered businesses do not pay income or payroll taxes, and because tax cuts, whether to favor the rich under President George W. Bush or to stimulate the economy under President Obama, have further reduced revenues. The shortfall in revenues compared with earlier administrations explains all of the increase in the federal deficit between the last year of the Bush administration (2008) and the last year of Obama's first term (2012).