# Fiscal Discipline DA

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# \*\*NEG\*\*

### 1NC Downgrade Shell

#### A. Fiscal discipline now – political pressure will lead to debt compromise

Washington Post 7/18

Washington Post 7/18/12, <http://www.columbiatribune.com/news/2012/jul/18/coalition-aims-to-head-off-debt-disaster/>

WASHINGTON — A coalition of business leaders, budget experts and former politicians launched a $25 million campaign yesterday to build political support for a far-reaching plan to raise taxes, cut popular retirement programs and tame the national debt. With anxiety rising over a major budget mess looming in January, the campaign — dubbed "Fix the Debt" — is founded on the notion that the moment is finally at hand when policymakers will be forced to compromise on an ambitious debt-reduction strategy. After nearly three years of bipartisan negotiations, the broad outlines of that strategy are clear, the group's leaders said during a news conference at the National Press Club: Raise more money through a simplified tax code and spend less on Social Security, Medicare and Medicaid, the primary drivers of future borrowing. "Everyone knows in their hearts and their minds what has to be done," said Democratic former Pennsylvania Gov. Ed Rendell, who is chairing the group with former New Hampshire Sen. Judd Gregg, a Republican. The goal of the campaign is to "create a safe environment where it's not only good policy, but good politics as well." The campaign was founded by former Clinton White House Chief of Staff Erskine Bowles and former Republican Sen. Alan Simpson of Wyoming. The two men led an independent fiscal commission that in 2010 produced a $4 trillion debt-reduction framework that has won praise from politicians across the political spectrum. But the Bowles-Simpson plan never won the explicit backing of President Barack Obama or GOP leaders and therefore never gained real traction in Congress. The campaign plans to launch a social media drive to persuade lawmakers to approve a plan similar to the Bowles-Simpson framework by July 4, 2013 — replacing $600 billion in abrupt tax hikes and sharp spending cuts that are otherwise set to take effect in January.

#### B. New infrastructure spending kills fiscal discipline – it undercuts the spirit of “shared sacrifice”

O’Hanlon 10

Michael O’Hanlon, senior fellow at the Brookings Institution, 12/22/10, “THE DEFENSE BUDGET AND AMERICAN POWER,” http://www.brookings.edu/~/media/Files/events/2010/1222\_defense\_budget/20101222\_defense\_budget.pdf

So the minute that someone says, well, defense is the top constitutional obligation of the federal government and therefore it should be protected regardless, and we should make our deficit reduction out of other accounts. If we start a conversation in those terms, then a big constituency is going to come up and say let's protect Social Security, or let's protect college loans for students because that's our future after all. Or let's protect science research or **infrastructural development**, and you get the idea pretty soon you've lost the spirit of shared sacrifice that I think is essential if we're going to have any hope of reducing the deficit in the coming years. So that's the basic motivation. We're not probably going to reduce the deficit effectively, and therefore strengthen our long-term economy and the foundation for our long-term military power, if we don't establish a spirit of shared sacrifice.

#### C. Loss of fiscal discipline causes a downgrade

Mark Gongloff, Wall Street Journal, 08/2/’11, [Moody’s Affirms US AAA Rating, <http://blogs.wsj.com/marketbeat/2011/08/02/moodys-affirms-us-aaa-rating/>] VN

Moody’s just came out and said, great job, USA, you get to keep your AAA rating. For now. This follows Fitch, which earlier said more or less that they were still reviewing the US rating, a process that could take through August. They didn’t promise they’d keep a AAA rating at the end of the process, but called the debt deal “a step in the right direction.” Now the big shoe dangling is S&P, which is really on the hook, having sounded the loudest warning about a downgrade. The size of the debt deal doesn’t seem to hit the $4 trillion mark S&P has said would be necessary to keep a AAA rating. My prediction? They’ll issue a similar placeholder statement soonish. Meanwhile, let’s hear what Moody’s has to say: Moody’s Investors Service has confirmed the Aaa government bond rating of the United States following the raising of the statutory debt limit on August 2. The rating outlook is now negative. Moody’s placed the rating on review for possible downgrade on July 13 due to the small but rising probability of a default on the government’s debt obligations because of a failure to increase the debt limit. The initial increase of the debt limit by $900 billion and the commitment to raise it by a further $1.2-1.5 trillion by yearend have virtually eliminated the risk of such a default, prompting the confirmation of the rating at Aaa. In confirming the Aaa rating, Moody’s also recognized that today’s agreement is a first step toward achieving the long-term fiscal consolidation needed to maintain the US government debt metrics within Aaa parameters over the long run. The legislation calls for $917 billion in specific spending cuts over the next decade and established a congressional committee charged with making recommendations for achieving a further $1.5 trillion in deficit reduction over the same time period. In the absence of the committee reaching an agreement, automatic spending cuts of $1.2 trillion would become effective. In assigning a negative outlook to the rating, **Moody’s indicated, however, that there would be a risk of downgrade if** (1) **there is a weakening in fiscal discipline in the coming year**; (2) further fiscal consolidation measures are not adopted in 2013; (3) the economic outlook deteriorates significantly; or (4) there is an appreciable rise in the US government’s funding costs over and above what is currently expected.

1NC Downgrade Shell

#### D. Further downgrades would create a debt spiral, crippling the economy

Rowley 12 Charles Rowley, Professor Emeritus of Economics at George Mason University, 6/15/12, “Renewed threats to U.S. credit rating,” Charles Rowley’s blog, http://charlesrowley.wordpress.com/2012/06/15/renewed-threats-to-u-s-credit-rating/

If Moody’s downgrades and if S & P further downgrades U.S. credit ratings, this would move the United States out of the exclusive club of AAA-rated nations, and throw into question the privileged status of U.S. Treasury securities as a safe haven for global investors. Any significant flight from Treasuries would raise Treasury bond rates, with crippling consequences for the economy. A 1-percentage point increase in rates would raise Treasury debt payments by $1 trillion over the next decade, wiping out the benefits of all the budget cuts enacted by Congress last year. The dynamics of such a process may prove to be devastating, moving the U.S. federal government onto a path of sovereign downgrades that accelerates an already worsening fiscal situation. Greece here we come.

E. Economic collapse causes global nuclear war.

Merlini, Senior Fellow – Brookings, 11

[Cesare Merlini, nonresident senior fellow at the Center on the United States and Europe and chairman of the Board of Trustees of the Italian Institute for International Affairs (IAI) in Rome. He served as IAI president from 1979 to 2001. Until 2009, he also occupied the position of executive vice chairman of the Council for the United States and Italy, which he co-founded in 1983. His areas of expertise include transatlantic relations, European integration and nuclear non-proliferation, with particular focus on nuclear science and technology. A Post-Secular World? DOI: 10.1080/00396338.2011.571015 Article Requests: Order Reprints : Request Permissions Published in: journal Survival, Volume 53, Issue 2 April 2011 , pages 117 - 130 Publication Frequency: 6 issues per year Download PDF Download PDF (~357 KB) View Related Articles To cite this Article: Merlini, Cesare 'A Post-Secular World?', Survival, 53:2, 117 – 130]

Two neatly opposed scenarios for the future of the world order illustrate the range of possibilities, albeit at the risk of oversimplification. The first scenario entails the premature crumbling of the post-Westphalian system. One or more of the acute tensions apparent today evolves into an open and traditional conflict between states, perhaps even involving the use of nuclear weapons. The crisis might be triggered by a collapse of the global economic and financial system, the vulnerability of which we have just experienced, and the prospect of a second Great Depression, with consequences for peace and democracy similar to those of the first. Whatever the trigger, the unlimited exercise of national sovereignty, exclusive self-interest and rejection of outside interference would likely be amplified, emptying, perhaps entirely, the half-full glass of multilateralism, including the UN and the European Union. Many of the more likely conflicts, such as between Israel and Iran or India and Pakistan, have potential religious dimensions. Short of war, tensions such as those related to immigration might become unbearable. Familiar issues of creed and identity could be exacerbated. One way or another, the secular rational approach would be sidestepped by a return to theocratic absolutes, competing or converging with secular absolutes such as unbridled nationalism.

## \*\*\*Uniqueness\*\*\*

### 2NC Uniqueness

Congress is willing to compromise in a bipartisan way to reduce the deficit - that's Washington Post 7/18

#### Fiscal discipline and consumer confidence now

Mike Dorning, John Detrixhe and Ian Katz, Bloomberg Press, 07/16/’12, [Downgrade Anniversary Shows Investors Gained Buying U.S., <http://www.bloomberg.com/news/2012-07-16/downgrade-anniversary-shows-investors-gained-buying-u-s-.html>] VN

Warren Buffett, the billionaire investor renowned for his focus on company fundamentals, turned out to be prescient in shrugging off the downgrade: “In Omaha, the U.S. is still triple-A,” Buffett said amid the uproar. “In fact, if there were a quadruple-A rating, I’d give the U.S. that.” Photo: Andrew Harrer/Bloomberg Republican presidential candidate Mitt Romney described it as a “meltdown” reminiscent of the economic crises of Jimmy Carter’s presidency. He warned of higher long-term interest rates and damage to foreign investors’ confidence in the U.S. U.S. House Budget Committee Chairman Paul Ryan said the government’s loss of its AAA rating would raise the cost of mortgages and car loans. Mohamed El-Erian, chief executive officer of Pacific Investment Management Co., said over time the standing of the dollar and U.S. financial markets would erode and credit costs rise “for virtually all American borrowers.” They were wrong. Almost a year later, mortgage rates have dropped to record lows, the government’s borrowing costs have eased, the dollar and the benchmark S&P stock index are up, and global investors’ enthusiasm for Treasury debt has strengthened. **“The U.S. Treasury is still the widest, deepest and most actively traded in the world,”** said Jeffrey Caughron, a partner at Baker Group LP in Oklahoma City, which advises community banks on investments of more than $40 billion. “That becomes all the more important when you have signs of weakening global economic growth and continued problems in Europe.” Even in a slow recovery, the U.S. has unparalleled assets in the global market, including the size and resilience of its economy and the dollar’s standing as the world’s reserve currency. Low Treasury yields show that most investors think the U.S. government will meet its obligations, no matter how dysfunctional the political climate becomes in Washington.

#### Fiscal discipline now

CRFB, Committee for a Responsible Federal Budget, 05/25/’12, [GOOD NEWS ON THE FISCAL CLIFF?, <http://crfb.org/blogs/good-news-fiscal-cliff>] VN

Each day the Fiscal Cliff gets closer and closer, adding more uncertainty to our economic situation. But, as Deutsche Borse Group reports today, there is some cause for hope. With the Congressional Budget Office (CBO) having released a report giving lawmakers an estimate as to what would happen if the all the policies scheduled to happen at year end would occur, there is news that there has been ongoing discussions and negotiations behind the scenes to get the job done - and better yet, to do so by enacting a full, comprehensive fiscal plan. To recap, the fiscal cliff is the expiration of a slew of policies, and the sequestration being activated, with the added bonus of needing to raise the debt ceiling. These policies combined, according to CBO would put the US economy into a double-dip recession for the first half of next year by having growth equal to negative 1.3 percent, but over the full year, would equal a still lackluster 0.5 percent. As we have explained previously, and as CRFB president Maya MacGuineas recently explained, "Instead of going over the fiscal cliff or allowing an ever growing mountain of debt, we should rise to the challenge and enact a comprehensive plan with more targeted and thoughtfully crafted measures."

#### Discipline now

MNI, Dutch Borse Group (Finance), 05/25/’12, [US BudgetWatch: Hill Braces For End-of-Yr Fiscal Cliff Battle, <https://mninews.deutsche-boerse.com/index.php/us-budgetwatch-hill-braces-end-yr-fiscal-cliff-battle?q=content/us-budgetwatch-hill-braces-end-yr-fiscal-cliff-battle>] VN

"Things are pretty quiet on the surface up here (in Congress), but beneath the surface there is a lot of careful, detailed and intense working occurring on a deficit reduction package, involving people from both parties," Conrad said. Conrad said meetings to assemble, draft, and score a major deficit reduction package are underway, adding that he would like to move forward with the package "as soon as possible. But he added that it's not very likely that such a package could move in Congress before the election. "I think we all know the kind of plan we need to pass and pass very soon. But I can't tell you that there is sufficient support up here to pass it now. The mood must change. But things do change. Events happen. The situation in Europe worsens. We want to be ready if there is an opportunity," Conrad said. Conrad said he is working with lawmakers both within the Senate Budget Committee and in informal groups such as the "Gang of Six" to develop a deficit reduction package. "This is incredibly detailed, difficult work. It takes months and months of careful preparation to be ready with a plan. Some of us are determined to be ready pretty soon with a plan. We hope the political moment comes that allows us to move the package," he said. .

Fiscal Discipline High

#### Congress will make a budget deal to avoid the fiscal cliff now

Leon Panetta, Secretary of Defense, 06/02/’12, [Department of Defense Transcript:, <http://www.iiss.org/conferences/the-shangri-la-dialogue/shangri-la-dialogue-2012/speeches/first-plenary-session/qa/>] VN

It’s been set because of the failure of the Super Committee sequester is now supposed to take effect in January. Both Republicans and Democrats recognize that that would be a disaster. Sequester would impose another $500 billion in defense cuts if it we were to go into effect. I know of no Republican, no Democrat who believes that should happen. Having said that, obviously, they have the responsibility then to take action now to de-trigger sequester from taking effect. I believe that they will work to do that. I really do, because I think there isn’t anyone that wants that to happen, so I’m confident that ultimately Republicans and Democrats will find a way to de-trigger that artificial crisis that they put in place. The third point is with regards to the confidence level I have that ultimately Republicans and Democrats will deal with the larger issues that we confront in our economy, particularly with regards to the deficit. In my history in the Congress, I participated in every budget – major budget summit beginning with Reagan, President Reagan, continuing with President Bush. As OMB director for President Clinton developed the budget, the deficit reduction plan that President Clinton put in place. In every one of those – every one of those – it was important for Republicans and Democrats to put everything on the table and to look at every area of spending, not just defense, not just domestic spending, but at entitlements and at revenues. And it was because we put all of those elements together in those packages that we ultimately were able to balance the budget. I know the politics of this is difficult both for Republicans and Democrats, but I ultimately believe that because it is so important to our country and to our economy that ultimately they will find the courage that is required here to be able to develop that kind of approach to deficit reduction.

#### No sequester – budget proposal

Mieke Eoyang & Matt Bennett (Director of Third Way’s National Security Program, Vice President of Public Affairs and Co-Founder of Third Way, Politico, 7/12, Sequester hovers like a guillotine) <http://www.politico.com/news/stories/0712/78406.html>

The president proposed a budget in February that, taken as a whole, would result in enough savings to avoid sequestration. He has now instructed the DOD not to bother planning for sequestration cuts — noting that they would be damaging and expecting that Congress will reach a real budget deal.

#### Bipartisan cuts coming

John Shaw (senior reporter for Market News International since 1991 and a vice president since 1998, MNI, 7/12, MNI Washington Bureau <https://mninews.deutsche-boerse.com/index.php/us-hoyerdems-fiscal-cliff-plan-would-boost-jobs-cut-deficit?q=content/us-hoyerdems-fiscal-cliff-plan-would-boost-jobs-cut-deficit>)

WASHINGTON (MNI) - House Minority Whip Steny Hoyer said Tuesday the Democratic plan to avert the coming fiscal cliff by passing a "big, bold, and bipartisan" deficit reduction plan would help boost growth and cut budget deficits. At a briefing, Hoyer said a deficit reduction plan along the lines of the Simpson-Bowles package should be enacted as a replacement to the fiscal cliff. Hoyer praised President Obama's plan to extend Bush era tax cuts only for those families making $250,000 or less. "The President's formulation is correct," Hoyer said. He said failing to pass this package of tax cuts would be "inimical to the economy and a depressant to the growth of the economy." But he added that "the Clinton tax rates got it about right." Hoyer said the coming across-the-board spending cuts, called sequestration, should not be dropped without a replacement deficit reduction package. He hammered Republicans for insisting on attaching conditions to the debt ceiling agreement last year--and now trying to flee from the spending cuts that have been triggered by this process. "They imposed a fiscal discipline but don't want to live with the fiscal discipline. They want to have it both ways," Hoyer said. Hoyer called for a clean congressional vote to pass a debt ceiling increase in the "very near term," but he did not have a recommendation for how much the debt ceiling increase should be. Treasury Secretary Tim Geithner has said that certain cash management moves could delay the need for a debt ceiling increase until next year.

#### Fiscal discipline now – military cuts

Mackenzie Eaglen, The Hill, 06/26/12, [Deal to stop sequestration will have more defense budget cuts and new tax increases, <http://thehill.com/blogs/congress-blog/economy-a-budget/234939-deal-to-stop-sequestration-will-have-more-defense-budget-cuts-and-new-tax-increases->] VN

As with taxes, Democrats will be pushing on an open door when it comes to pressuring Republicans to give in to additional defense cuts. Already in the Senate, nearly a dozen Republicans have implicitly signed up for as much as $886 billion in defense cuts through their support of the Simpson-Bowles and Gang of Six plans. When it comes time for Congress and the president to strike a final deal this winter, the common expectation will be for defense to “pay its fair share.” Despite contributing more to deficit reduction than any other federal agency, the military will be called on again for further cuts — and Republicans, for the most part, will not take issue.

Fiscal Discipline High

#### Fiscal Discipline Now

Emily Koff(Research Associate, The Heritage Foundation, 6/12, Congress Must Address Both Defense Sequestration and Deficit) <http://blog.heritage.org/2012/06/28/congress-must-address-both-defense-sequestration-and-deficits/>

While Congress works to shift automatic spending cuts away from defense, it should also enact spending reduction measures that reduce short- and long-term deficits and debt. While the White House is right to encourage this, its idea of deficit reduction solutions can be boiled down to two flawed policies: tax hikes and stimulus spending. Americans—and the economy—cannot afford tax hikes, and more stimulus spending would be a prescription for continued deficits and further indebtedness. Excessive spending is what got us into this mess, and spending should be the target for getting out of it. The House has already passed reconciliation legislation that addresses the automatic spending cuts. It would impose a cap on fiscal year 2013 discretionary spending that is in line with the House budget resolution. It also would enact entitlement program reforms, yielding savings to replace the automatic cuts. The bill is not perfect: It avoids the sequestration for only one year, and its savings on entitlement programs are a minuscule 1 percent of total entitlement spending over the next decade. It does, however, mark an important accomplishment by the House: to set spending priorities and enact reforms—essentially, to budget. Getting spending under control requires this exact budget discipline. Congress has a horrible penchant for waiting until the last minute to pass urgent legislation. America’s military and the defense industry cannot afford for it to continue this habit, and the longer Congress delays, the more damage it will do.

### AT: Infrastructure Spending Now

#### Governments are belt-tightening on infrastructure now

UBS, October 2009, “Outlook for Global Infrastructure”, <http://www.static-ubs.com/global/en/asset_management/infrastructure/additional_materials/_jcr_content/par/linklist/link_1.738664510.file/bGluay9wYXRoPS9jb250ZW50L2RhbS91YnMvZ2xvYmFsL2Fzc2V0X21hbmFnZW1lbnQvaW5mcmFzdHJ1Y3R1cmUvT3V0bG9vayBmb3IgZ2xvYmFsIGluZnJhc3RydWN0dXJlLnBkZg==/Outlook%2520for%2520global%2520infrastructure.pdf>

A key challenge for global infrastructure is financing. Recession, the high cost of financial sector bailouts, and the cost of under-funded pensions and healthcare plans suggest that governments will be hard-pressed to maintain elevated levels of public investment. Moreover, prevailing high market risk premiums mean that, for now anyway, private debt or equity financing of large-scale projects remains costly. Historically, nearly two-thirds of all public infrastructure spending is financed out of general government revenues. The challenge, however, is that advanced economies have experienced a sharp deterioration in their fiscal positions as a result of recession, financial bailouts, and discretionary fiscal stimulus. In the US, the budget deficit will approach 13.5% of GDP this year. The UK deficit will be nearly as large, while deficits in Japan and the Euro area are also rising. Fiscal austerity on the horizon As a result, tough decisions on taxation and spending cuts loom. In the UK marginal rates of taxation on personal income are slated to rise ten percentage points for top earners in April 2010. In Germany, legislation mandating a balanced budget by the middle of the next decade has become law. Fiscal positions are also handicapped in the longer run by a rapid increase in government debt. According to IMF estimates, US general government debt will reach 97% of GDP by 2010, up from 70.5% last year. The picture is worrisome in Europe and especially in Japan, where public sector debt is slated to exceed 200% of GDP this year, according to the IMF. Long-term competing needs These figures, moreover, exclude the cost of under-funded public pensions and healthcare commitments, which are expected to grow at rapid rates as dependency ratios rise due to rapidly ageing populations, particularly in Europe and Japan.

### 2NC Economy High

#### The Economy is making a slow but steady recovery. The creation of jobs prove

Fox 7/18/12 (“US economy adds 80,000 jobs in another weak month” http://www.foxnews.com/us/2012/07/06/us-employers-add-80000-jobs-as-economy-struggles/ )

WASHINGTON – The American job machine has jammed. Again. The economy added only 80,000 jobs in June, the government said Friday, erasing any doubt that the United States is in a summer slump for the third year in a row. "Let's just agree: This number stinks," said Dan Greenhaus, chief global strategist at the investment firm BTIG. It was the third consecutive month of weak job growth. From April through June, the economy produced an average of just 75,000 jobs a month, the weakest three months since August through October 2010. The unemployment rate stayed at 8.2 percent — a recession-level figure, even though the Great Recession has technically been over for three years. The numbers could hurt President Barack Obama's odds for re-election. Mitt Romney, the presumed Republican nominee, said they showed that Obama, in three and a half years on the job, had not "gotten America working again." "And the president is going to have to stand up and take responsibility for it," Romney said in Wolfeboro, N.H. "This kick in the gut has got to end." Obama, on a two-day bus tour through the contested states of Ohio and Pennsylvania, focused on private companies, which added 84,000 jobs in June, and took a longer view of the economic recovery. "Businesses have created 4.4 million new jobs over the past 28 months, including 500,000 new manufacturing jobs," the president said. "That's a step in the right direction." The Labor Department's report on job creation and unemployment is the most closely watched monthly indicator of the U.S. economy. There are four reports remaining before Election Day, including one on Friday, Nov. 2, four days before Americans vote. No president since World War II has faced re-election with unemployment over 8 percent. It was 7.8 percent when Gerald Ford lost to Jimmy Carter in 1976. Ronald Reagan faced 7.2 percent unemployment in 1984 and trounced Walter Mondale. Patrick Sims, director of research at the consulting firm Hamilton Place Strategies, said that "time has run out" for unemployment to fall below 8 percent by Election Day. That would require an average of about 220,000 jobs a month from July through October — more like the economy's performance from January through March, when it averaged 226,000 per month. Few economic analysts expect anything close to that. "The labor market is treading water," said Heidi Shierholz, an economist at the Economic Policy Institute. She called it an "ongoing, severe crisis for the American work force." The Labor Department report put investors in a sour mood. The Dow Jones industrial average dropped 124 points. Industrial and materials companies, which depend on economic growth, were among the stocks that fell the most. The price of oil fell $2.77 per barrel to $84.45. Money flowed instead into U.S. Treasurys, which investors perceive as safer than stocks when the economy is weakening. The yield on the benchmark 10-year U.S. Treasury note fell to 1.54 percent, from 1.59 percent on Thursday. Investors were already worried about a debt crisis that has gripped Europe for almost three years and recent signals that the powerhouse economy of China is slowing. Earlier this week, the European Central Bank and the central bank of China cut interest rates in hopes of encouraging people and businesses to borrow and spend money. For American investors, however, the jobs report fell into an uncomfortable middle ground. Federal Reserve Chairman Ben Bernanke promised last month that the Federal Reserve would take additional steps to help the economy "if we're not seeing a sustained improvement in the labor market." But some financial analysts said that the Labor Department report, while disappointing, was not weak enough to lock in further action by the Fed at its next meeting July 31 and Aug. 1. The slowdown in job growth has been stark. From December through February, the economy produced an average of 252,000 jobs a month, twice what is needed to keep up with population growth. But the jobs generator started sputtering in March, when job growth slowed to 143,000. At first, economists blamed the weather for warping the numbers. An unusually warm winter allowed construction companies and other employers to hire earlier in the year than usual, effectively stealing jobs from the spring, they said. But weird weather could only explain so much, and the bad news kept coming: The economy added just 68,000 jobs in April and 77,000 in May. Those figures reflect revisions from earlier estimates of 77,000 for April and 69,000 for May. June's dud of a number made it clear that the economy has fallen into the same pattern it followed in 2010 and 2011: It gets off to a relatively fast start, then fades at midyear. Offering some hope, the slowdowns the two previous years lasted just four months each. From June through September 2010, the economy lost an average of 75,000 jobs per month. From May through August 2011, the economy added an average of 80,000 per month. Both years, hiring picked up significantly when the weak stretches ended. To be sure, the United States is still suffering the hangover of a financial crisis and the worst recession since the 1930s. The economy lost 8.8 million jobs during and after the recession. It has regained 3.8 million. The economy isn't growing fast enough to create jobs at a healthy clip. That is primarily because three traditional pistons of the economic engine aren't firing the way they normally do: — Consumer spending since the recession has been weaker than in any other post-World War II recovery, partly because wage increases have been small. In such a weak job market, employers don't need to give big raises. And households are trying to pay off the debt they ran up in the mid-2000s. — Housing has been a dead weight on the economy for six years. Home-building usually powers economic recoveries, but construction spending is barely half what economists consider healthy. — Government, which usually picks up the slack in the job market when the economy is weak, isn't helping this time. Counting federal, state and local jobs, governments have cut 637,000 jobs since 2008. They have cut 49,000 the last three months. In the first three months of this year, it appeared state and local government job losses were coming to an end. "That turned out to be a temporary halt," said Stuart Hoffman, chief economist at PNC Financial. "Apparently, there's no end in sight." The figure of 80,000 jobs came from a Labor Department survey of businesses and government agencies. Another survey, of American households, looks better. It shows the number of employed Americans rose by 381,000 the past three months — 127,000 a month. The household survey can catch the self-employed and those working for very small businesses, who can be missed by the bigger business survey. But over time the two surveys usually tell the same story. The unemployment rate last month was unchanged from May. But a broader measure of weakness in the labor market, the so-called underemployment rate, deteriorated for the second straight month. In June, 14.9 percent of Americans either were unemployed, had been forced to settle for part-time employment, or had given up looking for work and were not counted as unemployed. The rate was 14.8 percent in May and 14.5 percent in April.

#### Recent reports and data show the US economy is actually growing

Adler (Editor and Publisher of the Wall Street Examiner) 7/18/12 (Lee “One Crucial Indicator Shows The US Economy Isn't Slowing At All” <http://www.businessinsider.com/federal-tax-revenues-economy-not-slowing-2012-7> )

The mainstream consensus has lately been that the economy is slowing. Based on my tracking of federal revenues in real time, I suspect that that view is incorrect. Instead the recent data reflects only normal oscillations within the ongoing slow growth trend. Total federal tax collections, including withholding taxes, are available to us with just a one day lag in the US Treasury’s Daily Treasury Statements, which makes them an excellent analytical resource. Withholding is mostly for compensation, and thus it is a good measure of the economy’s strength. However, it is extremely volatile day to day so I rely more on a monthly moving average of the 10 day total collections, comparing that with the prior year. Smoothing sacrifices a bit of timeliness to get a clearer picture of the trend without losing too much of the edge that the daily data provides. Unfortunately, I have found even the 10 day total data too noisy for meaningful comparison so I’ve had to resort to additional smoothing. As a result the smoothed data is a little slow, so I also look at raw month to date data after mid month. As of July 11, the 4 week average of the 10 day total of withholding taxes is now up 4.0% in nominal and 1.8% in real terms versus the same period in 2011 (adjusted by the monthly BLS data on average weekly employee compensation which in June rose by 2.2% year to year). This indicator has been in the +1% to +3% range since mid May, with most of that time above +2% suggesting that the economy’s current rate of growth is 2-3%, not the 1-1.6% that most Wall Street economists are now forecasting.Last week was the benchmark week for the BLS labor market data. At a growth rate of 1.8% versus last year, non farm payrolls, not seasonally adjusted (NSA)–in other words, actual–would grow from last year’s July level of 131.038 million to approximately 133.4 million. Such a straightforward analysis doesn’t always match the seasonally adjusted headline number because seasonal adjustment factors have a significant variance for the same period in each year. The resulting seasonally adjusted number is therefore somewhat arbitrary, and anything but real. Unfortunately, the markets don’t really care about that when the data is initially released. Traders and algos only care whether the number beat or fell short of equally arbitrary consensus estimates, which in turn depend almost entirely on the seasonal adjustment variance. If the withholding tax growth rate is applied to the SA payrolls data for July 2011, (1.0183 x 131.407 million) the SA number for July would be 133.812 million. That would be an increase of over 720,000 from the current June figure. Wouldn’t that be an August surprise (when released? But we know that’s not going to happen. The growth rate of withholding and the growth rate of jobs will remain at odds. But unless economists are forecasting very strong gains, the July number would beat if it tracks near the withholding data (More employment charts). The full figures for the month are available a day after the end of the month. Here’s what they looked like at the end of June along with my observations at the time. 7/6/12 As of June 29, the last business day of the month, month to date withholding tax receipts for the full month were up by 0.9% over the same period last year but that is misleading because there was one more calendar day in which taxes could be reported last year, as well as one more business day in which more people would have been at work. Looking at collections on a per diem basis, they were up 4.4% this June versus June 2011. On a per workday basis, the gain was 5.7%. This further supports the thesis that the seasonally adjusted jobs data for June was grossly misleading. 6/9/12 As of May 31, month to date withholding tax receipts for the full month were up by 2.1% versus the same period last year, on a nominal basis, not adjusted for inflation. May 31 month to date outlays were up by $24.2 billion pushed up somewhat after a calendar anomaly pushed expenses usually incurred in April into May, contributing to the bogus budget surplus in April. Conversely, the May deficit increase may also be an illusion. 7/6/12 Month to date outlays for the full month as of June 29 were up by $9.7 billion, absorbing nearly all of the revenue gain. The Administration will continue to spend as much as possible to boost its chances of getting rehired. June 15 was quarterly corporate tax collection day. Corporate taxes for the month were 16% ahead of last June’s collections. Some of this is due to improved business conditions, but if corporations are achieving this by cutting labor costs, that would be counterproductive over the long haul. The withholding tax data and raw unadjusted jobs data suggests that businesses were hiring. Excise taxes are due for the quarter at the end of June. This year they were up 5.9% over 2011. The Treasury releases its final monthly budget figures on the 8th business day after the close of the month, so this too is timely data offering a fascinating glimpse into the economy. The Treasury’s monthly statement for June showed a net revenue increase in nominal terms of 4.2% year over year. These are net revenues after refunds. Refunds for June are mostly tied to the prior year. Gross collections are more representative of the current period. Here are the comparisons by category on a net and gross basis. Wage withholding was down 5.5% in June versus June 2011, falsely suggesting a weakening economy. That was completely due to the last business day of the month falling on June 29. Semi weekly and twice monthly withholding for the end of June would be delayed into July. In fact, $23.3 billion in withholding taxes were remitted on July 2. That’s one third of all the withholding taxes previously collected in June. Conversely, July will look like a blockbuster month because of that. We’ll have to keep that in mind when reviewing next month’s statement Social security taxes were up 3.7%, which is really impressive considering the calendar effect. June is a quarterly estimated tax collection month. Self employment tax collections were up 3.2%. Those were due on June 15, so there are no calendar issues involved. That’s a decent indication of the strength of the economy in the second quarter, but it implies nothing about July. Considering inflation, it suggests real growth of around 1-1.5%. The Fed earned and paid the Treasury less than last year as interest rates plunged. The Fed does not mark to market. The surplus it returns to the Treasury is a result of interest income and sales. It made money in May when it closed sales of some of its Maiden Lane holdings. Year to year, revenues had been uptrending slightly suggesting modest economic growth. Meanwhile the deficit, which had been narrowing, grew materially wider in June. It had also widened in May. While revenues are climbing, the Obama administration has spent all of that and then some. It is, after all, election season, time to buy votes with strategic, economy boosting, government spending. This report is an excerpt from the weekly Treasury market update in the Wall Street Examiner Professional Edition. The Report also includes a review, analysis, and forecast of the past week’s and next week’s Treasury auctions, expected supply impacts on the market, analysis of demand via updated charts and discussion of Primary Dealer, foreign central bank, and US commercial bank buying trends, as well us US bond mutual fund flows. Also included are technical analysis of the Treasury bond market, and US dollar.

## \*\*\*Links\*\*\*

### 2NC Generic Link

#### Infrastructural development undercuts the spirit of shared sacrifice - crushing hopes of reducing the deficit - O'hanlon 10

#### Infrastructure is costly and inefficient

The Economist, 2/12/2012, “America’s Subterranean Malaise”, <http://www.economist.com/blogs/gulliver/2012/02/infrastructure?fsrc=scn%2Ftw%2Fte%2Fbl%2Famericanssubterraneanmalaise>

SALON‘s Will Doig had a nice piece last week riffing off a common theme: why does it take so long and cost so much for America to complete infrastructure projects when China seems to complete them in mere months for a fraction of the cost? On Dec. 31, the Chinese capital opened a new subway line and greatly expanded two others. This year it plans to open four more. A total of eight new lines are under construction. The city started expanding the system in the run-up to the 2008 Olympics, and has kept pushing forward ever since. In 2001 it had 33 miles of track. Today it has 231.Meanwhile, when you hear the completion dates for big U.S. transit projects you often have to calculate your age to figure out if you’ll still be alive. Los Angeles’s Westside subway extension is set to be finished in 2036. Just five years ago, New York’s Second Avenue Subway was supposed to be done by 2020, a goal that seems laughable now. The sub-headline of Mr Doig’s story promises suggestions for dealing with this problem, but the actual article focuses more on explaining why infrastructure projects take so much longer in America than they do in China. Bureaucracy, lack of money, politics and potential interference with existing infrastructure are the most convincing explanations he offers, although mismanagement and America’s deeper concern for things like private property rights and working conditions surely play a role, too. The Atlantic’s David Lepeska has some related thoughts on why New York’s Second Avenue subway line, which won’t be completed for years, is costing $1.7 billion per kilometre. He notes that such high-priced transport is not endemic in America: Washington, DC’s Silver Line is considerably cheaper per kilometre (partly because much of it is being built above ground) and light-rail projects in Minneapolis and Denver were comparative bargains. Slate’s Matt Yglesias, meanwhile, argues that Mr Doig and others who compare New York’s subway costs with China’s are missing the point. “The real issue Americans should be pondering is why our big infrastructure projects are so much slower and more costly than comparable projects in Europe or Japan,” he writes. After all, “even expensive projects in big, old, rich cities like London and Amsterdam come in far cheaper than a New York subway project.” This is indeed the right question to be asking, but the answers don’t come easily. American politicians often blame labour unions, but these are generally stronger in Europe than in the US. Benjamin Kabak, a blogger whom Mr Lepeska recommends, offers some theories. Alon Levy, a blogger whom we’ve linked to before, has a particularly interesting idea: he thinks the business culture and organisational structure of New York’s Metropolitan Transit Authority could be part of the problem. Mr Levy says the MTA’s in-house team managing infrastructure projects is probably too small and the agency could be too reliant on outside consultants.

Link – Generic

#### Transportation infrastructure causes fiscal crises

William Coyne is a Land Use Advocate for the Environment Colorado Research and Policy Center, December 2003, “The Fiscal Cost of Sprawl”, <http://www.impactfees.com/publications%20pdf/fiscalcostofsprawl12_03.pdf>

THE high cost of providing and maintaining infrastructure for sprawling development hurts taxpayers and contributes to the fiscal crises facing many Colorado local governments. Sprawling development does not generate enough tax revenue to cover the costs it incurs on local municipalities to provide new infrastructure and public services. Local governments and their taxpayers end up footing the bill to provide public services to sprawling developments. Research by Colorado State University found that in Colorado, “dispersed rural residential development costs county governments and schools $1.65 in service expenditures for every dollar of tax revenue generated.” Additionally, the cost to provide public infrastructure and services for a specific population in new sprawling development is higher than to service that same population in a smart growth or infill development. Sprawling and “leapfrog” developments (those built far away from the current urban area) tend to be dispersed across the land, requiring longer public roads and water and sewer lines to provide service. Such developments also impose higher costs on police and fire departments and schools. Research from around Colorado demonstrates the high fiscal cost of sprawl relative to compact development: • Research conducted by the Denver Regional Council of Governments (DRCOG) in the planning process for the Metro Vision 2020 update found that sprawling development would cost Denver-area governments $4.3 billion more in infrastructure costs than compact smart growth through 2020. • DRCOG found that a 12-square-mile expansion of the Urban Growth Boundary around Denver to accommodate additional sprawling growth would cost taxpayers $293 million dollars, $30 million of which would be subsidized by the region as a whole. • University of Colorado at Denver researchers determined that future sprawling development in Delta, Mesa, Montrose, and Ouray Counties would cost taxpayers and local governments $80 million more than smart growth development between 2000 and 2025. • New research from the Center for Colorado Policy Studies at the University of Colorado at Colorado Springs points to infill development and increased residential densities as important factors contributing to the substantial savings in infrastructure costs in Colorado Springs between 1980 and 2000. • A Federal Transit Administration report conducted by the Transit Cooperative Research Program estimates that smart growth would save the Denver-Boulder-Greeley area $4 billion in road and highway construction over 25 years—a savings of 21 percent. The costs of building and servicing infrastructure for new sprawling development is ultimately subsidized by the whole community. Local government generally bills the cost of new services and infrastructure on an average basis, rather than an incremental basis. That is, new costs are spread evenly among all taxpayers rather than charged only to those who generate the costs. This is, in effect, a subsidy from the whole community to new development. Existing residents, who were sufficiently served by the established infrastructure, must pay a share of the costly new infrastructure required to meet the expected demand of newcomers.

#### Federal spending on transportation is wasteful and requires constant federally funded maintenance

Barry Bosworth is a Senior Fellow in Economic Studies for the Brookings Institution and Sveta Milusheva is a Research Assistant at the Brookings Institution, October 2011, “Innovations in U.S. Infrastructure Financing: An Evaluation”, <http://www.brookings.edu/~/media/research/files/papers/2011/10/20%20infrastructure%20financing%20bosworth%20milusheva/1020_infrastructure_financing_bosworth_milusheva.pdf>

Their data are limited to public sector investments in transportation and water infrastructure, and do not include estimates of the stock of capital. The share of total public capital investments covered by the CBO data has fallen from about 45 percent in 1960 to 30 percent in 2007. The most important forms of excluded public capital are equipment, buildings, and power; but the CBO definition is closer to the definition of infrastructure used in most research studies. The CBO analysis illustrates two important aspects of infrastructure expenditures. First O&M represents more than half of the total spending on infrastructure, and in some areas, such as mass transit and aviation, the proportion is two-thirds or greater. Infrastructure systems involve much greater costs than just the initial investment to build them. They involve major commitments to future operating and repair costs that need to be funded on an ongoing basis. The inclusion of O&M thus highlights a fundamental problem of infrastructure in the United States: the failure to maintain the investments on a timely and efficient basis. There is an underlying bias in the funding of infrastructure in that ‘free money’ (federal grants) is available for new capital investments, but state and local governments must finance the vast bulk of their own O&M costs. Not surprisingly, the result is excess investments in facilities that local governments are not prepared to maintain. In those cases where federal funding is available for maintenance, the amounts are limited and beset by perverse incentives. O&M has represented only 8 percent of total federal grants since 2000. There is a federal program for bridge repair, the Highway Bridge Program (HPB), but priority is given to states with the worst rating of bridge conditions–hardly an incentive for timely maintenance.

Link – Generic

#### Prefer our link evidence - needs assessments of infrastructure projects are skewed – causing huge cost overruns

Claudia Copeland is a Specialist in Resources and Environmental Policy, Linda Levine is a Specialist in Labor Economics, and William J. Mallett is a Specialist in Transportation Policy, 9/21/11, Congressional Research Service, <http://www.fas.org/sgp/crs/misc/R42018.pdf>

Traditionally, setting priorities for infrastructure spending is based on a combination of factors. Estimates of funding needs are one factor that is commonly used as a measure of the dimension of a problem and to support spending on some activities relative to others, as in: funding needs for X are much greater than for Y, therefore, society should spend more heavily on X. One widely cited estimate of the nation’s infrastructure needs is presented in the finding of the American Society of Civil Engineers (ASCE) that the condition of the nation’s infrastructure merits a letter grade of “D.” According to ASCE, five-year funding needs total $2.2 trillion, while the “gap” between estimated investment needs and estimated spending is $1.8 trillion. ASCE reported the condition of a dozen categories of infrastructure, including roads (“Poor road conditions cost U.S. motorists $67 billion a year in repairs and operating costs—$333 per motorist”), dams (“The gap between dams needing repair and those actually repaired is growing significantly”), wastewater (“Aging, underdesigned, or inadequately maintained systems discharge billions of gallons of untreated wastewater into U.S. surface waters each year”), and schools (“No comprehensive, authoritative nationwide data on the condition of America’s school buildings has been collected in a decade. The National Education Association’s best estimate to bring the nation’s schools into good repair is $322 billion.”). 46 However, assessing “need” is complicated by differences in purpose, criteria, and timing, among other issues. In the infrastructure context, funding needs estimates try to identify the level of investment that is required to meet a defined level of quality or service. Essentially, this depiction of need is an engineering concept. It differs from economists’ conception that the appropriate level of new infrastructure investment, or the optimal stock of public capital (infrastructure) for society, is determined by calculating the amount of infrastructure for which social marginal benefits just equal marginal costs. The last comprehensive national infrastructure needs assessment was conducted by the National Council on Public Works Improvement that was created by the Public Works Improvement Act of 1984 (P.L. 98-501). The Council reported in 1988 that government outlays for public works capital totaled about $45 billion in 1985 and that a commitment to improve the nation’s infrastructure “could require an increase of up to 100 percent in the amount of capital the nation invests each year.” 47 This estimate of future needs by the Council may have been imprecise because of the inherent difficulties of needs assessments, something its report discusses in detail. 48 It is worth highlighting a few of these key difficulties as a cautionary note when attempting to interpret infrastructure needs assessments. One of the major difficulties in any needs assessment is defining what constitutes a “need,” a relative concept that is likely to generate a good deal of disagreement. For this reason, some needs assessments are anchored to a benchmark, such as current provision in terms of physical condition and/or performance. This current level of provision may be judged to be too high by some and too low by others, but nonetheless it provides a basis for comparison as future spending needs can be estimated in terms of maintaining or improving the current condition and performance of the infrastructure system. Needs estimates in highway and public transit are calculated in this way by the U.S. Department of Transportation (DOT). The Environmental Protection Agency (EPA) similarly estimates total U.S. funding needs for wastewater treatment facilities. EPA defines a “need” as the unfunded capital costs of projects that address a water quality or water quality-related public health problem existing as of January 1, 2008, or expected to occur within the next 20 years. 49 In some cases, estimates are intended to identify needs for categories of projects that are eligible for assistance under various federal programs. By being defined in that manner, assessments based solely on funding eligibility may not take into consideration needs for non-eligible categories, such as replacement of aging infrastructure or projects to enhance security. Some federal agencies estimate the funding necessary to bring the current infrastructure system to a state of good repair. The resulting funding estimate is sometimes referred to as the infrastructure “backlog.” Again, among other problems, such as inventorying the current condition of infrastructure and calculating repair costs, the needs estimate is affected by judgments about what constitutes a state of good repair. It is worth noting, too, that needs assessment are often conducted by organizations with a vested interest in the outcome. This is most obviously a concern when a needs assessment is conducted by an advocacy group, but may also occur with government agencies. A second major difficulty with needs assessments is estimating future conditions, especially consumer demand for services that infrastructure provides. To begin with, estimating demand is difficult because it is based on a host of assumptions such as the rate of population and economic growth. Typically, the longer the time period over which conditions are forecast, the harder it is to accurately predict them. Particularly hard to predict, and, thus, the effect they have on infrastructure needs, are structural changes in the economy and technological change. In addition, however, consumer demand can vary enormously depending on how a service is financed and priced, as well as other public policy decisions including regulation and conservation. For example, highway infrastructure is primarily financed by fuels and other taxes that provide a vague signal or no signal at all about the total cost of driving, particularly the external costs such as the fuel and time wasted in congested conditions. Highway tolls, on the other hand, particularly those that fluctuate in line with congestion, provide a direct price signal for a trip on a certain facility at a certain time of the day. Pricing highway infrastructure in this way has been found to reduce travel demand, thereby affecting infrastructure need. 50 Consumer demand can sometimes be met without infrastructure spending. For example, water supply needs can be reduced by employing water conservation methods. Finally, it is worth mentioning that the need for public funding to supply infrastructure, including federal support, may often be an open question because the roles of the public and private sector can and do shift over time. Even within the public sector, the roles of federal, state, and local governments change and these shifting intergovernmental relationships may even affect the assessments of infrastructure needs.

Link – Generic

#### Transportation infrastructure spending is wasteful – lack of funds and dozens of supplemental costs

Wall Street Journal, April 2012, “Why Your Highway Has Potholes”, <http://online.wsj.com/article/SB10001424052702303815404577333631864470566.html?mod=WSJ_Opinion_LEADTop>

Nothing shows off the worst of Congress like a highway bill. And this year's scramble for cash is worse than ever because the 18.4 cent a gallon gasoline tax will raise $70 billion less than the $263 billion Congress wants to spend over the next five years. Let the mayhem ensue. The Senate has passed a two-year $109 billion bill sponsored by Barbara Boxer of California that bails out the highway trust fund with general revenues, including some $12 billion for such nonessentials as the National Endowment for the Oceans and the Land and Water Conservation Fund. The bill requires little or no reform. The prevailing Senate view is the more concrete that gets poured, the more jobs back home. So more "shovel-ready" nonstimulus. House Republicans oppose the Senate version amid a $1.3 trillion deficit and have their own bill to give states more flexibility—though still not enough—on how to spend transportation dollars. Congress had to pass a temporary 90-day extension of highway funding through June 30 because the two sides can't agree. What's missing is any new thinking. Clear evidence of inefficient transportation spending comes from a new Treasury study estimating that traffic gridlock costs motorists more than $100 billion a year in delays and wasted gas. In cities like Los Angeles, commuters waste the equivalent of two extra weeks every year in traffic jams. This congestion could be alleviated by building more highway lanes where they are most needed and using market-based pricing—such as tolls—for using roads during peak travel times. That makes too much sense for Washington. In a typical year only about 65 cents of every gas tax dollar is spent on roads and highways. The rest is intercepted by the public transit lobby and Congressional earmarkers. Then there are the union wages that pad the cost of all federal projects. The New York Times reported in 2010 that 8,074 Metropolitan Transportation Authority employees made $100,000 or more in 2009 even as the system loses money. Transit is the biggest drain. Only in New York, San Francisco and Washington, D.C. does public transit account for more than 5% of commuter trips. Even with a recent 2.3% gain in bus and rail use due to high gas prices, public transit still accounts for a mere 2% of all inner-city trips and closer to 1% outside of New York. Enlarge Image Getty Images Since 1982 government mass-transit subsidies have totaled $750 billion (in today's dollars), yet the share of travelers using transit has fallen by nearly one-third, according to Heritage Foundation transportation expert Wendell Cox. Federal data indicate that in 2010 in most major cities more people walked to work or telecommuted than used public transit. Brookings Institution economist Cliff Winston finds that "the cost of building rail systems is notorious for exceeding expectations, while ridership levels tend to be much lower than anticipated." He calculates that the only major U.S. rail system in which the benefits outweigh the government subsidies is San Francisco's BART, and no others are close to break-even. One reason roads are shortchanged is that liberals believe too many Americans drive cars. Transportation Secretary Ray LaHood has been pushing a strange "livability" agenda, which he defines as "being able to take your kids to school, go to work, see a doctor, drop by the grocery or post office, go out to dinner and a movie, and play with your kids in a park, all without having to get in your car." This is the mind of the central planner at work, imagining that Americans all want to live in his little utopia. The current scheme also creates giant inequities. Politically powerful cities get a big chunk of the money, while many Western and Southern states get less back than they pay in. But why should people in Akron, Ohio or Casper, Wyoming have to pay gas taxes to finance the New York subway or light rail in Denver? One reason there is so much overspending on inefficient urban transit is that federal matching dollars require residents in other states to foot up to half the bill. The best solution would be to return all the gas tax money to the states, roughly in proportion to the money each pays in. This would allow states and localities to determine which roads and transit projects they really need—and are willing to pay for. California could decide for itself if it wants more roads, whether it can afford high-speed rail, and whether it wants to use congestion-pricing on crowded roads. The House Transportation Committee has found that getting a permit for a new road costs twice as much, and takes three times as long, when federal money is included than when financed with private or local dollars. Less federal control would also allow states to lure billions of dollars of private financing for new roads, which experts like Mr. Winston believe is the next big thing in transportation financing but is now generally prohibited. One of the worst features of Ms. Boxer's Senate bill is that she would exacerbate the funding shortage by adding new penalties if states leverage private dollars to build new toll roads and bridges. The Senate's highway-fund bailout will only perpetuate the spending misallocation that has contributed to traffic nightmares. It will also run up the deficit. If Congress really wants to enhance the livability of cities and suburbs, it will pass a highway bill that builds more roads.

Link – Generic

#### Infrastructure is expensive and wasteful

Dr. Jean Paul Rodrigue works at the Department of Global Studies & Georgaphy at Hofstra University in New York, 1998,  
The Geography of Transport Systems, “The Financing of Transportation Infrastructure”, <http://people.hofstra.edu/geotrans/eng/ch7en/appl7en/ch7a2en.html>

Facing the growing inability of governments to manage and fund transport infrastructure, the last decades has seen deregulation and more active private participation. Many factors have placed pressures on public officials to consider the privatization of transport infrastructure, including terminals:

Fiscal problems. The level of government expenses in a variety of social welfare practices is a growing burden on public finances, leaving limited options but divesture. Current fiscal trends clearly underline that all levels of governments have limited if any margin and that accumulated deficits have led to unsustainable debt levels. The matter becomes how public entities default on their commitments. Since transport infrastructures are assets of substantial value, they are commonly a target for privatization. This is also known as “monetization” where a government seeks a large lump sum by selling or leasing an infrastructure for budgetary relief.

High operating costs. Mainly due to managerial and labor costs issues, the operating costs of public transport infrastructure, including maintenance, tend to be higher than their private counterparts. Private interests tend to have a better control of technical and financial risks, are able to meet construction and operational guidelines as well as providing a higher quality of services to users. If publicly owned, any operating deficits must be covered by public funds, namely through cross-subsidies. Otherwise, users would be paying a higher cost than a privately managed system. This does not provide much incentives for publicly operated transport systems to improve their operating costs as inefficiencies are essentially subsidized by public funds. High operating costs are thus a significant incentive to privatize.

Cross-subsidies. Several transport infrastructures are subsidized by revenues from other streams since their operating costs cannot be compensated by existing revenue. For instance, public transport systems are subsidized in part by revenues coming from fuel taxes or tolls. Privatization can thus be a strategy to end cross-subsidizing by taping private capital markets instead of relying on public debt. The subsidies can either be reallocated to fund other projects (or pay existing debt) or removed altogether, thus reducing taxation levels.

Equalization. Since public investments are often a political process facing pressures from different constituents to receive their “fair share”, many investments come with “strings attached” in terms of budget allocation. An infrastructure investment in one region must often be compensated with a comparable investment in another region or project, even if this investment may not be necessary. This tends to significantly increase the general cost of public infrastructure investments, particularly if equalization creates non-revenue generating projects. Thus, privatization removes the equalization process for capital allocation as private enterprises are less bound to such a forced and often wasteful redistribution.

### General Link Multipliers

#### Transportation project spending is uncontrollable – biased cost analyses, lack of information, and other structural impediments

General Accounting Office, February 2000, “Funding Trends and Opportunities to Improve Investment Decisions”, <http://www.gao.gov/assets/590/588838.pdf>

Federal agencies and the Congress face several challenges in determining the appropriate levels of and effective approaches to infrastructure investment. First, there is a general lack of accurate, consistent information on the existing infrastructure and its future needs. For example, in some cases, the current information may not distinguish between genuine needs and “wish lists.” In other cases, the information may not identify all the needs. In addition, federal agencies have not taken a consistent approach to analyzing the costs and benefits of potential infrastructure projects, which would help in setting priorities and determining noncapital alternatives. Moreover, until recently, agencies have not been required to relate their planned infrastructure spending to their missions and goals, so evaluating these plans has presented a challenge to agencies and the Congress. Finally, the federal budget structure does not prompt explicit debate about infrastructure spending that is intended to have long-term benefits. Overcoming these impediments will not be easy. Recent guidance by the Office of Management and Budget and legislation such as the Government Performance and Results Act may provide interim steps toward doing so. However, these steps might not go far enough toward improving infrastructure investments because spending decisions are made by a variety of agencies and levels of government that have differing goals and missions. In order to better coordinate these investments to meet national, regional, and local goals and ensure that they are mutually supportive, it is crucial that agencies throughout the government reduce inefficiencies in their current investments and analyze potential investments to identify those that achieve the greatest benefits in the most cost-effective manner.

General Link Multipliers

#### Lack of revenues and profligate spending practices supercharge the link

Emily Goff and Alison Acosta Fraser are Research Associate and Director of Economic Policy Studies at the Heritage Foundation, respectively, “Transportation Conference Bill: Some Good Reforms, but Too Much Spending”, 6/28/2012,

<http://www.heritage.org/research/reports/2012/06/transportation-conference-bill-some-good-reforms-but-too-much-spending#_ftn4>

The bill spends too much, and to pay for this overspending, it contains transfers from the general fund, which are themselves paid for through new revenue streams. Some of the policy changes that yield new revenues are unacceptable, but beyond that, new revenue should not be used for new spending. The bill also continues diverting HTF funds to costly and wasteful transit programs. Spending Is Too High. To fund transportation programs through 2014, the bill would spend $120 billion, or $60 billion per year. Though consistent with current spending levels, it is well above what the HTF will collect: According to the Congressional Budget Office, the trust fund will run out of money in 2013, meaning spending is clearly outpacing revenues.[3] Keeping spending within the limit of the trust fund puts pressure on lawmakers to return control of transportation programs and their funding to the states. Transfers from the general fund to pay for the bill would be offset mostly by pension and flood insurance changes. One pension-related reform would allow private businesses to invest less money in their employees’ defined-benefit pension plans. This is terrible policy that would harm the position of many under-funded plans. It also increases taxpayer risk of a pension bailout through the Pension Benefit Guaranty Corporation (PBGC).[4] The other increases the premiums that an employer must pay to the PBGC for insurance. This change is good policy, but revenues should shore up PBGC instead of paying for additional spending. Similarly, revenue gained from higher premiums to the National Flood Insurance Program (NFIP) should begin to repay the $17.5 billion the program owes to taxpayers—not to pay for more spending.[5] A different change to the NFIP would require that homes located near a levee or similar structure must have NFIP coverage. This would protect both homeowners and taxpayers. However, new revenues generated by sound policy reforms should go toward reducing the country’s unsustainable deficits—not new spending. Continues Transit Diversion. The HTF is in an unhealthy state due to declining gas tax revenues, caused in part by changes in motorist habits, gas prices, and increasingly fuel-efficient cars. The diversion of up to 35 percent of funds to non-general-purpose road projects exacerbates this problem. Transit programs are the most egregious recipient, siphoning off 20 percent of revenues. They are incredibly costly, do not deliver on promises to reduce congestion or improve air quality, and commit state taxpayers to paying operating subsidies for years to come that they cannot afford. Continues Subsidizing Student Loans. The bill would extend the 3.4 percent interest rate on subsidized Stafford student loans, saving the average student about $7 per month.[6] However, keeping these college loan rates artificially low and saddling taxpayers with the $6 billion price tag fails to fundamentally drive down the cost of college in the long term. Ever-increasing federal higher education subsidies have exacerbated the college cost problem, and maintaining the 3.4 percent rate on Stafford loans is yet another federal subsidy. Part of the pension reform described above would offset the cost of extending the loan rates, but this amounts to one bad policy on top of another. Get Serious The federal government’s overreach into transportation program and funding decisions has increased, fueled by the misguided premise that Washington must have a say in how every transportation dollar is spent. With this has come more regulation—as well as funds being spent on programs that have little to do with general purpose roads. Some of the reforms in this bill that give states more flexibility over their money and reduce the burden of red tape are positive steps toward reversing those trends. Lawmakers are responsible for changing course, and that means cutting spending to live within the federal government’s means—in this case, within the limits of the HTF. This bill does not meet that goal. The use of new revenues—from both good and bad policy changes—to pay for the overspending is particularly unacceptable. Congress should demonstrate that it is serious about curbing its overspending habit.

### Link – Airports

#### Airport infrastructure Expensive

Jan Brueckner, Professor of Economics, University of California, Member, Institute of Transportation, Studies and Institute for Mathematical, Behavioral Sciences, UCI, Fall 09, http://www.uctc.net/access/35/access35\_Airport\_Congestion\_Management.pdf

One remedy is to invest in infrastructure, but new runways take a considerable amount of time to build, and they are expensive. Technological improvements in airtrafﬁc control could also increase the capacity of the nation’s airspace and reduce the impact of bad weather. A third remedy is demand management, either through congestion pricing or restrictions on airport slots

#### Developing Airplanes is expensive and inefficient

Dominic Gates, Parliamentary Fellowship Manager, Industry and Parliament Trust, 9-24-1, http://seattletimes.nwsource.com/html/businesstechnology/2016310102\_boeing25.html

A money pit Based on Boeing's published financial results, The Times estimates development costs have swollen to at least $15 billion. Boeing doesn't report its development costs for specific jet programs and declined to comment on that part of The Times estimate. Apart from that $15 billion, the company spent an additional $16 billion to build the 40 or so jets that were rolled out or partially completed by June 30, according to its latest regulatory report. (That figure doesn't include the first three planes, which Boeing has written off as unsellable.) At least $1 billion more was spent to buy out the partners in Charleston. The only way to dig out of that money pit is to quickly reduce the cost of building the jets. The initial planes in any program are vastly more expensive than those built once production is humming. The "learning curve" on the assembly line, the rate at which those costs come down, determines profitability. Including advance payments to suppliers and some tooling costs, the average direct cash cost to Boeing of manufacturing the airplanes built so far — excluding those first three off the line — is $400 million each. Consulting firm Avitas estimates those planes sold for about $100 million or less. In a June analysis, David Strauss, of UBS, wrote that even if Boeing manages to get costs down as fast as it did on its previous all-new plane, the 777, the manufacturing cost for years will vastly exceed the revenue coming in. "We see 787 burning $4 billion in cash on average annually through 2015," Strauss wrote. He figures Boeing's outlays for building the jets will swell from $16 billion now to $35 billion by 2019 before cash flow on the program becomes positive. It could take 1,900 planes before Boeing recovers those costs, Strauss estimated. Only after that would it begin recouping the $15 billion in development expenses. Using a much more optimistic alternative assumption on how fast Boeing could get its costs down, Strauss reckons Boeing could break even after 1,100 deliveries. An analysis by Doug Harned, of Bernstein Research, came up with a similar number. "You probably don't have another airplane program where you produce 1,000 units and you didn't have a penny of profit," said analyst Pilarski. "Over a decade, you don't even make a penny." Can the program ever make it into profit? Eventually, sometime in the 2020s, well after the first 1,000 deliveries, Boeing would hope to be making 20 percent margins per airplane — an estimated profit of about $23 million per 787 jet, based on the average value of the various Dreamliner models. It would take an additional 650 deliveries or so at that optimal return to recover the $15 billion in one-time development expenses. Yet the senior engineer puts his faith in the dramatic leaps in productivity and cost-cutting that Boeing has made on the 737 and 777 programs. "Lean (manufacturing) will save the program eventually," he predicted. "Break-even won't be as far out as current ugly projections suggest."

### Link – Bering Strait

#### Bearing Strait Tunnel most expensive

Discovery Chanel, 9-6-09, http://dsc.discovery.com/tv/mega-engineering/about/about.html

The Bering Strait tunnel would connect Russia and Alaska, creating a high-speed rail line, freight route, and a crucial oil pipeline. Twice as long as the channel tunnel, it would be the most ambitious and expensive tunneling project ever attempted. To build it, massive Tunnel Boring Machines would start on both sides of the strait -- 64 miles apart -- and meet in the middle. On either side, workers would lay almost 4,000 miles of railway to connect the nearest rail heads to the tunnel. All this would have to be built in some of the most difficult conditions anywhere on the planet: permafrost regions, mountains and summer swamps, and an entire region known for frequent large magnitude earthquakes that put everything, and everyone, at constant risk.

Link – Bering Strait

#### BST cost 15 billion

V.M. Abramson, Metroguiprotrans OJSC, 11-05, <http://www.sciencedirect.com/science/article/pii/S0886779805000672>

On transcontinental railway to the Beringstraits and to AlaskaThe idea of creating a transcontinental railway mainline between the Eurasian continent and North America through the Beringstraits is aimed at providing for all-year-round transit transportation links between American countries, on one part, and those of Europe, Asia and Africa, on the other part. Simultaneously, power supply and communication lines as well as product pipelines will be created. Basically, there are two mainline route corridors: the northern one that follows the shortest alignment between Yakutsk and the Beringstraits and the southern one that provides for an alignment passing through most developed areas of the region. Three or six tunnel mountain crossings, total length 7 or 23 km, will have to be created for the two corridors, respectively. The most challenging part of this tremendous project is tunnel crossing of the Beringstraits whose width and depth in the proposed crossing site (from Dezhnev Cape at Kamchatka to Prince Weles Cape at Alaska) makes about 113 km and less than 60 m, respectively. In a scientific research report developed in 1995 on the order of the RF State Construction Committee, the concept and main parameters of the project were outlined. Position of the tunnel under the Beringstraits in line and grade has got determined by physical, geographical and geological conditions of the region in conjunction with some technical considerations related to the tunnel construction and operation processes. The Diomede Islands (Ratmanov and Crouzenstern Islands) situated in the middle of the straits have made it possible to plan two intermediate shafts to be located there. It also makes possible to use these shafts to ventilate the tunnel at the operation stage as well as to create additional tunneling faces. A shaft will be arranged at each bank too. Given the portals, it will be possible to carry out tunneling from several faces simultaneously, the fact being of importance for any long tunnel construction project. Longitudinal profile of the tunnel was chosen so that a massive of undisturbed rock of a depth not less than 50 m is available between the tunnel and the straits bed. Total length of the tunnel made about 113 km. In order to make it possible for trains to move in the tunnel at speeds up to 160 km/h and more, plane curves are provided for the alignment (minimal radius 2500 m for horizontal curves and 10,000 m for vertical curves). Tunnel construction conditions corresponding to the recommended option may be considered as favorable on the whole: at 75% of the total 113 km length, the tunnel will be driven in sound or slightly fissurated and poorly watered rock, at its 15% the tunnel will pass through zones adjacent to faults and through weathered rock and only 10% of the alignment (10–11 km) will be formed by sections with unfavorable ground conditions where mix-shield TBMs or special unstable rock strengthening methods will have to be used. Two general tunnel design options were considered: (1) two one-track transport tunnels and service tunnel and (2) two-track transport tunnel and service tunnel. The tunnel cross-section size was determined on the basis of the C-type clearance applied for Russian railways (please refer to Fig. 7); however, we believe that the choice of the clearance and the rolling stock type should be reviewed in more detail together with the American Party at the design development stage. It should be taken into account that the mainline will most probably serve for fright traffic more than for passenger traffic and that clearances used for European and Japanese railroads are inferior to the C-type clearance. For example, inner diameter of the one-track Channel Tunnel is 7.6 m only, the fact making it possible in our case to reduce the cross-sectional area by almost 20%. Close to shafts 1, 2 and 4, the tunnel is provided with three station safety complexes including platform section of a length equal to that of the passenger train, 400 m long emergency passages along each track and two groups of repose chambers on each side of the station for a deficient train to be isolated. Given the considerable distances between neighbor safety stations (38 and 46 km) and in order to improve operational safety of the tunnel, the repose chambers in the two one-track tube option are provided approximately in the middle. It will make possible to pass the trains following the deficient one. In case of the two-track tunnel option, the repose chambers are provided within the two-track cross-section. Resulting from examination of the geological conditions, it proved possible to assess the expected loads on the tunnel lining and to propose structural and tunneling solutions fairly well corresponding to the present world tunneling experience. For the two one-track tunnel option, reinforced concrete lining of precast segments, inner diameter 9.5 m for the main tunnel tube and 5.5 m for the service tunnel, is proposed. The service tunnel is placed exactly between the two transport tunnels at the distance of 23 m from them and 30 cm below. For the two-track one tunnel option, reinforced concrete lining of precast segments, outer diameter 11.8 m, is proposed. Since higher TBM advance rates result from installing precast linings, the precast lining option seems to be preferable. Proceeding from a 15-year optimistic construction schedule, the following average advance rates will have to be provided for: 500 m/months for service tunnel driven in stable rock and 150 m/months if driven in insufficiently stable rock; not less than 310 m/month for the transport tunnels in the average. In this case, our approximate assessment of the construction cost is in excess of $15 billion. At the end of this review of basic issues related to building underwater tunnels, it should be stated that after successful completion of unique transport tunnels at the Baikal–Amur mainline in Siberia, tunnels under the Tokio Bay, under the Great Belt straits, under the Elba river in Hamburg, the Lefortovo and the Serebriany Bor tunnels in Moscow, there is no any doubt on the part of tunneling specialists that implementation of the above described tunnels is technically possible. It is now a matter of thorough substantiation of the economical and geopolitical efficiency of the mainlines with due account of the interests of the countries involved.

### Link – Bike Lanes

#### Bike Lanes Expensive to build and maintain

Leslie Minora, Staff Writer at Dallas Observer,Columbia University - Graduate School of Journalism

New York University, 2-12, <http://blogs.dallasobserver.com/unfairpark/2012/02/dallas_bike_lanes_it_wont_be_e.php>

​The bureaucratic red tape for bike lanes is loosening in Dallas. Well, OK. There's talk of it loosening. Which, for those who like to want to ride their bicycles, who want to ride them where they like, is better than nothing. At today's meeting of the city council's Transportation and Environment Committee. Theresa O'Donnell, director of Sustainable Development and Construction, addressed two questions posed to her by several council members (and many others, directly or indirectly): Is there money for bike lanes? And, is it efficient to paint bike lanes as streets undergo routine re-striping? "It actually is quite a bit more intensive than normal striping," said O'Donnell, touching on a conversation that was explored in-depth in December, when council members learned that re-striping 840 miles of on-street bike routes would cost a hefty $16 million. And while 198 of 312 miles of road slated for re-striping overlap with the city's bike plan, council was also told it would cost an additional $4.1 to do so. Not to mention: Many of those miles would require thoroughfare plan amendments, which is a months-long public process similar to zoning. In a December column, Jim found that this thick bureaucratic quagmire is uniquely Dallas. Other cities around the country tag on bike striping to routine street maintenance, avoiding this conversation altogether. This afternoon, O'Donnell said it may be possible to group several street segments together for thoroughfare amendments or to streamline the whole process -- if the council agrees it's necessary. But one thing is still certain: "In most instances we wouldn't recommend striping the biking facility at the same time [as the rest of the street]," O'Donnell said. It would leave jangly bits of disconnected path and would be expensive to paint, even if the trucks are already on the street. But despite the complicating factors, O'Donnell said, "We found six [bike lane corridors] that make a lot of sense." The list: a link through downtown that would connect the Katy Trail and the Santa Fe Trail; striping along Fort Worth Avenue; along the Davis Corridor and West 7th Street in Oak Cliff; a "bike link" from neighborhoods to the Northhaven Trail; links to the Trinity from the Katy Trail and Bishop Arts; and a link from downtown to Oak Cliff. The Grand Total: 21 to 22 miles, $453,000 to $495,000, with $160,000 funding identified and a funding gap twice that -- oh, and maintenance, which doesn't come free. That last bit is the catch. Where will the money come from? The city's grant seeking has been unsuccessful thus far, and mutterings of leftover savings from a 2006 bond package sound far-fetched. As it stands now, private funding and prayers are the best bets. Nonetheless, O'Donnell said, "We think those certainly make sense for us to continue to pursue." Council member Delia Jasso provided her general thoughts on the issue, "As far as guidance, I think whatever is the easiest and the fastest ... I think you'll have a lot of private interest in this as well." She brought along a couple props, flashing bike lights, which are important for safety, and a "Please be kind to cyclists" bumper sticker, which she kindly gave to me. When O'Donnell was pressed further about funding by council member Sandy Grayson and others who echoed her concerns, O'Donnell said city staff is still exploring options. "We continue to kind of look under rocks," she said. But O'Donnell agreed to provide more information about the money next month. Pedal, pedal, pedal.

### Link – Dredging

#### Dredging expensive

Marsha Cohen, editor, 05, <http://www.dredging.org/documents/ceda/downloads/publications-dredging_the_facts.pdf>

Capital (or new) dredging projects can be both extensive and expensive. Maintenance dredging is often a regular, perhaps annual ongoing, long-term activity. In either case, what are the key elements of dredging? The dredging process consists of the following three elements: Excavation: this process involves the dislodgement and removal of sediments (soils) and/or rocks from the bed of the water body. A special machine - the dredger – is used to excavate the material either mechanically, hydraulically or by combined action. The main types of dredgers are described below. Transport of excavated material: transporting materials from the dredging area to the site of utilisation, disposal or intermediate treatment, is generally achieved by one of the following methods: (a) in self-contained hoppers of the dredgers; (b) in barges; (c) pumping through pipelines; and (d) using natural forces such as waves and currents. Other, rarely used transport methods are truck and conveyor belt transport. The method of transport is generally linked to the type of dredger being used. • Utilisation or disposal of dredged material: in construction projects, dredging is driven by the demand for dredged material. In navigation and remediation dredging, the project is driven by the objective of removing the material from its original place. Thus, the question of “what to do with the removed material?” arises. As a result of growing environmental pressure, ﬁnding an answer to this question has become increasingly difﬁcult, especially when the material is contaminated. The main alternatives for the management of the dredged material are described later in this document.

### Link – Ferries

#### Ferries are too expensive

Susannah Frame, Investigative reporter, 11-10, <http://www.king5.com/news/investigators/States-new-ferry-small-but-most-expensive-ever-107103363.html>

SEATTLE -- Pound for pound, it’s the most expensive ferry ever built in the United States - the MV Chetzemoka. Price tag? $80.1-million. The boat is about to make its maiden voyage on the Port Townsend-Keystone run which was recently renamed the Port Townsend-Coupeville run. The KING 5 Investigars have found that using the marine industry standard of looking at ferry construction costs by how many cars a vessel can carry, the Chetzemoka sits at the top of the heap by a long shot. The Chetzemoka is small. It can carry 64 cars total. That means taxpayers shelled out $1.2-million per car slot for the boat. That's more than two-and-a-half times per car slot than what it cost the state to build the fleet's biggest ferries in the late 90's. The "Jumbo Mark II's", which include the Wenatchee, the Tacoma and the Puyallup, cost $86-million a piece, or $425,000 per car slot. The Alakai, which operates out of Alaska is another big ticket ferry in the country. Shipbuilders in Alabama constructed it in 2007 for $85-million. The Alakai carries 282 cars. Per car slot cost? $320,000. The Chetzemoka cost four times that. The Chetzemoka is the first boat built in the state in over a decade. Director of Washington State Ferries David Moseley calls it a great day for the ferry system. "We're thrilled to have the Chetzemoka going into service on Sunday,” said Moseley. The boat will be a welcome sight to riders on the route. They've limped along without full service for three years. In 2007 their boats, the aging Steel Electric ferries, were yanked from service by Secretary of Transportation Paula Hammond because of safety concerns. "It couldn't have come at a worse time, today we have suspended service at Port Townsend, Keystone," said Hammond in 2007. Ever since, the state's been frantic to get the Chetzemoka in the water. The mandate from leaders: build a boat and build it fast, whatever it takes. "There was a premium we paid to get that boat in service this Sunday and I'm pleased we will get it in service this Sunday, not three or four months down the line,” said Moseley. Instead of starting from scratch, Washington State Ferries bought a design for the boat that was ready-to-go for $1.3 million. The design was originally for a boat called the Island Home which sails to Martha's Vineyard on the East Coast. After putting out a request for bids across the country, that ferry system, The Steamship Authority, had the Island Home built in Mississippi for $33 million, or $500,000 per car slot. But constructing that same design in Washington state cost much, much more. Cost Evolution With factors such as higher labors costs and stricter environmental standards in the Northwest compared with the South, Washington State Department of Transportation engineers first estimated it would take $49-and-a-half million to build the Island Home design here. Todd Pacific Shipyards, based in Seattle, was the only bidder for the work. They came in at $65-and-a-half million for the job. The state agreed. Expected changes and other fees brought the total to $77 million. Not expected were $5 million more in design changes. That brought the total cost to $80.1 million. Representative Larry Seaquist, D-Gig Harbor, serves a district dependent on the ferry system. "I think no matter first of class or not, this thing is way too expensive and we need an audit process and ask ourselves why did we end up spending this much money on a boat that may not suit our needs exactly," said Seaquist. How did the numbers get so mammoth to build the Island Home design in Washington? The price tag here ended up being $47 million more than the cost to build it in Mississippi. A big factor is a state law requiring ferries here to be built in-state by builders like Todd Shipyards. Putting out a request for bids nationally isn't an option for Washington State Ferries. There's very little competition to get the best price. In this case, no builder in the state even tried to compete with Todd for the work. "The fact that there was only one bidder was a budget issue, a cost issue," said Moseley. On top of that, the KING 5 Investigators have learned about costly mistakes. An extra million dollars to move an engine due to drawing errors by the state. $330,000 more for replacing the rub railing which is a sort of bumper around the boat to protect it from damage. The first rub railing was too small for the job. Retired ferry captain Frank Longmate worked on the Port Townsend run on and off for 34 years. "You'd think these guys would be smart enough to think of these things to figure it out before they build it,” said Longmate. He says the state should have known any boat on that rough weather route needs a sturdy rub rail. "Someone should have noticed that, right at the concept of the design work." Sources tell KING 5 the Chetzemoka's problems don't begin and end with a big bill. Several people who've worked on the boat say the design is flawed and plagued with problems. For example, they say the propellers are inefficient. Just last week a captain on the Chetzemoka wrote in an internal memo that the new, expensive rub rails deserve a grade of a D-minus. And they don’t like the fact that the ferry is lopsided. In video KING 5 shot recently, it is obvious the ferry is higher on one side than the other. Our video also shows the list is noticeable while the boat is sailing. While KING 5 sources say a listing boat isn’t efficient, and can create safety concerns, the company that designed the Island Home, Elliott Bay Design Group, disagrees. They say it’s designed to have a list, which is corrected when cars are on-board. "The single most important thing we can do for the ferry system is get them out of the business of building, designing and building boats and exclusively focused on operating a ferry system," said Seaquist. "The proof is in the sailing and the boat is sailing well, said Moseley. He says critics will eventually get on-board. The Chetzemoka is the first of three Island Home boats being built in the state, and that's where Moseley says there's good financial news. The second and third boats are currently under-budget so in the end he says the high cost of the Chetzemoka will be cancelled out. "I think the important thing to the taxpayers is: Can we bring this overall procurement program (all three boats) in line with the budget? I think we can," said Moseley. Washington State Ferries is the largest ferry system in the United States, carrying more than 23-million passengers a year.

### Link – HSR

#### Bullet Trains Expensive and problematic

Walter Russell Mead, Professor of Foreign Affairs and Humanities at Bard College Editor-at-Large of The American Interest magazine, Paraphrases UCLA study, 6-12, http://blogs.the-american-interest.com/wrm/2012/07/14/ucla-study-bullet-train-wont-create-growth/

UCLA Study: Bullet Train Won’t Create Growth A UCLA study of Japan’s high-speed rail system concludes that bullet trains don’t create economic growth, undermining one of the major justifications for California’s own high-speed train system. [Jerry] Nickelsburg [the UCLA economist who led the study] examined the growth rates of cities and regions served by Japan’s system, compared to the nation’s overall rate of growth, and found that the introduction of high-speed passenger service had no discernible effect. The analysis looked at nearly a dozen urban and rural prefectures and found no evidence that the introduction of bullet train service improved tax revenues, which was used as a proxy for local gross domestic product. In one case, one region without high-speed rail service grew just as quickly as a similar region with it. The study examined economic activity over a 30-year period. Last week, a Via Meadia commenter brought up a good point about high-speed rail: Only people whose homes are near the terminals will benefit. Everywhere else, land will be blocked off from productive use — worse than blocked off, converted from use that is productive for the locals—for the benefit of the few who live near the station. This is why voters and municipalities on the San Fransisco peninsula, from Burlingame to San Jose, are vehemently opposed to this expropriation. To make the train useful to them, it would have to stop there… at which point it stops being high-speed. The bad news about California’s absurdly expensive and increasingly unpopular bullet train system continues to pile up. By the time this white elephant is finished — if it ever is — it will be even more useless than it now looks. Transport technology will have changed, as innovations like self-driving cars challenge the assumptions on which the high speed rail backers make their case. Improvements in telcom technology and changes in work habits by new generations that grow up with new technologies will make telecommuting and teleconferencing integral to the way business works

### Link – Public/Private

#### Private-Public Partnerships in transportation infrastructure get downgraded

Glazier 12 (Kyle Glazier , over economic indicators and national transportation news for @TheBondBuyer in Washington, D.C. , The bond Buyer: INFRASTRUCTURE Vol. 121 No. 134, July 13, 2012 “Moody's: P3s a Credit Risk If a Participant's Rating Is Downgraded,”)hhs-ps

WASHINGTON - An analysis of rating actions on bonds issued for projects involving public-private partnerships reveals that P3s are vulnerable to credit risk following downgrades of participants even if the projects are going well, according to a [Moody's Investors Service](http://www.lexisnexis.com.ezproxy.baylor.edu/lnacui2api/search/XMLCrossLinkSearch.do?bct=A&risb=21_T15160866208&returnToId=20_T15160866277&csi=303185&A=0.4367739669498675&sourceCSI=3652&indexTerm=%23CC0009P6T%23&searchTerm=Moody's%20Investors%20Service%20&indexType=C) report released Thursday. P3s are gaining popularity in the United States, where more states are enacting, or seeking to enact, laws authorizing such arrangements. Government and industry leaders like Transportation Secretary Ray LaHood and the American Association of State Highway and Transportation officials are actively promoting the potential of the P3 finance method. However, these arrangements leave projects exposed to risk from downgrades of governments, banks and construction companies, said Moody's senior credit officer Catherine Deluz. The debt of P3 projects can be downgraded if proper safeguards aren't in place. Deluz said that since Moody's began rating P3s about 10 years ago, more than half of downgrades, reassignments to negative outlooks, or reviews for downgrade have been at least partially connected to a downgrade of one or more of the project's participating parties. Project participants represent key risk factors during different phases of a project, the report demonstrates. A downgrade of the firm constructing the project is potentially most damaging early on, but becomes less so as the project nears completion and begins operating, Deluz said. The report points out some common characteristics of P3s that make them sensitive to participant risk. "They usually do not keep a large amount of cash apart from the minimum required to be kept in various reserves," the report states. "That limits their ability to meet unexpected material cash requirements." Additionally, Deluz wrote, many types of P3s don't have a means of increasing revenue or liquidating assets to meet sudden cash needs. Some types of P3s, such as toll roads, do have that flexibility. To protect against the possibility of one party's weakened credit damaging the entire project, most P3 arrangements include a mechanism that "de-links" the participants' credit with that of the project. The mechanism can take the form of an obligation to replace one company with another if the risk reaches a certain level, according to the report. "However, even when de-linkage of the framework is strong, it is not bullet-proof," the report said. "Unexpected events often shine a light on management's approach to risk mitigation, and where an issuer fails to take prudent measures to mitigate an emerging risk, e.g. by contracting with weaker counterparties while stronger alternatives remain available, this in itself will likely weigh on its ratings."

### Link – Shipping

#### Ships are expensive, the government can’t take care of what it has now

Joseph Keefe; Captain, Professional Journalist, Massachusetts Maritime Academy; 7-11, http://www.maritimeprofessional.com/Blogs/The-Final-Word-with-Joseph-Keefe/August-2011/DOJ--Way-Off-Course-in-Shipyard-Litigation.aspx

Showing questionable wisdom, the United States and its justice department have filed suit against Bollinger Shipyards Inc., Bollinger Shipyards Lockport LLC and Halter Bollinger Joint Venture LLC. In general terms, the government alleges that the Louisiana shipbuilder misrepresented the hull strength of a series of vessels that it was improving and lengthening about five years ago. The first converted cutter, according to the government, suffered hull failure when put into service. Eventually, said the U.S. Justice Department in a prepared statement, “Efforts to repair the Matagorda and the other converted vessels were unsuccessful. The cutters are unseaworthy and have been taken out of service.” As the government seeks damages from Bollinger for the loss of the eight vessels – the upgrades alone said to be worth about $95 million – the Coast Guard itself continues to struggle in an effort to renew an aging fleet and related equipment. Ten years after launching the aggressive, $25 billion so-called “Deepwater” program to do just that, the nation’s fifth military, uniformed service has little to show for the $7 billion already spent. The latest DOJ action, coming years after the work itself was complete, cannot hope to hide those failures. Bollinger Responds for its part, Bollinger responded to the suit by saying in a prepared statement dated August 17, “Since its founding, Bollinger Shipyards has operated on the principle that ‘quality is remembered long after the price is forgotten.’ Three generations of the Bollinger family have earned a spotless record for honest and fair dealing with every customer, including the U.S. Navy and Coast Guard, our largest client. Since 1984, Bollinger has built every patrol boat the Coast Guard has purchased; to date some 122 have been delivered.” The statement went on to say, “We are disappointed with the Department of Justice’s decision to file a complaint related to work completed in 2006. Throughout this process, Bollinger has been open and cooperative with the government, and we remain committed to providing the government all necessary information and assistance to bring this matter to a close. Bollinger has tried to find a way to resolve this matter short of litigation, but we are fully prepared to defend our good name aggressively in a court of law. As we have for the last 65 years, Bollinger will continue to deliver the highest quality and contract-compliant products to the United States Coast Guard and to each and every customer.” Indeed, and as if to underscore their response, Bollinger this week also noted the launch of the U.S. Coast Guard’s second, 154-foot Fast Response Cutter from its Lockport, LA shipyards last Thursday. The event – according to the Coast Guard itself – marks a significant milestone in the Coast Guard’s acquisition of the Sentinel-class patrol boats. And, the third Fast Response Cutter is tentatively scheduled to be launched Nov. 10. Let’s sum up: 122 Coast Guard patrol boats delivered since 1984, an ongoing relationship with the Coast Guard (Bollinger’s largest client) and a continued record of typically delivering what the Coast Guard wants in a timely fashion. Not bad for an outfit now accused of misrepresenting the facts. Blame Game From where I sit, there is probably plenty of blame to go around, but don’t take my word for it. The recent (28 July) GAO Report about the Coast Guard’s Deepwater program is also telling. The 86-page Report, GAO-11-173, “Coast Guard: Action Needed As Approved Deepwater Program Remains Unachievable,” says, among other things, “The Deepwater Program continues to exceed the cost and schedule baselines approved by DHS in 2007.” None of that is any secret, of course, and the report goes on to list numerous problem and setbacks associated with the star-crossed efforts. Central to the Coast Guard’s troubles in the Deepwater effort was its own failure to properly oversee the effort from the beginning. Coast Guard Commandant ADM Robert Papp himself was recently quoted as saying, "I'll be the first to admit, we weren't prepared to start spending this money and supervising a project this big." Leaving the details and supervision of the projects to the contractors themselves, the Coast Guard eventually lost control of the multi-billion dollar project. Today, a cash-strapped Congress is pushing back against what they characterize as inadequate steps by the Coast Guard to right their wildly off-course and over budget effort. The government’s action against Bollinger also comes as a cost-conscious Congress, led by Rep. Frank Lobiondo (R - NJ), are on record as saying that they will no longer provide a “blank check” to the Coast Guard. And, while that makes sense on many levels, it also comes at a time when the Coast Guard’s efforts in the rapidly thawing Arctic are also ramping up significantly, with inadequate resources – particularly in way of icebreakers that can cost up to $1 billion each – to do the job. Catch 22 In numerous interviews over the past few years, especially where it comes to Deepwater and ship acquisition efforts, the Coast Guard leadership has opted to look ahead, not behind. The party line has become, “Don’t look at where we’ve been; instead look how far we’ve come.” Fair enough. Today, however, and as the Coast Guard implores Congress to forget the past, the Department of Justice seems just as intent upon dredging it up. But, it doesn’t seem right to let them have it both ways, does it? Bollinger certainly won’t be afforded that luxury. At the end of the day, you have to wonder how much it will cost Bollinger and ultimately, the U.S. taxpayers, to defend and prosecute a case from which virtually nothing good can come. Did the shipyard drop the ball or was the Coast Guard deficient in their contract administration? I honestly have no idea. Five years down the road, it is a curious time to be finding out. It will also be expensive. How many patrol boats could we be building with that money? Finally, and perhaps most importantly, who will build these boats and others, if and when, years from now, the government triumphs?

### Link – State Grants

Funding states is wasteful – worsens downturn

Inman (Professor of Finance and Economics at the Wharton School at University of Pennsylvania) 2010 (Robert “Using states for macroeconomic fiscal policy” <http://www.voxeu.org/article/shortcomings-using-states-federal-macroeconomic-fiscal-policy> )

The recession of 2007 is perhaps the deepest, longest, and most damaging economic event of the last 75 years. In response, all tools of macroeconomic policy management were called into use: from direct easing of interest rates and purchasing of public and private debt to tax cuts and government spending. There is every reason to think that this across-the-line defence was necessary to prevent a major recession from turning into what might have been a worldwide depression. But not all tools in the arsenal were effective as protection against the downturn, and one in particular – national government transfers to state governments in federal economies – may lead to more long-run harm than short-term benefits.

### Link – Subways

#### Subways too expensive in US

David Lepeska, writer for The New York Times, Monocle, and other publications, 11-11, <http://www.theatlanticcities.com/commute/2011/11/1-billion-doesnt-buy-much-transit-infrastructure-anymore/456/>

Chicago Mayor Rahm Emanuel recently announced a $1 billion plan to overhaul the city's L trains, which are run by the Chicago Transit Authority and began operations in 1892. "The public will get a new CTA," he said at a press conference. That's a bit of an exaggeration. In reality, the money will be used to lay new rail tracks between 18th and 95th streets on the Red Line to eliminate “slow zones," replace ties on the Purple Line and improve underground ventilation and electrical substations. In addition, nine stations will receive modest technical upgrades and—finally, the most significant addition—two stations on the North Side will be rebuilt. It seems $1 billion doesn't go very far in subway construction these days. Look at New York, where the 8.5-mile Second Avenue subway line is expected to cost more than $17 billion. Internationally, subway construction costs remain considerably lower. Sao Paulo's new 11-km Yellow Line, completed last year, cost $1.6 billion, with fully automated trains and free high-speed wireless Internet at each of 11 stations. Singapore's new Circle Line runs 22 miles with 28 stations and cost $4.8 billion, or $130 million per kilometer. Upon completion next year, it will become the world's longest fully automatic underground transit line, and among its most advanced. In Europe, too, subways cost less. Madrid's recently-opened Metrosur line is 41 km long, with 28 stations, yet was completed in four years at around $58m per km. Recent expansions in Paris and Berlin cost about $250 million per km. New York, meanwhile, is building the most expensive subway line of all time, at $1.7b per km. This figure makes London's 16-km-long Jubilee line and Amsterdam's 10-km North-South line, which both faced delays and controversy and cost $350m and $400m per km, respectively, seem reasonable in comparison. New York's astronomical subway costs are partially explained by pricier real-estate and labor and the expense of tunnel boring into Manhattan bedrock. Blogger Benjamin Kabak thinks exorbitant consultant and design fees and stunningly over-priced construction contracts also play a part. Another concern is age. Robert Paaswell, engineering professor at the City College of New York and director of the University Transportation Research Center, says costs are so high in Chicago and New York because their systems are the country's oldest and thus the most expensive to upgrade. The New York City subway, which began operations in the 1870s as an elevated system, has experienced three derailments in the past six months. This helps explain why Washington, D.C., where the Metro opened in 1976, laid more than three new miles of track and built two new stations, a 2,200-car parking structure and a rail car storage facility as part of a subway extension into Prince George's County, Maryland, all for $456 million. Paaswell also cites New York's higher regulation costs, over-conservative labor laws and financing via bonds, which lead to longer-term debt plans. Finally, Americans and Europeans generally hold different views of major public transport projects. The latter see the expense as justified, even necessary, while the former tend to embrace driving and view major construction projects as a potential hassle. “There's no urgency by governments or citizens here to get subways done, and when it finally happens the construction causes so much inconvenience that people don't like it,” said Paaswell, a former CTA executive director. “In Europe, they don't care too much about it, they just blast right through and get it done.” For this reason, less dense U.S. cities often prefer light rail, which averages about half the cost of subways and can often dovetail on highway projects. The new SouthEast rail line portion of Denver's T-Rex transport project cost $970 million for 19 miles of new lines and 13 stations. And Minneapolis' 19km, 17-station Hiawatha, or Blue Line, which opened in 2008 and connects the Twin Cities' international airport and the Mall of America to downtown, cost $715 million and has far exceeded its ridership targets. City officials still looking to justify exorbitant spending on subway expansion might want to cite a 1918 essay by Julius Glaser, a design engineer for the city of New York. Why do we build subways? They're expensive. They cost several times as much, mile for mile, as elevated railroads, and their construction entails more inconvenience to the public and to business, and for a longer time. They interfere with and endanger the sewers, gas pipes, water mains, electric conduits, and other subsurface structures, for an extended period, and then, when finally completed, many people dislike to ride in them. Yet we build subways, because, when finished, unlike elevated railroads, so far as street conditions are concerned, they are noiseless, invisible and do not obstruct light, air or traffic. Train operation is never interfered with by weather conditions, and real estate along the route is enhanced in value. The permanent advantages of underground railroads far outweigh the temporary inconveniences during the construction period.

## \*\*\*Downgrade ILs\*\*\*

### 2NC Spending = Downgrade

moody's said that a weakening in fiscal discipline leads to a downgrade - gongloff 11

**Fitch will downgrade US credit rating if spending increases – assumes underlying market strengths**

Dow Jones Newswires 12 (Dow Hones Newswires, “Fitch May Cut U.S. Rating If No 'Credible' Fiscal Plan” 06-07-12, <http://www.nasdaq.com/article/fitch-eyes-us-downgrade-without-credible-fiscal-plan-20120607-00970> )hhs-ps

Fitch would likely downgrade U.S. debt if the government does not get its fiscal house in order --Fitch sovereign group managing director Ed Parker says the firm is looking for a fiscal plan after the elections --The firm rates the U.S. at triple-A but put it on negative outlook last November A Fitch Ratings executive said Thursday that the firm would likely downgrade U.S. debt if the federal government does not get its fiscal house in order. Speaking at the firm's global banking conference in New York, Fitch sovereign group managing director Ed Parker said " the U.S. does not have a credible fiscal consolidation plan" and that "if we don't see one after the election, I would expect a downgrade." Fitch rates the U.S. at triple-A but put it on negative outlook last November, and Mr. Parker's comments were a reiteration of the firm's position. In its original note placing the U.S. on negative outlook last year, Fitch cited the country's uncertain economic growth prospects, and said projections showed federal debt exceeding 90% of GDP by the end of the decade. "In Fitch's opinion, such a level of government indebtedness would no longer be consistent with the U.S. retaining its "AAA" status despite its underlying strengths," the firm said at the time. Fitch has the U.S., U.K. and France on negative outlook because of high debt-to-gross-domestic-product-ratios. Mr. Parker noted that the three countries, plus Germany, are the most heavily indebted nations among those with the top credit rating (Germany is not on negative outlook because its debt-to-GDP ratio has already peaked and the country is on a path toward more stable finances). Negative outlook implies an increased likelihood of a downgrade in a two-year time horizon. "There is a limit to how high these government debt levels can go," Mr. Parker said.

#### Deficit spending raises chances of downgrade—fiscal consolidation solves

Newsmax 12 Newsmax, 6/7/12, “Fitch: US Risks 2013 Rating Downgrade Without 'Credible' Deficit Plan,” Newsmax, http://www.newsmax.com/Newswidget/Fitch-US-Rating-Cut/2012/06/07/id/441536?promo\_code=EF02-1&utm\_source=Shark&utm\_medium=nmwidget&utm\_campaign=widgetphase1

Fitch Ratings reiterated that it would cut its sovereign credit rating for the United States next year if Washington cannot come to grips with its deficits and create a "credible" fiscal consolidation plan. It also said it would immediately cut the credit ratings on Cyprus, Ireland, Italy, Spain and Portugal if Greece were to exit the eurozone. Additionally, all eurozone nations would have their ratings put on its negative ratings watch list, setting a six-month time frame for a potential downgrade. Europe's ongoing sovereign credit crisis undermines already below-trend growth seen in the United States, the world's biggest economy. Editor's Note: Startling Proof of the End of America’s Middle Class. Details in the Video "The United States is the only country (of four major AAA-rated countries) which does not have a credible fiscal consolidation plan," and its debt-to-GDP ratio, or how much debt it has relative to the size of the economy, is expected to increase over the medium term, Ed Parker, sovereign ratings analyst, told a Fitch conference in New York. Lower credit ratings typically lead to higher borrowing costs, putting more strain on government balance sheets already straining to cut spending without sending their economies into a tailspin. Only in the last week have European leaders broached the prospect of closer economic and political ties to overcome the crisis which has forced severe austerity budgets on Europe's citizens. German and European Union officials are looking into ways to rescue Spain's debt-stricken banks even though Madrid has not called for aid and resisted international supervision. A voter backlash returned a socialist government in France and boosted the chances for the same in Greece which could put its 130-billion-euro international bailout plan in jeopardy. Fitch revised down its credit outlook for the United States to negative in November from stable after a special congressional committee failed to agree on at least $1.2 trillion in deficit-reduction measures. At the time it said there was a chance for a U.S. downgrade in 2013, saying the failure of the committee increases the fiscal burden on the next administration. A change in an outlook sets a 12-18 month time frame for making a decision. A negative outlook signifies there is a greater than 50 percent chance for a downgrade, and vice versa if the outlook is positive. "The United States is the only one of the four largest economies whose debt as a percentage of GDP is expected to increase over the next five or six years," Parker said, referring to the United States, Britain, Germany and France. The U.S. economy's growth rate in the first quarter was revised down last month to 1.9 percent from a prior estimate of 2.2 percent as businesses restocked shelves at a moderate pace and government spending declined sharply. It grew 3.0 percent in the fourth quarter of 2011. Standard & Poor's made history in August 2011 when it cut the U.S. credit rating to AA-plus from AAA. It has held it with a negative outlook ever since. Moody's Investors Service has the United States rated at Aaa, also with a negative outlook as of November last year. All three of the ratings agencies have said they essentially do not expect much change in the U.S. budget situation or fiscal position until after the November presidential election. The negative outlook from S&P gives it a six-to-24-month window for making a decision while Moody's defines its time frame as 12 to 18 months. Fitch respects the size and flexibility of the U.S. economy but the "rising trajectory" of its debt could lead to the same kind of economic stagnancy that has long plagued Japan, Parker said.

#### More deficit means downgrade

Reuters 12 Reuters, 7/11/12, “Fitch affirms US’ top AAA rating,” RT, http://rt.com/business/news/fitch-usa-aaa-rating-872/

Fitch Ratings has affirmed the United States (U.S.) long-term foreign and local currency Issuer Default Ratings (IDRs) and Fitch-rated U.S. Treasury security ratings at 'AAA'. Fitch has also simultaneously affirmed the U.S. Country Ceiling at 'AAA' and the short-term foreign currency rating at 'F1+'. The Rating Outlook on the long-term rating remains Negative. The affirmation of the U.S. 'AAA' rating is underpinned by its highly productive, diversified and wealthy economy; monetary and exchange rate flexibility; and the exceptional financing flexibility afforded by the global reserve currency status of the U.S. dollar. Fiscal and macroeconomic risks emanating from the financial sector are moderate and diminishing. The U.S. sovereign credit profile also benefits from the respect for property rights, the rule of law and high degree of political and social stability. Fitch's current assessment is that the weak recovery reflects the gradual rebalancing of the economy, notably the unwinding of excessive household debt and the housing market correction, rather than a permanent downshift in the potential growth rate of the economy. With household debt falling towards pre-crisis levels, the housing market beginning to stabilise and healthy corporate sector finances, Fitch expects the economic recovery to gradually accelerate into 2013 and 2014 and over the medium term, Fitch projects the economy to expand at an annual average rate of around 2.5%. The risks to the forecasts are mostly to the downside in light of the uncertainty regarding U.S. fiscal policy and the European debt crisis and recession. Moreover, the space for significant U.S. fiscal and monetary policy stimulus is much diminished. Additional information is available in Fitch's May 2 special report, 'Gauging the Benefits, Costs and Sustainability of US Stimulus', available at ' www.fitchratings.com '. Following the failure of the Congressional Joint Select Committee on Deficit Reduction ('the Supercommittee') to reach agreement, Fitch revised the Rating Outlook for the United States to Negative from Stable on Nov. 28 2011. This was primarily due to Fitch's diminished confidence that timely fiscal measures necessary to place U.S. public finances on a sustainable path would be forthcoming. The Negative Outlook also reflects the risks associated with the lack of broad public and political agreement on how to secure deficit reduction. The uncertainty over tax and spending policies associated with the so-called 'fiscal cliff' weighs on the near-term economic outlook. A 5% of GDP fiscal contraction in 2013 implied under current law would, if permanent, push the US into an unnecessary and avoidable recession. Moreover, the burden of government debt on the economy will continue to rise with potentially adverse implications for potential growth as well as increasing the risk of a fiscal crisis if agreement is not reached on reducing the budget deficit and addressing the long-term fiscal challenges associated with rising health care costs, an aging population and a narrow and volatile tax base. In Fitch's opinion, it is likely that all or some of the tax increases and spending cuts implied under current law will be voided or at least temporarily deferred. Fitch's fiscal and economic forecasts are premised on a reduction in the federal budget deficit of around 1.5% of GDP in 2013 rather than the 3% to 5% contraction implied by the 'fiscal cliff'. Consequently, Fitch forecasts the U.S. economic recovery to accelerate to 2.6% in 2013 from 2.2% this year and unemployment to fall below 8%. Fitch's 'Global Economic Outlook, New Threats and Old Risks' report from June 15 goes into more detail. The debt ceiling will likely become binding from mid-November, though the Treasury Secretary can deploy 'extraordinary measures' to extend the Treasury's borrowing authority into early 2013. Fitch continues to judge that the risk of a payment default on a Treasury security arising from operation of the debt ceiling to be extremely low. Nonetheless, last-minute agreements to raise the debt ceiling and regular threats of payment default threaten the U.S. 'AAA' rating. A repeat of the August 2011 'debt ceiling crisis' would prompt Fitch to review the U.S. sovereign rating, as discussed in Fitch's special report, 'US Fiscal Outlook - Mired in Uncertainty', published today and also available at ' www.fitchratings.com ' or by clicking on the above link. The low cost and security of fiscal funding are key credit strengths and imply that the U.S can support a higher debt burden relative to its 'AAA' and high-grade peers. The profound benefits that accrue from the US dollar's status as the world's reserve currency and Treasury securities as the global benchmark fixed-income instrument mean that the U.S. can minimise the output and employment costs of fiscal consolidation with a gradualist reform-orientated approach. But the absence of market pressure also renders it easier to defer and avoid difficult choices on tax and spending necessary to stabilise government debt to GDP ratio over the medium-term and ensure fiscal space to absorb future shocks. Including the debt of state and local governments as well as that of the federal government, gross general government debt is equivalent to 103% of GDP (and 96% on a comparable basis with highly-rated European sovereign peers), the highest level of indebtedness of any Fitch-rated 'AAA' sovereign and double the current 'AAA' median of less than 50%. Federal debt held by the public stands at 70% of GDP compared to a current 'AAA' median for central government debt to GDP of 43%, though it is similar to that of France (rated 'AAA' with a Negative Outlook by Fitch) and much less than the 85% of GDP for the U.K. (rated 'AAA' with a Negative Outlook). Fitch currently projects federal debt held by the public and gross general government debt to reach 79% and 108% of GDP respectively by 2014. On current policies, Fitch projects the federal budget deficit to stabilise at between 4% and 5% of GDP from 2014-15. Under current assumptions regarding economic growth and interest rates, this would be insufficient to prevent government debt to GDP ratio from continuing to rise over the medium to long-term. More information is available in Fitch's Dec. 21, 2011 special report, 'U.S. Public Finances - An Update'. Absent material adverse shocks, Fitch does not expect to resolve the Negative Outlook until late 2013. Fitch will take into account any deficit-reduction strategy that may emerge after Congressional and Presidential elections in addition to an updated assessment of the medium-term economic and fiscal outlook. Agreement on a multi-year deficit reduction plan that would stabilise government indebtedness and secure confidence in the long-run sustainability of public finances would likely result in Fitch affirming U.S. 'AAA' status and revising the Rating Outlook to Stable. Conversely, failure to secure agreement on deficit-reduction that implies a continuing rise in government indebtedness over the remainder of the decade would likely result in Fitch downgrading the U.S. sovereign rating.

#### Unsustainable fiscal policy causes downgrade

Schroeder 12 Peter Schroeder, writer for The Hill, 5/25/12, “Rating agencies warn feds risks downgrade without deficit plan,” The Hill, http://thehill.com/blogs/on-the-money/budget/229599-rating-agencies-warn-government-risks-downgrade-without-deficit-plan

“We’d have to assess the actual content of any temporary agreement,” Hess said. “How likely is it that that will require a credible plan to be implemented within whatever time frame they come up with? It’s the actual deficit and debt trajectories that we expect that will be the most important determinant.” Only Standard and Poor’s has so far downgraded the U.S. credit rating, though Fitch and Moody’s have both put the United States on negative outlook, suggesting future downgrades are coming without a change in course. When Fitch assigned the negative outlook, it identified 2013 as a crucial year for the United States to take action on its debt. Currently, it sees better-than-even odds that it will downgrade the United States, but such a decision would not come until the end of 2013 as it waits to see how the deficit will be addressed following the elections. Still, experts closely following the debate say a pure punt would raise doubts that the federal government’s seriousness on the deficit, raising the chance of an impending downgrade. “If Congress doesn’t put in place a process that assures people that this will be addressed in a real manner … then there is no doubt in my mind that our sovereign debt will be downgraded,” said Steve Bell, a former Republican budget staffer who is now the senior director of economic policy at the Bipartisan Policy Center. “Markets throughout the world are going to be looking at the action of the United States government.”

Spending = Downgrade

**Spending increases cause Fitch to downgrade US credit rating**

Reuters 12 (“Fitch Repeats Warning Of U.S. Downgrade In 2013, Reuters Says,” Jun 7, 2012, <http://www.bloomberg.com/news/2012-06-07/fitch-repeats-warning-of-u-s-downgrade-in-2013-reuters-says.html> )hhs-ps

The U.S. may lose its AAA rating next year unless politicians reach an agreement to significantly cut the [budget deficit](http://topics.bloomberg.com/budget-deficit/), an analyst at [Fitch Ratings](http://topics.bloomberg.com/fitch-ratings/) said. The U.S. lacks a credible plan to reduce spending and stop the growth of the national debt, [Edward Parker](http://topics.bloomberg.com/edward-parker/), a sovereign analyst, said at the firm’s Global Banking Conference in New York, according to Reuters. The comments were consistent with the third-biggest ratings firm’s statements in November, when it assigned a negative outlook to the U.S. and said the probability of a downgrade is greater than 50 percent over two years. [Standard & Poor’s](http://topics.bloomberg.com/standard-%26-poor%27s/), the world’s largest ratings company, downgraded the U.S. to AA+ in August, saying lawmakers had failed to agree on enough budget cuts. Moody’s Investors Service, the second-largest, has had a negative outlook on the country’s Aaa rating since August. Fitch’s analysts didn’t announce any changes to their views at the conference, Brian Bertsch, a spokesman in [New York](http://topics.bloomberg.com/new-york/), said in an e-mail. Fitch forecasts federal public debt will exceed 90 percent of gross domestic product by the end of the decade unless the government addresses rising health and social security spending through tax increases or reductions in expenditures. The “high and rising federal and general government debt burden is not consistent with the U.S. retaining its AAA status even with its other fundamental sovereign credit strengths,” Fitch said Dec. 21 in a statement.

#### Discipline key – downgrade otherwise

Thriving Tools, Financial Advisor, 20’12, [The U.S. Credit Rating Downgrade. <http://www.thrivingtools.com/government/the-u-s-credit-rating-downgrade/>] VN

Standard and Poor’s made the decision to downgrade the U.S. debt because of concerns about the rising debt. The ratings company also viewed the political climate as affecting the government’s ability to implement a process to deal with the U.S. debt. Even though a new budget deal to raise the debt ceiling had passed before the ratings organization made its U.S. credit rating downgrade, a spokesperson for Standard and Poor stated that **the company did not feel the budget deal did enough to deal with America’s financial problems.**  The continued governmental deadlock between the Republicans and Democrats only heightened the concern of the rating company. Even though the two other main NRSROs did not downgrade the U.S. credit ratings, they hold similar concerns. **A spokesperson for Fitch Ratings stated that the government needed to implement policies that would address the weakness in the American economy**. The company decided to keep the triple A U.S. debt rating because it was felt that the chances of a U.S. default is very low but the company would still like to see an increase in government revenue and a cut to entitlement payments. Moody’s Investor Services also held concerns about government plans to deal with the current debt. The company issues a press release stating that they may still drop the U.S. debt rating if there are significant rises in government funding costs beyond the expected increase as well as if further plans to deal with the financial situation are not put in place by 2013. **A U.S. debt downgrade may also occur if the economy deteriorates or the government does not keep control over spending.**

Spending = Downgrade

#### Downgrades without fiscal discipline

Thriving Tools, Financial Advisor, 20’12, [The U.S. Credit Rating Downgrade. <http://www.thrivingtools.com/government/the-u-s-credit-rating-downgrade/>] VN

Standard and Poor’s recently reviewed the U.S. debt downgrade made in 2011 and stated that they were not prepared to raise the U.S. credit ratings back up to triple A. The rating would remain at AA+ with a negative outlook because of continuing problems with the debt burden. The rating agency felt that the government was not doing enough to deal with the debt problem. In fact, **Standard and Poor’s have issued a warning that unless the government takes steps to deal with the financial situation, they may downgrade the U.S. debt rating even lower.**  Fitch Ratings has also raised concerns about the lack of progress seen in dealing with the financial situation. The rating company has stated that if the government does not find a way to tackle its rising debt problems then the organization may downgrade the U.S. debt rating next year after the election. Just recently, on April 5, 2012, another NRSRO, Egan-Jones, has downgraded the U.S. credit ratings even lower to AA with a negative outlook. A spokesperson for the company stated that this is the second time in nine months that they have downgraded the U.S. debt rating. The U.S. credit rating downgrade was a result of the rising debt to GDP ratio and the lack of any progress in addressing the financial problems faced by the U.S. In the face of all these warnings, it seems evident that **unless the U.S. government can come up with a realistic plan to deal with its financial situation then the U.S. credit rating will not be raised and may in fact be lowered again**. If the U.S. wants to avoid this outcome, then positive steps need to be taken.

Spending is the sole internal link to downgrade – cuts are key

Rory Cooper, Director of Strategic Communications at the Heritage Foundation, 8-8-11, <http://blog.heritage.org/2011/08/08/morning-bell-its-the-spending/>

On Friday evening, Standard & Poor’s (S&P) [downgraded the U.S. credit rating](http://www.heritage.org/Research/Reports/2011/08/US-Credit-Rating-Downgraded-Now-Theyve-Done-It) from AAA to AA+. As we and other conservatives warned, the spending reductions in the deal negotiated by President Obama to raise the debt ceiling were inadequate, and S&P reacted as we predicted but sooner. Neither Moody’s nor Fitch, two other rating agencies, have downgraded federal debt yet, but they are not providing much rosier outlooks. Decades of over-spending and over-borrowing by the federal government have damaged America’s creditworthiness. Congress after Congress, President after President, the federal government spent every penny it took in—and borrowed over $14 trillion on top of that—to try to keep happy the voters to whom the government made promises it could not afford. The government kept shifting the burden of paying the bills forward onto future generations. Well, the future has arrived, and it is bleak. Our economy is weak, millions of Americans are out of work, and America is so deep in debt that we have lost our good credit rating. Our nation needs to drive federal spending, including our ever-growing entitlement programs, down toward a balanced budget while maintaining our ability to protect America and without raising taxes. That is the sound path forward to a stronger economy with smaller government and more real jobs. The White House’s first reaction to this news was to [blame S&P itself](http://www.bloomberg.com/news/2011-08-08/obama-allies-see-tea-party-downgrade-as-they-seek-to-reassure-investors.html), claiming that their math was wrong as spokesmen pointed out S&P’s past rating failures. Correcting the math didn’t correct the problem, however, and so S&P went ahead with its downgrade. Debating S&P’s credibility misses the more important point, which is there for all to see: Projected deficit spending properly raises questions about U.S. credit quality. We cannot waste time shooting the messenger when the message itself is impossible to ignore: It’s the spending. Unsustainable entitlement programs have been built up over many Congresses and Presidents. Elected officials from both parties over many decades helped push us closer to this point. But the last chance to start correcting the problem before damage to America’s credit occurred was during the recent debate over the debt limit.

Spending = Downgrade

**Brink is now—credit outlooks already negative, new spending pushes the brink over into a credit downgrade**

Reuters 12 (“Fitch warns of U.S. downgrade if no budget deal in 2013,” Nov 28, 2011, <http://www.reuters.com/article/2011/11/29/us-usa-ratings-fitch-idUSTRE7AR28J20111129>)hhs-ps

The ratings agency on Monday revised to negative from stable the outlook on the U.S. credit rating after a special congressional committee failed last week to agree on at least $1.2 trillion in deficit-reduction measures. The committee failure made it unlikely that any meaningful deficit plan will be adopted next year, increasing the fiscal burden on the next administration that will be elected in late 2012, Fitch said. "The negative outlook reflects Fitch's declining confidence that timely fiscal measures necessary to place U.S. public finances on a sustainable path and secure the U.S. AAA sovereign rating will be forthcoming," the ratings agency said in a statement, adding that the chance of a downgrade is "slightly greater than 50 percent" now. The news had little market impact, as a negative outlook from Fitch was widely expected. "What it shows is that Fitch is putting the U.S. on warning that this cannot go on forever," said Michael Yoshikami, chief investment strategist at YCMNET Advisors in Walnut Creek, California. "The markets already assumed this was going to happen. It would be different if it was a downgrade but a negative outlook is not the end of the world." Like Moody's Investors Service, which also has a negative outlook on the U.S. Aaa rating, Fitch does not expect meaningful deficit-reduction measures in 2012, when presidential elections should exacerbate political divisions in Washington. Rival agency Standard & Poor's cut the U.S. rating to AA-plus in an unprecedented decision on August 5, citing concerns about the government's budget deficit and rising debt burden. It maintains a negative outlook on the credit.

**Spending triggers another downgrade**

Reuters 12 (Reuters, “UPDATE 2-US rating faces 2013 cut if no credible plan-Fitch ,” Jun 7, 2012, <http://in.reuters.com/article/2012/06/07/usa-rating-fitch-idINL1E8H763B20120607>)hhs-ps

(Reuters) - Fitch Ratings reiterated on Thursday it would cut its sovereign credit rating for the United States next year if Washington cannot come to grips with its deficits and create a "credible" fiscal consolidation plan. It also said it would immediately cut the credit ratings on Cyprus, Ireland, Italy, Spain and Portugal if Greece were to exit the euro zone. Additionally, all euro zone nations would have their ratings put on its negative ratings watch list, setting a six-month time frame for a potential downgrade. Europe's ongoing sovereign credit crisis undermines already below-trend growth seen in the United States, the world's biggest economy. "The United States is the only country (of four major AAA-rated countries) which does not have a credible fiscal consolidation plan," and its debt-to-GDP ratio, or how much debt it has relative to the size of the economy, is expected to increase over the medium term, Ed Parker, sovereign ratings analyst, told a Fitch conference in New York. Lower credit ratings typically lead to higher borrowing costs, putting more strain on government balance sheets already straining to cut spending without sending their economies into a tailspin. Only in the last week have European leaders broached the prospect of closer economic and political ties to overcome the crisis which has forced severe austerity budgets on Europe's citizens. German and European Union officials are looking into ways to rescue Spain's debt-stricken banks even though Madrid has not called for aid and resisted international supervision. A voter backlash returned a socialist government in France and boosted the chances for the same in Greece which could put its 130-billion-euro international bailout plan in jeopardy. Fitch revised down its credit outlook for the United States to negative in November from stable after a special congressional committee failed to agree on at least $1.2 trillion in deficit-reduction measures. At the time it said there was a chance for a U.S. downgrade in 2013, saying the failure of the committee increases the fiscal burden on the next administration

Spending = Downgrade

**Fitch maintaining US credit rating – any perceived action against deficit reduction triggers a downgrade**

Gordon 12 (By MARCY GORDON, AP Business Writer, Tuesday, Jul. 10, 2012, “Fitch Ratings keeps US at top 'AAA' credit rating,” <http://www.charlotteobserver.com/2012/07/10/3374300/fitch-ratings-keeps-us-at-top.html> )hhs-ps

WASHINGTON Fitch Ratings has retained the U.S. at its top 'AAA' credit rating but also left the outlook negative, citing the failure of Congress and the Obama administration to forge an agreement on reducing the budget deficit. Fitch says that uncertainty over federal tax and spending policies related to the so-called fiscal cliff "weighs on the near-term economic outlook" and raises the prospect of another recession. A massive budget showdown could begin after the elections in November and stretch well into next year, despite the threat of the fiscal cliff - $500 billion in impending tax increases and spending cuts. Fitch also says the burden of government debt on the economy will continue to rise and could hurt growth if an agreement isn't reached on the deficit. The major credit rating agencies have been warning for months of possible downgrades if deficit reduction isn't worked out. The sting still reverberates from Standard & Poor's move nearly a year ago cutting its rating of long-term U.S. Treasury securities by a notch from 'AAA" to 'AA+' - the first downgrade of U.S. government debt in history. On the plus side, Fitch said Tuesday that its retention of the U.S. sterling 'AAA' is based on the country's "highly productive, diversified and wealthy economy," its flexibility in monetary and exchange rates, and the dollar's status as a reserve currency around the world. In addition, the risks to the financial system and economy stemming from the 2008 crisis are "moderate and diminishing," Fitch said. The rating agency said it doesn't expect to resolve the negative outlook until late next year, assuming there aren't major new economic shocks. Fitch said it will take into account any strategy to trim the deficit that may emerge after the elections, in addition to an updated assessment of the economic and budget outlook.

#### Failure to reach a deficit deal causes downgrade

Reuters 12 (“Fitch warns of U.S. downgrade if no budget deal in 2013,” Nov 28, 2011, <http://www.reuters.com/article/2011/11/29/us-usa-ratings-fitch-idUSTRE7AR28J20111129>)hhs-ps

The so-called "Super Committee" of six Democrats and six Republicans was seen by Fitch as the last chance of an agreement before elections. Last week, however, its members announced they were unable to agree on a deficit reduction plan, setting in motion automatic cuts worth $1.2 trillion over 10 years. The cuts are designed to be split evenly between domestic and military programs. Both S&P and Moody's said on November 21 the committee's failure would have no immediate impact on their ratings. However, Moody's on November 23 warned the United States that its rating could be in jeopardy if lawmakers backtrack on the automatic cuts of $1.2 trillion due to take effect starting in 2013. In a statement issued after Fitch's decision, the U.S. Treasury said "Fitch's action is a reminder of the need for Congress to reduce the country's long-term deficit in a balanced manner and to avoid efforts that would undo the $1.2 trillion in automatic cuts negotiated last summer." Fitch is now willing to give the new government that will take office in January 2013 several months to come up with a "sound" deficit reduction plan, top credit analyst David Riley told Reuters in an interview. "Once we move to the second half (of 2013) and it looks as if a deal can't be done, then the (negative) outlook would likely result in a downgrade," Riley said. Until then, there is little change of a "material adverse shock" that would trigger an early downgrade of the U.S. rating, he said, playing down concerns about the economic impact of the euro-zone debt crisis.

### 2NC — 2nd Downgrade Key

#### A second downgrade would cause investors to shift to international investments

Adriana Reyneri, Millionaire Corner, Investor Website, 06/27/2012, [Would a New U.S. Credit Downgrade Worry the High Net Worth?, <http://www.millionairecorner.com/article/would-new-us-credit-downgrade-worry-high-net-worth>] VN

How have rumblings of a second downgrade to the U.S. credit rating affected high net worth investors? According to the latest Millionaire Corner research, the majority of Millionaires would change some of their investment strategies in response to a credit rating cut. Earlier this month Standard and Poor’s Ratings Services reaffirmed its long-term negative outlook for the U.S. credit rating and, in a statement, said it could downgrade the current AA+ long-term rating by 2014. The ratings agency issued the first-ever downgrade to the nation’s once-perfect AAA credit rating in August 2011. **Key factors contributing to this negative outlook are the nation’s debt burden and the waning effectiveness of policymakers and political institutions**, according to the S&P statement, which predicts little will change as a result of the 2012 presidential election. (Millionaire Corner research shows the economy is the biggest factor for affluent investors selecting a new president) How would high net worth investors respond to another downgrade? A large share of high net worth investors do not appear concerned by the prospect, according a Millionaire Corner survey conducted in June, which shows that more than 47 percent of Millionaires would not alter their investment strategies in response to a downgrade. (Millionaire Corner research also shows that investor confidence among Millionaires has reached a five-month low due to concerns on the economy.) But, a drop in the U.S. credit rating would prompt most high net worth investors to take some sort of action. More than one-third (35 percent) of high net worth investors said they would consult with a financial advisor or other expert to “know what to do” in the event of a downgrade. And, 20 percent said they would invest more conservatively. A small percentage (4 percent) would allocate more assets from domestic to foreign holdings, and a few (3 percent) would buy more Treasury bonds. Close to 2 percent said a downgrade would prompt them to sell their Treasuries. The first U.S. credit downgrade had a sobering effect on high net worth investors surveyed by Millionaire Corner at the end of 2011. More than 80 percent of investors with a net worth of $5 million to $25 million said they would invest more conservatively as a result of the downgrade, and 10 percent of these high net worth individuals said they would invest more internationally.

#### Further downgrades will cause a double dip

Gabriel 11 Michael Gabriel, writer for Vitaver and Associates, Inc., 8/1/11, “How the Recent U.S. Credit Downgrade Can Affect Job Hiring,” Vitaver and Associates, Inc., http://www.vitaver.com/blog/2011/08/recent-us-credit-downgrade-affect-jobs/

Just like that, the United States’ credit rating has dropped from AAA to AA+, according to Standard and Poor’s. Though AA+ isn’t bad at all, since it means that the country still has a strong capability to meet its financial obligations, nothing still beats triple A, and a downgrade isn’t really something you’d expect from a superpower such as America. Needless to say, a downgrade can be a prelude to a more negative economic outlook, worse a double-dip recession. This may also mean that other credit rating agencies such as Fitch Group and Moody’s may follow suit, further propelling the country down. Since all factors in economics are interdependent, you can surely expect some changes in the way businesses work and hire workers. Though a lot of reports suggest that thousands of people have been actually hired and that there’s a reduction in unemployment claims, many things could happen between today and tomorrow. These include the following scenarios: 1. Companies may freeze hiring. They may try to implement the “wait and see” attitude. Although many organizations won’t terminate thier employees, they may stop getting new hires until they can surely feel that the economy starts to pick up. 2. Businesses may become choosy. Firms across the US will try their best to reduce their overhead expenditures as much as possible. One of the possible steps they might take is to avoid hiring fresh graduates or those who lack experience. Training can cost a lot of money for companies, especially for start-ups. 3. Enterprises may decide to look for workers elsewhere. To be more specific, they may opt to outsource a lot of jobs to telecommute or home-based workers (both local and international). This can be both a good and a bad thing for you. It’s ideal since you’ll have more time at home. You can make the most out of your utilities, such as your phone and Internet connection, as well as spend less on outdoor expenses. However, home-based jobs may also make things unstable. Unless you have a contract from the company, the business owner has the prerogative to kick you out or lay you off even without the typical 30 days’ notice. 4. Organizations may lay off employees. This is something that should be avoided. Businesses should continue to operate in order to keep the economy going. However, if things take a much worst turn, such as getting more downgrades from other agencies, companies may simply decide to lay off employees while it’s still early. It also doesn’t help that Europe, one of America’s biggest markets for exports and imports, is also experiencing its own economic troubles. 5. Companies may do nothing at all. A common effect of a downgrade is an increase in interest rates. This way, the government can gather more money to pay off debts. Fortunately, the Federal Reserves has already announced that it’s going to keep interest rates low for the next two years. If businesses are happy with that, or if they believe they have good leaders and committed government agencies, they may just continue on with their normal operations, with hardly any changes.

#### A second downgrade would cause investors to shift to international investments

Adriana Reyneri, Millionaire Corner, Investor Website, 06/27/2012, [Would a New U.S. Credit Downgrade Worry the High Net Worth?, <http://www.millionairecorner.com/article/would-new-us-credit-downgrade-worry-high-net-worth>] VN

How have rumblings of a second downgrade to the U.S. credit rating affected high net worth investors? According to the latest Millionaire Corner research, the majority of Millionaires would change some of their investment strategies in response to a credit rating cut. Earlier this month Standard and Poor’s Ratings Services reaffirmed its long-term negative outlook for the U.S. credit rating and, in a statement, said it could downgrade the current AA+ long-term rating by 2014. The ratings agency issued the first-ever downgrade to the nation’s once-perfect AAA credit rating in August 2011. **Key factors contributing to this negative outlook are the nation’s debt burden and the waning effectiveness of policymakers and political institutions**, according to the S&P statement, which predicts little will change as a result of the 2012 presidential election. (Millionaire Corner research shows the economy is the biggest factor for affluent investors selecting a new president) How would high net worth investors respond to another downgrade? A large share of high net worth investors do not appear concerned by the prospect, according a Millionaire Corner survey conducted in June, which shows that more than 47 percent of Millionaires would not alter their investment strategies in response to a downgrade. (Millionaire Corner research also shows that investor confidence among Millionaires has reached a five-month low due to concerns on the economy.) But, a drop in the U.S. credit rating would prompt most high net worth investors to take some sort of action. More than one-third (35 percent) of high net worth investors said they would consult with a financial advisor or other expert to “know what to do” in the event of a downgrade. And, 20 percent said they would invest more conservatively. A small percentage (4 percent) would allocate more assets from domestic to foreign holdings, and a few (3 percent) would buy more Treasury bonds. Close to 2 percent said a downgrade would prompt them to sell their Treasuries. The first U.S. credit downgrade had a sobering effect on high net worth investors surveyed by Millionaire Corner at the end of 2011. More than 80 percent of investors with a net worth of $5 million to $25 million said they would invest more conservatively as a result of the downgrade, and 10 percent of these high net worth individuals said they would invest more internationally.

2nd Downgrade Key

#### A second downgrade will increase borrowing costs and kill confidence

Mike Dorning, John Detrixhe and Ian Katz, Bloomberg Press, 07/16/’12, [Downgrade Anniversary Shows Investors Gained Buying U.S., <http://www.bloomberg.com/news/2012-07-16/downgrade-anniversary-shows-investors-gained-buying-u-s-.html>] VN\

Still, the possibility of another downgrade will weigh on policy makers, said William Daley, Obama’s former White House chief of staff. Even though Treasury yields fell, “consumer confidence dropped dramatically after the downgrade, and do we really want to test that again?” he said. The Conference Board’s Consumer Confidence index plunged from 59.2 in July 2011 to 45.2 in August in the wake of the debt standoff and credit downgrade. The index didn’t recover to its July level until December. Growth in consumer spending slowed from 0.8 percent in July of last year to 0.1 percent in August before rebounding to 0.7 percent in September. Investors in America Romney, speaking to reporters in Concord, New Hampshire, three days after the downgrade, said the ratings cut “has a consequence not only for our borrowing cost long-term, but also for the ability of America to have the confidence of people around the world as investors in America.” Glenn Hubbard, a Romney economic adviser, said in a July 12 telephone interview that the Republican candidate “was and is absolutely right.” Flight of capital out of Europe, a slowing world economy and the Fed’s program of replacing holdings of short-term debt with longer-term securities have obscured the impact of the downgrade, he said. Ryan, a Wisconsin Republican, also defended his warning, saying interest rates haven’t gone up only because so many other nations are in such bad shape. Save Haven “We are a safe haven for now” for investors because of Europe’s debt crisis, Ryan said in an interview. Rates will rise, he predicted. “We just don’t know when, and I don’t want to tempt fate.”

#### Further downgrades will spook investors

Reuters 11 Reuters, 8/19/11, “Does a downgrade cost anything?,” Reuters, http://blogs.reuters.com/muniland/2011/08/19/snapshot-does-a-downgrade-cost-anything/

The debt of the United States was downgraded by Standard & Poor’s several weeks ago, but the price of U.S. Treasuries have skyrocketed since then. This confuses many people because a baseline relationship in the fixed-income markets is that lower-rated, less-creditworthy bonds will be relatively cheap and investors will demand higher interest rates to compensate for additional risk.To see this bond market truism, it’s much more instructive to look at the downgrade of the debt of New Jersey. Fitch lowered the state’s credit rating Wednesday citing heavy debt and benefit obligations. This followed downgrades by Moody’s and S&P earlier in the year. Municipal bond and credit default swap markets didn’t like this third downgrade and did what you would expect them to do: they required more yield in the case of cash bonds and more payment in the case of credit default swaps. The graph above charts muni CDS prices for New Jersey (data supplied by Markit). You can see the move up in CDS prices began in June when Governor Christie and the state legislature made the final run to their agreement on the fiscal 2011 budget, which began on July 1. The uncertainty and contentiousness of the process must have spooked investors and dealers. The most widely-used measure of credit risk for municipal bonds is the Thomson Reuters Municipal Market Data (MMD) AAA GO Scale. MMD’s Daniel Berger in his daily note talks about how New Jersey bonds got riskier and cheaper ahead of the downgrade and suggests that cash-bond selling started happening ahead of the Fitch downgrade. New Jersey has approximately $31 bln of appropriation backed-debt and $2.6 bln in GO [general obligation] debt. The spread of New Jersey’s 10yr GO bonds has steadily risen this past week and closed last night at +47bps to MMD’s AAA GO scale. Last Friday this spread was +40bps. It looks as if traders were anticipating this move by Fitch and this confirms our thesis that spreads are a leading indicator of credit. For the latest 12-month period this spread averaged +56.3bps which ranks sixth highest among the states actively monitored by MMD. The MMD chart perfectly shows how traders and investors responded to rating downgrades and how they demanded higher interest rates starting September 22, 1010. This was the date that Moody’s put New Jersey on “negative outlook,” the advance notice of a possible downgrade. The long, flat, tabletop-like area is the period of market confusion following Meredith Whitney’s pronouncement of default doom. Markets settled down after that with a decline in New Jersey’s risk profile before turning up again ahead of Fitch’s downgrade. MMD data on cash bonds and Markit data on municipal CDS don’t track each other perfectly but they both show the market demanding higher interest rates on New Jersey’s debt and higher prices on default insurance with each downgrade. It’s a snapshot of the cost of increased risk. Downgrades do cost something.

2nd Downgrade Key

Downgrades will end the dollar

Erik Wasson, The Hill, 10/24/’11, [Fears of another US credit downgrade are growing on Wall Street, <http://thehill.com/homenews/house/189497-fear-of-another-downgrade-sparks-worry-on-wall-street>] VN

Wall Street is growing nervous about the congressional supercommittee amid warnings from major banks that failure to reach a deal could lead to another downgrade of U.S. debt. The bipartisan, 12-member panel has only until Nov. 23 to find at least $1.2 trillion in deficit cuts. Failure to strike a deal could rattle confidence in Washington and depress stock prices well into 2012, analysts say. Fitch Ratings, one of the three major credit raters, said in August that failure by the supercommittee to agree to a $1.2 trillion deficit-reduction package “would likely result in negative rating action.” There have been no signs of progress from the secretive talks thus far. Sources close to the panel say members are deadlocked on basic questions about what policy issues to address and what budget scenarios to use. In its outlook for this week, Bank of America Merrill Lynch said it “expects” a downgrade by one of the three credit agencies “when the supercommittee crashes.” Those analysts said the “not-so-super” committee is “very unlikely to come up with a credible deficit-reduction plan” because it is “hard to imagine” Democrats cutting entitlements or Republicans agreeing to tax increases. Supercommittee members are feeling the heat from Wall Street, aides said, and know the markets are watching their every move. “The potential threat of another credit downgrade underscores the need for the committee to reach a bipartisan agreement that helps create jobs and reduces the deficit in a balanced way,” committee member Rep. Chris Van Hollen (D-Md.) said when asked via email about the pressure from Wall Street. Banks are monitoring the supercommittee for fear of a Washington-driven market shock like the one that hit in August, when Standard & Poor’s downgraded U.S. bonds. That decision sent stocks spiraling and preceded a month of heavy losses for investors. The Bank of America report predicts that the impact of another downgrade would be less than the 7 percent drop that came after S&P’s move in August, though the consequences for markets would linger into next year. There have been signs of a market rebound in recent weeks despite the troubles in the economy and the European debt crisis. The S&P index reached positive territory for the year Monday, and the Dow Jones index inched closer to 12,000. But the bull market could be short-lived if the supercommittee comes up empty-handed. In its weekly analysis Friday, Deutsche Bank said the supercommittee report is “perhaps” the most important issue facing the markets. “The fiscal calendar is likely to be a source of considerable volatility,” the report warned. If the deficit panel fails to meet its goals, automatic cuts to defense and nondefense spending will begin in 2013. But Wall Street fears Congress will be tempted to remove the “triggers” if the supercommittee fails, wiping out the second round of deficit reduction in the debt-ceiling deal and putting the nation at risk of another downgrade. Moody’s Investors Service analyst Stephen Hess confirmed to The Hill on Monday that a failure of the supercommittee would be a factor in re-evaluating the U.S. credit rating. He said Moody’s is “agnostic” on whether spending cuts, taxes or the trigger are the best path to deficit reduction. “For us, the composition is less important than the actual magnitude [of the cuts],” Hess said. In the aftermath of the standoff over the debt ceiling, S&P lowered the U.S. credit rating from AAA to AA+ with a negative outlook — leaving open the possibility of a further downgrade. S&P made clear that the inability of Congress to deal with the nation’s fiscal problems prompted the rating dip. The decision was met in Washington with another round of finger pointing from Democrats and Republicans over which side was to blame. Despite the partisan atmosphere, Goldman Sachs expressed optimism that the supercommittee is on track for a deal, saying in its weekly outlook that an “agreement of some type is the most likely scenario.” Goldman nonetheless cautioned there remains “the potential for a downside surprise.” **“While also possible, it is much harder to see an agreement reaching or exceeding the $1.2 trillion target,” Goldman political analyst Alec Phillips wrote. “Further sovereign downgrades remain a significant risk.”**  Morgan Stanley wants to see Washington agree on stimulus measures to pump up the economy and said the market is looking at the supercommittee for signs that Washington can get things done. But it said in its outlook for the week that the supercommittee appears to be in “gridlock” and that “failure of the supercommittee would also make it more difficult to find a path forward for consideration of fiscal stimulus next year.” Michael Cembalest, chief investment officer for JP Morgan Chase, wrote that **failure by the group could even herald the end of the dollar as a reserve currency.**

2nd Downgrade Key

#### Another downgrade would force investors to sell T bills

Rob **Curran** (Reporter at Dow Jones Newswires, Dow Jones, 10/**11**, The Dow Jones Newswires)

JUST as Europe's sovereign debt storm is clearing up somewhat, investors see a day of reckoning for US debt on the horizon. Ethan Harris, North American chief economist for Bank of America/Merrill Lynch, has set the cat among the pigeons by saying that his firm expected another downgrade of Treasuries in November or December. That's when the 'supercommittee', the legislators appointed by President Barack Obama to make recommendations on more than US$1 trillion in deficit cuts to the broader Congress, is expected to publish its recommendations. Or, in Mr Harris's words, that's when the deadlocked committee 'crashes'. If that happens, a downgrade could follow. And a downgrade could spell trouble. When Standard & Poor's downgraded Treasuries in the summer, it threw the markets into a downward spiral. Now all eyes are on Moody's Investors Service and Fitch Ratings, the two other internationally recognised credit ratings agencies, which will both review their ratings after the supercommittee process. While Fitch is unlikely to downgrade because it has not put the US on any kind of watch, Moody's does have a negative outlook on Treasuries. Mr Harris is not the only one pessimistic about the chances of a 'super' compromise in Washington. 'I'd like to think it's going to happen but I'm not a believer in their ability to find common ground, especially leading up to an election year,' said Jeffrey Pavlik, the principal of Pavlik Capital Management, a hedge-fund firm in Chicago. The main question is not whether the downgrades come but how the Treasury markets react to whatever transpires, said Axel Merk, president and chief investment officer of investment firm Merk Funds. Investors were terrified by the S&P downgrade because they thought it would cause a spike in interest rates as international investors dumped their US debt holdings. Those fears didn't materialise. It might be days or years away but the spike will come, said Mr Merk. That's because a spike in interest rates is the only thing that will break the political deadlock over tax rates and entitlement programmes such as Social Security, he said. 'As we learned in Europe, the only language the policy makers understand is that of the bond market,' he said. 'Unless the bond market misbehaves, you're not going to get a reaction.' Still, he added: 'I'm not sure the downgrade is the catalyst.' Investors may continue to buy Treasuries after another downgrade because of continued hints from the Federal Reserve about another round of quantitative easing, when the central bank buys Treasuries. Or investors may continue to buy Treasuries because they are the best of a bad lot of sovereign bonds, said Mr Pavlik. He said a friend of his invests in real estate in California's depressed Orange County market. As high credit ratings became increasingly rare among home buyers in Southern California, mortgage lenders had no choice but to lower their standards on credit scores. Similarly, in sovereign bonds, Mr Pavlik believes 'Double A is the new Triple A'. If Germany and France take on massive debts to save the euro, they will likely face downgrades, too. At that point, there would be very few significant sovereign bond issuers left with the Triple A ratings. 'If the top 5 are Double A instead of Triple A, you're still going to put your money somewhere, you're still going to buy bonds,' said Mr Pavlik. For him, the main risk of a market selloff from another downgrade comes from a technical issue. Many mutual fund, money-market, insurance company and pension-fund charters only allow the managers to buy Triple-A rated issues. The definition of Triple A in these charters is based on the average of the three major ratings agencies. While the Federal Reserve may be able to exempt US funds from their charters, according to a report on Forbes magazine's website, overseas funds with such charters may be forced to sell Treasuries in the event of another downgrade. The respite from the European bond-market storm - if there is a respite - may be brief.

2nd Downgrade Key

#### Even the threat of additional downgrade will cause credit to dry up

Jeffery **Mans** (Associate Professor of Law at George Washington University, The International Tribune 8/**11** The revenge of the rating agencies) <http://www.lexisnexis.com/hottopics/lnacademic/?>

The credit rating agencies are taking advantage of America's financial problems to increase their own political power. They want to ensure that regulators do not reduce their autonomy and influence. Their strategy is brilliant. They are not piling on all at once by downgrading the United States in concert. Standard & Poor's is the bad cop for now, taking the first swipe at the United States last Friday, and seeing its influence confirmed by the stock market's dramatic reaction. Moody's and Fitch are playing the good cop - exercising restraint about a potential downgrade, yet still flexing their muscles by criticizing the government both publicly and behind the scenes. The rating agencies have the federal government over a barrel. If politicians ignore the rating agencies' warnings, they risk a withering assault of additional downgrades that could undercut confidence in the government and inflict soaring interest rates. The good-cop, bad-cop routine is especially potent because a downgrade by two of the three major rating agencies could lead to negative consequences, such as requiring some bond issuers to secure additional collateral. Since the 1970s, federal statutes and regulations have mandated that debt issuers obtain ratings as evidence of creditworthiness. An oligopoly of rating agencies used this authority to effectively control access to the financial system. Even a threat of a downgrade from a rating agency could cause credit to dry up, and few inside or outside of Washington dared to challenge their dominance. The financial crisis jeopardized the agencies' privileged position. Politicians and pundits accused them of being asleep at the wheel, if not complicit with issuers, in camouflaging risks and misleading investors during the run-up to the subprime mortgage crisis. The Dodd-Frank Wall Street reform law, enacted a year ago but not fully implemented yet, threatened to introduce unprecedented oversight and regulation. The law called for exposing rating agencies to civil liability in securities lawsuits if their ratings were inaccurate. It also challenged the oligopoly's dominance by calling for the Securities and Exchange Commission to explore the feasibility of having an independent organization select rating agencies for asset-backed securities, instead of having the bond issuers select and pay the agencies, as they now do. But the rating agencies struck back, first through civil disobedience. To evade potential liability, they threatened to freeze the markets for asset-backed securities by refusing to allow their ratings to be quoted in S.E.C. filings. The S.E.C. quickly caved and suspended the rule. Meanwhile, the rating agencies have begun a guerrilla campaign of behind-the-scenes lobbying to weaken the commission's efforts to carry out other parts of Dodd-Frank. The S.& P. downgrade has elevated this simmering standoff to an overt clash. Politicians will be tempted to wave a white flag by granting the agencies a pass from tough regulation in exchange for the agencies' not downgrading federal debt further. While that approach may give the United States breathing room in the short run, the government should not give in to such extortion. Instead, politicians must take the hard medicine of a downgrade in stride and get America's house in order, because the country faces ruin if the budget imbalances continue, regardless of what rating agencies say. At the same time, they should not forget the rating agencies' role in the crisis and allow these monitors of creditworthiness to revert to their pre-crisis ways of lax ratings and blindness to deception.

### 2NC — Downgrade Kills the Economy

another downgrade would have devastating consequences for the economy -that's rowley 12

#### nuclear weapons would be triggered by a collapse of the global financial system- causing war - that's merlini 11

#### Downgrade causes new recession—spikes interest rates and drops dollar value

Manier 11 George Maniere, contributor to Seeking Alpha, 7/28/11, “U.S. Debt Downgrade and Its Consequences Too Close for Comfort,” Seeking Alpha, http://seekingalpha.com/article/282627-u-s-debt-downgrade-and-its-consequences-too-close-for-comfort

Despite what you may have heard in the media let me clarify something, the probability of the U.S. defaulting on its debt is very low. The probability of the credit rating getting downgraded grows with every minute. The consequences of a lowering of our credit rating would have disastrous effects. A downgrading of our “AAA” credit rating would mean higher interest rates and subsequently higher costs not only for the U.S. debt but for home loans, credit card rates, student loans and loans to small businesses. The cost of borrowing money would skyrocket for consumers and businesses alike. Likewise, states and municipalities would also face higher borrowing costs. The cost of all capital projects like road repairs, water systems, hospitals and schools would become much more expensive. The ensuing credit crunch would lead to higher borrowing costs for all and we would find ourselves back in March of 2008, only this time we would be 14 trillion dollars deeper in debt. Add to this, with the dollar already in a year-long slump it would continue to sink against the other world’s currencies. S&P has estimated that a downgrade would cause the dollar to drop 10% or more in value. And a downgrade would cause the dollar to lose its status as the world’s reserve currency, an event that would be catastrophic for the U.S. economy. Combine all of the factors above and I think you will conclude as I have that the already shaky economy would implode. A recession would return - but this time with a vengeance. If Congress cannot get a measure passed in 6 short days I see the economy sinking even lower than it did in 2008 – 2009. The worst part of all is that this scenario would cause the global markets to freeze up and make the failure at Lehman Brothers look like a day at the beach.

#### A downgrade would ripple throughout the monetary system and kill the dollar

The Washington Post, News Source, 11 (April 19th 2011, “U.S. credit rating downgrade: the Armageddon scenario,” http://www.washingtonpost.com/blogs/political-economy/post/us-ratings-downgrade-the-armageddon-scenario/2011/04/19/AFnE0n5D\_blog.html)

A credit rating downgrade for the United States would spell even more financial trouble for the U.S. government, hampering its ability to borrow money as investors demand higher yields to make up for the increased risk. That would cause its national debt to balloon further and increase the need to hike taxes or make even more painful cuts in spending. But the real Armageddon scenario would occur when the impact of a sovereign downgrade hit the rest of the U.S. economy. The U.S. “risks eroding its standing at the core of the global monetary system,” Mohamed El-Erian, chief executive and co-chief investment officer at PIMCO, wrote in a commentary piece for the Financial Times. Pension funds and investment trusts that are bound by covenant to invest only in AAA-rated debt could be forced to dump U.S. holdings. Banks that do the bulk of their business in the U.S. could themselves face downgrades. Eventually, the dollar could lose its status as the world’s reserve currency. The ripple effects of Standard & Poors’ decision to downgrade its outlook for the U.S. were already spreading on Monday. The agency also downgraded its outlook for five AAA-rated U.S. insurance groups: Knights of Columbus, New York Life Insurance, Northwestern Mutual Life Insurance, Teachers Insurance & Annuity Association of America and United Services Automobile Association. In downgrading their outlook from stable to negative, S&P noted that these companies are “constrained by the U.S. sovereign credit rating because their businesses and assets are highly concentrated in the U.S.” S&P analyst David Zuber and his colleagues wrote that they took into account “direct and indirect sovereign risks—such as the impact of macroeconomic volatility, currency devaluation, asset impairment, and investment portfolio deterioration.” How likely is this nightmare scenario to happen? There are 19 sovereigns rated AAA by the S&P. Of those, only the United States has a negative outlook. There are a number of countries that have lost AAA ratings over the past 20 years—including Canada, Denmark, Finland and Sweden—but they ended up regaining them. Goldman Sachs analyst Alec Phillips wrote in a research note on Tuesday that while he agrees with S&P that the “current trajectory of fiscal policy is unsustainable over the long-term” and that the U.S. “already appears to be on the edge of AAA territory,” he has a somewhat more optimistic view of the U.S. situation over the next few years and assumes that some fiscal tightening is likely to occur.

Downgrade Kills the Economy

#### A credit downgrade will ultimately have disastrous results

Kevin D. Williamson, 7/19/11, deputy managing editor of the National Review, “The Democrat Downgrade: Reality and Repercussions”, http://www.nationalreview.com/exchequer/272257/democrat-downgrade-reality-and-repercussions

The direct consequences of a downgrade of Uncle Sam’s credit on U.S. public finances would be pretty bad. But, as with natural disasters, the aftershocks of this man-made catastrophe might prove more devastating than the main event. In this case, imagine a tsunami of rolling corporate downgrades following the earthquake of a Treasury downgrade, a run on the banks, a discredited FDIC, frozen money-market funds, and a plunging dollar. It’s not Beijing that’s going to take it in the shorts — it’s our still-fragile financial system. Standard & Poor currently gives AAA ratings to six major insurance companies: New York Life, Northwestern Mutual, etc. Those companies already are on the watch-list for a downgrade, simply because of their extensive holdings of U.S. Treasury securities — regardless of the fact that Treasuries themselves have not yet been downgraded. Many banks could find themselves downgraded as well, just because of all the U.S. government debt on their balance sheets. One of our old friends from the bailout days, the AAA-rated Temporary Liquidity Guarantee Program, could get downgraded as well, along with Fannie Mae, Freddie Mac, the Federal Home Loan Banks, and, critically, the FDIC. And Fannie and Freddie still prop up a bunch of mortgage-backed securities. What happens to them? Here’s what Fitch says: “Ratings on bonds with direct credit enhancement provided by Fannie Mae, Freddie Mac, or other GSEs would generally reflect the ratings of the credit enhancement provider.” In English: If the government isn’t AAA, nothing that the government backs is AAA, either. Fitch also warns that money-market funds could face “liquidity pressure,” something to keep in mind if there’s a run on downgraded banks backed by a downgraded FDIC. So, who’s who in this world of hurt? The ten major holders of U.S. Treasury debt are, in order: 1. the Fed, which has more than doubled its holdings of U.S. sovereign debt in the past few years; 2. individual investors, mostly in the United States; 3. the Chinese; 4. the Japanese; 5. pension funds; 6. mutual funds; 7. state and local governments; 8. the Brits; 9. the banks; and 10. insurance companies. (More here.) The national governments have worries of their own already — some of them are in pretty dire straits (the Japanese national debt is 200 percent of GDP) and some of their situations are basically unknowable (China). God alone knows what the Fed will do. Even if the banks and insurances companies don’t get downgraded, a Treasury downgrade is still going to be enormously disruptive to their businesses. Typically, regulated financial institutions are required to hold “investment grade” assets, which does not limit them to AAA bonds. AA is still “investment grade.” So they don’t have to dump all their Treasuries. (Which is not to say they won’t.) But capital-requirement rules — which govern the amount of money a financial institution has to hold in reserve — naturally take into account whether bonds are AAA, AA, or something else. That’s because $1 worth of Exxon debt is not really worth the same thing as $1 worth of debt from Barney’s Subprime Bait-’n’-Tackle, and $1 million in Swiss bonds is not the same thing as $1 million in Haitian bonds. A downgrade of U.S. Treasuries would mean that basically every bank and insurance company of any stature would immediately have to raise a great deal of capital to offset the downgrade of the more than $1 trillion worth of U.S. Treasury debt they are holding. They’ll have to try to raise that capital in a market suffering a jacklighted panic over that sovereign downgrade, scrambling for investment in an environment in which the U.S. government is no longer considered a gold-plated, top-shelf safe haven. In terms of a “credit event,” that’s probably going to make 2008 look like a day relaxing upon the sandy beaches of Calais with tropical-themed umbrella-garnished drinks. State and local governments are holding another $1 trillion or so in Treasuries, meaning that the credit profile of our already struggling states and cities would have about as much credibility as Dominique Strauss-Kahn’s wedding vows. A lot of that pension-fund exposure to Treasury debt is for state and local government retirees, too, so Austin and Sacramento and Boise and Augusta will be right between the hammer and the anvil, getting pounded. And so will Springfield — the Typhoid Mary of fiscal contagion at the state level. As I’ve written before, I suspect that Illinois will be the first state to go into something like a full-blown insolvency, largely due to its unfunded pension liabilities. Just Monday, Ben Bernanke confessed himself worried about the situation in Illinois and California. And if I may be forgiven for repeating myself: Most states have either statutory or constitutional obligations to pay those pensions, so they cannot just reduce them or walk away. There’s really no such thing as a state-bankruptcy law, so nobody knows how a default would unfold. How’s that for uncertainty in the markets? Back to those banks and insurance guys: Contrary to what our dear leaders in Washington have claimed, the world’s financial system has not been reformed. In fact, a great deal of the bailouts and the legislation that followed them was designed specifically to prevent the kind of fundamental reforms that are needed. A global financial system brought to its knees by a raft of bad mortgages is going to be knocked ass-over-teakettle by a downgrade of U.S. Treasury debt.

## \*\*\*Other Spending Bad \*\*\*

### Spending Bad – General

#### US deficit spending hurts the global economy

Chris Kitze, writer for the Market Oracle, ’11 (March 10 2011, “Signs of Impending Doom for Global Economy 2011,” http://www.marketoracle.co.uk/Article26811.html)

Meanwhile, the United States is also covered in a sea of red ink and the economic situation in the largest economy on earth continues to deteriorate rapidly. It is as if the entire world financial system has caught a virus that it just can't shake, and now it looks like another massive wave of financial disaster could be about to strike. Does the global economy have enough strength to weather a major oil crisis in 2011? How much debt can the largest nations in North America and Europe take on before the entire system collapses under the weight? Will 2011 be a repeat of 2008 or are we going to be able to get through the rest of the year okay? Only time will tell. But it is quickly becoming clear that we are reaching a tipping point. If the price of oil keeps going up, all hopes for any kind of an "economic recovery" will be completely wiped out. But if the globe does experience another economic slowdown, it could potentially turn the simmering sovereign debt crisis into an absolute nightmare. The U.S. and most nations in Europe are having a very difficult time servicing their debts and they desperately need tax revenues to increase. If another major economic downturn causes tax revenues to go down again it could unleash absolute chaos on world financial markets. The global economy is more interconnected than ever, and so a major crisis in one area of the world can have a cascading effect on the rest of the globe. Just as we saw back in 2008, if financial disaster strikes nobody is going to escape completely unscathed.

#### Failure to reduce the deficit kills the economy – increased interest rates, crowd out, and loss of investor confidence

National Commission on Fiscal Responsibility and Reform ’10 (12/1/10, “The Moment of Truth: Report of the National Commission on Fiscal Responsibility and Reform,” pg online @ lexisnexis)

Federal debt this high is unsustainable. It will drive up interest rates for all borrowers - businesses and individuals - and curtail economic growth by crowding out private investment.By making it more expensive for entrepreneurs and businesses to raise capital, innovate, and create jobs, rising debt could reduce per-capita GDP, each American's share of the nation's economy, by as much as 15 percent by 2035. Rising debt will also hamstring the government, depriving it of the resources needed to respond to future crises and invest in other priorities. Deficit spending is often used to respond to short-term financial "emergency" needs such as wars or recessions. If our national debt grows higher, the federal government may even have difficulty borrowing funds at an affordable interest rate, preventing it from effectively responding. Large debt will put America at risk by exposing it to foreign creditors. They currently own more than half our public debt, and the interest we pay them reduces our own standard of living. The single largest foreign holder of our debt is China, a nation that may not share our country's aspirations and strategic interests. In a worst- case scenario, investors could lose confidence that our nation is able or willing to repay its loans - possibly triggering a debt crisis that would force the government to implement the most stringent of austerity measures.

#### Spending Increases perpetuate recession – we’re already beyond our means

Israel Ortega, Editor of the Spanish Page of the Heritage Foundation, ’11 (The Heritage Foundation, April 22nd 2011, “Time to Face Economic Reality,” http://www.heritage.org/Research/Commentary/2011/04/Time-to-Face-Economic-Reality)

Here are the official government numbers. According to the Department of the Treasury, our current total public debt is more than $14 trillion. Our public debt represents the sum of how much we currently owe to other financial institutions and foreign countries. To give you a sense of what $14 trillion looks like, imagine filling the entire Estadio Azteca in Mexico City (with a capacity of 104,000) with $100 bills from the bottom to the brim.This staggering debt is a burden to every single American. It’s also a sobering reminder that we are spending beyond our means. And yet, powerful voices are asking us to ignore the perilous reality and fight to increase federal spending at every turn. This hysteria was evident in Congress’ recent battle over last year’s budget spending bill when politicians calling for necessary spending cuts were labeled heartless and cruel. The irony of the recent debate is that it was dealing with only a fraction of our entire federal budget, and it pales in comparison to what’s necessary to get our financial house in order. The truth is that the federal government will need to exercise even more financial restraint if we are to ensure that our economy can get out of this recession and remain competitive in the global market.

Spending Bad – General

#### Gov’t spending hurts the economy, not the other way around – 4 independent studies go neg

Clemens et. al(Director of Research at the Pacific Research Institute) October 2010

(Jason, Niels Veldhuis is the Fraser Institute President and one of Canada’s most-read private-sector economists, Julie Kaszton is a research fellow at the Pacific Research Institute, “No Bang for the Taxpayer’s Buck: Why California Must Reform Spending and Trim Government,” http://www.pacificresearch.org/docLib/20101013\_CAProsp\_3\_F%284%29.pdf)

Similarly, Stefan Folster and Magnus Henrekson examined data from 1970 to 1995 and found a negative relationship between government spending and economic growth in OECD countries.23 They concluded that a 10-percent increase in government spending as a percent of GDP decreased economic growth by 0.7 to 0.8 percentage points.24 Internationally renowned fiscal policy expert and Harvard professor Alberto Alesina and his colleagues investigated the effects of large changes in government fiscal policy on business investment.25 Their 2002 study, published in the prestigious *American Economic Review,* examined 16 OECD countries from 1960 to 1996 and found a negative relationship between increased government spending and private sector investment, a critical determinant of economic growth. In addition, they found that fiscal stabilizations (when countries stabilize and reduce their debt-to-GDP ratios through spending reductions or tax increases) that led to economic growth consisted mainly of spending cuts while those associated with downturns were characterized by tax increases. These findings confirm the powerful relationship between the size of government and economic growth. Several recent studies buttress these conclusions. In a 2008 study for the European Central Bank, Antonio Afonso and Davide Furceri examined the effect of government size (pending and revenues as a percent of GDP) on per person economic growth for 28 OECD countries and a small subset of 15 EU countries from 1970 to 2004.26 The results suggest that total revenue and total expenditures negatively impact real growth of per person GDP both for the OECD and the EU countries.27 In particular, the authors found that a 10 percentage point increase in the share of total expenditures would decrease output by 1.2 and 1.3 percentage points respectively for the OECD and EU countries. Afonso and Furceri concluded that relevant policy implications can be garnered from the results; most notably, cuts in government consumption and subsidies will contribute positively to economic growth.28 Similarly, a 2009 study by Minnesota State University professor Atrayee Ghosh Roy examined the impact of the size of government on economic growth in the United States from 1950 to 1998.29 Ghosh Roy found that the size of government (government spending as a share of national income) had a direct and negative effect on economic growth. She found that a 10 percentage point increase in government expenditures as a percent of GDP decreased economic growth by 1.9 percentage points. The author concluded that the result “underscores the importance of reducing the size of the government in the United States.” Most recently, Andreas Bergh and Martin Karlsson in a 2010 paper examined the relationship between the size of government and economic growth for a sample of “rich” countries over the period 1970 to 2005.31 Using two measures of government size, total tax revenue and total expenditures as a share of GDP, the author found that a large government is negatively related to economic growth.

Spending Bad – General

#### Budget deficits are harmful and slow economic growth—5 reasons

Brookings Institution 04 The Brookings Institution, an independent organization devoted to nonpartisan research, education, and publication in economics, government, foreign policy, and the social sciences, Jan 2004, Edited by Alice M. Rivlin and Isabel Sawhill, “RESTORING FISCAL SANITY: HOW TO BALANCE THE BUDGET,” The Brookings Institution, http://www.brookings.edu/es/research/projects/budget/fiscalsanity/full.pdf

This book argues that deficits matter a lot and that better policies are possible and urgently needed. Not all budget deficits are harmful—indeed, recent deficits have ameliorated the recession that began in 2001. However, large persistent deficits weaken the economy and lower family incomes. The authors also believe that passing on large and unnecessary fiscal burdens to future generations is unfair and irresponsible. More specifically, deficits are harmful for five reasons: —They slow economic growth. By 2014, the average family’s income will be an estimated $1,800 lower because of the slower income growth that results when government competes with the private sector for a limited pool of savings or borrows more from abroad. —They increase household borrowing costs. A family with a $250,000, thirty-year mortgage, for example, will pay an additional $2,000 a year in interest. —They increase indebtedness to foreigners, which is both expensive and risky. The United States is the largest net debtor in the world. The income of Americans will ultimately be reduced by the interest, dividends, and profits paid to foreigners who have invested in the United States. Moreover, if foreigners lose confidence in the American economy—or begin to worry that we are not managing our fiscal affairs responsibly—they may reduce their investment here. This can reduce the value of the dollar and raise the prices we have to pay for imported goods. If the fall in the dollar ii were precipitous, it could cause rapid increases in interest rates, possibly recession, or even a serious financial crisis. —They require that a growing proportion of revenues be devoted to paying interest on the national debt, estimated to increase by $5.3 trillion over the next decade. By 2014 this increase in government borrowing will cost the average household $3,000 in added interest on the debt alone. —They impose enormous burdens on future generations. Today’s children and young adults and their descendants will have to pay more because this generation has chosen to be irresponsible. Meanwhile, deficits and rising interest costs are likely to put downward pressure on spending for education, nutrition, and health care that could make today’s children more productive and thus better able to pay these future obligations.

#### Spending is responsible for debt and Euro crisis

Chris Edwards, B.A. and M.A. in economics, 9-20-11, Cato Institute <http://www.cato.org/publications/congressional-testimony/damaging-rise-federal-spending-debt>

Federal spending and debt have soared over the past decade. As a share of gross domestic product, spending grew from 18 percent in 2001 to 24 percent in 2011, while debt held by the public jumped from 33 percent to 67 percent. The causes of this expansion include the costs of wars, growing entitlement programs, rising spending on discretionary programs, and the 2009 economic stimulus bill. Projections from the Congressional Budget Office show that without reforms spending and debt will keep on rising for decades to come.1 Under the CBO's "alternative fiscal scenario," spending will grow to about 34 percent of GDP by 2035, as shown in Figure 1, and debt held by the public will increase to at least 187 percent of GDP.2Hopefully, we will never reach anywhere near those levels of spending and debt. Going down that path would surely trigger major financial crises, as the ongoing debt problems in Europe illustrate. It is also very unlikely that Americans would support such a huge expansion of the government. The results of the 2010 elections suggest that the public has already started to revolt against excessive federal spending and debt.

Spending Bad – General

#### Spending kills revenue – turns their confidence arguments

Niall Ferguson, Laurence A. Tish Professor of History at Harvard, 5-13-10, Event Transcript: “Fiscal Crises and Imperial Collapses: Historical Perspective on Current Predicaments,” <http://www.iie.com/publications/papers/niarchos-ferguson-2010.pdf>

Just to be clear, by fiscal adjustment, what I mean here is the percentage of GDP by which fiscal policy has to contract—either through tax increases or through spending cuts, probably through some combination of the two—to prevent a public debt explosion. I’ve ranked the problem so that you can see who’s worst off. Japan is worst off. It would have to achieve a fiscal tightening of 13.4 percent GDP to stabilize its debt-GDP ratio even at 80 percent. Then I’m afraid, and I say I’m afraid for the sake of David Cameron and George Osborne because it’s their harsh task to clear up this mess, then comes the United Kingdom and of course it’s not surprising to see the usual suspects lined up behind them: Ireland, Spain, Greece, Portugal—but oh, before we get to Portugal, there’s the United States. The fiscal adjustment the United States would have to make in order to stabilize its debtGDP ratio is in fact 0.2 percent of GDP less than that which Greece has to make. So there is really no significant fiscal difference, though there is a difference in monetary regime between Greece and the United States. Many people find this hard to believe. In fact, it causes all kinds of disquiet when I make this point to audiences, but I didn’t make these numbers up; they’re numbers, as I’ve said, from the International Monetary Fund. And here’s perhaps the most striking chart I can show you about our present and future predicament. The BIS has calculated projected interest payments in relation to GDP for all the major developed countries, and yeah, the picture is certainly pretty bleak for Greece, which on its present course, would end up spending more than 20 percent of GDP on interest by 2040. But look at the right-hand chart and you’ll see that powering ahead in the interest payment stakes are once again, the United Kingdom and the United States. This projection suggests that by 2040, unless there’s a radical change of course, the United States will be spending over 20 percent of GDP on interest payments on the federal debt. Guess what, that’s exactly the percentage of GDP that the CBO, the Congressional Budget Office, estimates will be raised as tax revenue by the federal government. Once again, you don’t need a PhD in economics to do this math. That implies that by 2040, unless we radically change course, all federal tax revenues will be consumed by debt service.

#### Public sector reliance kills growth and stimulus fails – recent examples

Daniel Mitchell, Senior Fellow at the Cato Institute, 2-1-10, <http://www.cato.org/publications/commentary/spending-our-way-stagnation>

Popularized by John Maynard Keynes in the 1930s, the theory is based on the notion that government can "prime the pump" by spending money, which then begins to circulate through the economy. Keynesian theory sounds good but it overlooks the fact that, in the real world, government can't inject money into the economy without first taking money out of the economy. Any money that the government puts in the economy's right pocket must be borrowed, which means the money comes out of the economy's left pocket. doesn't boost national income, it merely redistributes it. The Obama Administration claimed that spending more money would keep the unemployment rate below 8% in the United States, yet it climbed to 10%. The United Kingdom and Canada also suffered continued stagnation after adopting so-called stimulus packages. Ironically, statist nations such as France and Germany that resisted the siren song of Keynesianism better weathered the global economic storm. The recent trend toward bigger government is particularly worrisome because most nations have oversized public sectors. Government spending in industrialized nations now consumes, on average, nearly 45% of GDP with Canada and the United States slightly below average. Australia, Switzerland, South Korea, and Slovakia are the only nations where the public sector claims less than 40% of economic output. To put these numbers in context, government spending in the industrialized world consumed about 30% of economic output in the mid-1960s, less than 20% of GDP between the First and Second World Wars and only about 10% of GDP during the golden century between the end of the Napoleonic wars and the First World War. While many factors influence economic performance, the negative impact of government spending is one reason why small-government jurisdictions such as Hong Kong (where the burden of the public sector is below 20% of GDP) have higher growth rates than nations that have medium-sized government, such as Canada and the United States. The same principle explains in part why big-government countries such as France often suffer from economic stagnation.

Spending Bad – General

#### More deficit spending kills competitiveness and investment and harms economic growth

Bergsten 11 C. Fred Bergsten, Director, Peterson Institute for International Economics, 5/6/11, edited by the Economist, “The Budget Deficit and U.S. Competitiveness,” Council on Foreign Relations, http://www.cfr.org/economics/budget-deficit-us-competitiveness/p24910

Early and effective correction of the budget deficit is critical to the global competitiveness of the U.S. economy. This is because there are only two possible financial consequences of our continuing to run deficits of more than $1 trillion annually as now projected for the next decade or more. One is sky-high interest rates that would crowd out private investment. The other is huge borrowing from the rest of the world that would push the exchange rate of the dollar so high as to price U.S. products out of international markets. Either outcome would severely undermine U.S. global competitiveness. The saving rate of the U.S. private sector, despite modest recovery from its rock-bottom lows prior to the recent crisis, is far too meager to finance enough investment to grow U.S. productivity and economic output at an acceptable rate. Government deficits anywhere near current levels tap such a large share of this pool of funds that they starve the capital needs of productive enterprise. Elimination of the fiscal imbalance, and preferably the maintenance of a modest surplus, is imperative to avoid further severe deterioration of the international economic position of the United States. The traditional "escape value" from this dilemma, facilitated by the central international role of the dollar, is for the United States to borrow abroad. We can do so in only two ways, however: by offering interest rates so high that they will also stultify domestic investment or, more likely, by letting the dollar climb to levels that are substantially overvalued in terms of U.S. trade competitiveness. Every rise of a mere 1 percent in the trade-weighted average of the dollar in fact reduces the U.S. current account balance by $20 to $25 billion, after a lag of two years, cutting economic growth and destroying 100,000 to 150,000 jobs in an economy already suffering from high unemployment. Partly as a result of persistent budget deficits, the dollar has been overvalued by at least 10 percent--and frequently by much more--over the past forty years. As a result, U.S. competitiveness and the entire U.S. economy have been severely undermined. In addition, the United States has become by far the world's largest debtor country, and its external balance is on a wholly unsustainable trajectory.

#### Spending slows growth—cutting solves

Mitchell 11 Daniel Mitchell, Senior Fellow, Cato Institute, 5/6/11, edited by the Economist, “The Budget Deficit and U.S. Competitiveness,” Council on Foreign Relations, http://www.cfr.org/economics/budget-deficit-us-competitiveness/p24910

Fiscal policy also is an important part of the mix. Excessive government spending can slow growth by diverting labor and capital from more productive uses. Punitive tax rates can hinder prosperity by discouraging work, saving, investment, and entrepreneurship. And large budget deficits can undermine competitiveness by "crowding out" private capital and building negative expectations of future tax increases. In extreme cases, high budget deficits can destabilize entire economies, either because a government resorts to the printing press to finance deficits or because investors lose faith in a government's ability to service debt, thus leading to a sovereign debt crisis. The United States hopefully is not close to becoming either Argentina or Greece, but the trend in recent years is not very encouraging. The burden of government spending has exploded, which, combined with temporarily low tax receipts because of a weak economy, has pushed annual red ink above $1 trillion per year. The good news is that the deficit situation will get a bit better in coming years. Even modest growth rates will cause revenues to climb (that's the kind of tax increase nobody opposes). Indeed, revenues will soon be above their long-run average, as a share of economic output. The bad news is that we'll still have too much red ink because the federal government's budget is about twice as big as it was when Bill Clinton left office. Even more worrisome, government borrowing actually will begin to increase again by the end of the decade because of demographic changes such as retiring baby boomers. The best way to control this red ink while also boosting competitiveness is to cap the growth of government spending. If revenues increase by an average of 7 percent each year (as the president's budget projects, even without tax increases), then we can reduce deficits by making sure spending grows by less than 7 percent annually. Given the enormous size of the budget deficit, this doesn't solve the problem overnight. If spending was allowed to grow 2 percent each year, the budget wouldn't be balanced until 2021. But it would be a big step on the road to fiscal recovery. To turn a phrase upside down, this makes a necessity out of virtue. Spending restraint is good for growth since it leaves a greater share of resources in the productive sector of the economy. And since this also happens to be the best way of letting revenue catch up to spending, it also solves the deficit issue.

Spending Bad – General

#### Deficit spending pushes up interest rates, kills investment, and causes fiscal crisis

MacGuineas 11 Maya MacGuineas, President, Committee for a Responsible Federal Budget, 5/6/11, edited by the Economist, “The Budget Deficit and U.S. Competitiveness,” Council on Foreign Relations, http://www.cfr.org/economics/budget-deficit-us-competitiveness/p24910

A balanced, multi-year fiscal consolidation plan needs to be a central part of a strategy to enhance U.S. growth and competitiveness. If we fail to reduce our borrowing needs, at some point there will be upward pressure on interest rates, increasing the cost of capital as well as the interest payments owed by the government, dampening investment, and harming economic growth. This could come on gradually or in the form of a full-blown fiscal crisis.

#### Escalating federal spending damages the economy and prevents effective crisis response

Brady 11 Kevin Brady, Joint Economic Committee Republicans Vice Chairman Designate, 3/15/11, “Spend Less, Owe Less, Grow the Economy,” Joint Economic Committee Republicans, http://www.speaker.gov/sites/speaker.house.gov/files/UploadedFiles/JEC\_Jobs\_Study.pdf

**The United States cannot maintain the current level of federal spending as a percentage of GDP—let alone allow it to escalate—without seriously damaging its economy.** Numerous studies have identified expansionary “non-Keynesian” effects from government spending reductions that offset at least some and possibly all of the contractionary “Keynesian” effects on aggregate demand. In some cases, these “**non-Keynesian” effects may be strong enough to make fiscal consolidation programs expansionary in the short term as well the long term.** **A number of developed countries have successfully reduced government spending, government budget deficits, and stabilized the level of government debt**. Fiscal consolidation **programs in Canada**, Sweden, and New Zealand, **among others, achieved their goals for government deficit reduction and government debt stabilization and boosted their real GDP growth rates by reducing government spending**. Obama Administration officials have emphasized the risk of starting a fiscal consolidation program now while ignoring the risk of delay. **There are significant external risk factors to the U.S. economy in both the short term and the long term that cannot be foreseen, such as: 1) resurging price inflation, (2) loss of confidence in the U.S. dollar** as the world’s reserve currency, (3) **euro-zone sovereign debt defaults, and (4) war in the Middle East.** But, **the United States will be in a better position to respond to any of these challenges by reducing federal spending sooner rather than later.**

Spending Bad – General

#### Failure to reach a budget deal kills the economy

Associated Press 7/17/12 (“Bernanke warns US economy could topple into recession if Congress doesn’t end budget impasse” <http://www.washingtonpost.com/politics/bernanke-goes-before-congressional-panels-as-us-economy-slumps-could-signal-feds-next-move/2012/07/17/gJQAf95NqW_story.html>)

WASHINGTON — Federal Reserve Chairman Ben Bernanke sketched a bleak picture of the U.S. economy Tuesday — and warned it will darken further if Congress doesn’t reach agreement soon to avert a budget crisis. Without an agreement, tax increases and deep spending cuts would take effect at year’s end. Bernanke noted what the Congressional Budget Office has warned: A recession would occur, and 1.25 million fewer jobs would be created in 2013. The Fed is prepared to take further action to try to help the economy if unemployment stays high, he said. Bernanke didn’t signal what steps the Fed might take or whether any action was imminent. And he noted there’s only so much the Fed can do. But the Fed chairman made clear his most urgent concern is what would happen to the economy if Congress can’t resolve its budget impasse before the year ends. Cuts in taxes on income, dividends and capital gains would expire. So would this year’s Social Security tax cut and businesses tax reductions. Defense and domestic programs would be slashed. And emergency benefits for the long-term unemployed would run out. All that “would greatly delay the recovery that we’re hoping to facilitate,” Bernanke said near the end of two hours of testimony to the Senate Banking Committee. Bernanke was giving his twice-a-year report to Congress on the state of the economy. He will testify Wednesday before the House Financial Services Committee. The economy is growing modestly but has weakened, Bernanke said. Manufacturing has slowed. Consumers are spending less. And job growth has slumped to an average of 75,000 a month in the April-June quarter from 226,000 a month from January through March. The unemployment rate is stuck at 8.2 percent. Bernanke noted that the economy, after growing at a 2.5 percent annual rate in the second half of 2011, slowed to roughly 2 percent from January through March. And it likely weakened further in the April-June period. Congress needs to resolve its impasse well before the year ends, Bernanke said. “Doing so would help reduce uncertainty and boost household and business confidence,” he said. The cuts that would kick in next year could cost as many as 2 million jobs, a trade group that represents manufacturers said in a report released Tuesday. The report came from the Aerospace Industries Association. A separate report Tuesday pointed to the budget crises many states are suffering, caused in part by shrinking revenue from the federal government. States are finding it harder to pay for basic services such as law enforcement, local schools and transportation, the report said. It was issued by the State Budget Crisis Task Force, a non-profit co-chaired by former Federal Reserve Chairman Paul Volcker and former New York Lieutenant Governor Richard Ravitch. Republicans in Congress are demanding deeper spending cuts while extending income tax cuts for everyone. Democrats want to extend the tax cuts for middle- and lower-class Americans. But they want them to expire for people in the highest-income brackets.

Spending Bad – General

#### Fiscal discipline key to the economy – multiple warrants

1. Higher interest rates
2. Higher taxes
3. Investor confidence

National Commission on Fiscal Responsibility ’10 (4/27/10, “National Commission on Fiscal Responsibility Holds Its Inaugural Meeting,” pg online @ lexisnexis)

The ultimate goal of the commission's efforts should be to put us on a path of fiscal sustainability. One widely accepted criterion for sustainability is that the ratio of federal debt held by the public to national income remain at least stable, or perhaps even decline in the longer term. This goal can be achieved by bringing spending, exclusive of interest payments, roughly into line with revenues. Unfortunately, most projections suggest that we are far from this goal, and that without significant changes to current policy, the ratio of federal debt to national income will continue to rise sharply. Thus, the reality is that the Congress, the administration and the American people will have to choose among making modifications to entitlement programs, such as Medicare and Social Security, restraining federal spending on everything else, accepting higher taxes, or some combination thereof. Achieving long-term fiscal sustainability will be difficult, but the costs of failing to do so could be very high. Increasing levels of government debt relative to the size of the economy can lead to higher interest rates, which inhibit capital formation and productivity growth and might even put the current economic recovery at risk. To the extent that higher debt increases our reliance on foreign borrowing, an ever-larger share of our future income would be devoted to interest payments on federal debt held abroad. Moreover, other things being equal, increased federal debt implies higher taxes in the future to cover the associated interest costs -- higher taxes that may create disincentives to work, save, hire and invest. High levels of debt also decrease the ability of policy-makers to respond to future economic and financial shocks. And, indeed, a loss of investor confidence in the ability of the government to achieve fiscal sustainability can itself be a source of significant economic and financial instability, as we have seen in a number of countries in recent decades. Neither experience nor economic theory clearly indicates the threshold at which government debt begins to endanger prosperity and economic stability. But given the significant costs and risks associated with a rapidly rising federal debt, our nation should soon put in place a credible plan for reducing deficits to sustainable levels over time. Doing so earlier, rather than later, will not only help maintain the U.S. government's credibility in financial markets, thereby holding down interest costs, but it will also ultimately prove less disruptive by avoiding abrupt shifts in policy and by giving those affected by budget changes more time to adapt. The path forward contains many difficult tradeoffs and choices, but postponing those choices and failing to put the nation's finances on a sustainable long-run trajectory would ultimately do great damage to our economy.

### Spending Bad – Crowdout

#### Spending crowds out and collapses private sector

Amerman No Date Daniel R. Amerman, Chartered Financial Analyst with MBA and BSBA degrees in finance, No date, “High Government Deficits "Crowd Out" Stock Market Returns,” danielamerman.com, http://danielamerman.com/articles/Crowding.htm

“Crowding out” is an obscure term if you're not an economist – but this replacement of the private sector economy with government spending may end up being one of the largest determinants of your standard of living during retirement. The investment problem is that the past, present and likely future of the US economy is one of rapidly growing government spending. Because the investment models that drive conventional financial planning assume a rapidly growing private sector, this sets up a fundamental competition between government growth and private sector growth for their shares of a single economy, and may lead to a collapse of stock market values and conventionally invested retirement portfolios. One of the sharpest economic changes in our lifetimes occurred between 2007 and 2009, as the private sector share of the United States economy collapsed to a depression level. About 75% of the collapse in the private sector was (and is) hidden by an explosive increase in government spending, which could not be paid for by taxes, but has instead created a "new normal" of fantastic annual government deficits without end. The current trillion dollar plus annual deficits which are used to cover up the continuing "hole" in the economy are not stable, however, but merely serve to "bridge" the gap between the private sector collapse and the rapidly accelerating future deficits that will be required to pay for Boomer social security and Medicare promises, as well as the increasing amount of the economy devoted to government transfer payments. On the most fundamental of levels, stock market valuations and traditional long-term investing are based upon a dependably growing private economy. However, when government spending is surging at rates sufficiently far in excess of overall economic growth, this means that the private economy is necessarily barely growing - or even shrinking. Therefore, the current situation creates a long-term and highly bearish scenario for stock valuations. The ripple effects of the government competing with the private sector for the limited real resources of the future may potentially collapse most pension funds – and their government and corporate sponsors – across not only the US, but the rest of the developed world.

Government spending drains the private sector

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His administration drained resources out of the private sector via taxes, then he signed his $825 billion "stimulus" bill, the American Recovery and Reinvestment Act of 2009 (ARRA), so that money could be redistributed among government bureaucracies. For instance, Obama authorized spending money to repair U.S. Department of Agriculture buildings, maintain the Farm Service Agency's computers and inform the electronically disadvantaged about digital TV. Obama essentially acknowledged that he didn't know or care about how to stimulate the private sector, since he provided hardly any specific guidance for spending the money. For instance, ARRA awarded $600 million to the National Oceanic and Atmospheric Administration, saying only that the money was "for procurement, acquisition and construction" — which could have meant almost anything. If the aim was really to stimulate recovery of the private sector, the most effective way of doing that would have been to leave the money in the private sector. After all, people tend to be more careful with their own money than they are with other people's money. Undoubtedly people would have spent their money on all sorts of things to help themselves, things worth stimulating like food, clothing, gasoline, downloads, cell phones and household repairs.

#### Spending spikes interest rates and crowds out private investment

US Budget Committee 11 U.S. Senate Budget Committee Republican, responsible for drafting Congress’ annual budget plan and for monitoring the federal budget, 5/12/11, “Spending Cuts And Economic Growth: What Does The Cross-Country Empirical Evidence Show?,” U.S. Senate Budget Committee Republican, http://budget.senate.gov/republican/public/index.cfm/committee?p=committee-history

With continued deficits and growing debt, more and more national savings go to servicing government debt rather than to investment in productive private capital goods such as factories, machines, and other such incubators of private job creation. That is, government spending “crowds out” private investment spending, leading to lower output and incomes and fewer jobs than would occur without a growing government. Some commentators, such as economist Paul Krugman, contend that government spending does not crowd out private spending in the current near-zero short-term interest rate environment. With interest rates as low as they are today, the argument goes, the traditional avenue of crowding out is not operative. That traditional avenue is where government competes for resources in financial markets with the private sector, driving up interest rates and choking off private investment spending. Short-term rates are indeed close to zero, for Treasury maturities of up to approximately one year. Those unusually low rates reflect the extraordinary intervention into financial markets by the Fed, and are not indicative of market-based supply and demand forces. Yet, even with low short-term rates, longer-term interest rates are not zero and are influenced by supply and demand forces in markets for long-term funds. The 10-year Treasury rate has averaged around 3.5 percent since the beginning of the financial crisis in August 2007. In fact, it remains the case that outsized borrowing by the Federal Government has exerted upward pressure on longer-term interest rates. Government borrowing, by pushing long-term interest rates higher, chokes off some private, productive investment spending that would otherwise occur. There remains further room for long-term interest rates to decline and stimulate private investment spending and the economy. Indeed, a major motivation for the Fed’s recent purchases of well over $600 billion of longer-term Treasury securities is its intention to lower longer-term interest rates in order to stimulate interest-sensitive spending, such as home purchases by households or capital expenditures by manufacturing firms. Thus, the Fed’s actions provide additional evidence that crowding out is occurring and is leading to higher long-term interest rates than would be the case without elevated demands for resources by government. This means the nation’s debt is leading to higher costs for businesses and American households to obtain long-term credit. Longer-term interest rates would be even lower today, and more stimulating of economic activity, if today’s deficit and government debt were lower.

Spending Bad - Crowdout

#### Deficit spending crowds out investment and causes fiscal crisis—cutting spending solves

CBO 10 Congressional Budget Office, has produced independent, nonpartisan, timely analysis of economic and budgetary issues to support the Congressional budget process, 7/27/10, “Federal Debt and the Risk of a Fiscal Crisis,” Congressional Budget Office, http://www.cbo.gov/publication/21625

Although deficits during or shortly after a recession generally hasten economic recovery, persistent deficits and continually mounting debt would have several negative economic consequences for the United States. Some of those consequences would arise gradually: A growing portion of peoples savings would go to purchase government debt rather than toward investments in productive capital goods such as factories and computers; that crowding out of investment would lead to lower output and incomes than would otherwise occur. In addition, if the payment of interest on the extra debt was financed by imposing higher marginal tax rates, those rates would discourage work and saving and further reduce output. Rising interest costs might also force reductions in spending on important government programs. Moreover, rising debt would increasingly restrict the ability of policymakers to use fiscal policy to respond to unexpected challenges, such as economic downturns or international crises. Beyond those gradual consequences, a growing level of federal debt would also increase the probability of a sudden fiscal crisis, during which investors would lose confidence in the governments ability to manage its budget, and the government would thereby lose its ability to borrow at affordable rates. It is possible that interest rates would rise gradually as investors confidence declined, giving legislators advance warning of the worsening situation and sufficient time to make policy choices that could avert a crisis. But as other countries experiences show, it is also possible that investors would lose confidence abruptly and interest rates on government debt would rise sharply. The exact point at which such a crisis might occur for the United States is unknown, in part because the ratio of federal debt to GDP is climbing into unfamiliar territory and in part because the risk of a crisis is influenced by a number of other factors, including the governments long-term budget outlook, its near-term borrowing needs, and the health of the economy. When fiscal crises do occur, they often happen during an economic downturn, which amplifies the difficulties of adjusting fiscal policy in response. If the United States encountered a fiscal crisis, the abrupt rise in interest rates would reflect investors fears that the government would renege on the terms of its existing debt or that it would increase the supply of money to finance its activities or pay creditors and thereby boost inflation. To restore investors confidence, policymakers would probably need to enact spending cuts or tax increases more drastic and painful than those that would have been necessary had the adjustments come sooner.

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#### Government spending is less effective than Private

Chris Edwards, B.A. and M.A. in economics, 9-20-11, Cato Institute <http://www.cato.org/publications/congressional-testimony/damaging-rise-federal-spending-debt>

Let's take a look at how federal spending damages the economy over the long-run. Federal spending is financed by extracting resources from current and future taxpayers. The resources consumed by the government cannot be used to produce goods in the private marketplace. For example, the engineers needed to build a $10 billion government high-speed rail project are taken away from building other products in the economy. The $10 billion rail project creates government-connected jobs, but it also kills $10 billion worth of private activities. Indeed, the private sector would actually lose more than $10 billion in this example. That is because government spending and taxing creates "deadweight losses," which result from distortions to working, investment, and other activities. The CBO says that deadweight loss estimates "range from 20 cents to 60 cents over and above the revenue raised."19 Harvard University's Martin Feldstein thinks that deadweight losses "may exceed one dollar per dollar of revenue raised, making the cost of incremental governmental spending more than two dollars for each dollar of government spending."20 Thus, a $10 billion high-speed rail line would cost the private economy $20 billion or more.

#### Excessive government spending will crowd out private investors

Stephen Dinan, 2/4/09, contributor for The Washington Times, “CBO: Obama stimulus harmful over long-term”, http://www.washingtontimes.com/news/2009/feb/04/cbo-obama-stimulus-harmful-over-long-haul/

President Obama’s economic recovery package will actually hurt the economy more in the long run than if he were to do nothing, the nonpartisan Congressional Budget Office said Wednesday. CBO, the official scorekeepers for legislation, said the House and Senate bills will help in the short term but result in so much government debt that within a few years they would crowd out private investment, actually leading to a lower Gross Domestic Product over the next 10 years than if the government had done nothing. CBO estimates that by 2019 the Senate legislation would reduce GDP by 0.1 percent to 0.3 percent on net. [The House bill] would have similar long-run effects, CBO said in a letter to Sen. Judd Gregg, New Hampshire Republican, who was tapped by Mr. Obama on Tuesday to be Commerce Secretary. The House last week passed a bill totaling about $820 billion while the Senate is working on a proposal reaching about $900 billion in spending increases and tax cuts. But Republicans and some moderate Democrats have balked at the size of the bill and at some of the spending items included in it, arguing they won’t produce immediate jobs, which is the stated goal of the bill. The budget office had previously estimated service the debt due to the new spending could add hundreds of millions of dollars to the cost of the bill — forcing the crowd-out. CBOs basic assumption is that, in the long run, each dollar of additional debt crowds out about a third of a dollars worth of private domestic capital, CBO said in its letter. CBO said there is no crowding out in the short term, so the plan would succeed in boosting growth in 2009 and 2010. The agency projected the Senate bill would produce between 1.4 percent and 4.1 percent higher growth in 2009 than if there was no action. For 2010, the plan would boost growth by 1.2 percent to 3.6 percent. CBO did project the bill would create jobs, though by 2011 the effects would be minuscule.

Spending Bad - Crowdout

#### More evidence: spending causes a crowd out

Scott Walter and Sandra Swirski, 3/26/10, By Scott Walter, former Special Assistant to the President for Domestic Policy in the last Administration, and Sandra Swirski, co-founder of Venn Strategies and a tax attorney, “Crowding Out Private Money: Why A Growing Government Undercuts American Philanthropy”, http://www.wlf.org/publishing/publication\_detail.asp?id=2150

The dramatic growth of government now underway makes most Americans rather uneasy. Economists in particular fear that higher spending by government causes long-term harm to business investment and economic growth, especially when the country already struggles under heavy public debt. But another danger must not be overlooked: the harm governmental expansion does to philanthropy. This vital sector of society will see its productivity drained as private dollars that would have been spent by charitable and philanthropic entrepreneurs are channeled instead into the hands of politicians and bureaucrats who may have short-sighted needs. The danger was detailed in a report on the nonprofit sector issued this past holiday season by the nonpartisan Congressional Research Service (CRS). It warned that government spending "can potentially crowd out private support for charities" and also "cause charities to reduce their fund-raising efforts." The effect is stark. One study cited by CRS estimated that government largess typically "crowds out" private donations by around 56 percent. That means every $1,000 in government grant money can reduce private donations by $560. See Molly F. Sherlock and Jane G. Gravelle, An Overview of the Nonprofit and Charitable Sector, Congressional Research Service report, Nov. 17, 2009. But the immediate cost in dollars is just the beginning of the harm, because $1,000 guided by private hands isn't the same as $1,000 doled out by government. Innovation and efficiency are the hallmarks of independent entrepreneurs, not the federal government, and that is especially true in philanthropy. Yet despite the great potential for harm, few in the political class have raised any alarms. Perhaps that isn't surprising. After all, for two years in a row proposals have been advanced which would take big chunks out of the charitable income tax deduction -- that mighty Mississippi of American generosity through which billions flow each year towards those most in need, such as schools, the aged, the arts, and those reeling from economic upheaval. Nor is the charitable deduction cut the only threat. Indeed, the aforementioned proposal won't even take effect unless Congress enacts it through new legislation, which lawmakers declined to do last year. But two other threats to the charitable sector require no action by Congress to become reality, namely, a jump-up in tax rates for the nation's biggest taxpayers and a cut in the same people's ability to claim itemized deductions. Specifically, if congressional inaction allows the 2003 tax cuts to expire at year's end, persons earning more than $200,000 a year ($250,000 for married couples) will see their marginal income tax rates rise around 10 percent, and their tax rates on capital gains and dividends rise 33 percent. This drain on upper-income taxpayers will have a significant effect on philanthropy, because households whose wealth exceeds $1 million (roughly 7 percent of the population) provide around half of all charitable donations. See Arthur C. Brooks, WHO REALLY CARES: AMERICA'S CHARITY DIVIDE--WHO GIVES, WHO DOESN'T, AND WHY IT MATTERS (New York: Basic Books, 2006). Taking more money out of these Americans' pockets, in short, means less money for charity. By contrast, a vigorous economy that spins off greater income for all Americans sends more dollars flowing into the philanthropic sector. As researcher Arthur Brooks observes, the booming economy of 1995-2000 saw real income per capita rise by 12 percent, while household giving, spurred by stock market and home value gains, exploded by 54 percent. Id. Too many in Washington seem to have forgotten that America's greatness, and her liberty, are tightly linked to the fact that her citizens are the most charitable on earth. Nearly two centuries ago the French thinker Alexis de Tocqueville observed that while Frenchmen would wait on government to deal with their problems, and Englishmen would await a nobleman's aid and leadership, Americans spontaneously join together in private groups, voluntarily giving time and treasure to respond to the day's most pressing needs.

### 2NC — Spending Bad – Confidence

#### Unsustainable spending kills investor confidence and causes fiscal crisis

Senate Committee on Finance 12 US Senate Committee on Finance, 6/5/12, “Hatch on CBO’s Long-term Budget Outlook,” US Senate Committee on Finance, http://www.finance.senate.gov/newsroom/ranking/release/?id=920faaa9-33ba-4e2f-9f81-6cdac51f4a68

U.S. Senator Orrin Hatch (R-Utah), Ranking Member of the Senate Finance Committee, said today that the Congressional Budget Office’s (CBO) Long-Term Budget Outlook should serve as a stark reminder of the urgent need to tackle out-of-control spending driven by the nation’s unsustainable entitlement programs. Hatch called on President Obama to confront the crisis and demonstrate real leadership to put America back on a sustainable fiscal path. “This report’s findings are chilling: debt reaching 200 percent of our economy and potentially causing a full blown financial crisis; health care spending rising unabated to record levels; and Medicare and Social Security on a glide path to insolvency,” Hatch said. “Driven by unsustainable spending, America has reached a dangerous crossroads that demands immediate action, but the President is nowhere to be found. He’s decided that instead of leading, he’ll play politics and blame everyone else for our weak economy, for the debt, and for our high unemployment rate. But the American people elected the President to lead, and it’s well past time for him to provide the leadership taxpayers deserve to reform our entitlement programs dominating the federal budget, to tackle our debt that threatens our economic security, and to ensure that every American taxpayer doesn’t face the largest tax increase in history by the end of the year.” Below are several key findings from CBO’s report that was released today: Unsustainable debt: “Federal debt would grow rapidly from its already high level, exceeding 90 percent of GDP in 2022. After that…[d]ebt as a share of GDP would exceed its historical peak of 109 percent by 2026, and it would approach 200 percent in 2037,” and that is a “…clearly unsustainable path for federal borrowing.” Impact of record debt on the economy: As a result of this level of debt, “[r]eal [Gross National Product] GNP would be reduced by 4 ½ percent in 2027 and by about 13 ½ percent in 2037, according to CBO’s central estimates.” Interest payments on the debt: “As debt grew, so would net federal spending on interest, which would rise from about 1 ½ percent of GDP today to ten percent by 2037.” Need for timely policy changes to put us on a sustainable course: “The explosive path of federal debt under the alternative scenario underscores the need for large and timely policy changes to put the federal government on a sustainable fiscal course.” Growing debt increases risk of fiscal crisis: “Growing debt would increase the probability of a sudden fiscal crisis, during which investors would lose confidence in the government’s ability to manage its budget and the government would thereby lose its ability to borrow at affordable rates.”

#### Massive spending increases hurts investor confidence

The Bank for International Settlements, organization of central banks, **11** (June 26th 2011, “Overview of the economic chapters,” http://www.bis.org/publ/arpdf/ar2011e\_ov.htm)

Over the past year, the global economy has continued to improve. In emerging markets, growth has been strong, and advanced economies have been moving towards a self-sustaining recovery. But it would be a mistake for policymakers to relax. From our vantage point, numerous legacies and lessons of the financial crisis require attention. In many advanced economies, high debt levels still burden households as well as financial and non-financial institutions, and the consolidation of fiscal accounts has barely started. International financial imbalances are re-emerging. Highly accommodative monetary policies are fast becoming a threat to price stability. Financial reforms have yet to be completed and fully implemented. And the data frameworks that should serve as an early warning system for financial stress remain underdeveloped. These are the challenges we examine in this year's Annual Report. Interrelated imbalances made pre-crisis growth in several advanced countries unsustainable. Rapidly increasing debt and asset prices resulted in bloated housing and financial sectors. The boom also masked serious longterm fiscal vulnerabilities that, if left unchecked, could trigger the next crisis. We should make no mistake here: the market turbulence surrounding the fiscal crises in Greece, Ireland and Portugal would pale beside the devastation that would follow a loss of investor confidence in the sovereign debt of a major economy.Addressing overindebtedness, private as well as public, is the key to building a solid foundation for high, balanced real growth and a stable financial system. That means both driving up private saving and taking substantial action now to reduce deficits in the countries that were at the core of the crisis.

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#### Spending kills investor confidence and spikes interest rates, hinders economic growth

US Budget Committee 11 U.S. Senate Budget Committee Republican, responsible for drafting Congress’ annual budget plan and for monitoring the federal budget, 5/12/11, “Spending Cuts And Economic Growth: What Does The Cross-Country Empirical Evidence Show?,” U.S. Senate Budget Committee Republican, http://budget.senate.gov/republican/public/index.cfm/committee?p=committee-history

Having received numerous warnings from a variety of sources, the U.S. can no longer kick its fiscal problems further down the road. Given the recent debt-outlook downgrade from Standard & Poor’s, the U.S. faces a loss of its top-tier credit rating if it waits to constrain growing deficits. The economy will suffer dearly if financial markets and our creditors lose faith in the Federal Government’s commitment to paying off its obligations in full. Fearing default either explicitly or through inflationary policies, financial markets will demand ever increasing compensation for the risk through higher and higher interest rates. The resulting increased interest payments will choke off the ability of government to operate and will choke off private, interest-sensitive spending. The economy will be harmed, perhaps precipitously. The U.S. can avoid catastrophe by curtailing spending immediately, and this need not threaten expansion of our private economy. Indeed, a large and growing body of empirical research identifies positive effects on economic growth from fiscal consolidations that relied primarily on spending cuts rather than tax hikes. The nation faces stark and critical decisions about the size of government it desires. As experiences in many European countries have shown, high levels of government spending have negative economic effects, including persistently high unemployment rates. [32] Government spending in the United States over the past two years has exploded. Recent levels of spending, if locked in and financed by increased taxes, will severely inhibit the very economic growth necessary for the nation to pay down its unsustainably high levels of debt. Without bringing spending down toward historic norms, we face an unnecessarily weaker economic future. In contrast, by reducing expenditures the U.S. can decide to strengthen incentives to invest in labor and capital, harness the productive potential of the strong American workforce, and ensure for our children that the United States will still have the most dynamic, productive, and resilient economy in the world.

#### Deficit spending kills confidence, spikes interest rates, and chokes economic activity

US Budget Committee 11 U.S. Senate Budget Committee Republican, responsible for drafting Congress’ annual budget plan and for monitoring the federal budget, 5/12/11, “Spending Cuts And Economic Growth: What Does The Cross-Country Empirical Evidence Show?,” U.S. Senate Budget Committee Republican, http://budget.senate.gov/republican/public/index.cfm/committee?p=committee-history

As deficits and debt have grown extraordinarily, so too have warnings that our unsustainable fiscal path will lead to crisis. Recent experiences of Greece and other fiscally challenged Eurozone countries have made clear that a fiscal crisis involves painful and precipitous increases in interest rates. Rates rise as sovereign debt investors demand greater compensation for growing perceived default risks. This has become the reality for a number of European countries with unsustainable indebtedness—see Figure 2. The cost of issuing three-year debt for Greece has roughly tripled over a one-year period and the cost for Ireland and Portugal has risen roughly fourfold. The rapid and sudden increases in funding costs force sudden and painful choices, as previously profligate governments are forced to scale back social benefit promises and the size of government workforces. Those who counted on the promises are disappointed; disappointment fuels unrest. What would a large increase in funding cost mean to the U.S.? CBO, in a recent analysis of alternative interest rate scenarios, estimates that if the 10-year Treasury rate were to rise from an average of 3.8 percent in 2011 to around the average levels of over 10 percent during the high-rate period of 1981-1990, then deficits would rise by over $12 trillion between 2012 and 2021. Debt held by the public under such a scenario would rise by over $23 trillion by 2021. [2] Deficits and debt of those magnitudes would choke off private investment as the government absorbs ever increasing amounts of resources from markets, pricing out and crowding out private productive investment spending. The ensuing economic downfall would likely lead to a precipitous financial crisis. Recent experiences in financial markets demonstrate that shifts in market sentiments and asset prices can occur quickly and be executed, through automatic electronic orders, even faster. According to the recent Financial Crisis Inquiry Report (2011), quoting Federal Reserve (Fed) Chairman Ben Bernanke concerning the speed of the crisis: “… out of maybe the 13, 13 of the most important financial institutions in the United States, 12 were at risk of failure within a period of a week or two.” [3] Given the level of debt that the U.S. has accumulated, the nation faces a growing risk of sudden reversal of sentiment in the global market for its debt. Any sudden loss of confidence can, with bank-run rapidity, lead to spikes in interest rates that would choke off economic activity and any chance for sustained economic recovery.

Spending Bad – Confidence

#### Deficit spending kills investor confidence—spending cuts solve

US Budget Committee 11 U.S. Senate Budget Committee Republican, responsible for drafting Congress’ annual budget plan and for monitoring the federal budget, 5/12/11, “Spending Cuts And Economic Growth: What Does The Cross-Country Empirical Evidence Show?,” U.S. Senate Budget Committee Republican, http://budget.senate.gov/republican/public/index.cfm/committee?p=committee-history

What might a debt crisis mean for the United States? CBO paints the following picture: In a fiscal crisis, investors would lose confidence in the government’s ability to manage its budget, and the government would thereby lose its ability to borrow at affordable rates. It is possible that interest rates would rise gradually as investors’ confidence declined, giving legislators advance warning of the worsening situation and sufficient time to make policy choices that could avert a crisis. But as other countries’ experiences show, it is also possible that investors would lose confidence abruptly and interest rates on government debt would rise sharply. The exact point at which such a crisis might occur for the United States is unknown, in part because the ratio of federal debt to GDP is climbing into unfamiliar territory. If the United States encountered a fiscal crisis, the abrupt rise in interest rates would reflect investors’ fears that the government would renege on the terms of its existing debt or that it would increase the supply of money to finance its activities or pay creditors and thereby boost inflation. To restore investors’ confidence, policymakers would probably need to enact spending cuts or tax increases more drastic and painful than those that would have been necessary had the adjustments come sooner. [4]

Spending Bad – Confidence

#### Federal debt risks investor confidence

Congressional Budget Office, 7-27-10 <http://www.cbo.gov/publication/21625>

Beyond those gradual consequences, a growing level of federal debt would also increase the probability of a sudden fiscal crisis, during which investors would lose confidence in the governments ability to manage its budget, and the government would thereby lose its ability to borrow at affordable rates. It is possible that interest rates would rise gradually as investors confidence declined, giving legislators advance warning of the worsening situation and sufficient time to make policy choices that could avert a crisis. But as other countries experiences show, it is also possible that investors would lose confidence abruptly and interest rates on government debt would rise sharply. The exact point at which such a crisis might occur for the United States is unknown, in part because the ratio of federal debt to GDP is climbing into unfamiliar territory and in part because the risk of a crisis is influenced by a number of other factors, including the governments long-term budget outlook, its near-term borrowing needs, and the health of the economy. When fiscal crises do occur, they often happen during an economic downturn, which amplifies the difficulties of adjusting fiscal policy in response. If the United States encountered a fiscal crisis, the abrupt rise in interest rates would reflect investors fears that the government would renege on the terms of its existing debt or that it would increase the supply of money to finance its activities or pay creditors and thereby boost inflation. To restore investors confidence, policymakers would probably need to enact spending cuts or tax increases more drastic and painful than those that would have been necessary had the adjustments come sooner.

#### Cuts solve – signals change and increases household wealth

Robert Perotti, PhD in Economics from MIT and Full Professor of Economics and Universita Bocconi, 11, “The ‘Austerity Myth’: Gain Without Pain?”, November, <http://www.nber.org/chapters/c12652.pdf>

Second, if the answer to the first question is in the affirmative, how useful is the experience of the past as a guide to the present? For instance, if fiscal consolidations were expansionary in the past   because they caused a steep decline in interest rates or inflation, it is unlikely that the same mechanism can be relied on in the present circumstances, with low inflation and interest rates close to zero. Or, if consolidations were expansionary mainly    because they were associated with large increases in net exports, this mechanism is obviously not available to a large group of countries highly integrated between them.   That private consumption should boom when government spending falls would come as no surprise to believers in a standard neoclassical model with forward looking agents. Although in that model alternative time paths of government spending and distortionary taxation can create virtually any response of private consumption, from negative to positive, the basic idea is straightforward; lower government spending means lower taxes and higher households’ wealth, hence higher consumption. This is sometimes dubbed the “confidence channel” of fiscal consolidations. 2 Lower taxes also mean less distortions, hence they can lead to higher output and investment. More generally, a large fiscal consolidation may signal a change in regime in a country that is in the midst of a recession, and may boost  investment through this channel. In open economies alternative effects may be at play. A fiscal consolidation might reinforce and make credible a process of wage moderation, either implicitly or by trading explicitly less labor taxes for wage moderation; this in turn feeds into a real effective depreciation and boosts exports. Or, it might reinforce the decline in interest rates, by reducing the risk premium or by making a peg more credible. These alternative channels were highlighted for instance in Alesina and Perotti (1995) and (1997) and Alesina and Ardagna (1998).

Spending Bad – Confidence

#### Spending kills confidence – Europe proves

Veronique de Rugy, Ph.D, senior research fellow Mercatus Center at George Mason University, columnist for Reason magazine, 9/10/10 http://reason.org/news/printer/austerity-agonistes

Across Europe, governments are announcing new austerity packages of spending cuts and higher taxes rather than Obama-style stimulus spending. In response, American economists such as Paul Krugman and Brad DeLong are warning that these policies will throw Europe back into a depression and should be avoided at all costs in the United States. “The next time you hear serious-sounding people explaining the need for fiscal austerity,” Krugman wrote in The New York Times in July, “try to parse their argument. Almost surely, you’ll discover that what sounds like hardheaded realism actually rests on a foundation of fantasy, on the belief that invisible vigilantes will punish us if we’re bad and the confidence fairy will reward us if we’re good.” One crucial point Krugman leaves out is that most European Union member states have no alternative. Countries that rely heavily on foreign investors—such as Greece, France, Ireland, Italy, and Spain—must cut spending to avoid being shut off from the global capital markets. Contrary to common belief, investors don’t judge sovereign default risks based on public debt as a percentage of gross domestic product. Instead, bond professionals grade on a curve, assessing one country’s fiscal behavior against another’s. When investors lose confidence in a government’s fiscal rectitude relative to its competitors, they withdraw, and the snubbed country suffers. Capital being a scarce good, the result is increased interest rates and a higher price for debt. One of the key signaling devices for international investors is how a government behaves under financial duress—how it balances the demands of its debtors with those of its welfare recipients. Announcements of lower spending and higher taxes tell investors a country is willing to go to great lengths not to default on its debt obligations. If the government instead focuses on preserving its welfare state and public employee benefits, investors know default is more likely and will shy away from that country’s bonds. Japan has the world’s biggest debt as a percentage of GDP, at 227 percent, nearly four times the economist-recommended 60 percent ceiling. It has gotten away with its carelessness without risking default because the country relies more heavily than most on domestic investors to fund its follies. The United States, despite a dangerous debt burden relative to GDP (66 percent) and a structural deficit among the highest of developed countries (almost 4 percent), has so far also escaped investor censure, thanks to the perception that the dollar remains the safest currency in the world. European countries don’t have that luxury. But the benefits of austerity go far beyond signaling investors. Goldman Sachs economists Ben Broadbent and Kevin Daly, surveying the data of 44 large fiscal adjustments across the globe since 1975, concluded in a 2010 report that cutting annual spending by 1 percent triggers a net 0.6 percent in economic growth. As we will see below, this is a good deal compared to the $1.10 reduction in GDP we get for each $1 spent by the government to stimulate the economy. Lower spending reduces the fear of higher taxes, which leads to an increase in consumer and business demand and growth. The notion that austerity is bad and stimulus is good rests on the Keynesian theory that if government spends a lot of money, that money will create more value in economic growth. This purported increase in gross domestic product is what economists call the “multiplier effect.” It’s a nice story, but like most fairy tales, it has scant basis in reality. In a 2010 paper published by George Mason University’s Mercatus Center (where I work), economists Robert Barro and Charles Redlick showed that in the best-case scenario, a dollar of government spending produces much less than a dollar in economic growth—between 40 and 70 cents. If that was the rate of return on our private-sector investments, America would soon cease to be a leading economic force. Barro and Redlick also looked at the economic impact of raising taxes to pay for spending increases. They found that for every $1 in tax-financed spending, the economy actually shrinks by $1.10. In other words, greater spending financed by tax increases damages the economy. The stimulus isn’t working, because the economic theory it is based on is fundamentally flawed. The findings from my own quarterly reports on stimulus spending (mercatus.org/publication/stimulus-facts-data) further illustrate why these packages don’t work. My analysis is based on the tens of thousands of reports from stimulus recipients published on recovery.gov each quarter, along with economic and political data from the Bureau of Labor Statistics, the Census Bureau, GovTrack.us, and other sources. My most recent analysis found that the total number of jobs the government attributed to stimulus spending as of April was 682,000. Factoring in stimulus dollars spent up to that point, the average cost of these jobs was $282,000. That’s a lot of money. Worse, four-fifths of these jobs were in the public sector. This outcome is far afield from the administration’s original promise that the stimulus would create 3.5 million jobs over two years, 90 percent of them in the private sector. A 2002 paper in the Economic Policy Journal, written by the French economists Yann Algan, Pierre Cahuc, and Andre Zylberberg, looked at the impact of public employment on overall labor market performance. Using data for a sample of OECD countries from 1960 to 2000, they found that, on average, the creation of 100 public jobs eliminated about 150 private-sector jobs, decreased by a slight margin overall labor market participation, and increased by about 33 the number of unemployed workers. Their explanation was that public employment crowds out private employment and increases overall unemployment by offering comparatively attractive working conditions. Basically, public jobs, especially ones that also exist in the private sector in fields such as transportation and education, offer higher wages and benefits, require low effort, and therefore crowd out many private jobs. When these new employees are paid with taxes it negatively impacts the economy. The data released by the Bureau of Labor Statistics in June, then, were bad news. (See the chart.) They showed that since the passage of the stimulus bill, the private sector has lost 2.55 million jobs while the federal government gained 416,000. The understandable temptation to take action in a time of recession should not lead lawmakers down unproductive paths. Stimulus by government spending doesn’t work. European and American governments have tried it without success. Now is the time to tighten spending, no matter what some American economists might say.

Spending Bad – Confidence

#### Deficit reduction key to investor confidence and a strong economy

Thornburgh ’11 (Dick Thornburgh, former U.S. Attorney General and two-term governor of Pennsylvania, 7/20/11, “Deficits Need Balanced-Budget Amendment Fix: Dick Thornburgh,” Bloomberg, pg online @ http://www.bloomberg.com/news/2011-07-21/deficits-need-balanced-budget-amendment-fix-dick-thornburgh.html)

Second, critics will argue that the adoption of a balanced- budget amendment wouldn’t solve the deficit problem overnight. This is absolutely correct, but begs the issue. Serious supporters of the amendment recognize that a phasing-in of five to 10 years would be required. During this interim period, however, budget makers would have to meet declining deficit targets in order to reach a final balanced budget by the established deadline. As pointed out by former Commerce Secretary Peter G. Peterson, such “steady progress toward eliminating the deficit will maintain investor confidence, keep long-term interest rates headed down and keep our economy growing.” Third, it will be argued that such an amendment would require vast cuts in social services, entitlements and defense spending. Not necessarily. True, these programs would have to be paid for on a current basis rather than heaped on the backs of future generations. Difficult choices would have to be made about priorities and program funding. But the very purpose of the amendment is to discipline the executive and legislative branches, not to propose or perpetuate vast spending programs without providing the revenue to fund them.

#### Excessive government spending hurts investor confidence

Sharon Wrobel, 11/22/07, business writer for the Jerusalem Post, “Higher gov’t spending could jeopardize investor confidence”, http://www.jpost.com/Business/BusinessNews/Article.aspx?id=82842

Economists warned on Wednesday that increasing the government's annual spending ceiling in the 2008 budget, as proposed by a new bill this week, could damage international investor confidence and threaten the positive momentum spurring economic growth. Labor MK Avishay Braverman submitted a private bill on Tuesday to increase the spending growth target of the 2008 state budget by 2.5 percent, or NIS 2 billion, instead of the 1.7% originally set by the Finance Ministry. "After the government already passed the 2008 budget in a first reading, changes to the spending ceiling would have a very severe impact on the markets and damage investor confidence of the international community," Prof. Rafi Melnick, Dean of the Lauder School of Government, Diplomacy and Strategy at the Interdisciplinary Center Herzliya and former senior economist at the Bank of Israel told The Jerusalem Post. "This is not the right time for Israel to deviate from investors' expectations, a time when there is much uncertainty over the state of the global economy, which is poised to slow down and when borrowing money could become more expensive." Prof. Melnick added that relative to other economies, Israel's economy was very stable and is growing at a fast pace; driven by foreign investor confidence and adherence to fiscal discipline, which the government would not want to jeopardize. Discussing the bill proposal at the Knesset Finance Committee this week, Braverman argued that in a situation such as now in which the economy is prospering and enjoying a budget surplus, money should be allocated to serve socio-economic issues such as investment into welfare, schools and hospitals. According to Braverman, the bill was backed by 69 of the 120 members of parliament. "Braverman's proposal to raise government spending by two thirds of the growth rate is based on a procyclic policy- one that moves in the same direction as the economy, which has proven in the past to be destabilizing, while government spending growth of 1.7% pertains to a countercyclic rule and one that moves in the opposite direction as the economy is stabilizing," Melnick said. Since the beginning of the year, the government has registered a budget surplus of NIS 8.7b. "2007 is likely to conclude with a budget surplus reaching up to 0.5% of GDP. This is in contrast to an original budget deficit target of 2.9% of GDP," Dr. Gil Bufman, chief economist at Bank Leumi wrote in a recent economic update. Other economists raised skepticism over the bill proposal. "What's important is not so much the height of the spending ceiling, but the structure of the budget. If spending is being raised to invest into infrastructure to improve schools, education and welfare, then we might see an economic benefit but not if money is spent on raising benefits," said Shlomo Maoz, chief economist at Excellence Nessuah. Only a few weeks ago, representatives of the international credit rating agency Standard & Poor's came to Israel to meet with Prof. Stanley Fischer, the governor of the Bank of Israel, and Finance Minister Ronnie Bar-On, for a review of Israel's economy. Fischer has been boasting about the growth of the local economy warranting an upgrade of Israel's credit rating, saying that debt-to-GDP ratio had fallen to 80%, the economy has not been affected by the US sub-prime mortgage crisis and that Israel was a candidate for membership in the OECD. S&P is in the process of reviewing Israel's credit rating and is expected to publish its update by mid-February. "Fiscal performance is an important component, which has an impact on our rating," VÃ©ronique Paillat-Chayrigues, credit analyst at S&P told the Post. "It's never good news if expenditures are increased. We would consider a downgrade of Israel's rating in the case of significant deviations from the fiscal policy expectations set by the Finance Ministry, although there are other components which determine the rating." In July, S&P warned that the country's credit rating outlook could be at risk if the government failed to maintain budget discipline. S&P warned that it would lower Israel's credit rating from "positive" to "stable" if the 2008 budget deviates from fiscal policy lines set by the government between 2005 and 2007. "Our positive outlook on the Israeli rating incorporates our expectation that fiscal strengthening will remain a key political priority and that the debt burden will fall at a regular pace. Should these expectations be misplaced, the outlook on the ratings could revert to 'stable,'" S&P cautioned.

Spending Bad – Confidence

#### A spending cap will boost investor confidence – Georgia proves

Helena Bedwell, 10/15/09, reporter for Bloomberg Business & Financial News, “IMF Says Georgian Spending Cap Will Boost Investor Confidence”, http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aXcUhNAqCN28

Oct. 15 (Bloomberg) -- Georgian President Mikheil Saakashvili’s plan to cap government spending, budget deficits and state debt will boost investor confidence in the former Soviet republic’s economy, according to the IMF. Saakashvili’s proposed Economic Liberty Act “will reinforce the government’s credibility and have a positive impact on investment,” Edward Gardner, the International Monetary Fund’s senior resident representative in Georgia, said in an interview in the capital Tbilisi today. Foreign investment fell to $92.2 million in the second quarter from $605.4 million in the year-earlier period as Georgia struggled to recover from an August 2008 war with Russia and the global economic slump. Georgia’s $12.8 billion economy is shrinking for the first time since the so-called Rose Revolution in 2003 that swept Saakashvili to power. The government forecasts a contraction of 1.5 percent in 2009 and 2 percent growth in 2010. The economy may rebound in the fourth quarter, a year after it entered a recession, though 2009 foreign investment won’t exceed $1 billion, compared with $2 billion initially forecast by the government, Finance Minister Kakha Baindurashvili said on Oct. 6. Gardner said the IMF had “always projected no more than $1 billion in investment.” He agreed with Baindurashvili that the economy may resume growth in the fourth quarter. To achieve this, “you need quite a considerable pick-up in the second half of the year,” he said. In addition to spending and debt caps, Saakashvili called for referenda for tax changes and a ban on creating new regulatory agencies. His proposals must be approved by parliament.

**Government cuts improve stock market**

Columbia Tribune, 7/20/11, “‘Gang of Six’ progress helps stocks rebound”, http://www.columbiatribune.com/news/2011/jul/20/gang-of-six-progress-helps-stocks-rebound/

Strong profits and a bipartisan plan to lift the U.S. debt limit drove a stock market rebound yesterday. Stock indexes rose after Coca-Cola, IBM and other companies reported better second-quarter earnings. The indexes added to their gains in the afternoon after President Barack Obama backed a proposal by six senators that would cut debt by $3.7 trillion over the next decade and raise the country’s $14.3 trillion debt ceiling. The Dow Jones industrial average posted its largest one-day jump this year. “The stock market had been looking for a reason to have a relief rally, said Burt White, chief investment officer at LPL Financial in Boston. “And it looks like they got the start of one today. “

### Spending Bad - Investment

#### Deficit spending lowers demand for domestic assets and investment

Ball and Mankiw 95 Laurence Ball, Professor of Economics at Johns Hopkins University, And N. Gregory Mankiw, Professor of Economics at Harvard University, 9/2/95, “What Do Budget Deficits Do?”, pp. 101-103, Budget Deficits and Debt: Issues and Options

Why might the demand for a country’s assets fall? There are two distinct but complementary stories about how a rising national debt could lead to lower demand for domestic assets. The first story emphasizes the effect of deficits on a country’s net-foreign-asset position. As we have discussed, budget deficits tend to produce trade deficits, which a country finances by selling assets abroad. Yet there may be limits to the quantity of domestic assets foreigners are willing to hold. For various reasons (such as lack of information, exchange-rate risk, or sheer xenophobia), international diversification is far from perfect. This fact is consistent with the finding of Feldstein and Horioka (1980) that a country’s saving roughly balances its investment over long periods. As a country’s net-foreign-asset position deteriorates, foreign investors may become less and less willing to purchase additional domestic assets. A second story is that a rising level of government debt makes investors fear government default or a similar policy aimed at holders of domestic assets. Unlike the first story, this story is relevant even if a country has not reached a negative net-foreignasset position. And in this story, domestic as well as foreign investors flee domestic assets. In speculating about a loss of investor confidence, one is naturally led to draw on the experience of the debt crisis in less developed countries (LDC) during the 1980s. (The case of Mexico in 1994 is less relevant, because it involves imprudent monetary and exchange-rate policy as well as debt.) In the LDC debt crisis, capital inflows in the form of bank loans dried up when countries began having trouble servicing their debts, leading to fears of widespread default. It is tempting to imagine that this experience is not relevant to countries like the United States—that rich countries would never default. But Orange County, California is even richer than the United States, and it is about to default on its debt. Orange County voters, turning down a tax increase needed to honor the debt, appear to reject the idea that they should pay for their government’s mistakes. It is easy to imagine such arguments at the national level—or at least a fear on the part of investors that such arguments will arise. There is, however, a reason that the LDC debt crisis is an imperfect guide to hard landings in the United States or European countries. The Latin American debt was external: it was owed to foreigners. Thus the direct effect of default was a loss to foreigners, making default a relatively attractive way out of a fiscal crisis. The same is true for Orange County: most of its debt was owned outside of the county. In the United States, by contrast, most of the national debt is owned by American citizens. Since an internal debt makes default less tempting, it is likely to delay a hard landing: it takes a higher level of debt to spook investors. The fact that a debt is internal also affects the nature of the prospective policies that might spark a hard landing. If the debt-income ratio spins out of control, something must be done or default is unavoidable. And it might remain impossible politically to raise income taxes sufficiently. One possible outcome is a general tax on wealth. The government might require owners of its bonds to “share in the sacrifice” through partial default, but it would also tax the holders of other assets. The tax could extend to foreign owners of domestic assets to reduce the burden on domestic citizens. An unsustainable path of debt and a worsening net foreign asset position could lead investors to fear other unpleasant consequences as well. Extensive foreign ownership of U.S. assets could lead to restrictions on capital outflows. Perhaps as debt grows and wages fall relative to those of other countries, political outrage will produce a government that increases interference in the economy. Many U.S. politicians, for example, are tempted to blame domestic problems on Japanese trade practices; a trade war is not an unthinkable result of a general decline in living standards. Similarly, many less developed countries have unhappy histories in which economic problems create political pressures for policies that discourage investment and make the problems even worse. Fear of these outcomes—or just a belief that something bad must happen if debt continues to grow— could lead to a fall in the demand for domestic assets.

Spending Bad - Investment

#### Long-term deficit spending reduces investment and productivity

Ball and Mankiw 95 Laurence Ball, Professor of Economics at Johns Hopkins University, And N. Gregory Mankiw, Professor of Economics at Harvard University, 9/2/95, “What Do Budget Deficits Do?” pp. 100-101, Budget Deficits and Debt: Issues and Options

The effects described so far begin as soon as the government begins to run a budget deficit. Suppose, as is often the case, that the government runs deficits for a sustained period, building up a stock of debt. In this case, the accumulated effects of the deficits alter the economy’s output and wealth. In the long run, an economy’s output is determined by its productive capacity, which, in turn, is partly determined by its stock of capital. When deficits reduce investment, the capital stock grows more slowly than it otherwise would. Over a year or two, this crowding out of investment has a negligible effect on the capital stock. But if deficits continue for a decade or more, they can substantially reduce the economy’s capacity to produce goods and services. The flow of assets overseas has similar effects. When foreigners increase their ownership of domestic bonds, real estate, or equity, more of the income from production flows overseas in the form of interest, rent, and profit. National income—the value of production that accrues to residents of a nation—falls when foreigners receive more of the return on domestic assets. Recall that budget deficits, by reducing national saving, must reduce either investment or net exports. As a result, they must lead to some combination of a smaller capital stock and greater foreign ownership of domestic assets. Although there is controversy about which of these effects is larger, this issue is not crucial for the impact on national income. If budget deficits crowd out capital, national income falls because less is produced; if budget deficits lead to trade deficits, just as much is produced, but less of the income from production accrues to domestic residents. In addition to affecting total income, deficits also alter factor prices: wages (the return to labor) and profits (the return to the owners of capital). According to the standard theory of factor markets, the marginal product of labor determines the real wage, and the marginal product of capital determines the rate of profit. When deficits reduce the capital stock, the marginal product of labor falls, for each worker has less capital to work with. At the same time, the marginal product of capital rises, for the scarcity of capital makes the marginal unit of capital more valuable. Thus, to the extent that budget deficits reduce the capital stock, they lead to lower real wages and higher rates of profit.

### Spending Bad – Interest Rates

#### Increased government spending will raise interest rates

Reed Garfield, 3/27/95, senior economist for Joint Economic Committee of the Congress of the U.S., “Government Spending and Economic Growth”, http://www.house.gov/jec/fiscal/budget/spending/spending.htm

The growth of plant and equipment, or capital investment, is negatively impacted by government spending. Simply put, government spending "crowds out" private investment. When government uses resources, there are fewer resources for private purposes. Temporarily, government spending and private investment can be complementary. Government's grab for resources can be met through reduction in savings or capital inflows from abroad. In the long-run, private investment must fall as government increases spending. Government may invest the resources it controls in productive areas, but political forces are less likely than private markets to allocate resources where the returns are the highest. The state invests resources where the political demands are greatest not where the profit opportunities are large. Government spending also can raise interest rates. Higher interest rates discourage private sector investment because it ends up costing the investor more over the long run. As interest rates rise, the returns to investment fall. Capital projects that made economic sense at lower interest rates are no longer viable. All these effects serve to lower the long-term growth rate of the capital stock. Rent-Seeking Economic growth is adversely impacted when the government imposes itself through spending and regulations. As more resources are channeled through the political process, the opportunities for rent-seeking increase. Rent-seeking is the manipulation of the political process for personal gain. Individuals, or special interests, attempt to create government-sanctioned monopolies or impose costs upon other people without those people receiving the full, or any, benefit from the action. Rent-seekers expend government resources to capture these monopoly gains. The resources expended on rent-seeking are a net loss to society. As the state grows, it provides increasing opportunities for transfers of rents. It also increases the profitability of rent-seeking. Expanding the opportunity for rent-seeking increases waste and permanently lowers the growth rate of the economy. The productivity of rent-seeking activity is zero, or negative, for the economy because rent-seeking reduces potential economic output. Conclusion Some government spending is crucial for a well-functioning economy. However, currently the United States and most developed countries' governments spend excessively which reduces economic growth.[3] In other words, as governments divert resources away from private entrepreneurs, jobs, investment, and productivity decline which ultimately slows down the economy.

#### Government spending will continue to push interest rates way up: empirically proven by Nigeria

Nigerian Business Community, 5/5/11, Business Community Platform for Nigeria, “Government borrowing, spending push interest rates way up”, http://www.nigerianpro.com/content/government-borrowing-spending-push-interest-rate-upwards

The Central Bank of Nigeria (CBN) has said that as long as the federal government continues to patronize the bond market, it would be difficult to achieve low interest rates. CBN deputy governor, economic policy, Sarah Alade, said while the central bank is striving to achieve an inclusive economy that would capture more Nigerians, that effort was being made difficult by the huge borrowing and expenditure of government. According to her, government needs to begin to control its level of spending in order for the real economy to have access to cheap funds. "In terms of interest rate being high, when government borrows money, offering banks higher rates than the private sector can offer, banks naturally lend to government. So as long as the Debt Management Office keeps selling bonds, this expansionary fiscal policy, and interest rate will remain high." She said when control is placed on government spending, then ordinary Nigerians can enjoy low interest rate. Speaking at the presentation of the regional outlook for sub-Saharan Africa by the International Monetary Fund in Lagos on Tuesday, Mrs Alade said the central bank was working at improving access to finance for Nigerians by reforms of the payment system. "We are thinking about agency banking where you use the post office, so that more people will be able to save and receive money. For access to finance, we are doing a lot of things," she said. Permanent secretary in the ministry of finance, Danladi Kifase who represented the finance minister, Olusegun Aganga, said government has already embarked on measures that would cut down on its expensive and improve the quality of its expenditure. "Government is determined to bring the budget back to balance. We are working to diversify our revenue base away from oil and gas by strengthening the tax base. The use of performance-based budgeting will help toward delivering efficiency in spending," the minister said. He said the establishment of the sovereign wealth fund was geared towards ensuring discipline in government spending and to ensure that excess revenue are saved for judiciously applied. According to Mr Kifase, government needs to continue to spend money in order to keep the economy running. "We cannot keep money in the bank when people need roads. The problem is the quality of spending." He said government would improve on its expenditure to achieve growth in the economy.

### Spending Bad – Mismanagement

#### Governments misuse funds – optimal involvement won’t happen

Clemens et. al(Director of Research at the Pacific Research Institute) October 2010

(Jason, Niels Veldhuis is the Fraser Institute President and one of Canada’s most-read private-sector economists, Julie Kaszton is a research fellow at the Pacific Research Institute, “No Bang for the Taxpayer’s Buck: Why California Must Reform Spending and Trim Government,” http://www.pacificresearch.org/docLib/20101013\_CAProsp\_3\_F%284%29.pdf)

A broad summary of the research on the economic effects of government spending shows that many governments operate where they are not needed. The resources expended, along with the taxes to finance them, do not contribute to economic growth. Government beyond the optimal level contributes little, if anything, to economic prosperity and social progress. At a little more than 40 percent of GDP, total government spending in the United States is clearly much greater than any of the specific estimates for economic-growth maximization or social progress.

The government mismanages the economy – empirically it produces unintended negative consequences

Peter Foster is a staff writer for the National Post, 8/26/09, “Keynesian road to ruin”, Proquest

The U.S.'s "cash for clunkers" program ended this week amid a frenzy of paperwork and widespread dealer complaints about Washington's sloth in getting those proverbial cheques in the mail. Nevertheless, President Obama has called the scheme -- under which car buyers received up to US$4,500 for trading in their gas guzzlers -- "successful beyond anybody's imagination." But surely anybody with the slightest economic imagination could have forecast that the program would be wildly popular. Its likely "success" could have been gauged simply by looking across the Atlantic. Similar schemes in Europe have also been big hits, both with the public and to national budgets. Germany's, for example, was among those expanded and extended. But then Wolfgang Franz, chairman of German Chancellor Angela Merkel's council of independent economic advisors, noted with admirable candour that "Every decent economist would agree that this decision is economic nonsense." Good point. How economically challenged does one have to be to believe that this program could put the auto industry on the "road to recovery" without putting the economy more broadly on the road to ruin? The U.S. Car Allowance Rebate System, CARS (do bureaucrats get bonuses for coining annoying acronyms?), which started last month, was due to run until November. The original US$1-billion budget disappeared in a week and was topped up by another US$2-billion, which disappeared as of yesterday. As the Post's auto writer David 'Motor Mouth' Booth noted a couple of weeks ago (in a column that put most naive economics reporters to shame), this policy was based on the kind of rash and desperate incentives that had helped put GM and Chrysler under in the first place! It's difficult to know how to categorize such policy lunacy: Cargo cult economics? Single-entry bookkeeping? The Broken Window Fallacy? The cargo cult was based on mistaking form for substance (as in primitive tribes last century observing that airplanes were good for trade, so imagining that prosperity would follow if they built one out of sticks and shoots in the jungle!). Similarly, CARS was based on the notion that since spending is part of a healthy economy, stimulating spending must be good! Which brings us to single-entry bookkeeping, because it is widely ignored that the "stimulus" has to be paid for later. Every credit needs a debit. Then Frederic Bastiat's Broken Window Fallacy comes into play because, again, nobody seems to be taking account of where money might have been spent if it hadn't been diverted towards replacing deliberately broken cars. Bastiat was a Frenchman, so another relatively recent event might be used to illuminate his point: that of rioting youths torching cars. They too, were "stimulating" auto sales. In fact, all these numbskull notions are subsumed under the master fallacy that is now, yet again, stalking the globe: Keynesianism, the policy of wise government macro-management that most observers thought had been buried in the 1970s. The rebirth of Keynesianism is in fact symptomatic of policy bankruptcy. Still, a drowning wonk will grab at a straw, or even a traded-in two-ton pickup. Robert Lucas, one of several prominent Nobel economists to disassemble the fallacies of Keynesianism, noted last year, "I guess everyone is a Keynesian in a foxhole." However -- to follow Professor Lucas' reference back to its roots -- while belief in God can certainly do no harm when facing death, because if you're wrong you won't be around to kick yourself, belief in Keynesianism is different, because it has real world consequences. In the meantime, and inevitably, cash for clunkers has produced an array of unintended and perverse results. The increasingly-less Big Three were concerned from the beginning that people would buy non-American cars with their Obamavouchers, and sure enough, just 41% of cars sold under the scheme came from GM, Ford or Chrysler. The big winners have been Toyota and Honda, whose Corolla and Civic have been, respectively, the biggest sellers. This is perceived as (temporary) good news for the Canadian plants of the Japanese manufacturers, which again is ironic because the Harper government has so far resisted the bleating of Canadian auto manufacturers that Canada is "missing out" on the opportunity to waste more taxpayers' money on top of the horrendous costs of "saving" GM and Chrysler jobs. The Harper government has certainly dabbled in dumb bureaucratic schemes, such as "feebates" and the "ecoAUTO" program. Also, earlier this year Ottawa introduced a cash for clunkers scheme in the form of a modest $300 rebate (or a bicycle voucher) to "Retire Your Ride." Critics called the program a "wet noodle," but they were missing the point. Wet policy noodles are good. The less the program had been a wet noodle, the more it would have been an improvised exploding economic device, like all Keynesian policy clunkers. Meanwhile, starting this week, the tumbleweeds will again be rolling though U.S. car dealerships.

## AT: Spending Good/Stimulus

### AT: Stimulus

#### Keynesian theory is wrong—multiplier effect is small, investment causes crowding-out, and studies show negative correlation between spending and growth

Stratmann and Okolski 10 Thomas Stratmann, a scholar at the Mercatus Center and a professor of economics at George Mason University, And Gabriel Lucjan Okolski, Presidential Management Fellow in the Department of Transportation, 6/10/10, “Does Government Spending Affect Economic Growth?” MERCATUS CENTER AT GEORGE MASON UNIVERSITY, http://mercatus.org/publication/does-government-spending-affect-economic-growth

THE CONSEQUENCES OF UNPRODUCTIVE SPENDING AND THE MULTIPLIER EFFECT Proponents of government spending often point to the fiscal multiplier as a way that spending can fuel growth. The multiplier is a factor by which some measure of economy-wide output (such as GDP) increases in response to a given amount of government spending. According to the multiplier theory, an initial burst of government spending trickles through the economy and is re-spent over and over again, thus growing the economy. A multiplier of 1.0 implies that if government created a project that hired 100 people, it would put exactly 100 (100 x 1.0) people into the workforce. A multiplier larger than 1 implies more employment, and a number smaller than 1 implies a net job loss. In its 2009 assessment of the job effects of the stimulus plan, the incoming Obama administration used a multiplier estimate of approximately 1.5 for government spending for most quarters. This would mean that for every dollar of government stimulus spending, GDP would increase by one and a half dollars.8 In practice, however, unproductive government spending is likely to have a smaller multiplier effect. In a September 2009 National Bureau of Economic Research (NBER) paper, Harvard economists Robert Barro and Charles Redlick estimated that the multiplier from government defense spending reaches 1.0 at high levels of unemployment but is less than 1.0 at lower unemployment rates. Non-defense spending may have an even smaller multiplier effect.9 Another recent study corroborates this finding. NBER economist Valerie A. Ramey estimates a spending multiplier range from 0.6 to 1.1.10 Barro and Ramey's multiplier figures, far lower than the Obama administration estimates, indicate that government spending may actually decrease economic growth, possibly due to inefficient use of money. CROWDING OUT PRIVATE SPENDING AND EMPIRICAL EVIDENCE Taxes finance government spending; therefore, an increase in government spending increases the tax burden on citizens—either now or in the future—which leads to a reduction in private spending and investment. This effect is known as "crowding out." In addition to crowding out private spending, government outlays may also crowd out interest-sensitive investment.11 Government spending reduces savings in the economy, thus increasing interest rates. This can lead to less investment in areas such as home building and productive capacity, which includes the facilities and infrastructure used to contribute to the economy's output. An NBER paper that analyzes a panel of OECD countries found that government spending also has a strong negative correlation with business investment.12 Conversely, when governments cut spending, there is a surge in private investment. Robert Barro discusses some of the major papers on this topic that find a negative correlation between government spending and GDP growth.13 Additionally, in a study of 76 countries, the University of Vienna's Dennis C. Mueller and George Mason University's Thomas Stratmann found a statistically significant negative correlation between government size and economic growth.14 Though a large portion of the literature finds no positive correlation between government spending and economic growth, some empirical studies have. For example, a 1993 paper by economists William Easterly and Sergio Rebelo looked at empirical data from approximately 100 countries from 1970-1988 and found a positive correlation between general government investment and GDP growth.15 This lack of consensus in the empirical findings indicates the inherent difficulties with measuring such correlations in a complex economy. However, despite the lack of empirical consensus, the theoretical literature indicates that government spending is unlikely to be as productive for economic growth as simply leaving the money in the private sector.

#### Massive stimulus fails—empirics prove

Stratmann and Okolski 10 Thomas Stratmann, a scholar at the Mercatus Center and a professor of economics at George Mason University, And Gabriel Lucjan Okolski, Presidential Management Fellow in the Department of Transportation, 6/10/10, “Does Government Spending Affect Economic Growth?” MERCATUS CENTER AT GEORGE MASON UNIVERSITY, http://mercatus.org/publication/does-government-spending-affect-economic-growth

Government spending, even in a time of crisis, is not an automatic boon for an economy's growth. A body of empirical evidence shows that, in practice, government outlays designed to stimulate the economy may fall short of that goal. Such findings have serious consequences as the United States embarks on a massive government spending initiative. Before it approves any additional spending to boost growth, the government should use the best peer-reviewed literature to estimate whether such spending is likely to stimulate growth and report how much uncertainty surrounds those estimates. These analyses should be made available to the public for comment prior to enacting this kind of legislation.

AT: Stimulus

#### Keynesian theory is wrong—budget deficits don’t affect interest rates and investment crowds out business

Brady 11 Kevin Brady, Joint Economic Committee Republicans Vice Chairman Designate, 3/15/11, “Spend Less, Owe Less, Grow the Economy,” Joint Economic Committee Republicans, http://www.speaker.gov/sites/speaker.house.gov/files/UploadedFiles/JEC\_Jobs\_Study.pdf

While Keynesian theory may sound plausible, it is not well supported. First, the relationship between government budget deficits or surpluses (or government debt) and real interest rates is more complex and smaller than Keynesians contend. Increases in federal budget deficits due to temporary factors—e.g., recession or war—which financial market participants expect to be transitory and reversed do not affect real interest rates. However, a permanent increase in federal budget deficits does elicit a small, but statistically significant increase in real interest rates. For example, Engen and Hubbard (2004) found that “an increase in government debt equivalent to one percentage point of GDP” would increase real interest rates by 2 to 3 basis points.8 Moreover, Laubach (2009) found that a projected increase in the federal budget deficit equal to 1% of GDP raises the five-year-ahead 10-year forward Treasury rate by 20 to 29 basis points. Alternatively, Laubach found that a projected increase in the federal debt held by the public equal to 1% of GDP increased the five-year-ahead 10-year forward Treasury rate by 3 to 4 basis points.9 Relationship among government budget deficits and debt, real interest rates, and business investment. Second, recent empirical studies have found that government debt, the real interest rate, and business investment are not as statistically related as Keynesians contend. In a study examining whether additional government debt “crowds out” private investment through a higher real interest rate, Traum and Yang (2010) found “no systematic relationship among [government] debt, the real interest rate, and [business] investment.”10 Short term. Additional government debt, in the short term, may either “crowd in” or “crowd out” business depending on what caused government debt as a percentage of GDP to increase. If higher government debt as a percentage of GDP is due to a reduction in “distortionary taxes”—e.g., high marginal tax rates on capital income – that increase the after-tax rate of return on business investment, then higher government debt is associated with a short-term increase in business investment. On the other hand, if higher government debt as a percentage of GDP is due to an increase in government spending as a percentage of GDP— particularly for higher government consumption and transfer payments to households and firms—then higher government debt is associated with a short-term decrease in business investment. Long term. Higher government debt as a percentage of GDP, in the long term, reduces business investment. Imposing higher taxes in order to service the increase in government debt as a percentage of GDP drives this negative long-term relationship with business investment.

#### Spending policy fails to produce Keynesian stimulus

Filger 10 Sheldon Filger, political writer, 2/21/10, “A Keynesian Leap Off the Financial Cliff,” Global Economic Crisis, http://www.globaleconomiccrisis.com/blog/archives/956

Though John Maynard Keynes is portrayed as a deficit-loving interventionist, in reality he was not. What is left out of the description of his theory in regards to counter-cyclical fiscal policy is that Keynes also believed that in times of relative prosperity sovereigns should create budget surpluses. He belief was that booms and busts were an integral characteristic of modern capitalism, and that the accumulation of reserves during times of plenty would enable governments to engage in temporary deficit spending to combat a severe recession, without creating the long-term danger of exploding national debt to GDP ratios. This is an aspect of Keynes’s views on fiscal policy that has been conveniently forgotten by the modern interpreters of Keynesian economics. Since World War II, the U.S. has seldom run balanced budgets. If generally accepted accounting principles were applied to official U.S. federal government budget reports, which require taking into account future liabilities for Social Security and Medicare, then during this period the United States has always run large fiscal deficits, even during times of relative economic prosperity. What this means in reality is that the conditions laid out by John Maynard Keynes for allowing a sovereign to engage in deficit spending during a recession, namely building budget surpluses during periods of economic expansion, have never been adhered to. During the Great Depression, the U.S. government did engage in substantial deficit spending within the framework of the New Deal, but with a ratio to GDP far lower than what is currently occurring on President Obama’s watch. This fiscal policy was engaged in with a cumulative national debt to GDP ratio nowhere near the current level, and with a large base of domestic savers prepared to buy U.S. government debt, in contrast with the present day reliance on foreign buyers of U.S. Treasury Bills. If John Maynard Keynes were alive today, I suspect he would be horrified at the manner in which his economic theories have been distorted, and the likely outcome of such fiscal profligacy.

AT: Stimulus

#### Stimulus fails – austerity hasn’t been implemented correctly

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As fiscal policy, government “stimulus” schemes have a good reputation, but undeservedly so. Invariably they only undermine and delay recoveries. “The economy,” remember, is what remains today of our private system of production; it can’t be “stimulated” by government taking more of its precious resources (savings) through borrowing, and then spending the proceeds on those who don’t work (i.e., don’t produce wealth) or on those who exhibit a greater “propensity to consume” (i.e., to destroy wealth). In contrast, fiscal “austerity” plans tend to have a bad reputation, but also undeservedly. Invariably such plans entail additional taxation of the private sector but no real restraints on government spending. Austerity programs, in truth, are perfectly compatible with renewed prosperity, if by “austerity” is meant not additional tax burdens laid on a struggling, ailing economy but material reductions in the size, scope and cost of government.

#### Japan proves stimulus fails – Krugman is wrong

Richard Salsman (Richard Salsman is president and chief market strategist of [InterMarket Forecasting, Inc.](http://www.intermarketforecasting.com/), a research and forecasting firm, 6/12, Forbes  <http://www.forbes.com/sites/richardsalsman/2012/06/26/fiscal-austerity-and-economic-prosperity-pt-iii-why-government-spending-retards-growth/>)

According to Keynesian Paul Krugman, austerity plans are “self-defeating.”As he puts it, “there’s quite a good case to be made that austerity in the face of a depressed economy is, literally, a false economy – that it actually makes long-run budget problems worse.” Well, “yes,” if austerity means more taxes imposed on the economy’s producers, but “no,” if instead it means spending cuts imposed on the economy’s non-producers (politicians). Krugman denies this, because he opposes reductions in government spending, and wants higher taxes on the rich, even in today’s context, a context he describes as a “depression,” and which, he adds, has been caused not by vast stimulus spending, to date, but by too little of it. In the 1990s it was Krugman who most loudly championed Japan’s innumerable and reckless “stimulus” schemes, together with dozens of rounds of “quantitative easing” (fiat money printing). Japan followed his advice and ever since then has suffered a secular stagnation. Since 1990 Japan’s public debt has ballooned from 68% to 233% of GDP; its money supply is up 286%, while its industrial output is lower by 3.4% and its equity index is down by 73%. This is what Keynesians “stimulus” has done for Japan – and Krugman wants the same for the U.S.

Zero historical evidence supports stimulus

Robert Barro. professor of economics at Harvard and a senior fellow at Stanford's Hoover Institution. 9-24-11.Wall street Journal. 1http://online.wsj.com/article/SB10001424053111903596904576516412073445854.html

Theorizing aside, Keynesian policy conclusions, such as the wisdom of additional stimulus geared to money transfers, should come down to empirical evidence. And there is zero evidence that deficit-financed transfers raise GDP and employment—not to mention evidence for a multiplier of two.

Spending only works in the short term - empirics

Robert Barro. professor of economics at Harvard and a senior fellow at Stanford's Hoover Institution.5-9-12. Wall street Journal <http://online.wsj.com/article/SB10001424052702304451104577390482019129156.html?KEYWORDS=ROBERT+J+BARRO>

For the U.S., my view is that the large fiscal deficits had a moderately positive effect on GDP growth in 2009, but this effect faded quickly and most likely became negative for 2011 and 2012. Yet many Keynesian economists look at the weak U.S. recovery and conclude that the problem was that the government lacked sufficient commitment to fiscal expansion; it should have been even larger and pursued over an extended period. This viewpoint is dangerously unstable. Every time heightened fiscal deficits fail to produce desirable outcomes, the policy advice is to choose still larger deficits. If, as I believe to be true, fiscal deficits have only a short-run expansionary impact on growth and then become negative, the results from following this policy advice are persistently low economic growth and an exploding ratio of public debt to GDP. The last conclusion is not just academic, because it fits with the behavior of Japan over the past two decades. Once a comparatively low public-debt nation, Japan apparently bought the Keynesian message many years ago. The consequence for today is a ratio of government debt to GDP around 210%—the largest in the world.

AT: Stimulus

#### Stimulus fails

Uhlig and Drautzburg (Chairman and Professor of Department of Economics of the University of Chicago. PhD candidate in Economics at the University of Chicago) 2011 (Harald and Thorsten “Financing fiscal stimulus” <http://www.voxeu.org/article/financing-fiscal-stimulus> )

Raising output in the crisis need not increase the welfare of everyone to stabilise GDP in response to a crisis. With this caveat in mind, consider how output effects should be measured. It is instructive to examine the components of the stimulus bill, which are plotted in Figure 1 as a percentage of GDP. Two features stand out. First, the expenditure is split unevenly over time. Second, only about a quarter of the stimulus is spent on government consumption. To address the first feature of the data, spending and its output effect have to be aggregated over time. A natural choice is to discount costs and benefits by the discount rate the government faces on its debt. The ratio of the resulting present discounted values of the output effect relative to the cost of the stimulus is called the long-run multiplier. This statistic states how much GDP rises for each dollar spent on the ARRA. Figure 1. Components of the American Recovery and Reinvestment Act, in % of 2008 GDP To do justice to the different components of government spending, we proceed by extending standard macro models as they do not distinguish government consumption from government investment, and allow no role for distortionary taxes and transfer payments. Which model to use? A natural point of departure for the analysis of fiscal policy in the recent financial crisis is the medium-scale macro models, such as Smets and Wouters (2007), that are commonly used in the analysis of monetary policy. In such a model, the financial crisis can be modelled as either an exogenously fixed nominal interest rate or as an endogenously generated binding lower bound. Addressing the fiscal stimulus properly requires, however, a more detailed government sector, which is where our extensions come in. Starting with the largest component of the stimulus plan, transfer payments play no role in these monetary macro models. Ricardian equivalence holds, meaning that issuing more debt to finance transfers today in exchange for a reduction in future transfers is irrelevant. Financing increased transfers today with distortionary taxes tomorrow would already break this equivalence. It would, however, not be in the spirit of the actual stimulus, which was meant to stimulate private sector consumption. A work-around is to introduce heterogeneous households, some of which consume their current period income and do not save, possibly because they are very impatient. While government consumption is standard in monetary macro models, government investment is not. It does matter, however, and comprises between 3-4% of GDP. An intuitive way to model government capital is analogous to public infrastructure: it increases private sector productivity, but is subject to congestion. The government may then choose an optimal amount of investment to equate the discounted social marginal product of government capital to the cost. We can then consider how exogenous increases to government investment affect the economy. Going back to the observation that in practice raising revenue for the government is costly, distortionary taxation should also be incorporated into the extended model. We follow Uhlig (2010), who considers distortionary taxes on consumption, hours worked, and capital. The government can issue debt, but eventually has to raise enough taxes to pay back the debt. In our baseline scenario, labour tax rates are adjusted. Such an extended model features many parameters, only some of which are easily calibrated. Following the common practice in monetary macro models, we estimate a linearised version of the model using Bayesian techniques as a natural way to parameterise the model. In what follows, the results of this exercise, based on US post-war data up to the 4th quarter of 2008, are summarised.

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#### **Keynesian spending hurts the economy**

Peter Suderman, senior editor of Reason magazine 11-18-2011 <http://www.opposingviews.com/i/money/recession/cbo-stimulus-will-hurt-economy-long-run>

Peter Suderman, our colleague over at Reason.com, points out recent testimony by Congressional Budget Office (CBO) director Douglas Elmendorf that the $800 billion stimulus package passed in February 2009 will have a "net negative effect on the growth of GDP over 10 years." This is quite notable (and Suderman links to the video testimony; listen for Elmendorf's comments around 1:20 mark.) It's also worth expanding on a little. The effects of the Stimulus program are being debated (see my extensive critique here from 2010), but the fact that the CBO recognizes the potential for all that money dumped into the economy becoming a drag in the long run implies at least their forecasting models recognize spending has to be productive in order for it to really lift the economy. Much of the support for the Stimulus package was based on a very crude Keynesian economic model that presumed that the problem with the economy was almost exclusively an artifact of depressed consumer spending. In this naive model, all you need to do is pump money into the economy so that people spend it. And, most forecasting models, don't differentiate between productive and unproductive spending. So, literally digging ditches and filling them back in again generates "positive" economic impact. (See also my comments on economic multipliers at Planetizen.com for more on this.) Of course, as national unemployment continues to hover around 9 percent, we can pretty much recognize the crude model didn't work. In the real world growth occurs when productivity is enhanced and investment is directed by entrepreneurs into the production of goods and services that people want. Whether the product or service has been determined by a bureaucrat to be "shovel ready" is irrelevant. It's not the spending per se that drives the economy, it's the succesful investment of resources in goods and services that improve our standard of living and quality of life in meaningful and tangible ways on a broad level that boosts economic growth. That's why Apple's investment in iPads and iPods is productive investment and boosts growth while unnecessarly replacing curbs and sidewalks because they are shovel ready does not. The hard-core truth is that the economy is in fact going through a major realignment. The housing market is in shambles, and, as my colleague Anthony Randazzo points out, we probably have a way to go before it really bottoms out. Developers, builders and buyers were responding to the wrong price signals for over a decade, creating a massive housing bubble. But the housing market is only part of the problem. Mixed into the housing market debacle is a financial system seriously out of whack. Until the financial market sorts itself out, capital won't be available for consumers or businesses to spend at the levels before the housing bust. And, it's going to take a while before businesses have a good read on what consumers really want. The good news is that if the government can keep from jumping back into the market too soon and further distort prices, the economy should be on a firmer foundation for sustained long-term growth. That's another way of saying the short-term spending focus of the Stimulus Package set us back more than it pushed us forward. It may have solved a political problem at the time, but it probably did more to delay the necessary re-adjustments than speed them up. That conclusion, I believe, is the takeaway from the CBO testimony.

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#### Keynesian economics is flawed – cuts work better

N. Gregory Mankiw; macroeconomist and Professor of Economics at Harvard University, chairman of the Council of Economic Advisers; 1-09; <http://www.nytimes.com/2009/01/11/business/economy/11view.html>

WHEN the Obama administration finally unveils its proposal to get the economy on the road to recovery, the centerpiece is likely to be a huge increase in government spending. But there are ample reasons to doubt whether this is what the economy needs. Arguably, the seeds of the spending proposal can be found in the classic textbook by Paul A. Samuelson, “Economics.” First published in 1948, the book and others like it dominated college courses in introductory economics for the next half-century. It is a fair bet that much of the Obama team started learning how the economy works through Mr. Samuelson’s eyes. Most notably, Lawrence H. Summers, the new head of the National Economic Council, is Mr. Samuelson’s nephew. Written in the shadow of the Great Depression and World War II, Mr. Samuelson’s text brought the insights of John Maynard Keynes to the masses. A main focus was how to avoid, or at least mitigate, the recurring slumps in economic activity. “When, and if, the next great depression comes along,” Mr. Samuelson wrote on the first page of the first edition, “any one of us may be completely unemployed — without income or prospects.” He added, “It is not too much to say that the widespread creation of dictatorships and the resulting World War II stemmed in no small measure from the world’s failure to meet this basic economic problem adequately.” Economic downturns, Mr. Keynes and Mr. Samuelson taught us, occur when the aggregate demand for goods and services is insufficient. The solution, they said, was for the government to provide demand when the private sector would not. Recent calls for increased infrastructure spending fit well with this textbook theory. But there is much to economics beyond what is taught in Econ 101. In several ways, these Keynesian prescriptions make avoiding depressions seem too easy. When debating increased spending to stimulate the economy, here are a few of the hard questions Congress should consider: HOW MUCH BANG FOR EACH BUCK? Economics textbooks, including Mr. Samuelson’s and my own more recent contribution, teach that each dollar of government spending can increase the nation’s gross domestic product by more than a dollar. When higher government spending increases G.D.P., consumers respond to the extra income they earn by spending more themselves. Higher consumer spending expands aggregate demand further, raising the G.D.P. yet again. And so on. This positive feedback loop is called the multiplier effect. In practice, however, the multiplier for government spending is not very large. The best evidence comes from a recent study by Valerie A. Ramey, an economist at the University of California, San Diego. Based on the United States’ historical record, Professor Ramey estimates that each dollar of government spending increases the G.D.P. by only 1.4 dollars. So, by doing the math, we find that when the G.D.P. expands, less than a third of the increase takes the form of private consumption and investment. Most is for what the government has ordered, which raises the next question. WILL THE EXTRA SPENDING BE ON THINGS WE NEED? If you hire your neighbor for $100 to dig a hole in your backyard and then fill it up, and he hires you to do the same in his yard, the government statisticians report that things are improving. The economy has created two jobs, and the G.D.P. rises by $200. But it is unlikely that, having wasted all that time digging and filling, either of you is better off. People don’t usually spend their money buying things they don’t want or need, so for private transactions, this kind of inefficient spending is not much of a problem. But the same cannot always be said of the government. If the stimulus package takes the form of bridges to nowhere, a result could be economic expansion as measured by standard statistics but little increase in economic well-being. The way to avoid this problem is a rigorous cost-benefit analysis of each government project. Such analysis is hard to do quickly, however, especially when vast sums are at stake. But if it is not done quickly, the economic downturn may be over before the stimulus arrives. HOW WILL IT ALL END? Over the last century, the largest increase in the size of the government occurred during the Great Depression and World War II. Even after these crises were over, they left a legacy of higher spending and taxes. To this day, we have yet to come to grips with how to pay for all that the government created during that era — a problem that will become acute as more baby boomers retire and start collecting the benefits promised. Rahm Emanuel, the incoming White House chief of staff, has said, “You don’t ever want to let a crisis go to waste: it’s an opportunity to do important things that you would otherwise avoid.” What he has in mind is not entirely clear. One possibility is that he wants to use a temporary crisis as a pretense for engineering a permanent increase in the size and scope of the government. Believers in limited government have reason to be wary. MIGHT TAX CUTS BE MORE POTENT? Textbook Keynesian theory says that tax cuts are less potent than spending increases for stimulating an economy. When the government spends a dollar, the dollar is spent. When the government gives a household a dollar back in taxes, the dollar might be saved, which does not add to aggregate demand. The evidence, however, is hard to square with the theory. A recent study by Christina D. Romer and David H. Romer, then economists at the University of California, Berkeley, finds that a dollar of tax cuts raises the G.D.P. by about $3. According to the Romers, the multiplier for tax cuts is more than twice what Professor Ramey finds for spending increases. Why this is so remains a puzzle. One can easily conjecture about what the textbook theory leaves out, but it will take more research to sort things out. And whether these results based on historical data apply to our current extraordinary circumstances is open to debate. Christina Romer, incidentally, has been chosen as the chairwoman of the Council of Economic Advisers in the new administration. Perhaps this fact helps explain why, according to recent reports, tax cuts will be a larger piece of the Obama recovery plan than was previously expected. All these questions should give Congress pause as it considers whether to increase spending to stimulate the economy. But don’t expect such qualms to stop the juggernaut. The prevailing orthodoxy among the nation’s elite holds that increased government spending is the right medicine for what ails the economy. Mr. Samuelson once said, “I don’t care who writes a nation’s laws or crafts its advanced treaties, if I can write its economics textbooks.” The coming stimulus bill, warts and all, will demonstrate brilliantly what he had in mind.

AT: Stimulus

#### Government spending is the worst stimulus – most comprehensive studies

David R. Henderson, PhD. in economics, research fellow with the Hoover Institution and an associate professor of economics at the Graduate School of Business and Public Policy at the Naval Postgraduate School, previously the senior economist for energy policy with President Reagan’s Council of Economic Advisers,’10 (The Hoover Institution, December 1st 2010, “Good on Taxes, Bad on Trade,” http://www.hoover.org/publications/policy-review/article/58036)

Start with the positives. The strongest chapter, by far, is the one titled, “Why You Can’t Stimulate Your Way to Prosperity.” This case against using increases in government spending as a countercyclical policy to end a recession is a nice blend of economic and political analysis. Hubbard and Navarro point out what has long been an argument against such policies: the often long lag between when a law increases spending and when the spending actually occurs. But they go further and draw on some more-recent researchby Harvard economists Alberto Alesina and Silvia Ardagnathat has justifiably received much attention. Alesina and Ardagna, examining fiscal stimulus in 21 countries, found that the most successful ones relied “almost entirely on cuts in business and income taxes” and that the least successful relied on increased government spending.

#### Cutting spending creates a better stimulus than raising spending

A. Adrianson, the Heritage Foundation, ’10 (September 16th 2010, "Spending Cuts Are Good for the Economy," http://blog.heritage.org/2010/09/16/spending-cuts-are-good-for-the-economy/)

Reducing budget deficits by cutting government spending has a stronger record of economic stimulus than either reducing the deficit with tax increases or increasing government spending. That’s what Harvard economists Albert Alesina and Silvia Ardagna have found in their recent research. They examined 107 instances of large reductions (at least 1.5 percent in one year) in budget deficits as well as 91 instances of large increases (over 1.5 percent in one year) in budget deficits over the past 40 years. They found that when an economy expands following deficit reduction, spending cuts were the largest part of the adjustment. At the same time, when recessions followed deficit reduction, tax increases were the predominant policy. The authors also found that when budget deficits increased, tax cuts had a more expansionary impact on the economy than spending increases.

#### Their authors are wrong – Keynesian economics is too outdated

Jason Bradley, former military member, ‘11 (June 27th 2011, “Keynesians Are both Wrong and Dangerous,”

http://biggovernment.com/jbradley/2011/06/27/keynesians-are-both-wrong-and-dangerous/)

The Keynesian school of thought on the economy is that of the potential instability of the private sector and the undependability of the market driven self-adjustment factor. Keynes during his day said that in times of depression (or deep recessions) the government should focus entirely on spending by injecting the national economy with lots of cash. So the task was simple: spend more on goods and services thereby shifting aggregate demand in the other direction and presto we are out of the recession. However, Keynes put forth these thoughts during the Great Depression. In which inflation was not a threat, prices were falling, and unemployment was reaching 25 percent. Since the goal was to get the national economy back to full employment, the only model used for analysis was the aggregate demand curve in relation to real GDP gaps. There was no need to study aggregate supply and aggregate demand, prices and real job growth because he was only interested in what market participants would buy during the depression if the economy was producing at full capacity. So a new model called the Keynesian Cross was coined which basically focuses on the differences in total spending to the value of total output. It doesn’t account for true distinctions for price levels and real output, i.e., real job growth. An increase in aggregate demand effects real output and prices but doesn’t always translate to a dollar-for-dollar improvement in real GDP. Again, and to his defense, Keynes’ ideas were during the Great Depression — falling prices, etc., — this is not the Great Depression, so when supply and demand increases so do prices. As a result we still stay short of full employment, consumer spending stays down, wages become relatively low, the economy fails to rebound and possibly falls back into recession.

AT: Stimulus

#### Keynesian stimulus has already failed – current economic trends prove

Allan H. Meltzer is a professor of Public Policy at the Tepper School at Carnegie Mellon University, 10/28/11, “Four Reasons Keynesians Keep Getting It Wrong”, Wall Street Journal, ProQuest

Those who heaped high praise on Keynesian policies have grown silent as government spending has failed to bring an economic recovery. Except for a few diehards who want still more government spending, and those who make the unverifiable claim that the economy would have collapsed without it, most now recognize that more than a trillion dollars of spending by the Bush and Obama administrations has left the economy in a slump and unemployment hovering above 9%. Why is the economic response to increased government spending so different from the response predicted by Keynesian models? What is missing from the models that makes their forecasts so inaccurate? Those should be the questions asked by both proponents and opponents of more government spending. Allow me to suggest four major omissions from Keynesian models: First, big increases in spending and government deficits raise the prospect of future tax increases. Many people understand that increased spending must be paid for sooner or later. Meanwhile, President Obama makes certain that many more will reach that conclusion by continuing to demand permanent tax increases. His demands are a deterrent for those who do most of the saving and investing. Concern over future tax rates is one of the main reasons for heightened uncertainty and reduced confidence. Potential investors hold cash and wait. Second, most of the government spending programs redistribute income from workers to the unemployed. This, Keynesians argue, increases the welfare of many hurt by the recession. What their models ignore, however, is the reduced productivity that follows a shift of resources toward redistribution and away from productive investment. Keynesian theory argues that each dollar of government spending has a larger effect on output than a dollar of tax reduction. But in reality the reverse has proven true. Permanent tax reduction generates more expansion than increased government spending of the same dollars. I believe that the resulting difference in productivity is a main reason for the difference in results. Third, Keynesian models totally ignore the negative effects of the stream of costly new regulations that pour out of the Obama bureaucracy. Who can guess the size of the cost increases required by these programs? ObamaCare is not the only source of this uncertainty, though it makes a large contribution. We also have an excessively eager group of environmental regulators, protectors of labor unions, and financial regulators. Their decisions raise future costs and increase uncertainty. How can a corporate staff hope to estimate future return on new investment when tax rates and costs are unknowable? Holding cash and waiting for less uncertainty is the principal response. Thus, the recession drags on. Fourth, U.S. fiscal and monetary policies are mainly directed at getting a near-term result. The estimated cost of new jobs in President Obama's latest jobs bill is at least $200,000 per job, based on administration estimates of the number of jobs and their cost. How can that appeal to the taxpayers who will pay those costs? Once the subsidies end, the jobs disappear -- but the bonds that financed them remain and must be serviced. These medium and long-term effects are ignored in Keynesian models. Perhaps that's why estimates of the additional spending generated by Keynesian stimulus -- the "multiplier effect" -- have failed to live up to expectations. The Federal Reserve, too, has long been overly concerned about the next quarter, never more than in the current downturn. Fears of a double-dip recession, fanned by Wall Street, have led to continued easing and seemingly endless near-zero interest rates. Here, too, uncertainty abounds. When will the Fed tell us how and when it is going to sell more than $1 trillion of mortgage-related securities? Will Fannie Mae, for example, have to buy them to hold down mortgage interest rates? By now even the Fed should understand that we do not have a liquidity shortage. It has done more than enough by adding excess reserves beyond any reasonable amount. Instead of more short-term tinkering, it's time for a coherent program to start gradually reducing excess reserves. Clearly, a more effective economic policy would aim at restoring the long-term growth rate by reducing uncertainty and restoring investor and consumer confidence. Here are four proposals to help get us there: First, Congress and the administration should agree on a 10-year program of government spending cuts to reduce the deficit. The Ryan and Simpson-Bowles budget proposals are a constructive start. (Note to Republican presidential candidates: Permanent tax reduction can only be achieved by reducing government spending.) Second, reduce corporate tax rates and expense capital investment by closing loopholes. Third, announce a five-year moratorium on new regulations. Fourth, adopt an enforceable 0%-2% inflation target to allay fears of future high inflation. Now that the Keynesian euphoria has again faded, perhaps this administration -- or more likely the next -- will recognize the reasons for the failure and stop asking for more of the same.

AT: Stimulus

Ontario’s eHealth program disproves the fundamental tenets of Keynesianism

Terence Corcoran is a Staff Writer for the National Post, 2/14/12, “Keynesian Meltdown”, ProQuest

The fiscal mess in Ontario is now common knowledge across the country, thanks in part to a sensational report from the Conference Board of Canada demonstrating that unless the government slashes spending and/or raises taxes, health care and education will have to be decimated. The report was no surprise to people who tracked Premier Dalton McGuinty's march into Keynesian fiscal stimulus spending. The surprise was the appearance of the Conference Board as the harbinger of doom. Is this the same Conference Board that only two years ago, in March, 2010, awarded Ontario "a gold star for stimulus" spending, according to ReNew Canada magazine? The province's massive deficit spending, announced in 2009, would be creating hundreds of thousands of jobs and adding to the provincial growth rate. According to the Conference Board's 2010 report - commissioned by the Ontario government to document the impact of its multi-billion dollar Keynesian stimulus effort - the deficit spending on infrastructure would also boost productivity, offset the recession, and set the stage for recovery. Two years later, the Conference Board returned to the scene of the crime to report that Ontario is in rough fiscal shape, growth isn't happening, spending will have to be cut, taxes raised and the province needs "transformative changes." Missing from the Conference Board report was any acknowledgement that Ontario might be sinking under the weight of the stimulus gold star the board had awarded the province. Like most other economists who are now issuing alarming reports and projections that Ontario faces a future of perpetual deficits, slow growth and rising taxes, the Conference Board appears to be wilfully blind to the dead corpus of Keynesian economic policy that is behind Ontario's plight - policy that they all endorsed as the province's economic salvation. The McGuinty Liberals cannot be expected to admit that the massive stimulus balloon - which began with a $19-billion deficit in 2009-10 and has since expanded to an $80billion-and-climbing monster that appears to be beyond control - has been a misguided disaster carried out under the influence of the finest economic minds in the country, if not the world. If a U.S. President can go crazy with US$1.5-trillion deficits, why shouldn't the Premier of Canada's largest province ring up $100-billion in deficits? At the Toronto Economic Club on Monday, Ontario Finance Minister Dwight Duncan was towing his Keynesian gold star around. "The McGuinty government, like many others, invested heavily in stimulus - building roads, bridges and other important infrastructure." This spending allegedly protected and created jobs, and will make Ontario "more competitive." Nobody really expects politicians to know what impact their actions have on the economy. They do what the economists, the Bay Street and in-house variety, tell them will work. And what the economists told them, via the Conference Board, bank reports and other outlets, is that running up billions in deficits is the ethanol that will keep the engine of growth going. That the forecasters and theorists turned out to be dead wrong comes back to haunt no one. In Ontario's 2009 budget, the province predicted that its total debt would rise gently to just over 30% of the province's gross domestic product before beginning a decline. GDP growth, according to a consensus of Keynesian private-sector economic modellers, would rise to 3.3%, in part under the stimulus helium provided by the deficits. As it turned out, within two years forecasts had turned sour. The new debt-to-GDP ratio looked set to top 40% (see graph above). What happened is (a) the deficits kept growing and (b) the forecast growth rates began to look a little rosy. Rates of 3% and 3.5% were expected, presumably the result of all the infrastructure spending and productivity gains. Now, however, the forecast average growth rate is said to be unlikely to exceed 2%. If we can't expect politicians to take the blame for following the Keynesian deficit-spending policies advocated by their economic advisors, shouldn't we turn to the economic experts to get them to explain themselves? The same people who supported and advised the McGuinty Liberals - and the Obama Democrats, the Greek and Portuguese politicians, the French and Canadian governments - to run up spending to rescue the economy will spend the next decade telling governments how to get out of the mess they helped create. Ontario's current circumstances create a perfect opportunity to confront the economic establishment and lay blame for the fiscal disaster that is Ontario. Government spending has been soaring for years. It all looks good if growth rates stay strong. Where were the dire economic warnings through the last decade that the expansion in government activity cannot continue without hitting a wall? A table on Ontario's spending habits (below) captures the disconnect between the government and the people. While the personal income of the people dragged at 26% growth, government spending soared more than 60%. On Wednesday, former TD Bank economist Don Drummond will deliver a set of tax and spending options to the McGuinty government, a road map on how the province can resolve its fiscal problems. It would be nice if Mr. Drummond also charted the Keynesian fallacies that got Ontario into this mess.

AT: Stimulus

Keynesian stimulus has failed to restore the economy

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From the beginning, our representatives in Washington have approached this economic downturn with old-fashioned, Keynesian economics. Keynesianism -- named after the British economist John Maynard Keynes -- is the theory that you fight an economic downturn by pumping money into the economy to "encourage demand" and "create jobs." The result of our recent Keynesian stimulus bills? The longest recession since World War II -- 21 months and counting -- with no clear end in sight. Borrowing close to a trillion dollars out of the private economy to increase government spending by close to a trillion dollars does nothing to increase incentives for investment and entrepreneurship. The record speaks for itself: In February 2008, President George W. Bush cut a deal with congressional Democrats to pass a $152 billion Keynesian stimulus bill based on countering the recession with increased deficits. The centerpiece was a tax rebate of up to $600 per person, which had no significant effect on economic incentives, as reductions in tax rates do. Learning nothing from this Keynesian failure, which he vigorously supported from the U.S. Senate, President Barack Obama came back in February 2009 to support a $787 billion, purely Keynesian stimulus bill. Even the tax-cut portion of that bill, which Mr. Obama is still wildly touting to the public, was purely Keynesian. The centerpiece was a $400-per-worker tax credit, which, again, has no significant effect on economic incentives. While Mr. Obama is proclaiming that this delivered on his campaign promise to cut taxes for 95% of Americans, the tax credit disappears after next year. The Obama administration is claiming success, not because of recovery, but because of the slowdown in economic decline. Last month, just 216,000 jobs were lost, and the economy declined by only 1% in the second quarter. Based on his rhetoric, Mr. Obama expects credit for anyone who still has a job. The fallacies of Keynesian economics were exposed decades ago by Friedrich Hayek and Milton Friedman. Keynesian thinking was then discredited in practice in the 1970s, when the Keynesians could neither explain nor cure the double-digit inflation, interest rates, and unemployment that resulted from their policies. Ronald Reagan's decision to dump Keynesianism in favor of supply-side policies -- which emphasize incentives for investment -- produced a 25-year economic boom. That boom ended as the Bush administration abandoned every component of Reaganomics one by one, culminating in Treasury Secretary Henry Paulson's throwback Keynesian stimulus in early 2008. Mr. Obama showed up in early 2009 with the dismissive certitude that none of this history ever happened, and suddenly national economic policy was back in the 1930s. Instead of the change voters thought they were getting, Mr. Obama quintupled down on Mr. Bush's 2008 Keynesianism. The result is the continuation of the economic policy disaster we have suffered since the end of 2007. Mr. Obama promised that his stimulus would prevent unemployment from climbing over 8%. It jumped to 9.7% last month. Some 14.9 million Americans are unemployed, another 9.1 million are stuck in part-time jobs and can't find full-time work, and another 2.3 million looked for work in the past year and never found it. That's a total of 26.3 million unemployed or underemployed, for a total jobless rate of 16.8%. Personal income is also down $427 billion from its peak in May 2008. Rejecting Keynesianism in favor of fiscal restraint, France and Germany saw economic growth return in the second quarter this year. India, Brazil and even communist China are enjoying growth as well. Canada enjoyed job growth last month. U.S. economic recovery and a permanent reduction in unemployment will only come from private, job-creating investment. Nothing in the Obama economic recovery program, or in the Bush 2008 program, helps with that. Producing long-term economic growth will require a fundamental change in economic policies -- lower, not higher, tax rates; reliable, low-cost energy supplies, not higher energy costs through cap and trade; and not unreliable alternative energy surviving only on costly taxpayer subsidies. Unfortunately, Mr. Obama seems to be wedded to his political talking points, and his ideological blinders seem to be permanently affixed. So don't expect any policy changes. Expect an eventual return to 1970s-style economic results instead.

AT: Stimulus

Keynesian policies hamper economic growth by ignoring free trade and tax increases

Richard A. Epstein is a Professor of Law at UChicago, “WHY I WILL NEVER BE A KEYNESIAN”, Harvard Journal of Law and Public Policy, ProQuest

At first glance, we should all be impressed by the apparent breadth of Keynes's title, which seeks to link employment, interest, and money into a single theory. Success in unifying these three large classes of events has to count as a signal achievement in economic thought. But, by the same token, that synthesis should not be regarded as a comprehensive explanation of how the economy works in practice. Its scope is incomplete, and hence it gives only weak information about how to correct perceived economic imbalances, whether during the Great Depression or today. So it is useful to mention some of the issues that are missing from the Keynesian theory, each of which plays a real role in the operation of the economy. Free trade is the first topic not covered by Keynes's title, nor mentioned in Posner's recent salute to his new master. Keynes's writing on this point seems to indicate some sympathy with the laissez-faire position, for he surely understood the risks of mercantilist policies.6 By the same token, however, Keynes also thinks that a bit of governmental oversight would not be all that bad/ Indeed, it would be hard for Keynes to maintain a strong free trade perspective given his own view that we cannot trust laissez-faire capitalism to determine "the current volume of investment."8 The connection between the foreign and domestic markets is too intimate to let international trade run its course. Yet notAvithstanding Keynes's doubts on the subject, vibrant international trade is clearly important to the overall health of the economy today, and it was also important (albeit at a smaller level) when transportation and communications costs were higher during the Depression. This observation is hardly new; the debate over free trade came to a head just before the passage of the Smoot-Hawley Tariff Act of 1930,9 which put a serious kibosh on international exchange. The basic mechanics of comparative advantage as they apply to free trade have been well discussed in the work of Adam Smith10 and David Ricardo,11 in the late eighteenth and early nineteenth centuries. Their insights were widely disregarded by the Republican Party, whose 1928 platform revealed protectionist preferences that later became law.12 The danger of this protectionist position was not completely lost in the pre-Keynes years. In 1930, a large group of economists, 1028 in all, led by Paul Douglas of the University of Chicago, drafted an impassioned plea to Congress not to pass the legislation.13 That denunciation of Smoot-Hawley noted that any tariff increase would force distortions in domestic and foreign markets that would reduce overall levels of production to the detriment of consumers, encourage retaliation that would only make matters worse, hamper those in local service industries who had nothing to fear from foreign competition, and harm farmers by forcing them to pay more as consumers and shutting down their access to foreign markets. The letter even quoted President Herbert Hoover's cautionary words that "[i]t is obviously unwise protection which sacrifices a greater amount of employment in exports to gain a less amount of employment from imports."14 There may be some doubt as to the exact extent of the damage caused by Smoot-Hawley given that total exports and imports were less than six percent of Gross Domestic Product at the time.15 But there can be no doubt that it had a negative effect. President Hoover may have known all this, but the business pressure for protectionism was tough to resist. World trade shriveled, and, in part because of poor economic circumstances, a climate of unrest led to the rise of fascism and Nazism. It is not, of course, proper to charge Keynes with fostering these counterproductive maneuvers. It is sufficient to say that his general theory neglected to warn against such misguided government interventions, which are easily condemned within the standard neoclassical framework. So even if we were to classify Keynes and Posner as ardent champions of free trade, nothing about that position stems from the unique insights of a Keynesian theory. Nor should we regard these insights as unimportant today. We are blessed insofar as there is no powerful coalition in support of a return to Smoot-Hawley. The defenders of protectionism tend to rely instead on more modest claims, such as the inability to conduct "free and fair" trade -fear the "fair" in this formulationwith nations that do not maintain appropriate labor or environmental standards. Concern for fair trade has, for example, stalled various bilateral free trade agreements with Colombia.16 But this effort to use trade policy to meddle in the internal business of foreign nations is a dead loser. We should trade with them whenever it works to our mutual advantage. The lure of foreign trade should help to discipline and rationalize internal productive capacities in both nations (thus bleeding out the monopoly power of unions), and with the increase in domestic wealth, we can confidently predict an expansion in efforts at environmental protection. No one wants to live in a mansion if he cannot breathe the outside air when he steps into his backyard. And so prosperity from free trade, and not protectionism, will increase pressure foT sustainable environmental improvements. Tax policy also deserves more attention. It represented one of the key mistakes of the Hoover Administration, which in its own way was as misguided on tax matters as President Franklin Delano Roosevelt's New Deal was on social politics. In particular, President Hoover's Revenue Act of 1932 raised the top marginal tax rate from twenty-five to sixty-three percent in order to staunch the deficit at the federal level.17 We hear similar calls for higher taxes today for much the same reason: We do not want to live in a society where a huge fraction of the population has to scrimp by on the government dole or toil at low-paying jobs while the rich live in the lap of luxury. But it is a mistake to think of taxation policy solely, or even largely, in terms of income distribution. Taxation has allocative as well as distributive consequences. In many cases, the imposition of progressive taxes contributes to the decline of investment and the withdrawal of human capital from the labor markets. It becomes almost selfdefeating to find moral support for the very tax regime that has helped to contribute to a societal slowdown and to the current economic distress. In general, the opposite approach is better. If the flat tax is preferred in good times, as I think is the case, it should be preferred in bad times as well.18 The advantages in good times include the simplification of the overall tax structure, the removal of incentives for people to split or assign income in counterproductive ways, and the elimination of the political risk of allowing, as now is the case in California, for a very large portion of the population to enact tax increases that only a small slice of its richest citizens pay. The long term political dynamic of any steeply progressive system of taxation is to level off government expenditure, which in turn will reduce the overall level of production. In an ideal world, then, we do not constantly have to figure out how to switch tax structures as good times become bad and bad times become good. We follow instead the advice of David Hume, who thought that the stability of possession (by which he meant the institution of property generally) was the key to long-term success. We do not, however, reside in perfect times. So one question that arises is what to do if current tax levels are high and there is no practical means to reduce them in the short run, precisely because of the strong populist impulse toward progressive taxes. At this point, we have to bite the bullet and recognize that something must be done in a second-best world to offset the loss of wealth (for both consumption and investment) in the private sector. One way to do so is to prime the pump to spend the revenue quickly. But, make no mistake about it, this spending binge by government is a distinct second-best solution. There is no reason to think that the government knows what projects to invest in, or why. To be sure, there is always room for government investment in infrastructure under any sensible theory of laissez-faire,19 but in general the effort should be to invest only to the point where the last dollar on public expenditure has the same rate of return as the last dollar on the private side. That ratio need not change as times get bad, especially if infrastructure were properly cared for in good times. Yet that is not how matters sit with the new Keynesians. Posner seeks to find a larger space for public investment in a downturn by declaring that "[an a]mbitious public-works program can be a conñdence builder," seeking to tap into Keynes's explanation of how the government can promote the "return of confidence." But the argument ignores the obvious indignant response that a poorly run government program can destroy confidence and further demoralize businesses who think that higher taxes will snatch away the fruits of their efforts. Only by assuming the eternal and unalterable benevolence of government can one posit that all soft externalities will move in the same direction. Think of the public cynicism about the Alaskan "bridge to nowhere," or foolish public expenditures that led to the construction of the Murtha-Johnstown-Cambria Airport. **These projects shatter public confidence**. What is missing from this entire paean to public works and expenditures is any sense of the public-choice dynamics that make pork barrel politics the order of the day. I am no social historian, but I suspect that public expenditures were also hijacked for partisan advantage in the Great Depression. But by the same token, I think that the size of the heists are far greater in a $787 billion pork barrel package, most of which is directed toward delayed capital expenditures that do not have (if any expenditure has) their supposed stimulus effect. In the end, it seems clear that the best solution is to lower taxes and not to leverage high taxes as an excuse for expanded public spending.

AT: Stimulus

Keynesian policies impair industry through cartelization

Richard A. Epstein is a Professor of Law at UChicago, “WHY I WILL NEVER BE A KEYNESIAN”, Harvard Journal of Law and Public Policy, ProQuest

A third area that attracts little or no attention from Keynes is the extensive New Deal drive toward cartelization of industries, which may well have had a parallel impulse in Great Britain. American industrial cartelization was no modest endeavor. In the eighteen months between August 1933 and February 1935, FDR's administrative agencies churned out some 546 Codes and 185 Supplemental Codes, pursuant to which they issued over eleven thousand administrative orders in the relentless pursuit of "fair" competition.20 The National Industrial Recovery Act (NIRA) was of course opposed to using these industrial codes to promote monopoly.21 But that spurt of generosity arose only because the Roosevelt political agenda organized cartels instead, which did not "oppress small enterprises [or] operate to discriminate against them."22 These codes set minimum prices or, alternatively, requirements that goods be sold only above cost, generously defined, which is an indirect way to impose price floors. The social losses resulting from cartels are well established in economic theory and flow to the bottom line no matter what fiscal or monetary policies are in place. Their removal should have been a top priority of the very Roosevelt Administration that established them. Trie same can be said about the continued use of the various agricultural marketing orders that have similar effects today.23 The New Deal efforts on this score were not limited to product markets. Before the first round of codes was struck down on grounds of improper delegation in A.L.A. Schechter Poultry Corp. v. United States,2\* the New Dealers included a minimum wage and maximum hours standard, intended to cartelize labor markets. This was no accidental adjunct to the Roosevelt program. It was yet another manifestation of the relentless progressive agenda to substitute cartels for competition whenever possible. Indeed, the NIRA interventions did not die with the invalidation of the statute that created them. Because Schechter Poultry was decided on broad nondelegation grounds, the entire issue resurfaced in a statute with greater particularity, the Fair Labor Standards Act of 1938 (FLSA),25 which was sustained with great fanfare in United States v. Darby.26 The FLSA provided a solid statutory foundation for regulations of the minimum wage, maximum hours, and overtime that have expanded in scope relentlessly from the time of its initial passage.27 Nor were NlRA and FLSA the only misguided efforts to cartelize labor markets. Many of the low points of the Great Depression involved misguided labor statutes that had an adverse impact on unemployment. The year 1931 saw the adoption of the DavisBacon Act,28 which required wages on government contracts to be set at the "prevailing" level within the local community.29 There is some dispute as to whether the legislation was passed with an explicit intent to keep African- American workers from the South from competing with white laborers from the North.30 But even if the statute had no racist element, its protectionist origins against interstate competition cannot be disputed. Nor is it possible to deny the consequences of shielding incumbent workers from external competition: small local gains at the expense of larger national losses. Davis-Bacon is hardly a winning strategy to beef up national labor markets in times of high unemployment. Its repeal is seventy-nine years overdue. Next on the list is the Norris-LaGuardia Act of 1932, 31 which sharply limited the use of labor injunctions in trade disputes. Most importantly, it followed the pattern of the English Trade Disputes Act of 190632 by refusing to issue injunctions when labor unions tried to induce workers to unionize secretly in violation of their terms of employment. Previously the employer had been able to stop the offending union in its tracks by obtaining injunctive relief, a right of action that the Supreme Court upheld in Hitchman Coal & Coke Co. v. Lewis.33 The statute thus strengthened the hands of unions in ways that once again pushed wages for labor further from the competitive equilibrium, with a consequent loss in social welfare. That statute was followed by an elaborate effort to organize collective bargaining arrangements under the NIRA. That act was struck down in Schechter Poultry,34 only to reappear in much more institutionalized form in the National Labor Relations Act of 1935,35 which created a new enforcement mechanism in the National Labor Relations Board. So a statute intended to usher in an era of labor peace brought in its wake labor instability that certainly failed to draw capital into labor intensive industries. It is easy to understand the sense of desperation that led to the passage of these acts, but it is impossible to ignore the role that they played in keeping levels of unemployment high. Here, again, it hardly matters whether Keynes, Krugman, or Posner (especially the last two) supports these statutes or not. If they support or ignore these statutes, they have allowed macroeconomic concerns to blind them. If they oppose these statutes, they do so for microeconomic reasons that have nothing to do with the grand Keynesian synthesis. But either way, it is hard to defend the position that these midlevel changes do not matter, and harder still today to think that the situation would not get worse with the passage of the Employee Free Choice Act, against which I have argued at every possible opportunity.36 Posner himself is opposed to passage of the statute but thinks that its effect will be moderated by the global nature of labor markets.37 That perception is at odds with the perception of the American business community, which recoils at the prospect of a card-check device for selecting unions followed by a mandatory arbitration of the substantive term of the labor contract. This latter requirement is a real job killer if anything is.38 Put otherwise, the favor that the Obama Administration shows to organized labor is a real disincentive to economic recovery in employment markets. One does not have to be a Keynesian to explain why unemployment rates now stubbornly persist at around ten percent, with no decline in sight. The threat of more labor and environmental legislation acts as a real deterrent to new jobs. And the recent passage of ObamaCare will roil labor markets for years to come.

AT: Stimulus

Keynesianism is an inadequate economic model – failure to predict stagflation

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Last, there is the question about the stability and operation of financial markets, and here too the case for some Keynesian explanation for the failure of these markets looks to be vanishingly thin. As before, there are some conventional explanations that Keynesians may embrace, but these are hardly distinguishable from the more traditional Chicago-style explanations. Thus, the obvious culprits are the easy money policies of the Federal Reserve and the unwise guarantee policies of both Fannie Mae and Freddie Mac. Proving we have not learned our lesson, the Federal Housing Administration (FHA) is now replicating these policies and has begun to specialize in making risky loans on a 3.5% down payment.39 In addition, it looks as though it will commit yet another $50 billion to salvage homeowners who are in default or whose properties are worth less than the mortgages on them.40 Once again, it does not take a Keynesian to note that the low rates of interest will generate a bubble, which will surely burst once there are no greater fools to step into the gap. Nor does it take a Keynesian to examine the role, if any, that mark-to-market accounting had in spurring the downward cycle in asset values as private banking houses had to sell off asset after asset to make back their margins.41 There is some debate about the extent to which these policies are attributable to securities regulation or to private covenants. The right answer is some mixture of both, which suggests that both public and private parties did not perform ideally in the financial meltdown. But that observation hardly makes the case for more extensive governmental control over lending markets. Rather, the key question is who learns more quickly from their mistakes. There are only two choices: government bureaucrats who are systematically immunized from the consequences of their decisions or private lenders who (even with imperfect employment contracts) are not. No private bank will lend on the terms that the FHA is prepared to supply. The reasons are too evident to require extended discussion. The situation only gets worse when we look at the rules in place once mortgages go into default. From the outset I have taken the uncompromising position that the only person who should be entitled to renegotiate loans or waive foreclosure is the bank or syndicate that holds the paper.42 The current policy reintroduces the worst features of the Depression strategy that sought delayed foreclosures in ways that only prolonged the agony for the individual parties and prevented the restabilization of the market. Everyone should have some sympathy for the plight of borrowers in the 1930s, given that the major deflation forced them to pay back loans with more expensive dollars than those they borrowed. But that problem can only be cured by keeping currencies stable- which is harder to do with one, or more, large stimulus programs waiting in the wings. Today, we do not have deflation to justify government intervention, and the various programs of forced delay have done exactly what one would have predicted. Very few of the borrowers who were in arrears brought their payments current during the foreclosure moratorium.43 The common result was eventual foreclosure at additional expense, at which time the underlying properties were worth less than before. The systematic effect of debtor relief is to keep these units out of the resale market, to keep prices artificially high, and to put obstacles in the path of new home buyers who were guilty of no indiscretions of their own. It does not take a Keynesian to realize that the insecurity of ail forward transactions saps the confidence that governments should build in markets. Even people who have excellent "animal spirits"44 will be loathe to invest in a market in which neither politicians nor courts give credence to "stable expectations."45 Animal spirits lurk in all individuals who take joy in their work. The question is whether that private satisfaction from productive labor is enough to offset the additional burdens and uncertainty of oppressive regLilation. The motivations of individuals are, of course, not amenable to public intervention, but the rules that either shackle or encourage innovation are. Figuring out what these are, and how they relate to the current malaise is difficult because some of the policies to which I refer have been in effect for a long time, and others are of much more recent vintage. But even older policies may have greater salience as time marches on. One need only look to the ever greater threats to solvency in Medicare, Medicaid, and Social Security to realize that incremental changes and adjustments can produce long-term effects. The same can be said about the accumulated public pension liabilities that are now the norm in states like New York and California, owing to the enormous strength of their public unions. My own sense, therefore, is that we must start dismantling these programs if we as a nation are to get out of the long-term stagflation (or inflation?) that is our due. The Keynesians have little distinct to say about this dilemma. Nor, in the end, do they have much useful to say about the issues of employment, consumption, investment, and savings that lie at the core of their theory.

AT: Stimulus

Keynesianism is invalid - doesn’t assume vote-buying and credit-claiming by politicians

Peter Foster is a staff writer for the National Post, 10/09/09, “Keynesian Quagmire”, Proquest

John Maynard Keynes is frequently described as "the greatest economist of the 20th century." He might more accurately be called the most influential economist of the 20th century. That was because he provided an intellectual justification for activist government. It was to be expected in the wake of the recent crisis that market critics such as Paul Krugman and Joseph Stiglitz would be quick to claim that Keynes was "back," but the most depressing convert to the cause is Richard Posner, a highly-respected U.S. judge and expert in "law and economics" at the University of Chicago. Professor Posner also recently published a book, A Failure of Capitalism: The Crisis of '08 and the Descent into Depression. But if anything threatens Depression it is the Keynesian policies that Professor Posner has now embraced. Professor Posner certainly further undermines the notion that Chicago is some kind of free-market hotbed. Milton Friedman, the school's most famous economist, once explained that the reason Chicago stood out was that it was pretty much the only U.S. school with any market enthusiasts. It isn't famous for them any more. The best-known Chicago economist at the moment is Richard Thaler, whose field of "behavioural economics" provides allegedly fresh rationales for policy "nudges." This week, Professor Thaler was appointed a policy advisor to the British Conservative Party. Yes, Conservative Party. Professor Posner's hoary claim is that the prevailing view among economists is that individuals are rational and markets are perfect. Perhaps Chicago should adopt a Straw Man as its mascot. Human imperfection doesn't dilute the enormous power of the Invisible Hand to harness human ingenuity, but it certainly raises serious questions about "macro management." The most devastating critique of Keynesian economics -- and easiest to understand -- came from James Buchanan (an economist at one point chastised and even persecuted for promoting the power of markets). Professor Buchanan pointed out that Keynes seemed to assume that he was giving advice to philosopher kings. Insert real, vote-grubbing politicians into the equation -- which was unavoidable -- and the Keynesian fiction disintegrated. Professor Posner seems blind to these criticisms and even unaware that Keynesianism proved a bust in the stagflationary 1970s. He claims that the economist "profession" was blindsided by the crisis, but there is no economics profession. Economics remains a battle ground of ideas, not an objective science. He seems to confuse understanding how an economy works with possessing theories to control it. He seems to believe that it is economists' job to provide formulae for avoiding the unavoidable consequences of bad decisions. He largely ignores the role of bad policies in influencing those decisions. He also, in his book, seems to have fallen in with the notion that "greed did it" in the form of deliberately reckless decisions by overpaid bankers. This explanation has been enthusiastically promoted by politicians, but evidence for it is thin on the ground. He notes that Keynes was "suspicious of saving," the bedrock of capitalist investment. He also reports, apparently without his jaw dropping, Keynes' support for destroying farming inventories, because that would promote production! On that basis, the surest thing we could do to boost the economy would be to torch all our warehouses and factories! Keynes believed that an economy could be "stuck" in a high-unemployment "equilibrium." Professor Posner acknowledges that one of the main reasons for this is downward "stickiness" of wages. But this could only be caused by destructive, government-backed union power, confirming that all unions do is force up their own wages at the expense of other workers. Keynes opposed low wages as destructive of his all-important "demand," but in a freely operating market, prices would be falling too. Professor Posner claims that such a fall "imperils economic stability," but he doesn't say why. It should also be remembered that FDR attempted to force up wages, which in fact merely increased unemployment, as despised "classical" economics said it would. Like Keynes, Professor Posner dismisses businessmen as "animal spirits," subject to irrational exuberance one minute, "paralyzed" by fear into "hoarding" the next. This is where wise and competent government steps in to "arrest a downward economic spiral." "[T]he government," writes Professor Posner, "must do everything it can to convince businessmen and consumers that it is resolute in working for economic recovery. An ambitious public-works program can be a confidence builder." Has Professor Posner even been living on planet Earth? Robert Lucas won a Nobel Prize for pointing out that people adjust their behaviour to compensate for, and thus negate, this attempted con job. Meanwhile look at the ugly reality of government expenditure, such as Ontario's disastrous eHealth boondoggle. For a Keynesian, eHealth could be justified as a fine example of economic stimulus. All those consultants obviously spent or invested the money they received, so what's all the fuss? Just think of the Keynesian "multiplier!" Back in the real world, however, as Niels Veldhuis and Milagros Palacios of the Fraser Institute pointed out on this page yesterday, to the extent economies are turning around, it has little or nothing to do with artificial stimulus, whose only impact is to crowd out private investment in the short term and/or create a debt burden that will impoverish taxpayers in the long. Professor Posner, although a legal expert, seems strangely impervious to the impact of regulation in promoting the recent crisis. Jeffrey Friedman, a political scientist at the University of Texas, in a review of Professor Posner's book for The Weekly Standard, notes that the "rational self-interest" that Professor Posner indicts "follows the tens of thousands of pages of the tax code; it follows the millions of pages of the regulatory code." Professor Posner concludes that "we need a more active and intelligent government to keep our model of capitalism from running off the rails." "Active" we have. "Intelligent," not so much. But this failure of intelligence lies not in the absence of IQ, but in the conception of an economy as a machine with knobs and levers. This is the flawed Keynesian model that is so appealing to conceited wonks and desperate politicians, but for which the bill always has to be paid. Just like eHealth.

AT: Stimulus

Keynesian models are inaccurate – don’t factor in consumption of the unemployed

Predrag Rajsic is a postdoctoral researcher in the Department of Food, Agricultural, and Resource Economics at the University of Guelph in Ontario, Canada, 7/13/10, “The Self-Defeat of the Keynesian Cross”, http://mises.org/daily/4552

The Austrian business-cycle theory, initiated by Ludwig von Mises and further developed and elaborated by F.A. Hayek, is by many considered the cornerstone of this school of thought. However, in 1998, Paul Krugman plainly dismissed the theory as not "worthy of serious study." More recently in his New York Times blog, Professor Krugman claimed that the Austrian business-cycle theory fails to fully explain fluctuations in output and employment between recessions and booms. From this he concludes that the theory fails to demonstrate how a business cycle can be caused by government intervention. At the same time, he interprets this as a sign of Austrians' unconscious adherence to Keynesianism in explaining the booms but not the busts. Austrian economists, says Professor Krugman, seem to be "Keynesians during booms without knowing it." The assertions about the alleged inadequacy of the Austrian business-cycle theory have been addressed by Robert Murphy and will not be the focus of this article. Instead, I will demonstrate that the common interpretation of the theory that Krugman considers more worthy of studying seriously — J.M. Keynes' General Theory of Employment, Interest and Money — has serious logical flaws. Ironically, it turns out that these are the same flaws that Krugman attributes to the Austrian theory, namely the inability to explain continuous unemployment during a recession. The Basics of J.M. Keynes' Theory Keynes based his 1936 treatise The General Theory of Employment, Interest and Money on one key assumption, that involuntary unemployment is a possible market-equilibrium outcome. He defines involuntary unemployment in this way: Men are involuntarily unemployed if, in the event of a small rise in the price of wage-goods relatively to the money-wage, both the aggregate supply of labour willing to work for the current money-wage and the aggregate demand for it at that wage would be greater than the existing volume of employment.[1] Next, Keynes describes the basic elements of his theory: This theory can be summed up in the following propositions: In a given situation of technique, resources and costs, income (both money-income and real income) depends on the volume of employment N. The relationship between the community's income and what it can be expected to spend on consumption, designated by D1, will depend on the psychological characteristic of the community, which we shall call its propensity to consume. That is to say, consumption will depend on the level of aggregate income and, therefore, on the level of employment N, except when there is some change in the propensity to consume. The amount of labour N which the entrepreneurs decide to employ depends on the sum (D) of two quantities, namely D1, the amount which the community is expected to spend on consumption, and D2, the amount which it is expected to devote to new investment. D is what we have called above the effective demand. Since D1 + D2 = D = φ(N), where φ is the aggregate supply function, and since, as we have seen in (2) above, D1 is a function of N, which we may write χ(N), depending on the propensity to consume, it follows that φ(N) − χ(N) = D2. Hence the volume of employment in equilibrium depends on (i) the aggregate supply function, φ, (ii) the propensity to consume, χ, and (iii) the volume of investment, D2. This is the essence of the General Theory of Employment.[2] These propositions were later formulated by Paul Samuelson into what is now known as the Keynesian cross model.[3] This model has become one of the standard elements of undergraduate macroeconomics courses. Figure 1 shows a diagrammatic representation of the Keynesian cross, as generally presented in contemporary macroeconomics textbooks. The horizontal axis represents the aggregate output or income, and the vertical axis denotes the aggregate expenditure. The aggregate demand, D, is equal to the sum of the consumption expenditure, pc∙φ(N), and investment, D2. The consumption expenditure at any level of employment, N, is a product of the propensity to consume, pc, and the income, φ(N). While Keynes avoids using any explicit units for the aggregate income, expenditure, consumption and demand, implicitly, they are treated in terms of money outlays. The 45° line represents the locus of points where the aggregate expenditure equals aggregate output. Consequently, the economy is in equilibrium at the output level φ(N0), and N0 is the equilibrium level of employment. At this point, the aggregate expenditure is E0. If we assume that N0 is the total amount of labour available in the economy, this equilibrium corresponds to full employment. From this, it follows that the consumption expenditure at full employment is pc∙φ(N0). Figure 1. The Keynesian cross diagram The next step in the application of this model generally involves assuming that propensity to consume, which is an exogenous variable, fluctuates between some minimum and maximum value. Let these values be pc1 and pc2. This is shown in figure 2. If the propensity to consume fluctuates around the level that ensures full employment, pc0, the model suggests that, in times when the propensity to consume is below pc0 (i.e., pc1), aggregate demand, Dl, is low and there will be a period of reduction in output and employment. In contrast, as the propensity to consume increases above pc0, aggregate demand, Dh, is high, full employment and maximum output is reached and a period of increases in output prices can be observed. Figure 2. Changes in the aggregate demand due to the changes in propensity to consume This idea is graphically illustrated in figure 3. It shows cycles of price increases, output and employment loss, as the propensity to consume fluctuates over time. The periods of higher prices and output, according to this model, coincide with full employment while the periods of lower prices are accompanied by unemployment and a decrease in output. The typical interpretation of the model is that the observed cycles in output, prices, and employment are consequences of intertemporal fluctuations in the aggregate demand, caused by the changes in the population's propensity to consume in a market not stabilized by government intervention. Figure 3. Fluctuations in output price, employment, and output over time, as commonly interpreted using the Keynesian cross model The suggested remedy for these fluctuations, according to the Keynesian theory, involves either fiscal or monetary policy. The fiscal policy remedy would be to increase taxes during the inflationary periods and run budget deficit during the recessionary period. The monetary-policy intervention would involve a reduction in the money supply during the inflationary periods and an expansion of the money supply during the recessionary periods. The intended effect of these policies would be to reduce the aggregate demand when it is too high and increase it when it is too low. This would make the government the primary body that balances the economic activity in order to bring about full employment. This interpretation, on the surface, sounds plausible. However, when the internal logic of the model is examined, a serious error can be found. The next section elaborates on this. The Internal Contradiction N0 in figure 2 is the quantity of labor that produces the output/income φ(N0). The demand equation implies that, in equilibrium, some share of the total output, pc0, is consumed by the income earners — the employed laborers (N0) and the employers. Consequently, pc0∙φ(N0) is the aggregate (accounting) value[4] of the consumption goods and services exchanged on the market. Following this logic, the same relationship needs to hold in any other equilibrium. Thus, if there is some other equilibrium at the level of employment, N1, and another propensity to consume, pc1, the consumption, C1 = pc1∙φ(N1), is the aggregate accounting value of the consumption goods and services exchanged on the market. These are the goods and services produced by laborers, N1, and consumed by all those who earn income. However, if pc1 is less than the propensity to consume that corresponds to full employment, there will be some unemployed labor, equal to the difference between N0 and N1. In order for this labor to be available at another point in time, when the (exogenous) propensity to consume returns back to the level needed for full employment, these unemployed laborers need to have some nonzero level of consumption while being unemployed. Let CU = e∙N1 be this minimum consumption, where e is the physical quantity of output needed to sustain the life of an unemployed person. But consumption of the unemployed is not met by an equivalent expenditure because unemployed labor does not earn income. This physical output must be given to the unemployed without monetary compensation. However, nowhere in this model is it specified that there is some surplus production of physical output that will be given away to the unemployed without monetary compensation. Thus, it seems that the model assumes zero consumption for the unemployed, which directly implies that the unemployed will not be able to sustain their physical existence in a prolonged recession. If, on the other hand, one assumes nonzero consumption for the unemployed that is not included in the consumption expenditure of the employed, the actual physical output available for purchase at the level of employment, N1, is less than the quantity that results in the expenditure E1. In order to arrive at the actual value of goods exchanged on the market, say φ'(N1), the amount equal to the unpaid consumption of the unemployed must be subtracted from the existing supply: φ'(N1) = φ(N1) − P∙CU, where P is the price of output. But this lowers the aggregate quantity of the goods and services available for exchange in the market below the quantity that corresponds to φ(N1). This means that the actual supply available for exchange no longer meets the effective demand of the income earners at pc1. Thus, assuming nonzero consumption of the unemployed that is not included in the expenditure of the employed is not an equilibrium situation in the model presented above. In order for this situation to move towards equilibrium, the propensity to consume of the employed and the employers needs to be reduced below pc1 to meet the consumption needs of the unemployed. However, propensity to consume is an exogenous variable and is not a subject of individual choice in this model. Even if propensity to consume was subject to individual choice, a further reduction in the propensity to consume would only lead to more unemployment and disequilibrium — since the reduction in the propensity to consume, according to the model, caused the recession in the first place. The only stable equilibrium in this situation is zero output for the whole economy, which amounts to a complete annihilation of the economy. Therefore, we cannot assume that the consumption of the unemployed is not included in the expenditure of the employed. Alternatively, if the consumption of the unemployed were to be included in the expenditure of the employed (i.e., the employed used a portion of their income as charity for the unemployed), we would end up with a paradox: that, as the propensity to consume reduces, the employed are more able to feed more unemployed by spending ever smaller portions of their income. Thus, it must be concluded that, in this model, the consumption of the unemployed is not included in the consumption expenditure of the employed. But the model at the same time implies that the consumption of the unemployed cannot be outside of the expenditure of the employed if the model is expected to produce a nonzero equilibrium output. This leaves the only remaining option — the consumption of the unemployed must be zero. Thus, according to this model, in any continuous economy free of external intervention, if the initial reduction in the propensity to consume below the level that ensures full employment persists for long enough, the economy returns to equilibrium at a lower, newly established level of full employment, N1. This is shown in figure 4. Figure 4. A true restoration of equilibrium in the Keynesian cross model But, unlike the restoration of equilibrium where the unemployed find the yet undiscovered opportunities for employment, the true logic of the Keynesian model implies that the equilibrium is restored by the cessation of the physical existence of the unemployed (i.e., death). Any other outcome contains unresolved internal contradictions. Conclusion $22 $19 Contrary to the commonly used interpretation of the "Keynesian cross," continued fluctuations in output and employment cannot be produced by this model if its strict logic is coupled with the logic of human existence. In this case, the Keynesian model implies that prolonged business cycles could not persist in the absence of an intervention external to the market processes. However, for Keynes, government intervention was the cure, not the cause, of the business cycle. It then turns out that the Keynesians are Austrians during recessions "without even knowing it." Rhetoric aside, given the inadequacies of the Keynesian paradigm, anyone interested in explaining the origins of the business cycle would benefit from seriously studying other economic theories. This is why I cannot agree with Professor Krugman's statement that the Austrian business-cycle theory is not "worthy of serious study."

AT: Stimulus

Keynesianism retards growth by discouraging low taxes

Wall Street Journal, 7/26/10, “Course of Economy Hinges on Fight Over Stimulus”, http://online.wsj.com/article/SB10001424052748704720004575376923163437134.html

Eighteen months after President Barack Obama administered a massive dose of spending increases and tax cuts to a weak economy, a brawl has broken out among economists and politicians about whether fiscal-stimulus medicine is curing the illness or making it worse. The debate is more than academic. It is shaping congressional decisions on whether to respond to the distressing prognosis for the U.S. economy with more government spending or a dose of deficit reduction. Getty Images British economist John Maynard Keynes (1883 - 1946). One side says Mr. Obama's $862 billion fiscal stimulus prevented an even graver recession. Cutting the deficit right now, this side insists, would send the economy into a tailspin. The other side questions the benefits of the stimulus and argues addressing long-term deficits now is crucial to avoid higher interest rates and even bigger economic problems down the road. And then there is a camp in the middle—defending last year's stimulus, but urging a deficit-cutting plan now. The quarrel over deficits and the economy is at the center of many congressional disputes. Republicans battled against Mr. Obama's proposal to renew the extension of unemployment compensation benefits for up to 99 weeks, insisting on spending cuts elsewhere to avoid widening the deficit, but lost last week. The president argues the benefits are vital to millions of unemployed and would bolster consumer spending. Meanwhile, the White House says it will allow taxes to rise on families with incomes above $250,000. Republicans and a few Democrats argue that allowing President George W. Bush's income-tax cuts on those upper-income households to expire at year-end, as the law currently provides, will choke the economy. "Too many are searching for answers in the discredited economic playbook of borrow-and-spend Keynesian policies," Rep. Paul Ryan, a Wisconsin Republican who is pushing a long-run deficit cutting plan, said this month. "I reject the false premise that only forceful and sustained government intervention in the economy can secure this country's renewed prosperity." Richard Trumka, president of the AFL-CIO union alliance, says if the government starts cutting deficits now, "We'll slip back into recession and possibly depression." Public opinion seems to be with the deficit fighters. A June Wall Street Journal/NBC News poll asked respondents which statement came closest to their views: (1) The president and Congress should worry more about boosting the economy even if it means bigger deficits; or (2) The president and Congress should worry more about keeping the deficit down even if it means the economy will take longer to recover. Some 63% chose deficit-fighting. Most mainstream economists agree on some points: The U.S. economy needed some kind of fiscal help in 2009 as the financial system teetered and the Federal Reserve pushed interest rates near zero. The deficit has to be reined in eventually, in part by restraining the growth of spending on health and other benefits. And developing a long-term plan to do so now would reduce risks of a future financial market calamity and help hold interest rates down. But today, neither side can say with certainty whether the latest stimulus worked, because nobody knows what would have happened in its absence. Fed Chairman Ben Bernanke backed fiscal stimulus in early 2009. Now he says the economy still needs fiscal stimulus, but says it must be accompanied with a credible plan to reduce future deficits. Like the Obama administration, he doesn't think that plan should be implemented until the economy is on more solid footing. Unlike the U.S., Europe has embraced, at least rhetorically, the primacy of deficit-reduction now. In some instances this is because of pressure from markets and the International Monetary Fund, such as in the cases of Greece and Spain, and in other instances because of local politics, as in the cases as the U.K. and Germany. "It is an error to think that fiscal austerity is a threat to growth and job creation," European Central Bank President Jean-Claude Trichet said recently. "Economies embarking on austerity policies that lend credibility to their fiscal policy strengthen confidence, growth and job creation." The case that government deficit spending can be vital at times of recessions dates to John Maynard Keynes, the British economist whose teachings dominated economics for decades after the Great Depression. "Pyramid-building, earthquakes, even wars may serve to increase wealth," Mr. Keynes said in his 1936 classic, "The General Theory of Employment, Interest and Money." A counter-revolution led by Milton Friedman, of the University of Chicago, de-emphasized the role of government and gave rise to Ronald Reagan and Britain's Margaret Thatcher. Keynes lost favor during the stagflation of the late 1970s and early 1980s. The Fed and its manipulation of interest rates came to be seen as the best way for governments to manage the short-term ups and downs of the economy. One big issue: Lessons about fiscal policy in normal times aren't necessarily applicable to today, when the Fed has cut interest rates to zero and unemployment remains high. Skeptics of fiscal stimulus traditionally argue that government borrowing crowds out private investment and pushes up long-term interest rates. True, says Obama adviser Lawrence Summers, but not at times like these. When private-sector lending was drying up and the credit markets froze, "government investment and creation of demand for consumers was a form of alternative financing, not a threat to private investment," he says. Both camps emphasize past victories. Keynesians cite deficit spending as the eventual cure for the Great Depression and see parallels to today and to Japan's premature deficit-cutting in 1997 as the cause for its return to recession. The other side points to Margaret Thatcher, who in 1981—ignoring protests from hundreds of economists—raised taxes and tightened government purse strings to cut a budget deficit in mid-recession. The U.K. emerged with lower inflation, lower interest rates and a recovery. Keynesians say that episode isn't relevant today because the U.S. can't cut interest rates, as the British did. Another difference: The British pound lost half of its value in the 1980s, spurring exports. The dollar, by contrast, strengthened after the financial crisis hit because global investors saw it as a safe haven. The Obama administration is stocked with heirs of Mr. Keynes, including academics Christina Romer and Mr. Summers. Ms. Romer famously projected in January 2009 that without government support, the unemployment rate would reach 9%, but with support the government could keep it under 8%. It's 9.5% today. Some Obama administration officials privately acknowledge they set job-creation expectations too high. The economy, they argue, was in fact sicker in 2009 than they and most others realized at the time. But they insist unemployment would have been worse without the stimulus. In the first quarter of 2009, when stimulus was enacted, the economy shrank at a 6.4% annual rate. Since then it has grown at a 2.5% annual rate. And the U.S. recently has begun adding jobs, albeit slowly. It's hard to isolate the impact of fiscal stimulus from other actions. Congressional approval of the stimulus in February 2009 coincided with an improvement in the economy. But before Mr. Obama's stimulus was enacted, the Fed pushed short-term interest rates to zero and began buying mortgage-linked securities to drive down long-term interest rates. Soon after the stimulus was okayed, the Fed expanded its securities purchases. A turnaround in the stock market coincided with the Fed's expanded effort and with a separate Fed-Treasury "stress test" to shore up confidence in the nation's banks. The Obama stimulus, a third of which was temporary tax cuts and the rest spending on everything from infrastructure to unemployment insurance, is still affecting the economy. Robert Hall, a Stanford University professor, says there hasn't actually been that much extra government spending overall, because the increased federal spending has been largely offset by a large contraction in state and local government outlays. By the third quarter of 2009, he notes, federal government spending added $66 billion to economic output, less than 0.5% of total output, offset by a $43.1 billion contraction in state and local government spending, he says. A study of 91 fiscal stimulus programs in 21 developed economies between 1970 and 2007 by Harvard's Alberto Alesina found tax cuts were more stimulative than government spending. "I would have done more on the tax side than on the spending side," he says. Underlying the debate is a long-running argument about how much of a lift the government gets from spending more or taxing less. Keynesians argue that when the economy is distressed, a dollar spent by the government multiplies in value. It gives a worker income the private sector has failed to produce, which he spends, creating demand for goods and services. Ms. Romer argued last year that this "multiplier" for government meant every dollar spent created about $1.50 worth of demand. Some economists say that's too high. Valerie Ramey of the University of California at San Diego, initially thinking as a Keynesian, developed doubts after sifting through historical examples. During the military build-ups of World War II, the Korean War and the Reagan era, a dollar spent added roughly a dollar of growth, she says. Although Ms. Ramey supported stimulus in 2009 because the economy was so weak, she doesn't advocate more now. "We just don't have enough evidence to prove that it's good." Robert Barro, a Harvard economist, found even smaller multipliers: A government dollar spent creates about 80 cents worth of growth, or possibly less, he says. Government spending, he says, crowds out private sector spending that would otherwise be taking place. Keynesians say other things were happening at the same time as military build-ups that muddy the results. During World War II, for instance, consumer goods were rationed and Americans were exhorted not to spend. Economists who say Mr. Obama should have relied more on tax cuts cite research of an unlikely source: Ms. Romer, his adviser. In a study she and her husband, David Romer, conducted before she joined the administration, Ms. Romer found large multipliers from tax cuts, which she concluded "have very large and persistent positive output effects." Tax increases, she also found, hurt growth. That study didn't address whether spending is better than tax cuts, though. And she says the gravity of the economic situation called for both tax cuts and spending. Tax cuts haven't been a cure-all. President Bush tried $168 billion of tax rebates in 2008, and a recession ensued anyhow. Economists note that households tend to save temporary tax cuts or use them to pay down debt, so they don't provide much short-term stimulus. Before the debate over the efficacy the 2009 stimulus is resolved, Congress is turning to whether it's time to start cutting deficits. Mr. Alesina says it is: In 107 periods since 1980 when governments cut deficits, doing so tended to quicken economic growth, not slow it. But his study focused on periods when central banks could offset deficit cutting with lower interest rates. The Fed has exhausted that avenue. Carmen Reinhart, a University of Maryland economist who has studied the fiscal aftermath of financial crises, says more stimulus could be counterproductive because it could lead the public to expect even higher taxes in the future. Instead, policy makers now need to convince the public that they are committed to reducing future deficits, without acting on that commitment right away, she says. That could hold interest rates down, without yanking money from an ailing economy too quickly. "We are not in an easy position," she says. "Credibility is going to be difficult to achieve."

AT: Stimulus

Keynesianism is inaccurate – over reliant on Phillips curve

Robert J. Barro is THE Paul M. Warburg Professor of Economics at Harvard University, 1989, “New Classicals and Keynesians,

or the Good Guys and the Bad Guys”, ProQuest

One important function of a macroeconomic model is to isolate the sources of disturbances that cause aggregate business fluctuations. Keynesian analyses focus on shocks to aggregate demand, and typically attribute these shocks either to governmental actions (disruptive or corrective fiscal and monetary policies), or to shifts in private preferences that influence consumption or investment demand. Keynes's own discussion referred to the "animal spirits" of businessmen, and the onsequent volatility of investment demand due to shifting moods of optimism or pessimism. Thus, aside from governmental actions, the Keynesian model is not strong at pinpointing observable, objective events that cause recessions or booms. Schweiz. Zeitschrift für Volkswirtschaft und Statistik, Heft 3/1989 264 One reason that Keynes may not have been troubled by this "deficiency" is that he viewed the private economy as inherently unstable. It did not take large (and presumably objectively observable) shocks to trigger a recession, because even a small shock - when interacting with the multiplier (and, in some models, also the investment accelerator) - could generate a significant and sustained drop in output and employment. Curiously, however, later Keynesian developments deemphasized the multiplier. For example, in the well-known IS/LM model (in which interest rates adjust and matter for aggregate demand) or in Keynesian analyses that incorporate some version of the permanent-income hypothesis, multipliers need not exist. These extensions do improve the model's fit with some facts about business cycles, such as the apparent absence of a multiplicative response of output to changes in government purchases and the relative stability of consumption over the business cycle. But the elimination of the multiplier means also that large responses of output, as in a substantial recession, require large impulses; hence, it again becomes important to identify the kinds of shocks that typically matter for aggregate fluctuations. I think that the desire to find observable, aggregate shocks motivated many Keynesians - although not Keynes nor many of his immediate followers - to assign a substantial weight to monetary disturbances as a source of the business cycle. Within a framework where prices adjust slowly and output is determined by aggregate demand, it is easy to conclude that an increase in money raises output and also leads gradually to a higher price level. Moreover, the positive correlation between money and output - and perhaps between the price level and output - showed up in some data. During the 1960s and early 1970s, Keynesian analysis became increasingly identified with this Phillips curve-view of the world. Thus, this analysis also lost considerable prestige when the Phillips curve disappeared in the mid 1970s; the rise in unemployment along with the increasing rate of inflation was difficult to explain in this kind of model. New Keynesians have, however, demonstrated their flexibility by arguing that the old Keynesian model merely need to be patched up to incorporate the supply side. But this argument does not work. In a single market, one can think of quantity as determined by demand with the excess supply rationed - as in the Keynesian model - so that changes in quantity depend only on shocks to demand. Then if this situation applies to the majority of markets, one can generate orthodox Keynesian prescriptions for the government's macro policies. Alternatively, quantity in a typical market could be determined by supply with the excess demand rationed - as in markets subject to effective price controls - so that movements in quantity depend only on shocks to supply. If this situation holds for the majority of markets, one again gets prescriptions for the government's macro policies, but they are basically opposite to those from the Keynesian model. The serious alternative to either of these two polar cases is a framework where demand and supply are somehow balanced 01 equilibrated on the various markets. Although I regard this equilibrium approach 265 as the logical way to think about macroeconomics, this approach - pursued by new classical macroeconomists - turns out basically to be anathema to Keynesian thinking. T

AT: Stimulus

Keynesianism fails to explain unemployment

Robert J. Barro is THE Paul M. Warburg Professor of Economics at Harvard University, 1989, “New Classicals and Keynesians,

or the Good Guys and the Bad Guys”, ProQuest

According to a newspaper article that I read from Australia there is now a consensus among economists that a successful Keynesian revival is underway. (Unfortunately, the reporter neglected to mention that the consensus was acclaimed at a meeting of the Australian Economics Conference, where only Keynesians had been invited to attend.) No less than four new areas (the four horsemen of the new Keynesian economics?) are actively being pursued to provide Keynesian analysis with firm microeconomic underpinnings. Looked at this way, the mission of the new Keynesian economics (which I like to describe by the acronym NUKE) is peculiar. Instead of providing new theoretical results and hypotheses for empirical testing, the objective often seems to be to provide respectability for the basic viewpoint and policy prescriptions that characterize the old Keynesian models. It may well be more rewarding to look instead for new theoretical insights, empirical hypotheses, and policy implications. The first NUKE area - implicit or explicit long-term contracts for labor or goods - is intended to rationalize sticky wages or prices. Although these models may explain why some wages or prices are sticky, the approach has been less successful in relating this stickiness to Keynesian style behavior of employment and output. Basically, the introduction of an ability to undertake long-term contracts tends to make private markets function more efficiently, rather than less efficiently as in the Keynesian model. If the basic problem in business fluctuations is an inability of agents to coordinate decisions, then it would indeed be surprising if this problem originated from an ability to make contracts. As an example, in the context of a long-term labor agreement, it is possible to attain the appropriate variations over time in work effort without requiring day-to-day adjustments in pay. Workers agree at the outset - either formally or informally - that they will expend more effort when there is more work to do, with the understanding that they will also receive more leisure when there is less work. As long as the variations in effort are not too great or long-lasting, it is 270 unnecessary for wages to rise along with the extra work and vice versa. Thus, this analysis explains why the private economy can behave efficiently - as if markets cleared continuously - even if observed wages are sticky. The underlying shadow value of time is flexible, and the observed wages are merely installment payments that are part of a broader compensation package. Thus, in this view, it is also not surprising or disturbing if observed real wages do not correlate especially well with variations in labor supply. (There are some differences here in the predictions for movements in hours or effort from existing employees versus changes in the number of workers, because new employees are likely not covered by previous labor contracts.) Another point is that long-term contracting is an element of a real theory, and does not explain why monetary disturbances or the Phillips curve would be important. Moreover, it is just as likely that the real wages or relative prices determined in a long-term agreement would be "too low" as "too high." Thus, the implications for excess supply or demand are symmetric, and do not tend to support the Keynesian focus on aggregate demand. The second area of the new Keynesian economics allows for menu costs in the adjustment of prices or wages. Unlike long-term contracts, the idea here is that nominal prices are costly to change - thus, this theory does relate to monetary disturbances and to the interplay between nominal and real variables. In the absence of long-term contracts (as above), the "errors" in price formation could translate into inefficient choices of quantities. However, as with long-term contracts, this viewpoint does not point especially to the Keynesian case where nominal prices are too high rather than too low. That is, Keynesian excess supply would be no more likely than sustained excess demand. As a theoretical matter, it has long been known that direct costs of adjustment could explain some stickiness in prices. However, the basic misgiving about menu costs is that the direct costs of adjusting prices are typically trivial relative to the losses from choosing inappropriate quantities. (The costs for changing prices tend also to be much less significant than those for changing quantities.) Thus, the main contribution of the new literature on menu costs was to show that - starting from a position of market clearing - an error in price setting could involve costs that are second order privately but first order socially. (Under imperfect competition, the "market-clearing" price could also be allowed to deviate from marginal cost.) Unfortunately, this result does not hold if output and employment are already finite amounts away from their equilibrium values. In this situation, the private cost from setting a price a little further from its market-clearing value is also first order. Thus, if the costs of price adjustment are minor, this approach still fails to explain significant shortfalls in production and employment. New classical models with money were often criticized for their reliance on faulty perceptions about the general price level to explain major recessions. Since it was cheap to learn about the general price level, the overall analysis was unconvincing. But it is even more unconvincing to argue that major 271 contractions of output and employment arise because firms are unwilling to pay the small menu costs required to change their prices.

### AT: New Deal Proves

#### **New deal spending slowed recover and Obama should not repeat**

Amity Shlaes; director of the 4% Growth Project, Author, Columnist; 2-1-2009; <http://www.washingtonpost.com/wp-dyn/content/article/2009/01/30/AR2009013002760_2.html>

One evening in the 1930s, a 13-year-old named William Troeller hanged himself from the transom of his bedroom in Greenpoint, Brooklyn. William's father was laid up in Kings County Hospital awaiting surgery for an injury he'd suffered on the job at Brooklyn Edison. A federal jobs program was paying William's older brother Harold for temporary work. But the amount wasn't nearly enough to make ends meet. Gas and electricity to the family's apartment had been shut off for half a year. Harold told a New York Times reporter that both hunger and modesty had driven William to act. "He was reluctant about asking for food," read the headline in the paper. The surprising part of this story is not that it happened; most Americans know that after the 1929 stock-market crash, hard times sometimes led to suicide. The surprising part is that William Troeller killed himself not in 1930, when Herbert Hoover was president, but in 1937, in Franklin D. Roosevelt's second term. The New Deal was almost five years old, but the economy was not back. In fact, the country seemed farther from recovery than before. A new sense of futility was overcoming Americans. The British magazine the Economist sneered that the United States "seemed to have forgotten, for the moment, how to grow." The date matters, because our new president has made it clear that his model is Roosevelt. Barack Obama has spoken of creating 3 million jobs with his stimulus plan. As a new president in 1933, Roosevelt spoke of creating "one million jobs by October 1" through his spending packages. At about $850 billion, Obama's stimulus represents about 5.9 percent of gross domestic product. The spending programs of Roosevelt's National Recovery Administration amounted to almost precisely the same share. Then as now, the country was in what we might call an "illions" moment, when a nation contemplates federal spending of a magnitude previously unimaginable. The only difference is that today, we're discussing trillions instead of billions. It's reasonable that a new executive in a downturn would want to evoke Roosevelt the leader. Like no other president, Roosevelt inspired those in despair. He kindled hope with his fireside chats on a then-young medium, radio. The new president gives radio talks, but they are also made available on this era's young medium, the Internet. But Roosevelt the economist is unworthy of emulation. His first goal was to reduce unemployment. Of his own great stimulus package, the National Industrial Recovery Act, he said: "The law I have just signed was passed to put people back to work." Here, FDR failed abysmally. In the 1920s, unemployment had averaged below 5 percent. Blundering when they knew better, Herbert Hoover, his Treasury, the Federal Reserve and Congress drove that rate up to 25 percent. Roosevelt pulled unemployment down, but nowhere near enough to claim sustained recovery. From 1933 to 1940, FDR's first two terms, it averaged in the high teens. Even if you add in all the work relief jobs, as some economists do, Roosevelt-era unemployment averages well above 10 percent. That's a level Obama has referred to once or twice -- as a nightmare. The second goal of the New Deal was to stimulate the private sector. Instead, it supplanted it. To justify their own work, New Dealers attacked not merely those guilty of white-collar crimes but the entire business community -- the "princes of property," FDR called them. Washington's policy evolved into a lethal combo of spending and retribution. Never did either U.S. investors or foreigners get a sense that the United States was now open for business. As a result, the Depression lasted half a decade longer than it had to, from 1929 to 1940 rather than, say, 1929 to 1936. The Dow Jones industrial average didn't return to its summer 1929 high until 1954. The monetary shock of the first years of the Depression was immense, but it was this duration that made the Depression Great. This outcome is worth reviewing, component by component, for what it suggests about individual Obama administration projects. The first of these would be ambitious spending on infrastructure. Obama has said that he wants to "put people to work repairing crumbling roads, bridges and schools." In addition, he would like to modernize 75 percent of government buildings, as well as equip tens of thousands of schools with new technology. Roosevelt, too, proceeded boldly on infrastructure. The budget of his Public Works Administration was so large that it shocked even the man who ran it, Interior Secretary Harold Ickes. Sounding a bit like Republicans today, Ickes said of his $3.3 billion allowance: "It helped me to estimate its size by figuring that if we had it all in currency and should load it into trucks, we could set out with it from Washington for the Pacific Coast, shovel off one million dollars at every milepost and still have enough left to build a fleet of battleships." New Deal public-works spending did have a short-term effect, creating jobs and economic activity during Roosevelt's first term. Americans took heart at the sight of schools, swimming pools and auditoriums rising in nearly every county in the country. FDR so pumped up the federal government that 1936 was the first peacetime year when it spent more than states and towns. A master of timing, he even managed to get unemployment down to a low of 13.9 percent in November of that year, the month of the presidential election. The voters rewarded him by giving him 46 of 48 states. But many of the jobs that the early New Deal produced were not merely temporary but also limited in economic value. It was in these years that the political term "boondoggle," to describe costly make-work, was coined. It came from "boondoggling," the word for leather craft projects subsidized by New Deal work-relief programs. As was the case for the Troeller brothers, work-relief earnings were usually not sufficient to offset other Depression losses. After the 1936 election, Roosevelt found himself appalled at the budgetary deficit he had run up and turned frugal. Infrastructure spending slowed. Monetary authorities feared inflation and doubled reserve requirements at banks. The "Depression within the Depression" of the Troellers' time began. This cynical cycle -- spend on construction, hold election, tighten, confront new joblessness -- is familiar nowadays, especially in Latin America. But then, to Americans, it came as a bitter surprise. Another similarity also stirs concern. Obama is focusing on our country's most promising innovation, one that is among the most likely to generate recovery jobs -- the Internet. He wants to use stimulus dollars to give poorer Americans access to that technology. Specifically, the president wants to achieve the goal of "expanding broadband across America." The listener gets the impression that Obama wouldn't mind if the federal government ran some of this business if such involvement is what it takes to get universal access. Equity first. In Roosevelt's day, there was also an appealing new technology: electricity. Power was the industry that symbolized growth -- the Dow Jones utilities average was expected to lead the old industrial average into recovery. After all, access to electricity was so desirable that power companies' operating revenue rose even during the Depression. There were also private companies ready to supply power to the rural unwired. One was the Commonwealth and Southern Corp., fashioned by venture capitalists and industry leaders explicitly to raise the vast sums of capital necessary to light the South. Here Roosevelt, too, combined a stimulus project with his goals for social equity. He created the Rural Electrification Administration to wire the countryside. He also created the Tennessee Valley Authority to provide hydropower. One can picture private and public working together, and that's what Commonwealth and Southern imagined, too, at first. At a tense meeting at Washington's Cosmos Club in 1933, the company's chief executive, Wendell Willkie, begged a TVA officer, David Lilienthal, to strengthen public-private cooperation. Instead, Lilienthal waged war on Willkie, using the TVA's tax-free status to compete for customers and fighting Commonwealth and Southern in the courts. In 1935, Roosevelt signed a utilities law that so restricted private capital raising that it was known as the "Death Sentence Act." At the time, observers told themselves that the shift caused no economic loss. But the stock indexes told the real story. Instead of matching or outperforming the industrial average, the Dow Jones utilities average lagged behind. The great "stimulator," government, had emerged as an opponent. The effect, beyond the tragic unemployment, was to slow down the creation of new companies. Even the New Dealers despaired. "We have tried spending money," Treasury Secretary Henry Morgenthau said to the House Ways and Means Committee in the late 1930s. "We are spending more than we have ever spent before and it does not work. . . . I say, after eight years of this administration, we have just as much unemployment as when we started . . . and an enormous debt to boot." What the New Deal record tells us is that it's worthwhile imagining an alternate Washington program. A program that's merely about budget balancing is wrong in an hour when banks are wildly deleveraging. But Obama could put market reform before spending. It's time to keep plans to strengthen the regulation of markets and widen regulators' mandate so that they monitor most of what's traded and derivatives don't slip through the cracks. What about spending? The Depression tells us that public works are probably less effective than improving the environment for entrepreneurs and new companies. The president has already put forward a big tax cut for lower earners. He might offer a commensurate one for higher earners. He might expand the tax advantages he is currently offering to companies -- wider expensing of losses, for example -- and make them permanent. A discussion that permits the word "trillion" might also include the possibility of bringing down U.S. corporate taxes, taxes on interest, dividend and capital gains -- again, permanently. The cash that a relatively competitive United States draws from abroad will move the country forward faster than any stimulus. So the Depression and the New Deal are both worth going back to, but for different reasons than many suspect. We may rely on the best of the New Deal, the matter-of-fact bravery our parents and grandparents showed then, to help us through today's unexpected challenges. But we don't have to repeat New Deal stimulus experiments, because we know that they didn't work.

### AT: Austerity Bad

#### Debt causes crisis—spending cuts solve

US Budget Committee 11 U.S. Senate Budget Committee Republican, responsible for drafting Congress’ annual budget plan and for monitoring the federal budget, 5/12/11, “Spending Cuts And Economic Growth: What Does The Cross-Country Empirical Evidence Show?,” U.S. Senate Budget Committee Republican, http://budget.senate.gov/republican/public/index.cfm/committee?p=committee-history

The federal debt held by the public has doubled, in nominal terms, in less than four years. It now stands at over 62 percent of GDP, the highest level since 1951. What costs does this place on our economy? With our fragile economy still suffering high unemployment, can we risk attempting to slow the accumulation of more debt by reducing government spending? This paper examines these questions by surveying the available literature and empirical evidence regarding the economic effects of government debt and spending reductions on economic growth. The available evidence shows that: a national debt crisis could result in economic collapse; our high national debt already imposes sustained economic costs; our growing debt can be slowed by immediate reductions in government spending; reductions in federal spending, as part of successful fiscal consolidations, have demonstrably led to economic growth fiscal consolidations focused on spending cuts are far more successful than those relying on tax increases and those that evenly combine tax increases and spending cuts.

#### Spending cuts solves—empirics prove

US Budget Committee 11 U.S. Senate Budget Committee Republican, responsible for drafting Congress’ annual budget plan and for monitoring the federal budget, 5/12/11, “Spending Cuts And Economic Growth: What Does The Cross-Country Empirical Evidence Show?,” U.S. Senate Budget Committee Republican, http://budget.senate.gov/republican/public/index.cfm/committee?p=committee-history

Immediate reductions in spending will begin a necessary move to reduce deficits and reduce the pace of debt accumulation. For example, a Budget Committee analysis found that a $61 billion reduction in spending in fiscal year 2011 would immediately begin to tackle our spending problem and would save $862 billion over the next 10 years. Cutting spending can successfully bring our country out of debt, while moving our economy back toward a system that rewards private productivity, ingenuity, and American workers. Spending reductions do not necessarily mean, as Keynesian reasoning dictates, that the economy suffers. Indeed, a consistent and striking conclusion from a large and growing body of evidence is that successful efforts to climb out of debt are composed mostly of spending reductions, and that these reductions not only do not tend to harm economies but, rather tend to lead to economic growth. [24] For instance, a recent extensive review of countries that faced perilously high debt levels, by Andrew Biggs, Kevin Hassett, and Matthew Jensen, considered the experiences of 21 OECD countries over a 37 year period. [25] They find that countries that failed to successfully reduce their debt are more the rule than the exception—success appears to be achieved in approximately one-fifth of cases. On average, the typical unsuccessful country used a combination of 53 percent tax increases and 47 percent spending cuts. By contrast, the typical successful country used, on average, 85 percent spending cuts. The authors conclude that “…fiscal consolidations based upon expenditure cuts have tended to be more effective than tax-based consolidations based on the evidence from empirical studies.”

#### Interest rates make deficit spending cuts inevitable

US Budget Committee 11 U.S. Senate Budget Committee Republican, responsible for drafting Congress’ annual budget plan and for monitoring the federal budget, 5/12/11, “Spending Cuts And Economic Growth: What Does The Cross-Country Empirical Evidence Show?,” U.S. Senate Budget Committee Republican, http://budget.senate.gov/republican/public/index.cfm/committee?p=committee-history

As deficits and debt continue to mount, the power of compound interest means an ever-increasing amount of federal resources are being devoted to interest payments to help pay for past deficit spending. As Figure 3 shows, interest payments are projected to increase nearly fivefold under the President’s budget, to almost $1 trillion by 2021. This means desirable federal programs will have to be cut, in increasingly painful amounts, so that the government will be less and less able to provide resources for everything from nutrition assistance to highway maintenance and construction. (Revenue could be increased to diminish these reductions; this option will be discussed below.) To the extent these programs improve the country’s welfare and economic growth, they are already on a path to being squeezed.

AT: Austerity Bad

#### Spending cuts solve—empirics

Brady 11 Kevin Brady, Joint Economic Committee Republicans Vice Chairman Designate, 3/15/11, “Spend Less, Owe Less, Grow the Economy,” Joint Economic Committee Republicans, http://www.speaker.gov/sites/speaker.house.gov/files/UploadedFiles/JEC\_Jobs\_Study.pdf

Keynesians hold that fiscal consolidation programs are contractionary in the short term, because they reduce aggregate demand. However, **large government budget deficits create expectations for higher taxes to service government debt and affect the economy in the short term as well as the long term**. Consequently, f**iscal consolidation programs that reduce government spending decrease short-term uncertainty about taxes and diminish the specter of large tax increases in the future for both households and businesses.** **These** “non-Keynesian” **factors can boost GDP growth** in the short term as well as the long term **because**: **Households’ expectations of higher permanent disposable income create a wealth effect, which stimulates purchases of consumer durables** and home buying **thus driving up personal consumption** expenditures and residential investment in the short term. **Businesses expecting higher after-tax returns boost their investment in non-residential fixed assets** in the short term. WHAT AND HOW TO CUT. Certain kinds of government spending reductions generate significantly larger pro-growth effects than others. For the “non-Keynesian” effects to be significant, **government spending reductions must be viewed as large, credible, and politically difficult to reverse once made**. **Some examples are:**  Decreasing the number and compensation of government workers. **A smaller government workforce** increases the available supply of educated, skilled workers for private firms, thus lowering labor costs. **Eliminating agencies and programs**. **Eliminating transfer payments to firms**. Since government transfer payments entice firms to engage in otherwise unprofitable and unproductive activities, eliminating transfer payments will increase efficiency as firms cease these activities. **Reforming and reducing transfer payments** to households. Making major government programs, such as pension and health insurance benefits for the elderly, sustainably solvent will boost real GDP growth by (a) enhancing the credibility of fiscal consolidation plans, and (b) inducing younger workers to work more, save more, and retire later. This is true even if the reforms exempt current beneficiaries, are phased-in slowly, and any short-term spending reductions are very small. EXTENSIVE EMPIRICAL SUPPORT FOR SPENDING CUTS. Gabriele Giudice, Alessandro Turrini, and Jan in ‘t Veld (2003) identified **11 episodes based on size and 19 episodes based on duration of “pure” expansionary fiscal consolidations that consisted predominately or entirely of government spending reductions as a percentage of GDP in EU member-states over 33 years**. Alberto Alesina and Silvia Ardagna (2009) made the same finding for 26 episodes in nine OECD member-countries between 1970 and 2007. The IMF strikes a cautionary note on shortterm expansionary “non-Keynesian” factors offsetting contractionary Keynesian reductions in aggregate demand. But, the IMF is in agreement with the other studies that **fiscal consolidation programs based** predominately or entirely **on government spending reductions**—especially in transfer payments to households and firms—**are better for the economy in the short term** than programs in which tax increases play a significant role.

#### Spending cuts grow the economy

Kevin Brady (Senior member of the House Ways and Means Committee and vice chairman of the Joint Economic Committee.  7/12, The Hill Blog, <http://thehill.com/blogs/congress-blog/economy-a-budget/171559-cut-spending-to-grow-the-economy>)

The anemic 18,000 payroll jobs the United States gained last month clearly shows America’s job creators are on strike against President Obama’s failed big government policies. If we want to spur business investment that will create new jobs we must change our fiscal course. In his 1981 inaugural address, President Reagan said, “government is not the solution to our problem; government is the problem.” Reagan began to reduce the size and scope of the federal government and produced spectacular growth dividends. Over the next two decades, federal spending shrank from 22 percent to 18 percent of our economy, and the United States created 37 million private payroll jobs. Since 2001, Congress has allowed federal spending to expand once again to 24 percent of our economy. Not surprisingly, the United States has lost 2.7 million private payroll jobs since then. Since 2009, when the Obama stimulus was enacted, the United States lost 1.3 million private payroll jobs. The lesson is clear: we must shrink Washington to create jobs on Main Streets around America.

AT: Austerity Bad

#### Congressional Report shows spending cuts improve economy

Peter Roff, News Reporter, “The GOP Case for Spending Cuts to Boost the Economy”, 3/25/11, http://www.usnews.com/opinion/blogs/peter-roff/2011/03/25/the-gop-case-for-spending-cuts-to-boost-the-economy\_print.html

A recent report from Congressional Joint Economic Committee [Republicans](http://politics.usnews.com/topics/subjects/republican-party) points the way out of the nation’s current fiscal morass: “Spend Less, Owe Less, Grow the [Economy](http://politics.usnews.com/topics/subjects/unemployment).”[The report](http://tinyurl.com/4c4gvx9), which examines the behavior of all developed countries between 1970 and 2007, explains in rather simple language that the government’s financial problems do not come from revenue problems so much as they are the result of over-spending. “Clear and convincing empirical evidence proves countries that undertake programs to reduce government [budget deficits](http://politics.usnews.com/topics/subjects/deficit-and-national-debt) and stabilize the level of government debt (known as fiscal consolidations) can boost economic growth and job creation in the short term.”Of the three key findings, the most obvious is perhaps that “Spending cuts work. Tax increases don’t.”“Countries that lower their debt-to-GDP ratio predominately or entirely through spending cuts are more likely to achieve their goals of government budget deficit reduction and government debt stabilizationthan debt reduction efforts in which tax increases play a significant role.”The second key finding is that “Spending cuts can boost the economy in the short term too.”“While most economists agree that reducing government spending increases economic growth the long term,” the JEC said, “empirical studies have found that reducing government spending can boost economic growth and job creation in the short term as well.”The third key finding is that “Spending cuts must be credible to realize short-term growth benefits.”This is an important point that is often over-looked, especially by those who would rather talk about cutting spending than actually do it. Examples of the kind of spending the committee analysts who prepared the report found to be “credible” include reducing the number and compensation of government workers, eliminating agencies and programs, eliminating transfer payments to businesses and reforming and reducing transfer payments to households.

AT: Austerity Bad

#### PUBLIC AUSTERITY PROMOTES PRIVATE GROWTH

Veronica **De Rugy** (Ph.D., is a senior research fellow at the Mercatus Center at George Mason University and a columnist for the National Review, 5/**12**, The National Review, <http://www.nationalreview.com/corner/300915/public-sector-austerity-vs-private-sector-austerity-veronique-de-rugy>

For a few weeks I have been saying that pro-growth austerity imposes austerity on the public sector. That means reduction in government spending, reform of entitlements, reduction in the the rolls and salaries of government employees, and reduction of the government footprint in the private sector. Unfortunately, in most cases, governments would rather address their debt problems through an anti-growth version of austerity, meaning more taxes and more government intervention in our lives. David Malpass has a very good piece in the Wall Street Journal this morning that illustrates this point. As he explains, there is no conflict between growth and austerity: The conflict between growth and austerity is artificial and framed to favor bigger government. Growth comes from economic freedom within a framework of sound money, property rights, and a rule of law that restrains government overreach. Businesses won’t invest or hire as much in an environment where governments dominate the economy. Thus, government austerity is absolutely necessary for economic growth in both the short and long run. The only people who think that there is a conflict between growth and government austerity are economists (such as Keynesian economists) who believe that government spending decisions are as productive if not more productive than spending decisions made by the private sector or that disregard the impact of high level of debt on the economy. These assumptions, unfortunately, are reflected in every government scoring models and give us misguided policies like the stimulus. As Malpass correctly lays out, these absurd assumptions have produced the model for European austerity: one that requires the private sector to pay more taxes and pay for debt it didn’t incur so the governments can stay bloated. Case in point, Greece: The Greek government has been practicing a particularly aggressive form of antigrowth austerity. While the private sector shrank in 2011, Greece’s government grew to 49.7% of GDP from 49.6% in 2010. To accomplish this bad outcome, Greece’s government increased its value-added tax to 23%—a hidden sales tax so high that no one should be asked to pay it or support it—and created a national property tax that transfers private-sector wealth to the government and through it to foreign creditors. Meanwhile, Greece’s parliament kept full pay, full benefits, its fleet of BMWs, and a full staff. Greece maintained its sweetheart subsidies for businesses, banks, the army and those who choose not to work. Its sizeable delegations and facilities in Brussels, Vienna, Geneva and Washington are still large, as are the life-time pensions for politicians. Last week, Greek officials suspended work on the sale of government assets, one of the most pro-growth conditions in its IMF program. The reality is that Greece’s government is imposing too much austerity on others and not enough on itself. Now, the U.S. government is hoping it can get away with the same false austerity in here. You will see it play out in the next debt-ceiling debate and in the many debt-reduction proposals that will be introduced in the next few months and years. The president’s budget, which illustrates his idea to address our debt problem, is a good example of the government imposing austerity on the private sector so the public sector can stay bloated. That’s what Washington calls the balanced approach. (The various plans introduced by Republicans don’t reduce the size of the government enough either but at least they don’t insist on shrinking the private sector further.) This is also the path that Governor Brown in California wants to pursue in order to close the state’s $16 billion budget gap. But it won’t work. Like in the U.K., Ireland, Italy, Spain, and other European countries, California will see its private-sector growth slow down even further and its debt grow. And so will the U.S., if the federal government continues resisting the necessary reforms. You don’t believe it? Read the new paper by Carmen M. Reinhart, Vincent R. Reinhart, and Kenneth S. Rogoff on impact of debt on economic growth. It’s called “Debt Overhang: Past and Present.” They document 26 cases of debt overhang (at least five years during which debt exceeds 90 percent of GDP). What’s happening during that time? Economic growth is 1.2 percentage points lower than in other periods. It could go on for a long time: Their research finds “the average duration of debt-overhang episodes is 23 years, and it produces a ‘massive’ shortfall in output that is almost one-quarter less, on average, than in low-debt periods.” Moreover, the fact that bond markets in countries perceived as safe, such as the U.S., are blasé about the debt load tells you very little about how well they are doing. For all we know, these countries’ economy could even be shrinking: “Those waiting for financial markets to send the warning signal through higher interest rates that government policy will be detrimental to economic performance may be waiting a long time,” the authors wrote in their paper. That’s what happened to eleven out of the 26 cases in their samples. This paper turns on its face the theory that, as long as investors are willing to put their money in the U.S. and keep rates low, we have nothing to worry about. No, actually, we should worry because low interest rates in a high-debt environment could just mean that we aren’t the ugliest in the Investors’ Beauty Pageant. Oh and by the way, the U.S. is close to entering the Debt Overhang Gang.

AT: Austerity Bad

#### PUBLIC AUSTERITY K2 ECONOMY

Veronica **De Rugy** (Ph.D., is a senior research fellow at the Mercatus Center at George Mason University and a columnist for the National Review, 6/**12**, The National Review, <http://www.nationalreview.com/corner/301972/yes-public-sector-austerity-can-work-veronique-de-rugy> <http://imgur.com/r/AdviceAnimals/bw3lG>

Today is a good day. Two separate media stories have acknowledged that public sector austerity — meaning spending cuts rather than tax increases — can actually bring debt-to-GDP levels down, and it may even produce economic growth. First, this story reports that French IMF director Christine Lagarde hailed Latvia as a country where public-sector austerity worked: RIGA: IMF chief Christine Lagarde pointed yesterday to Latvia as model for states like Greece balking at belt-tightening as the euro-zone debates whether the focus should shift from austerity to growth.”Latvia decided to bite the bullet and instead of spreading the pain over a number of years-doing it gently … you decided to go hard and to go quickly,” Lagarde told delegates to an International Monetary Fund conference in the Latvian capital Riga on lessons from its spectacular recovery. Latvia and its Baltic neighbours Estonia and Lithuania in the EU’s northeastern corner consider austerity as the cure to their deep recessions sparked by the 2008 global financial crisis. Lagarde called Latvia’s performance under a 2008-2009 7.5-billion-euro ($9.4 billion) IMF-EU bailout “incredibly impressive,” with sharp spending cutbacks helping it reduce its public deficit by 8.0 percentage points of gross domestic product in one year. Latvia’s economy contracted by a cumulative 25 percent during the crisis, the deepest plunge recorded worldwide, but the ex-Soviet Baltic state of two million began to recover last year when it clocked 5.5 percent growth. The ‘bite-the-bullet’ approach stands in stark contrast to that of Greece, which has been slow to implement structural reforms and has repeatedly missed targets on reducing its public deficit. Earlier, Lagarde told the Swedish daily Svenska Dagbladet that one lesson from Latvia’s experience is that cutbacks need to be made early on,” noting the risk of reform fatigue if austerity measures are not introduced at once. I wonder what her conversation with Hollande will be next time she sees him. (Thanks to Don Boudreaux for the pointer). Second, this morning NPR also had a story about the recent successful fiscal adjustments in the Baltic nations through spending cuts, and their policy of allowing prices to fall. I, for one, wished we engaged in more of this behavior in the U.S., especially in the housing market. I wrote about the Baltic nations’ fiscal adjustments in the Washington Examiner a few weeks ago. The success in the Baltic nations, by the way, is also explained by their ability to use monetary policy to accommodate their fiscal restraints.

#### WW2 proves austerity to work

Charles Kadlec economics expert, senior writer for forbes 5-7-12 Forbes http://www.forbes.com/sites/charleskadlec/2012/05/07/why-european-austerity-fails/

An extreme example is provided by the U.S. experience after World War II. Total federal spending was slashed 38% in 1946 and another 38% in 1947 or by a combined 29% of GDP. That is equivalent to reducing current federal expenditures by $4.4 trillion in two years. The federal budget went from a $54 billion deficit to a $3 billion surplus. Eight million men and women (12 % of the workforce) were released from the armed forces. Real GDP did decline by 11% in 1946. But, the economy stabilized in 1947, and then grew by 4.4% in 1948.

European austerity fails because of taxes not, budget cuts

Charles Kadlec economics expert, senior writer for forbes 5-7-12 Forbes http://www.forbes.com/sites/charleskadlec/2012/05/07/why-european-austerity-fails/

The reason European austerity has failed is not because of the reductions in government spending, but because those spending cuts have been paired with tax increases. The Europeans are struggling to reduce government spending by less than 5% of GDP. But unlike the U.S., which paired extreme budget cuts with across-the-board reductions in personal income tax rates, the European austerity combines spending cuts with massive tax increases. The result is a toxic brew which shrinks both government and the private sector, producing recession, rising unemployment, and massive budget shortfalls. Here’s why: A tax increase does far more than simply take money out of the private sector and give it to the government. Increases in marginal tax rates also reduce the opportunities for domestic economic activities in the same manner as increases in tariffs shrink the opportunities for international trade. For example, a 2-percentage point increase in the Value Added Tax raises the price of goods and services by 2%. Faced with higher prices, individuals demand less, both because prices are higher (the incentive effect), and because the same amount of euros can now purchase 2% fewer goods and services (the cash flow effect). Suppliers, faced with the fall-off in demand, may choose to absorb some of the tax by lowering the price they receive. However, the lower price received reduces both their desire (incentive effect) and ability (cash flow effect) to maintain the current level of supply.

### AT: Jobs

#### Lack of fiscal discipline hurts the economy – sustains unemployment and perpetuates recession

Paul J. Sullivan, Professor at Georgetown University, 6/20 (Al Arabiya News – Washington, 6/20/2011, “Frightening profligacy, poor fiscal discipline, disputatious democracy and uncertain leadership in the United States,” http://english.alarabiya.net/articles/2011/06/20/153996.html)

Much of the fiscal indiscipline in many countries is due to the political invertebracy of many in the political leadership. The profligacy of the past is catching up with the present and could have deep repercussions in the future. The time for leadership, fiscal courage, and some hard thinking and choices is now. Otherwise, the financial crisis of the 2000s could seem quite mild compared to the brewing economic troubles out there. The effects of not getting things in order could spread far beyond the gates of Athens or the beltway of Washington. It is, however, not too late to get moving on the solutions and the tough decisions. I have an odd sense of foreboding mixed with cautious optimism about the US. In the past the US has worked its way out of very difficult times. One can think of the Great Depression and other deep recessions in its past going back even to the start of the country. One can also see a lot of strength in the inventiveness and entrepreneurial nature of the US. It is a powerful economy and society with many very hard working people.  However, this situation seems fundamentally different than in difficult times in the past because the culture of discipline, and especially fiscal discipline, and the society’s and governments views toward debts have changed – even since the 1980s – considerably. If anyone is struggling to figure out why the US unemployment rate will likely remain high for some time to come, and it could take many years to get back down to 5 to 6 percent unemployment rates, then look to the government, household and other debts that are drags on the economy.  Also, debt is what got the US economy and a good part of the rest of the world economy into the difficult positions they have been in recent years. Let’s hope our leaders in business, government, thought leaders in society, and others can do the right things on time, and the US economy, and by implication much of the rest of the world economy, can get back on track before the next economic storms hammer so many lives once again.

### AT: Tax Hikes Solve

#### High taxes crush small businesses and kill jobs

The Essene, a Daily Kos Community Site, ‘9 (July 16th 2009, “A Universal Tax to Pay for Universal Health Care,” http://www.dailykos.com/story/2009/07/16/754259/-A-Universal-Tax-to-Pay-for-Universal-Health-Care)

However, the high income tax surtax is not painless for the middle class.  Its cost will fall principally on those small family businesses that create 80% of our jobs, and the middle class already suffers from a desperate shortage of jobs.  Politicians can be sure that the middle class will notice a jobless recovery, assuming recovery can even begin.  Almost all small businesses have "pass-through treatment" where the owners include the business income in their federal income tax returns and then pay tax on it, whether they receive cash or not.  Thus, family and other small businesses pay tax not at corporate rates, but at individual rates.  Small business owners, therefore, have to pay the surtax or any tax increase in marginal rates on their business income whether they spend the money or reinvest it in their businesses, leaving the owners with less capital to expand or hire.  On the other hand, big international corporations pay nothing more in tax, leaving small businesses at a competitive disadvantage and unable to raise prices to offset the increased tax.

#### Republicans will oppose any tax increase – it’s their dogma

Albert R. Hurt, Executive Editor for Bloomberg News, 7/17/11, “Republicans’ Idealogy Dooms Deal on U.S. Debt” http://www.nytimes.com/2011/07/18/us/18iht-letter18.html

WASHINGTON — Vice President Joseph R. Biden Jr., in the heat of the high-level budget deliberations, told Republicans that their intransigence over taxes was a matter of ideology, not economics. It’s also about coalitions and contributors. Congressional Republicans rejected a grand-bargain deficit reduction plan that would have slashed spending, including on entitlements, while raising revenue. Raising taxes, charged Republicans like the House majority leader, Representative Eric Cantor of Virginia, would be a job killer in a struggling economy. Mr. Cantor pulled the rug out from the efforts of a fellow Republican, the House speaker, John A. Boehner, and President Barack Obama to strike a historic deal. It was about politics, not jobs. Both Presidents Ronald Reagan and Bill Clinton engineered big tax increases that were followed by robust economic gains. Politically, however, tax cuts are the glue that holds together the Republican coalition. It used to be anti-Communism until the Berlin Wall came down. There’s still a divide on social issues, and even a number of anti-abortion or anti-gay rights Republicans don’t consider these questions priorities. With the wars in Afghanistan and Libya, it’s tough to distinguish between the foreign policy positions of conservatives and those of liberals. There is no such confusion when it comes to taxes. With enforcers like the anti-tax crusader Grover Norquist looking over their shoulders, Republican politicians know that if they even entertain the idea of higher taxes, they throw away any national ambitions, may be threatened in a primary, and, if in a position of leadership, face a revolt from the rank and file.

#### No tax raises – Norquisit’s anti-tax pledge

Jason Hanna, 7/15/11, “Politicians’ pledges show interest groups’ sway” http://www.cnn.com/2011/POLITICS/07/14/pledges.interest.groups/

Some political analysts watching the debt ceiling talks in Washington lament that the no-tax-hike pledge signed by most congressional Republicans may prevent a grand compromise in which tax increases accompany spending cuts. To the man who leads the interest group behind the pledge, that's pretty much the idea.Grover Norquist, president of Americans for Tax Reform -- the group whose oppose-all-tax-increases vow was signed by 235 House members and 41 senators, almost all of them Republicans -- said the pledge is doing what it's supposed to: preventing what he says are mistakes of 1982 and 1990, namely agreeing to tax increases and watching promised spending cuts evaporate."When you take the pledge, it ends the constant badgering of people asking you to raise taxes here, there and everywhere," said Norquist, whose group wants to shrink the federal government and believes any new revenue would enable continued government growth. "Once you keep putting a tax increase on the table, spending cuts disappear." "If someone says that this makes it difficult to make a big budget deal (with tax increases), that's the point," he said. "... The only reason that (President Barack) Obama is even talking spending restraints is because of this pledge."

AT: Tax Hikes Solve

#### Tax hikes won’t happen – Republican refusal

CNN 6/29/11 Deirdre Walsh, Xuan Thai, and Kate Bolduan, “Republicans reject president’s call to include tax revenues in debt deal” http://politicalticker.blogs.cnn.com/2011/06/29/republicans-reject-presidents-call-to-include-tax-revenues-in-debt-deal/

Republican congressional leaders Wednesday rejected President Barack Obama's call to include tax revenues as part of a deal to raise the debt ceiling. Obama said at a White House press conference Wednesday that he's already made concessions to significantly cut spending for government programs. In return, he said, Republicans should now accept proposals to end corporate tax subsidies, such as those given to oil and gas companies or tax breaks for hedge fund managers. The president tried to label Republicans as more interested in protecting special interests than getting a deal done before the U.S. defaults on its financial obligations later this summer. He singled out one tax break that gives corporations a deduction for buying company planes. "You'll still be able to ride on your corporate jet. You'll just have to pay a little more." Obama said.But House Speaker John Boehner flatly dismissed any proposal that would add revenues to a debt limit agreement. "The president is sorely mistaken if he believes a bill to raise the debt ceiling and raise taxes would pass the House," Boehner said in a written statement.Boehner repeated his position that any deal to up the nation's borrowing authority must include spending cuts greater than the amount the debt limit is raised, reforms to control spending over the long term and be "free from tax hikes." "The longer the president denies these realities, the more difficult he makes this process," Boehner stated.

# \*\*AFF\*\*

### 2AC — Fiscal Discipline Low

#### Lack of cooperation in both houses leaves Congress with no solution to the economy

Sahadi (Senior Writer for CNNMoney. Specializing in taxes and deficit spending) 7/16/12 (Jeanne, “Fiscal Cliff Fight is On, and Economy Suffers” LexisNexis)

The inability of Democrats and Republicans to work out their differences on the fiscal cliff is already becoming a problem for the economy. And that problem will grow the longer the standoff lasts. In the latest turn of events, Sen. Patty Murray, a leading Senate Democrat, said Monday that no deal will be cut until Republicans agree to raise taxes on high-income households. "If we can't get a good deal, a balanced deal that calls on the wealthy to pay their fair share, then I will absolutely continue this debate into 2013 rather than lock in a long-term deal this year that throws middle class families under the bus," Murray said in prepared remarks at the Brookings Institution. The cliff represents a host of expiring tax cuts -- including the Bush tax cuts -- and nearly $1 trillion in across-the-board spending cuts that everyone agrees is a terrible way to reduce deficits. Republicans want to replace the scheduled defense cuts with deeper cuts in non-defense domestic programs. And they'd like to extend the Bush tax cuts for everyone. Democrats don't like the spending cuts either -- which will total roughly $110 billion next year. But if they're going to be averted or postponed, Democrats want a package deal. "None of the automatic cuts are good policy. They were packaged together ... and they will be replaced, or not, as a package," Murray said. And Democrats want the portion of Bush tax cuts that apply to high-income households to expire. Economists -- most recently at the International Monetary Fund - have urged lawmakers to ratchet back the effect of the fiscal cliff in 2013, lest it throw the economy back into recession. In 2013 alone, the combination tax increases and spending cuts would be a more than $500 billion hit to the economy. Practically, no one expects Congress to let the fiscal cliff take effect in full. But the uncertainty of how and when lawmakers will resolve the issue is hurting business confidence and weighing heavily on companies' investment and hiring decisions, said Nariman Behravesh, chief economist for IHS Global Insight. It won't kill the economy, Behravesh stressed, but it will curtail growth. "It'll mean growth -- employment growth, GDP growth -- will grind down," Behravesh said. Defense contractors have already indicated they're in a hiring lockdown and could have to send out layoff warning notices this fall. Federal agencies are also likely to put off signing contracts and making new hires. Uncertainty is also likely to cause tumult in the stock market. "Stocks have been under pressure, and will remain this way until there is some resolution," said Alex Hamilton, an analyst at EarlyBirdCapital, a boutique investment bank. Not everyone is worried that Murray's ultimatum - or House Speaker John Boehner's insistence that more spending cuts will be needed before the debt ceiling is raised again - are quite so inflexible. "Both sides will have to dial down tension ... as interest groups and market participants increase pressure for a path forward. ... Any politician who says they are willing to go over the ledge is likely bluffing to build leverage," said Sean West, director of U.S. policy at the Eurasia Group. West believes that if there's no sign of a deal near year's end, they would sign on to a short-term package to avert the cliff temporarily. That may be cold comfort, though, to those actually trying to run a business and hire people.

**America’s economy and fiscal discipline are worsening**

Blackden, 5/23 [Richard, 2012U.S. Business Editor, The Telegraph, “S economy risks falling back into recession because of 'fiscal cliff';

America will slump back into recession next year unless Congress prevents the economy falling off a "fiscal cliff", a US government agency has warned.” The world's biggest economy will shrink 1.3pc in the first half of 2013 if a mix of tax increases and spending cuts currently scheduled all come into force at the end of the year, the Congressional Budget Office (CBO) said. The CBO's warning is the loudest yet about a fiscal threat that is of increasing concern to Federal Reserve chairman Ben Bernanke as well as economists on Wall Street."Given the current state of the economy, immediate spending cuts or tax increases would represent an added drag on the weak economic expansion," said the CBO. At the moment, tax cuts first introduced by George W. Bush are set to expire at the end of the year, while more than $1 trillion (£637m) of spending cuts are also due to take effect in early January.Economists at Bank of America estimate that taken together, it will amount to a fiscal contraction of between 3.5pc and 4pc of US gross domestic product.The US finds itself in this predicament because Congress and President Barack Obama's administration have so far failed to strike an agreement on how to tackle the country's $15 trillion of debt without imperilling the recovery. While few expect Congress to allow the economy to fall off what Mr Bernanke has called a "fiscal cliff", there is concern that the uncertainty over the outcome will be enough to slow consumer and business spending in the second half of the year. The US economy expanded 0.6pc in the first quarter of the year.The CBO also estimated that if the tax cuts were extended and the spending cuts scrapped, the US would notch growth of 4.4pc in 2013. However, it warned that such a scenario would also risk a debt crisis.How America manages its own austerity is likely to move firmly onto the radar of investments and governments as November's presidential election draws closer.

#### Fiscal discipline low – payroll tax cuts

Daniel Indiviglio, Reuters Staff, 02/14/’12, [U.S. payroll tax fight shows faux fiscal restraint, <http://blogs.reuters.com/breakingviews/2012/02/14/u-s-payroll-tax-fight-shows-faux-fiscal-restraint/>] VN

The fight over U.S. payroll taxes just became exhibit A in political style over substance. Republicans in Congress, who have pounded the table on deficit reduction since last summer’s bruising debt battle, have backed down on a demand that spending be slashed to cover the cost of extending the tax cut. To let it ride for another 10 months will cost $100 billion. So much for fiscal discipline. It was bad enough when legislators leaned on seized mortgage backers Fannie Mae and Freddie Mac last December to enable 160 million American workers to keep paying a rate of 4.2 percent of their wages, instead of 6.2 percent, into the Social Security fund for a couple of extra months. Now, it’s about to get worse. Last year, when Republicans refused to raise the nation’s debt ceiling unless future deficits were shrunk, it led to a “super-committee” tasked with finding a way to lop off at least $1.2 trillion from future deficits. The group, predictably, failed. Instead, $1 trillion was automatically cut – a figure that dips to $900 billion if the payroll tax cut is extended. It’s easy to write this off as election-year politics, but that would neglect the deeper dogma at work. The GOP pledge not to raise taxes obviously trumps any rhetoric around the deficits that have been averaging $1.3 trillion for four years running. Of course, the Democrats aren’t acting any more responsibly. They’re happy to extend the payroll-tax cut without paying for it, too. And though willing to slash some spending elsewhere, Barack Obama’s party is still unwilling to tackle the real problem: safety-net programs. This was evidenced most recently by the president’s budget plan on Monday.

Fiscal Discipline Low

#### Fiscal discipline low

Geralyn Edward, Staff Writer on the Nation News, 02/23/’12, [Fiscal discipline key, says Volcker, <http://www.nationnews.com/articles/view/fiscal-discipline-key-says-volcker/>] VN

If there was one important piece of advice that eminent American economist Paul Volcker wanted to leave with Barbadians it was the need for fiscal discipline. He said countries had to become disciplined enough to avoid the “excesses” of spending too much, borrowing to build reserves. The respected former chairman of the United States Federal Reserve – the equivalent of the central bank – conceded that his country had not followed the advice that it often preached to other nations, and was now suffering the consequences. Speaking to a packed Frank Collymore Hall on Tuesday night, with the audience spilling into the foyer and also the Grande Salle, Volcker said: “In the United States, we don’t like to save very much. We spend a lot on consumer items produced in China. We bought a lot of stuff from China and we paid for it by selling them treasury bills, so they now have US$3 trillion and we have a lot of consumer goods that we have probably used up – and left ourselves with some very large debts.” During his 35-minute presentation, followed by an almost 45-minute question and answer session, Volcker said the same troubled road travelled by the United States had also been followed by Greece, Spain, Italy and Ireland. “It is a lack of discipline. It is very easy to borrow . . . and there were no restraints, so we all have big deficits and prudent finance has gone through the window,” said Volcker, the former chairman of President Barack Obama’s Economic Recovery Advisory Board.

#### The debt is unsustainable

Francisco Canseco, Rep. 23rd District of Texas, 07/28/’11, [Fiscal Discipline, <http://canseco.house.gov/Issues/Issue/?IssueID=56710>] VN

Simply put, our nation is on an unsustainable fiscal path. The federal government has run three consecutive $1 trillion-plus deficits, and our national debt now stands in excess of $15 trillion – which is more than $127,000 per American household. Under current projections of the federal budget, without reforms, by the end of the decade we will be spending almost $1 trillion to pay the interest on our nation’s debt ALONE, which is larger than the entire budget of the Department of Defense. In fact, our debt is almost as large as the entire U.S. economy, which is approximately $15 trillion. As a share of the economy – which measures the size of government compared to the economy – our budget has grown significantly over the past several years from its post-World War II average of 20% of GDP to almost 25%. As the Baby Boom generation retires, the federal budget is set to get even larger as programs as programs on auto-pilot, like Medicare and Social Security, will continue to grow until the federal budget has doubled from 20% to 40% within the next generation. A federal government at this size will result in a fundamentally different nation that the one we inherited from our parents and grandparents. However, under current projections, federal revenues are not expected to rise above their post-World War II average of approximately 18%. To sustain government at the size it’s projected to grow to, taxes will have to dramatically be increased or we will have to borrow the money. However, given the size of the gap between projected spending and projected revenues, borrowing at the levels that would be required simply isn’t realistic or sustainable. Therefore, massive tax increases would be the only realistic solution. According to the Congressional Budget Office, the revenue needed to sustain the current path of federal spending would require tax rates to more than double from where they are today. Such a tax burden would significantly reduce economic growth and leave American families with less money to spend on their priorities. We must cut spending and reduce our nation’s debt to put the federal budget back onto a sustainable path. Failure to do so will pose grave threats to our economic and national security. Our debt threatens our economic security because, as a share of the economy, our debt is almost as large as the entire $15 trillion U.S. economy, which is above the 90% debt to GDP ratio that economists have observed economic growth is reduced. Our debt threatens our national security, as nations that hold our debt – like China – could use their holdings to affect our decisions like the United States did with the British during the Suez Canal Crisis. In fact, former Chairman of the Joint Chiefs of Staff Admiral Mike Mullen said, “the biggest threat we have to our national security is our debt.”

### 2AC — Economy Low

Economy has gotten worse

AP 12 [Paul Wiseman, 7/24, “Global economy in worst shape since 2009”

http://www.google.com/hostednews/ap/article/ALeqM5iSpiI5aP4bDYB2tXJNVg5rDmOU1g?docId=6f1d7d6e48944cafb7b81d2b08ca46b3]

WASHINGTON (AP) — Mounting fears about Spain's financial health help illustrate why the global economy is in its worst shape since 2009. Six of the 17 countries that use the euro currency are in recession. The U.S. economy is struggling again. And the economic superstars of the developing world — China, India and Brazil — are in no position to come to the rescue. They're slowing, too. The lengthening shadow over the world's economy illustrates one of the consequences of globalization: There's nowhere to hide. Investors drove up Spain's borrowing rates Monday over concern that the government's debts might force it to seek a bailout. The interest rate on Spain's 10-year bond touched 7.56 percent — the highest since the euro began in 1999. Stocks around the world tumbled in response. Worries about Spain intensified after its central bank said the economy shrank 0.4 percent in the second quarter. The government predicts the economy will keep contracting next year as tax hikes and spending cuts hurt consumers and businesses. Italy has also been swept up by fears that it may need to request aid. Rates on Italy's government bonds jumped Monday, and stock prices sank. Economies around the world have never been so tightly linked — which means that as one region weakens, others do, too. That's why Europe's slowdown is hurting factories in China. And why those Chinese factories are buying less iron ore from Brazil. As a result of this global economic slowdown, the International Monetary Fund has reduced its forecast for world growth this year to 3.5 percent, the slowest since a 0.6 percent drop in 2009. Some economists predict the global economy will grow a full percentage point less. For now, few foresee another global recession. Central banks in China, Britain, Brazil, South Korea and Europe have cut interest rates in the past month to try to jolt growth. European leaders have begun to focus more on promoting growth, not just shrinking debt and cutting budgets. The Chinese government, in particular, is expected to do what it takes to protect its economy from deteriorating too quickly. And despite their slowdowns, China and India are still growing at rates America and Europe can only imagine. But many economists say European policymakers aren't moving fast enough to strengthen European banks and ease borrowing costs for Italy and Spain. They fear the global impact if Europe's economy deteriorates further. Stock prices in the United States and elsewhere are fluctuating almost daily depending on the outlook for a resolution of Europe's debt crisis. Around the world, sales at companies ranging from automakers to technology companies are falling. Advanced Micro Devices, a California-based maker of computer chips used in everything from slot machines to smart cameras, says revenue likely dropped 11 percent in the second quarter because of weaker-than-expected sales in China and Europe. At Jagemann Stamping Co. in Manitowoc, Wis., sales to Europe have dropped more than 10 percent from a year ago. The company makes metal parts for auto companies and other customers. It's still enjoying strong sales in the United States, so it hasn't had to cut workers because of falling business in Germany and the Czech Republic. "What it does is slow our new hiring," says company president Ralph Hardt. One growing concern about the global economy is there's little margin for error: Unemployment is already at recession levels in Europe and the United States. The United States, by far the world's biggest economy, has long pulled the global economy out of slumps. Now it needs help. Three years after the Great Recession officially ended, the American economy can't maintain momentum. For the third straight year, growth has stalled at mid-year after getting off to a promising start. Unemployment stood at 8.2 percent in June — the 41st straight month it's been above 8 percent. Americans spent less at retail businesses for a third straight month in June, the longest losing streak since the recession. Economists are downgrading their estimates of economic growth in the April-June quarter. When the government releases its first estimate on Friday, many think it won't even match the first quarter's sluggish 1.9 percent annual pace. The global slowdown is squeezing U.S. exports, which have accounted for an unusually large 43 percent share of U.S. growth since the recession officially ended in June 2009. Consumer confidence has fallen four straight months in the face of scant hiring and weak economic growth. U.S. companies are nervous about the threat of tax increases and spending cuts that are scheduled to kick in at year's end unless Congress breaks a deadlock. The IMF has warned of a spillover to the rest of the world if the U.S. economy falls off the so-called fiscal cliff. Europe's obstacles are even more severe. It's faced with crushing government debts, struggling banks and scant economic growth. Unemployment in the 17 countries that use the euro is 11 percent, the highest since the euro was adopted in 1999. Greece, Portugal, Italy and Spain are in recessions. Germany and France are faring better, but both are likely to grow more slowly this year than America. French retail giant Carrefour SA — the Wal-Mart of Europe — says its sales fell in the second quarter amid a slowdown in its core markets in Europe. Italy's Fiat lost nearly $260 million in Europe the first three months of the year. French carmaker PSA Peugeot-Citroen plans to slash 8,000 jobs in France and close a major factory. Europe's banks are stuck with bad real estate loans and shaky European government bonds. The European Central Bank has made massive amounts of money available to Europe's banks at cheap rates to try to revive lending. But borrowing by many businesses and consumers remains weak because they are uncertain about future income. Many fear that Greece and perhaps other countries will default on their debts and have to abandon the euro currency, which could ignite financial chaos across Europe. A summit of European leaders last month produced some agreements that helped calm markets for a few days. But optimism faded as investors recognized that governments are still saddled with big debts and banks with bad loans. And that Europe itself still faces the threat that growth will stall and the euro currency alliance will collapse. The European Commission predicts the 17-country eurozone economy will shrink 0.3 percent this year. Many economists fear it could be worse. Capital Economics says a recent drop in eurozone business confidence is consistent with a 1 percent decline in economic output. In the latest wallop to the global economy, China said last week that its economic growth fell to a three-year low. The world's second-largest economy grew 7.6 percent in the April-June quarter compared with the same quarter last year. That was the slowest growth since early 2009. Countries like China need fast growth to serve growing populations and millions of people leaving farms to seek work in cities. Chinese growth has decelerated for eight straight quarters. That's the longest slowdown in records dating to 1992, according to Yu Bin, a government researcher. The slowdown is partly deliberate. In 2010 and 2011, Chinese officials raised interest rates and took other steps to tame inflation and cool an overheated real estate market. "Mission accomplished," says Cameron Peacock, a market analyst at Australia's IG Markets. "China now has the room to re-stimulate its economy." But China is also feeling Europe's economic squeeze. Chinese exports to Italy dropped 24 percent in June from a year earlier. Exports to France fell 5 percent, those to Germany nearly 4 percent. Europe buys about 17 percent of China's exports. The impact of weak European demand for Chinese-made furniture, shoes, toys and other goods has fallen hardest on export-oriented manufacturers along China's southeastern coast. Some companies have closed. Others are cutting staff. China is the biggest trading partner of Brazil, which has the world's eighth-biggest economy. Brazil is likely to grow only 1.8 percent in 2012, according to Sao Paulo Federation of Industries. China's slowdown has reduced demand for Brazilian soy and iron ore. Brazilian manufacturers, such as aircraft maker Embraer, are hurting as Europe reduces its demand for manufactured goods. A relatively strong currency isn't helping. It makes Brazilian products more expensive to foreign buyers. Brazil also has a U.S.-style problem with consumer debt: Since 2003, about 40 million Brazilians have entered the middle class and brought a strong appetite for consumption. Brazilian leaders credited those consumers with invigorating the economy in recent years and helping protect it from external shocks. But most of the buying has been on credit. And those bills are adding up. In a report last week, London-based Capital Economics estimated that debt payments now eat up 20 percent of household income in Brazil. "The current pace of credit growth in Brazil remains unsustainable — and the longer it continues, the bigger the risk of a messy ending further down the line," Capital Economics warned. Similarly, the outlook has dimmed for India, the world's fourth-biggest economy. Its growth slowed to a 5.3 percent annual rate in the first three months of 2012, the slowest rate in nine years. Over the past two decades, India has emerged as a powerhouse in services — writing software, running call centers, making movies, drafting engineering plans. In a report last month, Andrew Kenningham, senior global economist at Capital Economics, said India's troubles are mostly self-inflicted. "Weak governance, although not new, is the most plausible explanation for the slowdown," he wrote. The government has reneged on promises to make it easier for foreigners to invest in India. It has taxed Indian firms that acquire companies overseas. Indian factories have cut production. And the pay of many Indians has been diminished by inflation, which has averaged more than 9 percent a year for the past two years. The slowdown in the developing world could make it harder for the economies of Europe and the United States to climb out of their ruts. And the weaker the rich countries get, the harder it will be for developing economies to regain their old fast pace. "In today's interconnected world, we can no longer afford to look only at what goes on within our national borders," IMF Managing Director Christine Lagarde said earlier this month. "This crisis does not recognize borders. This crisis is knocking at all our doors."

**US economy weak now – unemployment proves**

Fox 7/18/12 (“US economy adds 80,000 jobs in another weak month” http://www.foxnews.com/us/2012/07/06/us-employers-add-80000-jobs-as-economy-struggles/ )

WASHINGTON – The American job machine has jammed. Again. The economy added only 80,000 jobs in June, the government said Friday, erasing any doubt that the United States is in a summer slump for the third year in a row. "Let's just agree: This number stinks," said Dan Greenhaus, chief global strategist at the investment firm BTIG. It was the third consecutive month of weak job growth. From April through June, the economy produced an average of just 75,000 jobs a month, the weakest three months since August through October 2010. The unemployment rate stayed at 8.2 percent — a recession-level figure, even though the Great Recession has technically been over for three years. The numbers could hurt President Barack Obama's odds for re-election. Mitt Romney, the presumed Republican nominee, said they showed that Obama, in three and a half years on the job, had not "gotten America working again." "And the president is going to have to stand up and take responsibility for it," Romney said in Wolfeboro, N.H. "This kick in the gut has got to end." Obama, on a two-day bus tour through the contested states of Ohio and Pennsylvania, focused on private companies, which added 84,000 jobs in June, and took a longer view of the economic recovery. "Businesses have created 4.4 million new jobs over the past 28 months, including 500,000 new manufacturing jobs," the president said. "That's a step in the right direction." The Labor Department's report on job creation and unemployment is the most closely watched monthly indicator of the U.S. economy. There are four reports remaining before Election Day, including one on Friday, Nov. 2, four days before Americans vote. No president since World War II has faced re-election with unemployment over 8 percent. It was 7.8 percent when Gerald Ford lost to Jimmy Carter in 1976. Ronald Reagan faced 7.2 percent unemployment in 1984 and trounced Walter Mondale. Patrick Sims, director of research at the consulting firm Hamilton Place Strategies, said that "time has run out" for unemployment to fall below 8 percent by Election Day. That would require an average of about 220,000 jobs a month from July through October — more like the economy's performance from January through March, when it averaged 226,000 per month. Few economic analysts expect anything close to that. "The labor market is treading water," said Heidi Shierholz, an economist at the Economic Policy Institute. She called it an "ongoing, severe crisis for the American work force." The Labor Department report put investors in a sour mood. The Dow Jones industrial average dropped 124 points. Industrial and materials companies, which depend on economic growth, were among the stocks that fell the most. The price of oil fell $2.77 per barrel to $84.45. Money flowed instead into U.S. Treasurys, which investors perceive as safer than stocks when the economy is weakening. The yield on the benchmark 10-year U.S. Treasury note fell to 1.54 percent, from 1.59 percent on Thursday. Investors were already worried about a debt crisis that has gripped Europe for almost three years and recent signals that the powerhouse economy of China is slowing. Earlier this week, the European Central Bank and the central bank of China cut interest rates in hopes of encouraging people and businesses to borrow and spend money. For American investors, however, the jobs report fell into an uncomfortable middle ground. Federal Reserve Chairman Ben Bernanke promised last month that the Federal Reserve would take additional steps to help the economy "if we're not seeing a sustained improvement in the labor market." But some financial analysts said that the Labor Department report, while disappointing, was not weak enough to lock in further action by the Fed at its next meeting July 31 and Aug. 1. The slowdown in job growth has been stark. From December through February, the economy produced an average of 252,000 jobs a month, twice what is needed to keep up with population growth. But the jobs generator started sputtering in March, when job growth slowed to 143,000. At first, economists blamed the weather for warping the numbers. An unusually warm winter allowed construction companies and other employers to hire earlier in the year than usual, effectively stealing jobs from the spring, they said. But weird weather could only explain so much, and the bad news kept coming: The economy added just 68,000 jobs in April and 77,000 in May. Those figures reflect revisions from earlier estimates of 77,000 for April and 69,000 for May. June's dud of a number made it clear that the economy has fallen into the same pattern it followed in 2010 and 2011: It gets off to a relatively fast start, then fades at midyear. Offering some hope, the slowdowns the two previous years lasted just four months each. From June through September 2010, the economy lost an average of 75,000 jobs per month. From May through August 2011, the economy added an average of 80,000 per month. Both years, hiring picked up significantly when the weak stretches ended. To be sure, the United States is still suffering the hangover of a financial crisis and the worst recession since the 1930s. The economy lost 8.8 million jobs during and after the recession. It has regained 3.8 million. The economy isn't growing fast enough to create jobs at a healthy clip. That is primarily because three traditional pistons of the economic engine aren't firing the way they normally do: — Consumer spending since the recession has been weaker than in any other post-World War II recovery, partly because wage increases have been small. In such a weak job market, employers don't need to give big raises. And households are trying to pay off the debt they ran up in the mid-2000s. — Housing has been a dead weight on the economy for six years. Home-building usually powers economic recoveries, but construction spending is barely half what economists consider healthy. — Government, which usually picks up the slack in the job market when the economy is weak, isn't helping this time. Counting federal, state and local jobs, governments have cut 637,000 jobs since 2008. They have cut 49,000 the last three months. In the first three months of this year, it appeared state and local government job losses were coming to an end. "That turned out to be a temporary halt," said Stuart Hoffman, chief economist at PNC Financial. "Apparently, there's no end in sight." The figure of 80,000 jobs came from a Labor Department survey of businesses and government agencies. Another survey, of American households, looks better. It shows the number of employed Americans rose by 381,000 the past three months — 127,000 a month. The household survey can catch the self-employed and those working for very small businesses, who can be missed by the bigger business survey. But over time the two surveys usually tell the same story. The unemployment rate last month was unchanged from May. But a broader measure of weakness in the labor market, the so-called underemployment rate, deteriorated for the second straight month. In June, 14.9 percent of Americans either were unemployed, had been forced to settle for part-time employment, or had given up looking for work and were not counted as unemployed. The rate was 14.8 percent in May and 14.5 percent in April. The Labor Department report left economists grasping for good news. Average hourly pay rose 6 cents in June, the biggest monthly gain in nearly a year. The average workweek grew slightly, the first gain in four months. The extra hours and higher wages put more money in consumers' pockets. And companies hired 25,000 temporary workers, usually a sign that they will hire full-time workers soon. "That we latch on to these modest positives speaks to the bias of low expectations," Greenhaus said. Meantime, 12.7 million Americans remain officially unemployed. When Deborah Masse, 49, lost a job in 2007, she had a job offer within six weeks. This time has been different. Since being laid off in October 2011, she has sent thousands of resumes and had several phone interviews but received no offers. Masse, who lives in Stanton, Mich., with her husband and mother, has tried to make use of her free time. She has exercised more, learned some French and Spanish, and brushed up on her technology skills. "If nothing else," she said, "I will end up on Social Security, more fit, more intelligent and worldly — and broke."

#### US economy weak now – CFS reports conclude

WSJ 7/18/12 (MarketWatch “CFS June Money Supply Data; Weak Economy And Flight To Safe Haven Assets” <http://www.marketwatch.com/story/cfs-june-money-supply-data-weak-economy-and-flight-to-safe-haven-assets-2012-07-18> )

NEW YORK, July 18, 2012 /PRNewswire via COMTEX/ -- Today, the Center for Financial Stability (CFS) releases the most current and broadest measure of the money supply available for the US. CFS proprietary money supply data provide a crucial barometer to measure Fed actions, the **economy, and financial system in real time**. The most recent data for June 2012 illustrate that the US economy is extremely weak. **CFS Divisia M4 (DM4) growth registered 2.3% on a year-over-year basis in June 2012 - well below the 6% to 6.5**% typically associated with trend growth (see Figure 1). According to CFS President Lawrence Goodman, "CFS monetary data foreshadow a subpar expansion in coming months." "A flight to insured deposits highlights that investors and the public are flocking to safe haven assets," Goodman added. Commercial banks' savings deposits and demand deposits were the largest contributors to monetary growth in June. Similarly, the monetary base contracted for the first time since December 2010, highlighting recent pressures on risky assets as well as policy (see Figure 1). CFS Divisia monetary measures were developed under the direction of Professor William A. Barnett - one of the world's leading experts on monetary and financial aggregation theory. CFS money supply data are essential, especially since the Federal Reserve ceased production of M3 in 2006. Similarly, Divisia measures are superior, as they accurately weight various classifications of money from cash to leverage in the shadow banking system."Leading up to the financial crisis, private economic agents, including Wall Street participants, did not have adequate data to make well informed decisions and as a result took excessive risks without recognition of the potential consequences," according to Barnett, CFS Director of Advances in Monetary and Financial Measurement. Barnett adds **that** "CFS produces information we hope will be helpful in the future for market participants and public officials to assess risk more accurately." CFS provides the data on-line free of charge to promote and encourage deeper scrutiny of money and banking statistics.

**Lack of job growth and commercial sales leaves the US economy weak**

Allen (News Reporter for CNBC) 7/17/12 (Patrick “The US goes from “Hero to Zero”” <http://www.cnbc.com/id/48205608> )

Monday’s weak US retail sales showed that the world’s biggest economy is slowing very quickly, leading one economist to claim America has gone from “first half hero to second quarter zero.” John Foxx | Stockbyte | Getty Images The 0.5 percent fall for June was far worse than expected and the third monthly drop, the longest run of falling sales since 2008 when the Lehman crisis led America into recession. “Given how rapid the slowdown in job growth has been, it is hard to blame consumers for their increased caution,” said Capital Economics chief U.S. economist Paul Ashworth. Arguing that the data showed just how quickly the U.S. recovery has gone “from first-quarter hero to second-quarter zero.” Ashworth believes the slowdown echoes what we saw in the second quarter of 2010. That slowdown ultimately led the Federal Reserve to launch a second round of quantitative easing later that year, but Ashworth believes Federal Reserve Chairman Ben Bernanke will need more evidence before pulling the trigger on another round of easing. “The bar to QE3 is higher than for QE2, if only because there is considerable skepticism that balance sheet expansion will accomplish much,” said Ashworth. Others agree that the data is not surprising given the weak jobs data. “This softness coincides with a slower momentum in payrolls in recent months which has dampened growth in labor income,” said Dr Christoph Balz, a senior economist at Commerzbank in a research note. RELATED LINKS What the Surprise Retail Sales Drop Is Telling MarketsFewer US Companies Planning to Hire; Europe Looms‘Fiscal Cliff’ Could Trigger US Recession: IMF Economist Balz believes the data is even more sobering given the steep fall in gasoline prices, something which should have put more money in consumer’s pockets over recent months. In “the second quarter as a whole, consumers probably spent just 1.0 percent more than in the first quarter, a sharp slowdown from the 2.5 percent expansion in the previous quarter,” said Balz, who notes that with consumption making up 70 percent of U.S. GDP, second quarter growth data is likely to be very weak. Others believe the weak retail data could prove a tipping point for the Fed. “For all the concern about the recovery stalling at this time last year, underlying retail sales growth actually held up quite well,” said Steven Englander, the global head of G10 FX strategy at CitiFX on Monday. “While we would normally caution against reading too much into any single data release, June's retail sales may be the one that proves to be the tipping point that persuades the Fed to launch a third round of quantitative easing” said Englander.

Economy Low

**Stocks low – hurts overall economy**

Hwang (Reporter for Bloomberg News) 7/16/12 (Inyoung, “U.S Stocks Fall As Economy Concern Offsets Energy Gains” <http://www.businessweek.com/news/2012-07-16/u-dot-s-dot-stock-futures-slip-after-weekly-rally-goldman-falls>)

U.S. stocks fell, dragging the Standard & Poor’s 500 Index lower for the seventh time in eight days, after the International Monetary Fund cut its global economic forecast and retail sales unexpectedly dropped. JPMorgan Chase & Co. (JPM) (JPM) lost 2.7 percent while Home Depot Inc. and Caterpillar Inc. (CAT) (CAT) dropped more than 1 percent to lead the Dow Jones Industrial Average lower. Equities pared losses as energy companies rose with the price of oil while Visa (V) (V) Inc. and MasterCard (MA) (MA) Inc., the world’s biggest payment networks, gained at least 1.7 percent after agreeing to a settlement of at least $6.05 billion in a price-fixing case. The S&P 500 declined 0.2 percent to 1,353.64 at 4 p.m. New York time after earlier retreating as much as 0.6 percent. The Dow slipped 49.88 points, or 0.4 percent, to 12,727.21 today. “The retail sales gives you another indicator that uncertainty has showed up in the consumer side,” James Dunigan, who helps oversee $112 billion as chief investment officer in Philadelphia for PNC Wealth Management, said in a telephone interview. “We’re in a bit of the summer doldrums.” The S&P 500 is down 4.6 percent from a four-year high in April as economic data trails forecasts and investors brace for what is projected to be the first decrease in quarterly earnings since 2009. The Citigroup Economic Surprise Index for the U.S., which measures how much data from the past three months is beating or missing the median estimates in Bloomberg surveys, is at minus 64, near the almost 11-month low of minus 64.9 reached last week. Retail Sales U.S. retail sales dropped 0.5 percent in June, following a 0.2 percent decrease in May, Commerce Department figures showed today. The decline was worse than the most-pessimistic forecast in a Bloomberg News survey in which the median projection called for 0.2 percent rise. The IMF cut its 2013 global growth forecast as Europe’s debt crisis prolongs Spain’s recession and slows expansions in emerging markets. Growth worldwide will be 3.9 percent next year, less than the 4.1 percent estimate in April, the fund predicted in an update of its World Economic Outlook. Manufacturing in the New York region expanded in July at a faster pace than anticipated, signaling factories will keep contributing to growth. The Federal Reserve Bank of New York’s general economic index rose to 7.4 from 2.3 in June. The median forecast of 51 economists surveyed by Bloomberg News called for an increase to 4.0. Readings greater than zero signal expansion in the so-called Empire State Index that covers New York, northern New Jersey and southern Connecticut. Earnings Season Earnings beat estimates at 21 of the 32 companies in the S&P 500 that have reported quarterly results so far, data compiled by Bloomberg show. Profits probably decreased 2.1 percent in the second quarter, the first drop in almost three years, according to a Bloomberg survey of analysts. JPMorgan Chase, the largest U.S. bank by assets, fell 2.7 percent to $35.09 after rallying 6 percent on July 13 as Chief Executive Officer Jamie Dimon predicted the company will still post record earnings this year despite a $4.4 billion trading loss in the second quarter. The bank’s assertion that traders at its London chief investment office may have intentionally mismarked trades, masking losses that total at least $5.8 billion, makes little sense, according to former executives with direct knowledge of the unit’s operation. Home Depot, the nation’s largest home-improvement retailer, slumped 1.2 percent to $51.45. Caterpillar, the world’s biggest maker of construction equipment, declined 1.1 percent to $81.15. General Electric Co. lost 0.9 percent to $19.59, helping send industrial shares down 0.6 percent as a group for the biggest drop among 10 industries in the S&P 500. Morgan Stanley reduced its recommendation on the world’s biggest maker of jet engines, power generation equipment and locomotives to equalweight from overweight, citing the stock’s higher valuation relative to peers with or without GE Capital Corp. Coal Stocks Alpha Natural Resources Inc. (ANR) (ANR) declined 10 percent to $6.85 as Bank of Montreal cut its rating to underperform from outperform, citing potential financing issues. Arch Coal Inc. (ACI) (ACI), the fourth-largest U.S. producer of the fuel, sank 3.9 percent to $5.90 after BMO cut the stock to underperform from market perform. Energy stocks added 0.3 percent after earlier falling as much as 0.8 percent as the price of crude oil reversed earlier declines to rise 1.5 percent to $88.43 a barrel. Chevron Corp., the second-largest U.S. energy company, climbed 0.7 percent to $106.78. Denbury Resources Inc., the oil and natural-gas producer, rallied 3.8 percent to $14.77. MasterCard advanced 1.7 percent to $436.89 and Visa rose 2.5 percent to $127.15 after they agreed to settle a price- fixing case brought by retailers over credit-card swipe fees. Citigroup, Gannett Citigroup Inc. (C) (C), the third-biggest U.S. bank, advanced 0.6 percent to $26.81 after reporting second-quarter profit that beat analysts’ estimates on revenue from advising on mergers and underwriting stocks and bonds. Net income declined to $2.95 billion, or 95 cents a share, from $3.34 billion, or $1.09, a year earlier. Excluding accounting adjustments and a loss from the sale of a stake in a Turkish bank, earnings were $1 a share, compared with the average estimate of 89 cents in a Bloomberg survey of 18 analysts. Gannett Co., the owner of 82 daily newspapers including USA Today, rallied 2.7 percent to $14.69. The company reported second-quarter profit that topped analysts’ estimates, bolstered by growing Internet revenue. Excluding some items, profit was 56 cents a share in the period, beating the 53-cent average estimate by analysts, according to data compiled by Bloomberg.

Economy Low

#### Fiscal Cliff and small retail sales have the US economy in a slump

HAI7/17/12 (Helicopter Association International “ Sequestration, U.S. Economy, and the Financial Outlook” <http://rotor.com/Publications/RotorNewssupregsup/tabid/177/newsid1237/76054/mid/1237/Default.aspx> )

Chairman of the U.S. Federal Reserve, Benjamin Bernanke, warned of dire risks surrounding the approaching fiscal cliff in testimony before the Senate Banking Committee on July 17. The Fed chief put lawmakers on notice that a failure to resolve differences over taxes and spending by the end of the year could pose grave harm to an already weak U.S. economy. Meanwhile, U.S. Senator Kelly Ayotte (R-N.H.) held a press conference July 17 with the Aerospace Industries Association (AIA) warning of potential job losses related to the scheduled budget sequestration early next year. After stonewalling Republican demands on the defense sequester all year, the White House finally has agreed to send its budget director to Capitol Hill to discuss which programs would be cut. Director of the Office of Management and Budget, Jeffrey Zients, and Deputy Defense Secretary Ash Carter will face a grilling before the House of Representatives Armed Services Committee over why the administration is not doing more to plan for the looming $600 billion spending cuts. Conservatives want to force the Pentagon to the table so that Congress can make their case for exactly how much lead time the Department of Defense (DOD) really needs to meet the requirement. The movie by the White House could set up a whole new narrative going into the November elections. Meanwhile, retail sales fell for the third straight month in June, the longest stretch of declines since the 2008 recession, and another indicator that points to a decelerating recovery. The report surprised economists, who have revised down projections.

#### **Recent data confirms a weak US economy**

WSJ 7/16/12 (MarketWatch “U.S. growth forecasts slashed after weak data” <http://articles.marketwatch.com/2012-07-16/economy/32692688_1_fiscal-cliff-growth-forecasts-second-quarter-gdp-growth>)

WASHINGTON (MarketWatch) — The more data that gets released, the gloomier economists have become on growth for the second quarter. After the reports on retail sales and business inventories released Monday, a MarketWatch-compiled economist poll for second-quarter GDP growth is down to 1.3%, down from 1.5% on Friday, 2% a month ago, and as high as 2.6% six months ago. The gloomiest new forecast came from Stephen Stanley of Pierpont Securities, who now sees just 0.6% growth in the April-to-June quarter, and only 1.25% in the current September-ending quarter. “The economy has downshifted from muddling to near-stagnation,” said Stanley, who called the report showing retail sales sliding 0.5% in June “awful.” He does see two big implications from the ever-deteriorating economy. The first is that the Federal Reserve, which Stanley calls “hyperactive,” is likely to attempt to ride to the rescue. Federal Reserve Chairman Ben Bernanke is due to speak to the Senate Tuesday and the House of Representatives on Wednesday, but many see the annual Jackson Hole, Wyo. conference held by the Kansas City Fed at the end of August as the most likely venue for the chief to announce a third round of quantitative easing.Read Bernanke preview. The second implication, Stanley says, is that there is a “low” but increasing chance that Congress and the president could try to reach a deal to avoid the so-called fiscal cliff before the election. The fiscal cliff is the name given to the series of tax hikes and spending cuts that will be triggered at the beginning of 2013 unless legislative action is taken.

### 2AC — Competitiveness Low

US competitiveness is decreasing because of delay on infrastructure projects

Crossley 11

Infrastructure report, US not globally competitive From ULI, Ernst & Young David Crossley, May 17, 11. <http://www.houstontomorrow.org/livability/story/report-us-not-globally-competitive-for-infrastructure/>

In contrast with its global competition, the United States is lurching along a problematic course—potentially losing additional ground in terms of essential infrastructure development, according to a new report from the Urban Land Institute and Ernst & Young. Among other things, Infrastructure 2011: Strategic Priorities says: After more than 30 years of conspicuously underfunding infrastructure and faced with large budget deficits, increasing numbers of national and local leaders have come to recognize and discuss how to deal with evident problems. But a politically fractured government has mustered little appetite to confront the daunting challenges, which include finding an estimated $2 trillion just to rebuild deteriorating networks. Operating beyond their planned life cycles, these systems include roads, bridges, water lines, sewage treatment plants, and dams serving the nation’s primary economic centers. Although President Obama ranks infrastructure as one of his administration’s top three “win the future” initiatives (together with education and innovation), the chances for setting and executing national priorities appear to be foundering in partisan debate over tax burdens and how to cut exploding government debt. Plans for transformational networks—regional high-speed passenger rail, a new electric grid tied to energy-saving technologies, and state-of-the-art satellite air traffic control systems to replace obsolete radar stations—will probably get delayed, pared back, or shelved. Despite the nation’s unemployment woes, the vast job-creation potential of infrastructure projects is being sidetracked by concerns about government spending appetites and potential cost overruns. Related benefits from reducing carbon footprints—energy efficiencies and greater independence from problematic foreign energy sources—are also failing to gain much traction. The overriding stumbling block to generating support for rebuilding the country’s infrastructure remains simple public resistance to paying more for these systems—either through higher taxes or user fees. Although informed voters have passed bond issues and even some sales tax increases for new projects, Congress perennially refuses to raise the federal gasoline tax or allow states to put new tolls on interstate highways, which could help ramp up funding for mass transit alternatives and repair existing highways and bridges.

### AC — Downgrade Now

#### **Downgrade coming – can’t address debt**

The Hill 12 (Geneva Sands, the Hill, “Sen. Coburn: 'No doubt' US credit rating will be downgraded again,” 5/23/12, <http://thehill.com/video/senate/229105-coburn-no-doubt-us-credit-will-be-downgraded-again->)hhs-ps

The United States suffered the [first downgrade](http://thehill.com/blogs/on-the-money/801-economy/175735-sap-downgrades-us-credit-rating) to its credit rating in history when Standard & Poor's reduced the nation's rating from AAA to AA+ last August. "We should see another downgrade, because we have not done the structural things that will fix our country," he added. The battle over last summer's debt crisis was reignited when House Speaker John Boehner (R-Ohio) vowed earlier this month that the House would only raise the federal government’s $16.4 trillion debt ceiling if Democrats agree to further spending cuts and entitlement reforms. When asked if he agreed with Boehner's decision to push forward the tumultuous debt-ceiling debate, Coburn said, "I think that's exactly what our founders had in mind." He argued that the credit rating wasn't downgraded because of deadlock in Congress, but rather because the biggest cost drivers of U.S. debt were not addressed. Coburn, who was a member of President Obama's fiscal commission, called for changes to Medicare and Social Security, saying in order to stem the mounting U.S. debt, earnings limitations and age requirements will have to be reformed. "Those are all things people don't want to hear, but it's going to happen, because if we don't do it, the people who are loaning us the money are going to make us do it," he said. The GOP senator predicted that if nothing is done to reduce the federal debt, in two to five years the United States will face the same economic problems as Greece.

Downgrade Now

#### Downgrade coming – European issues

Credit Visionary 12 (Credit Visionary, “Moody s Should Downgrade Congress,” June 27, 2012, lexis)hhs-ps

Last summer, August 5 to be exact, Standard & Poor s dropped the rating of United States debt below AAA for the first time in history. This year, with our flippers and masks barely out of the pool equipment room, Moody s downgraded the ratings of fifteen mega banks, including major American institutions such as Goldman Sachs and J.P. Morgan Chase. Bank of America and [Citigroup](http://www.lexisnexis.com.ezproxy.baylor.edu/lnacui2api/search/XMLCrossLinkSearch.do?bct=A&risb=21_T15160866208&returnToId=20_T15160870405&csi=299488&A=0.9253127073541416&sourceCSI=3652&indexTerm=%23CC0002275%23&searchTerm=Citigroup%20&indexType=C) were downgraded to Baa2, just two ticks above junk status. Last year, S&P cited as one of the major reasons for its historic downgrade the Bedtime for Bonzo antics that went on in Congress in connection with, among other things, the once perfunctory act of raising the national debt limit. If you were otherwise engaged and missed the circus, don t worry, it will be coming back to town near election time this year. This year, Moody s did not have to make reference to our political paralysis (yet), they simply underscored our globalized exposure to the financial chaos in the Eurozone, describing its actions as follows: Moody s downgrades firms with global capital markets operations; which, among other things was a not-so-subtle reference to the recent revelation that J.P. Morgan Chase had casually dropped another $2-3 billion in a whaling adventure that went awry, a fact that produced a flurry of congressional posturing filled with sound and fury that seemed to signify very little. Meanwhile a host of Washington conservatives are continuing their efforts to undermine Dodd-Frank by introducing a series of nine bills in the House and the Senate and launching litigation (with a willing co-conspirator a bank in Texas) against the Consumer Financial Protection Bureau and select provisions of the law. Looking at these two downgrades, both of which were telegraphed well in advance by the rating agencies, I suppose one can t blame Washington for everything .. Scratch that yeah, we pretty much can. The S&P downgrade was a direct response to Congressional debt devilry, while the Moody sdowngrade was considered by many to be an unspoken but pointed commentary on both globalization and the dismal performance of federal regulation of the banking industry as a whole. There are those who argue that that the banking industry is overregulated while others opine that it is under-regulated. However, it s very difficult to argue that given the history of financial events in the last few years, the banking industry is effectively regulated. This month Gallup found that 17% of Americans approved of the way Congress was handling things. A low number, indeed, but it still feels wildly optimistic. I recently read Why Nations Fail by Daron Acemoglu and James A. Robinson. The authors are Harvard professors and widely respected scholars on the subject of economic development. They argue that relative prosperity among nations is largely dependent on the nature of the institutions that have developed in a given society. Those Institutions can be either inclusive prioritizing things like productivity, justice, education and technology for the benefit of the nation as a whole; or extractive intent upon directing wealth and resources away from some elements of society to benefit others. Although the authors were focused on analyzing the developing world, it struck me that our economy in general and this Congress in particular has become increasingly extractive. Income disparity in theUnited States has been rising steadily, and in the last few years, dramatically. Steadfast refusals to raise taxes even on the willing Warren Buffets of this country can only exacerbate the problem. Attacks on Medicare, Social Security, and other programs designed to benefit the poor, the middle-class and the elderly are one way to increase the relative status of the haves. Voter suppression initiatives and anti-union measures are supported in Congress even though many of these efforts are occurring in newly extractive state legislatures (Wisconsin, Michigan and Ohio to name a few). Finally, the Citizens United decision, which essentially put a for-sale sign on every American election, is likely to ensure that the next Congress will be even less inclusive than this one. To top it all off, the Washington Post recently reported that during the ugliest days of the of the financial crisis, 34 members of Congress on both sides of the aisle had reworked their own financial portfolios after having interacted with Hank Paulson, Ben Bernanke, or Timothy Geithner. As you might imagine, those legislators managed to catch an earlier flight to safety than most of us. It would be hard to imagine anything more extractive than that, wouldn t it? Despite these individual acts of self-interest, it has been Congress collective failing that is most notable. Dodd-Frank is a vast and essentially earnest attempt to reign in a financial system run amok, but in a number of respects it has been sufficiently watered down to leave many of the banking system s most serious systematic vulnerabilities intact. Congress total inability to effectively regulate our financial system puts all of us at risk. The downgrades in the credit ratings of those major banks mean very little to the average consumer, but the downgrade in the credibility of Congress and the mess we have made of our financial regulatory structure that at least in part fomented the ratings agencies analyses should give us all pause. This is not an easy fix to be sure. Our economy has become so complex many would argue that it can t be effectively regulated. Let s hope they re wrong and that our representatives will have an epiphany that lifts them from the tar pit of partisanship, election year or not, and makes them leaders, not slaves to ideology or Grover Norquist inspired oaths. They must screw up the courage to get this thing right. If they fail, once again, the consequences are far worse than winning or losing an election. Because if we don t fix this problem how shall I put this delicately? we re screwed.

Downgrade Now

#### Downgrade with happen anyway – Europe, debt

Reuters, 07/10/’12, [Fitch affirms U.S. AAA credit rating, outlook still negative, <http://articles.chicagotribune.com/2012-07-10/business/sns-rt-us-usa-rating-fitchbre8691d5-20120710_1_credit-rating-credit-outlook-negative-outlook>] VN

NEW YORK (Reuters) - Fitch Ratings on Tuesday affirmed its AAA credit rating on the United States and maintained a negative outlook, citing a diversified and wealthy economy that is undermined by the government's inability to agree on deficit reduction measures. "The uncertainty over tax and spending policies associated with the so-called 'fiscal cliff' weighs on the near-term economic outlook," Fitch said in a statement. A negative outlook gives Fitch 12 to 18 months by which it is expected to make a decision on the U.S. sovereign credit, pushing a decision well beyond the next presidential and congressional election cycle. "Absent material adverse shocks, Fitch does not expect to resolve the Negative Outlook until late 2013," Fitch said. Nearly a year ago, rival credit rating agency Standard & Poor's made an historic cut to the U.S. rating, dropping it by one notch to AA-plus. Moody's Investors Service holds the U.S. rating at AAA. All three agencies have negative outlooks with decisions by S&P and Moody's not expected until at least 2013. Additional risks to the U.S. credit outlook, Fitch said, **emanate from the uncertain U.S. fiscal policy as well as Europe's debt crisis and recession.** It also highlighted the diminished capacity of U.S. fiscal and monetary stimulus, referring to the near zero interest rate policy instituted by the U.S. Federal Reserve that is expected to remain in place through late 2014

### Stimulus True

#### **We control empirics – WWII proved Keynes right**

Brad Delong, professor of Economics and chair of the Political Economy major at the University of California, Berkeley. He served as Deputy Assistant Secretary of the United States Department of the Treasury in the Clinton Administration , research associate of the National Bureau of Economic Research, o-editor of The Economists' Voice, 2-09 <http://delong.typepad.com/sdj/2009/02/a-guide-for-the-perplexed-justin-fox-on-fiscal-policy.html>

Justin Fox is needlessly worried. He writes: The uncertainty of stimulus :: The Curious Capitalist - TIME.com: From a Congressional Budget Office estimate released today on the impact of some amendment or other to the Senate stimulus bill: The macroeconomic impacts of any economic stimulus program are very uncertain. Economic theories differ in their predictions about the effectiveness of stimulus. Furthermore, large fiscal stimulus is rarely attempted, so it is difficult to distinguish among alternative estimates of how large the macroeconomic effects would be. For those reasons, some economists remain skeptical that there would be any significant effects, while others expect very large ones. It's sort of like that mutual fund boilerplate, "Past performance is no guarantee of future results." Except that we're not even sure of what the past performance was. (And I say this as somebody who thinks the stimulus legislation is on balance a good idea.) Well, why should we be certain of what past performance was? There haven't been a great many uses of large-scale fiscal policy to try to cure depression. And in those cases in which it has been tried, a lot else has been going on. But when fiscal boost was tried on a large enough scale, it certainly did the job. And it is reasonable to infer (with all the caveats provided by the CBO) that what is true in the very large will be true in the merely large as well. Eugene Fama says that it is theoretically impossible for fiscal stimulus to boost output: World War II proves him wrong. Robert Barro says that the multiplier is zero: World War II proves him wrong. Benn Steil says that Jacques Rueff in 1947 conclusively proved that fiscal policy could not boost employment: World War II proves him wrong. The extent to which the Great Depression and World War II changed how economists thought--and how those who know their history still think--cannot be overstated. And even those economists who don't know their history should be forced to come up with a reason why the lessons of the Great Depression do not apply to today. As I am going to say in class a couple of weeks from now: The end in the Great Depression of laissez faire--the idea that the government should keep its hands off of the economy--as a doctrine for guiding economic policy did not mean the end of the market economy as a social resource allocation mechanism. "Keynesianism" and the doctrine of the "mixed economy" that it supported emerged in the nick of time, soon became the ruling ideologies in the industrial core of the world economy, and provided North America and western Europe with a Keynesian escape route from what had seemed the insoluble crises of the interwar period. The Keynesian escape route opened up key ground in the middle between fascist-style regimentation and socialist-style national planning. Keynes argued that the market economy and capitalist order could be salvaged, and salvaged by relatively minor reforms. An activist welfare-state government with a commitment to full employment had the tools to eliminate Great Depressions, and could put economies back onto the road to Utopia. If only governments would reduce interest rates to get private agents or would themselves spend money freely (without raising taxes) in times when total demand was low, and raise interest rates to reduce private spending and themselves raise taxes (without raising spending) in times when total demand was high, then fluctuations in employment and production could be greatly reduced, and Great Depressions avoided. Belief in this escape route was strongly reinforced by facts. Those countries that had tried it by accident during the Depression--had infiated early, printed money, ensured low interest rates, and run large budget deficits--managed to survive the Depression much more easily than others. World War II provided final proof, were any necessary--"vindication by Mars," as John Kenneth Galbraith calls it. That component of unemployment, called "structural" or "permanent" during the 1930s, that was seemingly-immune to both the self-adjusting forces of the market and the armament of the New Deal vanished entirely in the 1940s as the federal budget deficit approached and then exceeded the levels that had long been recommended by John Maynard Keynes. And the United States fought World War II without reducing civilian consumption: all of U.S. war production came from new capacity or from capacity that stood idle at the end of the 1930s. Demand expansion--deliberate attempts by governments to put the unemployed back to work by deficit spending and loose-money low interest rate policies--was successful in the 1930s and 1940s. It put the unemployed back to work. It did not contain within itself the seeds of a renewed Great Depression. It did not explode into hyperinflation. The coming of "stablization policy" enlarged the policy steps that could be undertaken without forcing a definitive break with the market-capitalist order, and without forcing a choice between Hitler's way and Stalin's. In later years--in the second and third post-World War II generation--tasks of macroeconomic management would prove harder, and the truth of the doctrines of Keynes's disciples if not of the doctrines of Keynes himself would become less clear.

Stimulus True

**Stimulus needed to be larger**

Dean Baker; co-director of the Centre for Economic and Policy Research, senior economist, Ph.D in economics University of Michigan, assistant professor at Bucknell University, 1-09; <http://www.guardian.co.uk/commentisfree/cifamerica/2009/jan/19/barack-obama-economic-stimulus>

There is much to celebrate this week. Topping the list of course is Barack Obama's inauguration. There is good reason to believe that we are seeing power pass from one of the country's worst presidents to one of its best. We should also be celebrating the fact that we will now have a president who knows that the economy is in serious trouble and is prepared to take the steps necessary to set it right. The $825bn (about 2.8% of GDP) two-year stimulus package that he put together with Congress is a good start. The main features of the bill are very much on the right track. The biggest problem is that it should be larger. This downturn is so severe that this package may not be sufficient to offset even half of its impact. The congressional budget office (CBO) projects that the unemployment rate will average 9% in 2010 (pdf) in the absence of a stimulus package, five full percentage points above its estimate of full employment (six percentage points above mine). A rule of thumb is that it takes a two-percentage-point increase in GDP to reduce the unemployment rate by one percentage point. This means that to get back to CBO's projection of full employment we would need to increase GDP in 2010 by 8% above its baseline, or $1.2tn. To reach my estimate (I have a better track record than CBO), it would be necessary to increase GDP in 2010 by 10% or $1.5tn. If we assume a multiplier effect of 1.4 for the stimulus package being debated in Congress, then the $400bn in annual spending will raise 2010 GDP by $560bn, less than half what would be needed to bring us back to full employment by CBO's estimate and just more than one-third by mine. Apart from the size, most of the money in the package looks to be well spent. Two-thirds of the stimulus goes to spending of various types. Much of this will take the form of aid to hard-pressed state and local governments in the form of increased funding for Medicaid and education. The package will also increase the generosity of unemployment benefits as well as modernising the programme so that more part-time and intermittent workers will be eligible for benefits. The package contains considerable funding for green initiatives, including money for retrofitting government buildings and homes, public transportation, promoting alternative energy and modernising the nation's electric grid. It also includes substantial funding for shovel-ready infrastructure projects. Much of this spending will go to badly needed repairs to roads and bridges. Fixing potholes and ensuring the safety of bridges should be a high priority. Unfortunately, some of this spending may take the form of sprawl promoting highways. Representative James Oberstar, the chairman of the House transportation committee, had proposed screens that would have blocked environmentally harmful projects. However, these screens were removed in the negotiating process. The rules of the House make it unlikely Oberstar's screens can be placed back in, but voters should keep this in mind. Another downside to the bill is that it contains substantial tax cuts for business, including some that will do nothing to stimulate the economy. At the top of this list is a provision that allows companies to write-off losses against five years of back taxes. For the most part, this is a giveaway to banks and builders, since few other firms have losses large enough to benefit from this provision. Fortunately, an amendment was slipped in that would prohibit recipients of Tarp funds from taking advantage of this tax break. Keeping this "one trip to the trough" rule in the bill may prove difficult since many senators are staunchly opposed to any limits on welfare for banks. People should watch this one closely. This bill is far from perfect, but it is a very important and substantial step toward addressing the extraordinary economic crisis facing the country. We will need much more spending through the rest of this year and 2010, and almost certainly beyond, to restore high levels of employment. This need will provide opportunities: universal healthcare, publicly funded clinical trials for prescription drugs, public support for open software, public support for creative workers (eg writers and artists, following the model of the Works Progress Administration) and tax subsidies for shorter workweeks, more vacation time and family friendly work places. The policy failures of the last three decades have given us an enormous to-do list. We finally have the opportunity to make progress, but it will be a long and difficult battle. The people who wrecked the economy are still there, and many still hold their hands on the levers of power. (The notion that people should be judged on their track record is still a radical proposition in Washington policy circles.) But for now we should celebrate. We have a new president who recognises the difficulties the economy and the country face and is prepared to take steps to set things right. We should help him.

Stimulus True

#### **Recent stimulus doesn’t disprove – it wasn’t big enough**

Dean Baker; co-director of the Centre for Economic and Policy Research, senior economist, Ph.D in economics University of Michigan, assistant professor at Bucknell University, 11-11; <http://www.guardian.co.uk/commentisfree/cifamerica/2011/dec/19/obama-stimulus-failure-dean-baker>

The economy badly needs stimulus. The collapse of the housing bubble caused us to lose more than $1.2tn in annual demand. Residential construction collapsed when the bubble burst, falling by more than 4 percentage points of GDP, which translates into approximately $600bn a year in lost annual demand. The collapse of the bubble also led to the destruction of close to $8tn of bubble-generated housing equity. The wealth effect of this equity on consumption generated close to $500bn in annual consumption demand. This also was lost when the bubble burst. In addition, the collapse of a bubble in non-residential real estate cost another $100bn or so in annual demand. Finally, the lost tax revenue from the collapse of the housing market and the resulting fallout have forced cuts of close to $150bn a year on state and local governments. In total, the economy has lost close to $1.3tn in annual demand as a result of the collapse of the housing bubble. This explains the economy's weak growth and high unemployment. There is no simple way to replace this demand. We can gather together a coven of market-worshipping Republicans and sacrifice all the workers and retirees we want, it still will not replace the demand gap. We can love the private sector as much as we want and it still will not make firms go out and invest and hire when they don't see demand for their products. That might be a painful truth for government-haters to take, but it is reality. Businesses don't invest when they don't think it is profitable and it won't be profitable as long as they don't see the demand. This means that we need the government to generate demand to boost the economy. That was the point of President Obama's stimulus. Of course it was nowhere near large enough, as his advisors told him at the time. The package produced around $300bn a year in stimulus in 2009 and 2010. This was nowhere near large enough to offset the drop in demand from the housing crash, but it did create 2-3 million jobs. If President Obama had been doing his job, he would have immediately begun pushing for more stimulus the day after the first one passed. He should have been straightforward with the American people and said that the stimulus approved by Congress was **a**n important first step, but that the severity of the downturn was so great we would likely need more. Instead of being honest with America, he started talking about the "green shoots of recovery" and said he was going to focus on the budget deficit. This was an error of unbelievable proportions. By raising the budget deficit front and centre, he backed himself into a corner from which it is almost impossible to now escape. It was essential that Obama keep leading the charge on stimulus, explaining to the country the cause of the economy's weakness was a lack of demand. This story is counterintuitive, so it requires the voice of the president, along with many others, to constantly explain the logic to the country. People had to understand that we are poor because the country as a whole is spending too little to keep the workforce fully employed, not because the government is spending too much. This is the context in which we are arguing over extending the reduction in the social security payroll tax for another two years. As stimulus, this is not an especially good measure. On a per-dollar basis, tax cuts will be much less effective, especially with people carrying so much debt, than direct spending. Furthermore, many of these tax dollars will go to better-off tax payers who are less willing to spend than moderate income families. The Making Work Pay tax credit was much better targeted. Finally, there is zero reason that this tax cut should be tied to social security in any way. As it stands, the trust fund is held harmless because the lost tax revenue is reimbursed from general revenue. But why even raise this as a potential issue for social security; why not just give everyone a tax cut equal to 2 percent of their wages up to $110,000? The only reason to tie the tax cut to social security is if the intention is to raise issues about the social security tax at some future point. The response of the Obama people to this complaint is that this is the only tax cut that the Republican Congress will approve and that we badly need the stimulus. The second claim is definitely true and the first one may well be also. But if that is the case, it only speaks to the incredible failure of this administration to define the agenda and speak honestly about the economy. It's not surprising that they don't have the political support for more effective stimulus when they abandoned the effort to make the case almost two years ago.

Stimulus True

#### Recent stimulus doesn’t invalidate Keynes

Paul Krugman; Nobel Prize winner for economics, Professor of Economics and International Affairs at the Woodrow Wilson School of Public and International Affairs at Princeton University, Centenary Professor at the London School of Economics, and an op-ed columnist for The New York Times; 9-11 <http://krugman.blogs.nytimes.com/2011/09/27/stimulus-tales>

Dean Baker is upset with David Brooks — not for the first time. Let me just put in a word here. The story of Keynesian economists and the Obama stimulus, as anyone who’s been reading me knows, runs as follows: When information about the planned stimulus began emerging, those of us who took our macro seriously warned, often and strenuously, that it was far short of what was needed — that given what we already knew about the likely depth of the slump, the plan would fill only a fraction of the hole. Worse yet, I in particular argued, the plan would probably be seen as a failure, making another round impossible. But never mind. What we keep hearing instead is a narrative that runs like this: “Keynesians said that the stimulus would solve the problems, then when it didn’t, instead of admitting they were wrong, they came back and said it wasn’t big enough. Heh heh heh.” That’s their story, and they’re sticking to it, never mind the facts. And what the facts say is that Keynesian policy didn’t fail, because it wasn’t tried. The only real tests we’ve had of Keynesian economics were the prediction that large budget deficits in a depressed economy wouldn’t drive up interest rates, and the prediction that austerity in depressed economies would deepen their depression. How do you think that turned out

#### The Economic Stimulus Act helped the housing market. It works. Plan would disrupt any economic stimulus now.

Woolsey (Senior Reporter for Forbes) 2008 (Matt “Economic Stimulus Biggest Real Estate Winners” <http://www.forbes.com/2008/03/05/stimulus-homes-property-forbeslife-cx_mw_0305stimulus.html> )

There's some good news on the horizon for homeowners in cities like San Diego, Washington D.C. and Sacramento, Calif., where the real estate boom and bust has left those markets reeling from the effects of overbuilding, bad loans and foreclosures. It's a provision of the recently signed Economic Stimulus Act of 2008 that is designed to boost sales in cities where high home prices have historically prevented government-sponsored enterprise (GSE) lenders Fannie Mae (nyse: FNM - news - people ) and Freddie Mac (nyse: FRE - news - people ) from securitizing mortgages, a process effectively akin to insurance that lowers risk for both lenders and borrowers. The provision calls for increasing GSE loan limits to 125% of a city's median home price. Previously, all housing markets were subject to a $417,000 limit. The adjusted limit is capped at $729,750. The hope is that in raising the limit, more local residents will secure mortgages and buying activity will rise. Before this took effect, in cities like San Francisco or New York, where the median home price is above $417,000, Freddie and Fannie couldn't securitize homes at the median level. Without securitization in a tight credit market, home sales volume drops. But now, loans originating between July 1, 2007 and Dec. 31, 2008, will see a temporary boost in the amount Fannie and Freddie can securitize. (Existing loans issued in the second half of 2007 can be refinanced under these new terms). For some cities, that's a monumental shift. Using median home prices that included condos, foreclosures and new construction, Radar Logic, a New York-based real estate research firm, calculated which markets' housing stock would be most affected by new loan limits. In Los Angeles, for example, a new loan limit of $700,000, or 125% of the current median price, would suddenly place 32% of homes in that metro under Freddie and Fannie's umbrella, according to Radar Logic. In San Diego, another hard-hit market, the new loan limits open up 18% of the market to Fannie and Freddie securitization. What do you think of the government's plan? Weigh in. Add your thoughts in the Reader Comments section below. In affected markets, this program helps in two ways. First, it makes home buying easier by making credit less risky for banks. Fannie and Freddie are backed by the federal government; the lower risk makes lenders more likely to offer credit because lenders know they'll still recoup costs in the case of a default. It also reduces consumer interest rates. Loans above Fannie and Freddie's limit are known as "jumbo" loans, and because they aren't backed by the government, these riskier loans carry higher interest rates. Under the limit increase in the stimulus package, loans that are recategorized from jumbos to conforming loans (54% in San Jose, 44% in San Francisco, 17% in New York) will carry lower interest rates. For potential buyers, this makes home buying more affordable, and for many current mortgage holders, it makes refinancing to a lower rate possible. Taken together, these benefits should make credit less risky for lenders and cheaper for home buyers, which could help boost transaction volume and lead to price recoveries. At least that's what the government is banking on.

Stimulus True

#### 2008 Tax rebates helped to stimulate the economy – data proves

Broda and Parker (Professor at The University of Chicago and Head of International Research at Barclays Capital. Professor of Finance at Kellogg School of Management at Northwestern University) 8-15-8 (Christian, Jonathan “The impact of the 2008 rebate” <http://www.voxeu.org/article/did-2008-us-tax-rebates-work>)

Early in 2008, in response to slowing economic growth, the US federal government enacted an economic stimulus package consisting mainly of a $100 billion tax rebate program. By 1 July 2008, more than 70 million American households had received tax rebates of $950 on average. The hope of policymakers was that by putting money directly back into the hands of US households, they would increase spending levels and avoid (or at least mitigate) the severity of the slowdown. Skeptics argued that households would not spend their tax rebates. People tend to dislike swings in their consumption levels, leading some to believe that the one-time stimulus payment would be spent only gradually over many years. This would imply that the spending effect of the rebate would be modest at best, rendering fiscal policy ineffective, as Martin Feldstein recently argued. Others argued that since the money to pay for fiscal programs has to be borrowed and paid back in taxes, it’s a wash for the economy as a whole, and thus using fiscal policy to get the economy going is like “taking a bucket of water from the deep end of a pool and dumping it into the shallow end.” Studies of the 2001 US tax rebates showed a significant consumption effect1, so how effective has the 2008 economic stimulus program been at getting people to spend? In very recent research, we answer this question by tracking the weekly expenditures of more than 30,000 households who have received or are going to receive rebates, and relating their spending levels to the timing of the receipt of their rebate.2 Because it was not administratively possible for the IRS to mail all rebate checks at once, rebates were mailed out to households during a nine-week period between mid-May and the end of July, or deposited into their accounts in one of the first three weeks of May. The particular week in which a check was mailed or deposited depended on the second-to-last digit of the taxpayer's Social Security number, a number that is effectively randomly assigned. This randomization allows us to identify the causal effect of the rebate by comparing the spending of households that received the rebate earlier to that of households that received it later. Because of the experimental nature of the timing of rebate receipt and the wealth of information that we are working with, we can identify the effect of the rebate on spending without the interference of other concurrent factors – like high gas prices or lower interest rates – or households characteristics that are typically hard to observe. Main findings We compare the weekly expenditures of households that received a rebate by June 14, to those that would later receive a rebate, but had not yet received it by that date. We use detailed expenditures covering a range of non-durable goods as reported by households in ACNielsen’s Homescan database. Because households report spending using bar-code scanners at home, we are mainly able to study spending at grocery stores, mass-merchandise outlets and drugstores.3 Our empirical specification allows for household fixed effects and weekly fixed effects, with the key being an indicator variable that takes the value of 1 in weeks where the household has already received the rebate and 0 in weeks prior to the rebate receipt. The coefficient on this variable can be interpreted as the average change in weekly spending on non-durable goods due to the receipt of the rebate. The more effective is fiscal policy, the higher is this coefficient. The table below shows the main results from this specification for different groups of households. The first column shows the results using all households in our sample that have or will receive a rebate. Almost 19,000 out of the 34,000 households examined reported receiving the rebate, while the remainder reported receiving a rebate later or reported that they are sure they will receive one. By the end of our sample, June 14, these households had typically had their rebates for 4 weeks. As shown in column 1, the average household increased its weekly expenditures on non-durable goods by 3.5% after receipt of the rebate. The impact is highest in the week where the rebate is received (not reported) with weekly spending increasing by almost 6% on average during the first week. We find no impact on spending in the few weeks prior to the receipt of the rebate.

#### The Economic Stimulus Act was successful

Broda and Parker (Professor at The University of Chicago and Head of International Research at Barclays Capital. Professor of Finance at Kellogg School of Management at Northwestern University) 8-15-8 (Christian, Jonathan “The impact of the 2008 rebate” <http://www.voxeu.org/article/did-2008-us-tax-rebates-work>)

The Economic Stimulus Act of 2008 was aimed at increasing disposable income temporarily through tax rebates in the hope this would stimulate spending and end or at least mitigate the severity of a US economic slowdown. We find that to a significant extent they succeeded. The stimulus payments are initially being spent at significant rates. These rates are slightly higher than those observed in 2001 when fiscal policy has been credited with helping end the 2001 recession.

Stimulus True

#### Government stimulation efforts can help the economy

Uhlig and Drautzburg (Chairman and Professor of Department of Economics of the University of Chicago. PhD candidate in Economics at the University of Chicago) 2011 (Harald and Thorsten “Financing fiscal stimulus” <http://www.voxeu.org/article/financing-fiscal-stimulus> )

Government expenditures have to be financed by taxes, eventually – a fact driven home by the current debate on US debt ceiling and the Eurozone sovereign-debt crisis. The difficult political debate also shows that financing government expenditure is not trivial. If governments could easily increase their tax revenue without hampering economic activity, the debt ceiling debate would be void and Greece would not be receiving outside support. In reality, taxes distort economic decisions. This simple insight carries through when analysing the costs and benefits of the fiscal stimulus in the aftermath of the recent financial crisis. Early analyses focused on quantifying the benefits of such a policy without modelling the government side in greater detail. Different policy rules to finance government debt make crucial differences when evaluating the recent stimulus. This is not to deny that the financial crisis does make a difference for the policy analysis. It does. Theoretically, this has been shown by Eggertsson (2011) and Christiano et al. (2011). Simplifying: In the presence of the zero lower bound the nominal interest rate cannot be adjusted to accommodate an increased desire to save. Incomes have to fall. If the government creates inflation expectations by increasing its consumption, it can prevent such a fall. If we analyse two economies, both with the same financial crisis but with and without fiscal intervention, the fiscal intervention causes output to rise, possibly dramatically. With the potentially large appeal of government expenditure programmes in mind, it is therefore worthwhile to evaluate what policymakers in early 2009 could have believed about the effectiveness of the programme they eventually enacted, i.e. the American Recovery and Reinvestment Act (ARRA). In Drautzburg and Uhlig (2011), we undertake this analysis. How to measure the effect of fiscal stimulus? To measure the effect of the ARRA, we need a measure that compares the counterfactual path of output in its absence with the path of the economy when the ARRA is enacted and executed. Also, a summary statistic for the output effect is needed. First, however, note that judging a policy by its output effects is not the same as a normative analysis.

### 2AC — Spending Good – General

#### Spending is the sole viable strategy – recession proves

Paul Krugman, Nobel Prize Winner for Economics, Professor of Economics and International Affairs at Princeton, 12-29-11, <http://www.nytimes.com/2011/12/30/opinion/keynes-was-right.html>

Unfortunately, in late 2010 and early 2011, politicians and policy makers in much of the Western world believed that they knew better, that we should focus on deficits, not jobs, even though our economies had barely begun to recover from the slump that followed the financial crisis. And by acting on that anti-Keynesian belief, they ended up proving Keynes right all over again. In declaring Keynesian economics vindicated I am, of course, at odds with conventional wisdom. In Washington, in particular, the failure of the Obama stimulus package to produce an employment boom is generally seen as having proved that government spending can’t create jobs. But those of us who did the math realized, right from the beginning, that the Recovery and Reinvestment Act of 2009 (more than a third of which, by the way, took the relatively ineffective form of tax cuts) was much too small given the depth of the slump. And we also predicted the resulting political backlash. So the real test of Keynesian economics hasn’t come from the half-hearted efforts of the U.S. federal government to boost the economy, which were largely offset by cuts at the state and local levels. It has, instead, come from European nations like Greece and Ireland that had to impose savage fiscal austerity as a condition for receiving emergency loans — and have suffered Depression-level economic slumps, with real G.D.P. in both countries down by double digits. This wasn’t supposed to happen, according to the ideology that dominates much of our political discourse. In March 2011, the Republican staff of Congress’s Joint Economic Committee released a report titled “Spend Less, Owe Less, Grow the Economy.” It ridiculed concerns that cutting spending in a slump would worsen that slump, arguing that spending cuts would improve consumer and business confidence, and that this might well lead to faster, not slower, growth. They should have known better even at the time: the alleged historical examples of “expansionary austerity” they used to make their case had already been thoroughly debunked. And there was also the embarrassing fact that many on the right had prematurely declared Ireland a success story, demonstrating the virtues of spending cuts, in mid-2010, only to see the Irish slump deepen and whatever confidence investors might have felt evaporate. Amazingly, by the way, it happened all over again this year. There were widespread proclamations that Ireland had turned the corner, proving that austerity works — and then the numbers came in, and they were as dismal as before. Yet the insistence on immediate spending cuts continued to dominate the political landscape, with malign effects on the U.S. economy. True, there weren’t major new austerity measures at the federal level, but there was a lot of “passive” austerity as the Obama stimulus faded out and cash-strapped state and local governments continued to cut. Now, you could argue that Greece and Ireland had no choice about imposing austerity, or, at any rate, no choices other than defaulting on their debts and leaving the euro. But another lesson of 2011 was that America did and does have a choice; Washington may be obsessed with the deficit, but financial markets are, if anything, signaling that we should borrow more. Again, this wasn’t supposed to happen. We entered 2011 amid dire warnings about a Greek-style debt crisis that would happen as soon as the Federal Reserve stopped buying bonds, or the rating agencies ended our triple-A status, or the superdupercommittee failed to reach a deal, or something. But the Fed ended its bond-purchase program in June; Standard & Poor’s downgraded America in August; the supercommittee deadlocked in November; and U.S. borrowing costs just kept falling. In fact, at this point, inflation-protected U.S. bonds pay negative interest: investors are willing to pay America to hold their money. The bottom line is that 2011 was a year in which our political elite obsessed over short-term deficits that aren’t actually a problem and, in the process, made the real problem — a depressed economy and mass unemployment — worse.

#### Austerity kills the economy

Sahadi (Senior Writer for CNNMoney. Specializing in taxes and deficit spending) 7/16/12 (Jeanne, “IMF: Deal with fiscal cliff and debt ceiling soon” LexisNexis)

Hit the brakes on the fiscal cliff and hit the gas on raising the debt ceiling. That was the message to Congress from the International Monetary Fund on Monday. The IMF and others have often advised that the United States come up with a serious plan to reduce its debt over time. But the so-called fiscal cliff - a series of expiring tax cuts and the onset of a record amount of spending cuts - would be anything but gradual when it comes to deficit reduction. The fiscal cliff includes the expiration of the Bush tax cuts, the onset of $1 trillion in blunt spending cuts, and a reduction in Medicare doctors' pay. If all the provisions go into effect, they would take more than $500 billion out of the economy in 2013 alone. Such an abrupt shift risks pushing the economy into recession, according to many economists. The mix of tax increases and spending cuts would slash the deficit in half - to 3.8% of gross domestic product, down from the 7.6% projected for this year. The IMF has recommended a slower course of deficit reduction, so that it drops by just 1 percentage point next year. "A more modest retrenchment in 2013 ... would be a better option," the agency said. The good news is that no one in Congress actually wants all the fiscal cliff measures to take effect. The bad news is that lawmakers cannot agree on more gradual debt-reduction measures to replace them. And the consensus is they won't seriously try to do so until after the November elections. That is around the same time the country's debt load will near its legal limit of $16.394 trillion, requiring another increase in the debt ceiling to pay all the bills the government has incurred. As last summer's debt ceiling showdown so vividly demonstrated, the vote to increase the country's borrowing limit can become a firestorm with very negative consequences for the economy and the United States' reputation. So it's little surprise that the IMF urged lawmakers to do the right thing this time and raise the ceiling without any drama. "Early action on the federal debt ceiling ... would mitigate risks of financial market disruptions and a loss in consumer and business confidence," the agency said.

#### Spending is key to reclaim borrowing roles from the private sector – no confidence loss

Paul Krugman and Richard Layard, Nobel Prize Winner for Economics, Professor of Economics and International Affairs at Princeton, and director of the Centre for Economic Performance at the London School of Economics, 6-28-12, “A Manifesto for Economic Sense,” <http://www.manifestoforeconomicsense.org/>

Their first argument is that government deficits will raise interest rates and thus prevent recovery. By contrast, they argue, austerity will increase confidence and thus encourage recovery. But there is no evidence at all in favour of this argument. First, despite exceptionally high deficits, interest rates today are unprecedentedly low in all major countries where there is a normally functioning central bank. This is true even in Japan where the government debt now exceeds 200% of annual GDP; and past downgrades by the rating agencies here have had no effect on Japanese interest rates. Interest rates are only high in some Euro countries, because the ECB is not allowed to act as lender of last resort to the government. Elsewhere the central bank can always, if needed, fund the deficit, leaving the bond market unaffected. Moreover past experience includes no relevant case where budget cuts have actually generated increased economic activity. The IMF has studied 173 cases of budget cuts in individual countries and found that the consistent result is economic contraction. In the handful of cases in which fiscal consolidation was followed by growth, the main channels were a currency depreciation against a strong world market, not a current possibility. The lesson of the IMF’s study is clear - budget cuts retard recovery. And that is what is happening now - the countries with the biggest budget cuts have experienced the biggest falls in output. For the truth is, as we can now see, that budget cuts do not inspire business confidence. Companies will only invest when they can foresee enough customers with enough income to spend. Austerity discourages investment. So there is massive evidence against the confidence argument; all the alleged evidence in favor of the doctrine has evaporated on closer examination. The causes. Many policy makers insist that the crisis was caused by irresponsible public borrowing. With very few exceptions - other than Greece - this is false. Instead, the conditions for crisis were created by excessive private sector borrowing and lending, including by over-leveraged banks. The collapse of this bubble led to massive falls in output and thus in tax revenue. So the large government deficits we see today are a consequence of the crisis, not its cause. The nature of the crisis. When real estate bubbles on both sides of the Atlantic burst, many parts of the private sector slashed spending in an attempt to pay down past debts. This was a rational response on the part of individuals, but - just like the similar response of debtors in the 1930s - it has proved collectively self-defeating, because one person’s spending is another person’s income. The result of the spending collapse has been an economic depression that has worsened the public debt. The appropriate response. At a time when the private sector is engaged in a collective effort to spend less, public policy should act as a stabilizing force, attempting to sustain spending. At the very least we should not be making things worse by big cuts in government spending or big increases in tax rates on ordinary people. Unfortunately, that’s exactly what many governments are now doing. The big mistake. After responding well in the first, acute phase of the economic crisis, conventional policy wisdom took a wrong turn - focusing on government deficits, which are mainly the result of a crisis-induced plunge in revenue, and arguing that the public sector should attempt to reduce its debts in tandem with the private sector. As a result, instead of playing a stabilizing role, fiscal policy has ended up reinforcing and exacerbating the dampening effects of private-sector spending cuts.

Spending Good - General

#### Spending is key to relocating debt – eliminates the need for itself

Paul Krugman, Nobel Prize Winner for Economics, Professor of Economics and International Affairs at Princeton, 10-25-10, <http://krugman.blogs.nytimes.com/2010/10/25/sam-janet-and-fiscal-policy/>

But what if inflation can’t or won’t be delivered? Well, suppose a third character can come in: Government Gus. Suppose that he can borrow for a while, using the borrowed money to buy useful things like rail tunnels under the Hudson. The true social cost of these things will be very low, because he’ll be putting resources that would otherwise be unemployed to work. And he’ll also make it easier for the Sams to pay down their debt; if he keeps it up long enough, he can bring them to the point where they’re no longer so severely balance-sheet constrained, and further deficit spending is no longer required to achieve full employment. Yes, private debt will in part have been replaced by public debt – but the point is that debt will have been shifted away from severely balance-sheet-constrained players, so that the economy’s problems will have been reduced even if the overall level of debt hasn’t fallen. The bottom line, then, is that the plausible-sounding argument that debt can’t cure debt is just wrong. On the contrary, it can – and the alternative is a prolonged period of economic weakness that actually makes the debt problem harder to resolve.

Spending Good – General

#### Spending is key – the problem is a demand shortage and benefits outweigh the possibility of mismanagement

Joseph Stiglitz, Nobel Prize winner in Economics, November 2010, “Comment: To choose austerity is to bet it all on the confidence fairy: The mystical belief is that a smaller deficit will lead to an investment boom. What Britain really needs now is another stimulus,” <http://search.proquest.com/docview/759371294>)

We should be clear. Most of the increase is not due to the stimulus but to the downturns and the bank bailouts. Those in the financial market are egging on politicians to ask whether we can afford another stimulus. I argue that Britain, and the world, cannot afford not to have another stimulus. We cannot afford austerity. In a better world, we might rightfully debate the size of the public sector. Even now there should be a debate about how government spends its money. But today cutbacks in spending will weaken Britain, and even worsen its long-term fiscal position relative to well-designed government spending. There is a shortage of aggregate demand - the demand for goods and services that generates jobs. Cutbacks in government spending will mean lower output and higher unemployment, unless something else fills the gap. Monetary policy won't. Short-term interest rates can't go any lower, and quantitative easing is not likely to substantially reduce the long-term interest rates government pays - and is even less likely to lead to substantial increases either in consumption or investment. If only one country does it, it might hope to gain an advantage through the weakening of its currency; but if anything the US is more likely to succeed in weakening its currency against sterling through its aggressive quantitative easing, worsening Britain's trade position. Critics say government won't spend the money well. To be sure, there will be waste. But even if money is not spent perfectly, the returns on government investments in education, technology and infrastructure are far higher than the government's cost of capital. Besides, the choices facing the country are bleak. If the government doesn't spend this money there will be massive waste of resources as its capital and human resources are under-utilised.

### 2AC — Spending Good – Jobs/Infra Specific

#### Infrastructure spending is a sound investment – stimulus works and cuts will only worsen problems

Henry Blodget, CEO and editor of *Business Insider*, BA from Yale, 4-24-12, <http://www.businessinsider.com/its-official-keynes-was-right-2012-4>

But I will also add this in defense of Keynesianism ... The Austerians love to point at the 1930s as "proof" that Keynes was wrong. Look at the huge "New Deal," they say. Look at all those expensive public works projects. Look at all the spending the government did to try to get us out of the Great Depression, and it never really worked. What got us out of the Depression, the Austerians smugly observe, was World War 2. But what was World War 2 if not an absolutely gigantic Keynesian stimulus? The Federal deficit in World War 2 was massive—much bigger than any time during the Great Depression. And we built up a huge Federal debt load. And ... we set the stage for two decades of amazing prosperity, in which we worked off those debts. Our current debt and deficit situation scares the bejeezus out of me.  We absolutely have to get our long-term budget problems under control, and doing so will involve both cutting spending and raising taxes. If we don't do that, we really will collapse, as Niall Ferguson et al have long been arguing.   
 But getting the budget under control by radically chopping spending or increasing taxes this minute, as many Austerians want to do, won't help. In fact, it will likely make the problems vastly worse, because it will put that many more people out of work and reduce tax revenue that much further (just take a look at Europe). Meanwhile, given that we've already racked up $15 trillion of debt, I certainly wouldn't be opposed to our spending another couple of trillion upgrading our piss-poor infrastructure. Incurring debt to build things that help all Americans, from unemployed folks to business leaders to children, is a trade-off I'm willing to make. Especially if the jobs created by this "stimulus" spending help alleviate our massive unemployment and inequality problems.

#### Spending creates jobs – outweighs benefits of austerity – Spain proves

Paul Krugman, Nobel Prize Winner for Economics, Professor of Economics and International Affairs at Princeton, 7-11-12, <http://krugman.blogs.nytimes.com/2012/07/11/pointless-pain-in-spain/>

It’s no fun being Prime Minister of a debtor nation without its own currency. Unlike the US or the UK, Spain has no easy options. That said, the new austerity measures just announced make no sense at all. According to news reports, Rajoy has announced [65 billion euros of tax increases and spending cuts](http://www.bloomberg.com/news/2012-07-11/rajoy-announces-65-billion-euros-in-budget-cuts-to-fight-crisis.html); this will clearly deepen Spain’s depression. So what purpose will this serve? Think of Spain as facing a three-level problem. The topmost level is the problem of the banks; set that aside for now. Below that is the problem of sovereign debt. What makes the debt problem so serious, however, is the underlying problem of competitiveness: Spain needs to increase exports to make up for the jobs lost when its housing bubble burst. And it faces years of a highly depressed economy until costs have fallen enough relative to the rest of Europe to achieve the needed gain in competitiveness. So, what do the new austerity measures contribute to the solution of these problems? Well, Spain’s deficit will be smaller. Not 63 billion euros smaller, since the further depression of Spain’s economy will reduce revenues; say it’s 40 or 45 billion euros less debt, which is around 4 percent of Spanish GDP. Does anyone think this will make a big difference to the long-run fiscal outlook, or restore investor confidence? What about competitiveness? Let’s be frank and brutal: the European strategy is basically for debtor nations to achieve relative deflation via high unemployment. Think of it in terms of a Phillips curve: I’ve drawn this curve very flat at high rates of unemployment – which is what all the evidence suggests. If nothing else, this crisis has given us overwhelming evidence that [downward nominal wage rigidity](http://krugman.blogs.nytimes.com/2012/06/24/revenge-of-the-optimum-currency-area/) is real and a major factor. Now think about what Spain is doing: basically, it’s moving from A to B – driving its unemployment rate even higher. This will possibly lead to a slight acceleration of the improvement in Spain’s competitiveness. Maybe. But it won’t be significant. So, Rajoy is imposing harsh further austerity that will raise unemployment while making no significant dent in either the fiscal problem or the competitiveness problem. And this makes sense why?

### Spending Good – Infrastructure Specific

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Henry Blodget, CEO and editor of *Business Insider*, BA from Yale, 4-24-12, <http://www.businessinsider.com/its-official-keynes-was-right-2012-4>

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#### Even if deficit spending is detrimental, we shouldn’t neglect public investments like transportation

Sawhill and Schultze 04 Isabel Sawhill, Senior Fellow at The Brookings Institution, And Charles Schultze, economist and public policy analyst, Jan 2004, “Restructuring Domestic Spending,” from RESTORING FISCAL SANITY: HOW TO BALANCE THE BUDGET, The Brookings Institution, http://www.brookings.edu/es/research/projects/budget/fiscalsanity/full.pdf

Eliminating the deficit without addressing important domestic priorities would not make economic or social sense. Although a large continuing deficit is detrimental to economic growth, so is neglect of public investments in education, health, transportation, and research. Public investment complements private investment in new technologies, facilities, and equipment that enhance growth. Furthermore, citizens value such things as a cleaner environment, shorter commuting times, and safer streets, which enhance their quality of life but do not show up in conventional measures of economic welfare. Moreover, while most Americans have benefited from the higher productivity that has accompanied rapid advances in technology and globalization, some mechanism is needed to cushion the losses suffered by those whose jobs have been destroyed in the process. Restructuring the social safety net to encourage work can simultaneously increase the incomes of the least fortunate and produce more jobs and more growth. For all these reasons, a balanced plan to reduce the deficit should make room for new domestic spending to achieve these objectives.

#### Their author concedes that infrastructure spending eventually boosts the private sector

Daniel Mitchell, Senior Fellow at the Cato Institute, 2-1-10, <http://www.cato.org/publications/commentary/spending-our-way-stagnation>

Interestingly, a large body of academic work attempts to measure the growth-optimizing level of government. This research is based on the notion there is not much prosperity in a state of anarchy. Governments solve this problem by imposing the rule of law (courts, police protection, etc). Those governmental functions cost money, but they yield big benefits. Moreover, government spending on "public goods" such as basic infrastructure also can facilitate the functioning of a market economy.

Spending Good – Infrastructure-Specific

#### Spending on infrastructure helps economy in short-term—stimulus and crowd-in

Bivens 12 Josh Bivens, Research and Policy Director at the Economic Policy Institute, 4/18/12, “Public investment The next ‘new thing’ for powering economic growth,” Economic Policy Institute, http://www.epi.org/publication/bp338-public-investments/

New spending in the near term would essentially constitute a macroeconomic “free lunch,” putting idle resources back to work without displacing any other economic activity. Indeed, by supporting overall economic activity without increasing interest rates, debt-financed spending in the next couple of years might even “crowd in” private-sector activity, since studies show that a primary determinant of business investment is the current state of the economy. The Obama administration made substantial infrastructure investments (nearly $100 billion worth) a central part of its American Jobs Act, a plan proposed in 2011 that, if passed, would move fiscal policy from being a serious economic drag to being a useful boost to growth in the next two years. Yet these infrastructure investments have not passed Congress. This is unfortunate, because infrastructure investment is about the most efficient fiscal support one can provide to a depressed economy—a finding supported by nearly all macroeconomic models and forecasts.3 Further, public investment provides a long-term growth payoff as well as a near-term boost to the job market.

#### Infrastructure investment boosts the economy – studies prove

Inman (Professor of Finance and Economics at the Wharton School at University of Pennsylvania) 2010 (Robert “Using states for macroeconomic fiscal policy” <http://www.voxeu.org/article/shortcomings-using-states-federal-macroeconomic-fiscal-policy> )

Central government fiscal policies for stimulating the private economy can come either as a cut in taxation or as an expansion in government spending. The micro-economic evidence suggests unexpected infrastructure spending (Ramey Forthcoming) and unexpected tax cuts, or expanded transfers to lower income, credit-constrained households (Johnson et al. 2006) are the most effective fiscal tools for a quick stimulus to aggregate demand. More aggregate evidence from the work of Blanchard and Perotti (2002) and Romer and Romer (2010) shows that such fiscal policies can be effective sources of new demand for a lagging macro economy. In most federal economies, however, the central government relies upon states to spend their money as state governments are thought to be the relatively more efficient provider of most public services. Inside the nation, inter-state fiscal competition also encourages production and tax efficiencies and, through sorting, a better match of services levels to the needs of households and firms. When there are inter-state tax or service spillovers, central government financing through inter-governmental grants can solve the problem; service provision can and should remain local. Oates (1999) provides a valuable summary of the arguments and the evidence.

Spending Good – Infrastructure Specific

#### **Decentralizing government power to states fails to stimulate the economy in the short run. Investing in infrastructure solves.**

Inman (Professor of Finance and Economics at the Wharton School at University of Pennsylvania) 2010 (Robert “Using states for macroeconomic fiscal policy” <http://www.voxeu.org/article/shortcomings-using-states-federal-macroeconomic-fiscal-policy> )

The virtue of decentralised provision has the potential to become a vice in times of deep recessions, however. In federal economies, the central government may decide expansionary spending policies, but state governments have in place the institutional structures needed to best implement those policies. States are the ones who contract to build roads and who write unemployment and income support checks. In federal economies, states are the “agents” of the central government for much of spending policy. Like any agent, however, states have their own agendas, and the available evidence suggests there is often a disconnect between central government intentions and state government responses. This is particularly so when the intention is aggregate demand stimulation that are likely to accrue primarily to residents outside a state. Edward Gramlich (1978), for example, studied the response of states to a national effort to stimulate state spending during the 1975 US recession and found that states saved much of their stimulus money for spending at a later date – after the national economy had recovered. Similarly, state policies towards lower income residents will be decided by politics dominated in most states by middle income voters. Poor households meant to receive extra federal assistance during deep recessions may not receive all the initially assigned federal money. This is why federal grants typically contain “maintenance-of-effort” provisions. But such requirements are hard to enforce. Most budget money is “fungible,” easily moved from category to category, so that federal aid simply replaces state money previously intended for the federal initiative. New research on the multiplier for federal transfers to states My recent work with Gerald Carlino (2010) using data to 2008 confirms Gramlich’s results. We extend the analysis of Blanchard and Perotti to explicitly allow for federal transfers to state and local governments. (They included such transfers as part of household income assuming that state governments are perfect agents for their residents.) When separated out, we find an income multiplier for federal transfers to states of only 40 cents for each dollar of federal aid even after 20 quarters. This income multiplier is significantly smaller than that found by Blanchard and Perotti and Romer and Romer for direct federal spending and tax relief. There is a further complication. National policy, presumably decided by the principal in the national interest, requires the approval of the agents who are to implement that policy. To implement beneficial fiscal policy, a president will typically need the approval of the elected representatives from a majority of states. If so, spending policies that might make the most sense for a fiscal stimulus – say targeted infrastructure spending and poverty and unemployment assistance to areas most in need – can get diluted so as to satisfy the local needs of a majority of states.

Spending Good – Infrastructure Specific

**Current start-stop funding of transportation is making a credit crisis inevitable—large-scale transportation investment solves second downgrade by S&P**

Hirsch 12 (Michelle Hirsch writes about economics and tax policy out of The Fiscal Times’ Washington, D.C. Bureau, The Fiscal Times, “S&P Credit Risk from Highway Funding Delays,” 4/4/2012,<http://www.thefiscaltimes.com/Articles/2012/04/04/SP-Credit-Risk-from-Highway-Funding-Delays.aspx#page1> )hhs-ps

Standard & Poor’s, which downgraded the U.S. [credit rating](http://www.thefiscaltimes.com/Articles/2011/08/06/Debt-Crisis-Blamed-for-US-Credit-Rating-Downgrade.aspx#page1) last August after the government came close to defaulting on its debt, is now warning that another credit crisis could occur unless the government adequately funds long-term transportation and infrastructure spending. In a new report, the major credit rating agency, which called highway, bridge and other transportation projects “the backbone of the U.S. economy,” raised concern that Congress has yet to pass a permanent extension of the U.S. highway spending bill. The latest continuing resolution, the 9th temporary extension, was approved by Congress on March 29 before lawmakers adjourned. RELATED: [Infrastructure Spending Gap Will Cost More Jobs](http://www.thefiscaltimes.com/Articles/2011/07/27/Infrastructure-Spending-Gap-Will-Cost-More-Jobs.aspx#page1) While the three-month extension will provide short-term spending for states and localities as they prepare for the summer construction season, many state officials remain concerned about the fate of long- term projects and planning. The federal government supplies states with about 45 percent of their funding for roads and bridges, according to the American Association of State Highway and Transportation Officials. “The combination of reduced or unpredictable federal support and lower demand could result in deferred maintenance projects that would keep our nation’s [transportation infrastructure](http://www.thefiscaltimes.com/Articles/2011/06/22/Americas-Third-World-Roads-Broken-and-Dangerous.aspx) in good repair,” the S&P report stated. “Such deferrals could hurt an entity’s credit if capital costs escalate over time, putting the system at risk.” State governments finance major highway and bridge projects with revenue-backed bonds, or so-called GARVEE debt-financing instruments backed by a pledge of future federal aid for debt service. But if the federal revenue stream is uncertain or disrupted, state governments may have trouble marketing those bonds or need to pay a higher interest rate. “The political gridlock in Washington, D.C., and the doubt surrounding federal funding are making it difficult for issuers throughout the infrastructure sector to define long-term plans for funding necessary capital projects,” the S&P report states. Last week Congress passed a [stopgap three-month bill](http://www.thefiscaltimes.com/Articles/2012/03/29/Highway-Bill-Extension-Passes.aspx#page1) to keep federal highway and transit aid flowing and avoid a widespread shutdown of construction projects. The move pushes congressional action on a long-term overhaul of transportation programs deeper into a highly contentious election year. Without action, Democrats estimated that as many as 1.8 million construction-related jobs were at risk just before the spring and summer construction season. The government [would also have lost](http://www.thefiscaltimes.com/Articles/2011/08/06/Debt-Crisis-Blamed-for-US-Credit-Rating-Downgrade.aspx#page1) about $110 million a day in uncollected gas and diesel taxes. The last long-term transportation law expired in 2009, but programs have continued under a series of short-term extensions. The vote capped a see-saw struggle by House GOP leaders to pass their own five-year transportation plan.

**Transportation investment solves downgrade**

Szakonyi 12 (“S&P: Lack of US Infrastructure Plan Could Spur Credit Crisis,” Mark Szakonyi, Associate Editor | Apr 5, 2012 5:23PM GMT *The Journal of Commerce Online - News Story)hhs-ps*

Agency says crisis possible if infrastructure, transportation funding not met Standard & Poor’s said the U.S. government’s inability to provide long-term infrastructure and transportation funding could create another credit crisis. The warning from the rating agency, which downgraded the U.S. credit rating in August, comes as Congress struggles to approve a multiyear surface transportation bill. Congress on March 29 [approved a three-month extension of highway funding](http://www.joc.com/washington/congress-votes-90-day-extension-highway-bill) after the House failed to pass its five-year, $260 billion plan to match the Senate’s already approved two-year, $109 billion bill. S&P warns “[reduced or unpredictable federal support](http://www.thefiscaltimes.com/Articles/2012/04/04/SP-Credit-Risk-from-Highway-Funding-Delays.aspx#page1) and lower demand could result in deferred maintenance projects that would keep our nation’s transportation infrastructure in good repair,” according to The Fiscal Times. Few transportation analysts expect [Congress to approve a plan](http://www.joc.com/hopes-dim-surface-bill-year) by the end of the year, making it difficult for state transportation agencies to commit to long-term projects.

### Austerity Bad – European Example

Spending cuts harm various aspects of the economy, European austerity proves

Sebastian Dullien Senior Policy Fellow at ECFR and a professor of International Economics at HTW Berlin 5-1-12 <http://ecfr.eu/content/entry/commentary_reinventing_europe_explaining_the_fiscal_compact>

As this tightening is done in a situation where monetary policy cannot be expected to react with large interest rate cuts (given that liquidity conditions are already very loose), and that several countries are now embarking on coordinated austerity policies that amplify the effect of national budget cuts, one can expect the current ‘fiscal multiplier’ to be at least one. This means that GDP growth is dampened by at least as much as the deficit is cut.[4] This then means that austerity measures alone would translate into a dampening effect on GDP growth of at least 1.5% this year, and of at least 1% in 2012 (distributed very unevenly as noted above). This reasoning suggests that austerity alone explains a large part of the current European recession, and indicates that any recovery into 2012 might be extremely weak if consolidation plans are left unaltered. Austerity is also increasingly seen as self-defeating as it reduces the absolute level of GDP, thereby increasing the debt burden as measured in debt-to-GDP-ratios.[5] If consolidation goes according to plan, the negative impact on growth will recede somewhat after 2013, when countries have reached the 3%-of-GDP threshold for their deficits. After this point, it can be expected that further progress towards the medium-term-budget objective of close to balance will be pursued in a slower manner. This might still dampen GDP growth in Europe by a few percentage points, but it will be much less dramatic than the impact in 2012/3. Another important question is whether the target of a (almost) balanced budget is too tight. Traditional golden rules usually call for a balanced budget over the cycle, excluding capital expenditure. The logic here is that investment yields return in the future, helping to service debt, and therefore should be treated differently from public transfers or public consumption. The EU rules do not make such a differentiation, and so can be seen as prescribing an overly tight fiscal policy that leaves insufficient room for investment. Empirical evidence from (especially large-scale) previous austerity drives shows that there are cuts to public investment, education and research and development, which may then also have a negative effect on long-term growth potential. There is a large risk of this being repeated by the EU’s current attempts to reach its own fiscal targets.

### 2AC — AT: Confidence

#### Empirics flow overwhelmingly aff – austerity fails and hurts confidence – infrastructure spending is uniquely good

Michael Shields, Chief Correspondent in Vienna for Reuters, 4-27-12, “Europe’s austerity drive is suicidal: Stiglitz,” <http://ca.reuters.com/article/businessNews/idCABRE83Q0GJ20120427>

Europe's attempt to save its way back to health is tantamount to economic suicide that could wreck the euro currency block, Nobel Prize-winning U.S. economist Joseph Stiglitz said, calling for the continent to focus instead on fostering growth. "I think Europe is headed to a suicide...There has never been any successful austerity program in any large country," the former World Bank economist told a panel discussion in Vienna late on Thursday. Austrian radio on Friday broadcast some of his comments, which chime with a growing backlash in Europe against the German-led push for more fiscal discipline as the way to end the debt crisis. "Decreasing growth is causing the deficit, not the other way around. I think that austerity approach is going to lead to high levels of unemployment that will be politically unacceptable and make deficits get worse," Stiglitz said. He urged rich European countries like Germany to invest more in infrastructure, education and technology, arguing that "the returns on those investments are an order of magnitude greater than the cost of capital". Insisting on cutting debt and deficits as the way to shore up confidence in euro zone countries - as agreed by the currency bloc's leaders late last year - could end up having the opposite impact, Stiglitz said. "What they have agreed to do last December is a recipe to make sure that (the euro zone) dies as we know it," he said, although he imagined a "core euro" shared among a handful of countries with the strongest economies could survive. "I hope...the debate will be what are the things we can do to promote growth rather than how do we strangle each other together."

#### Turn – cuts worsen things, killing confidence – multiple studies prove spending is better

Joseph Stiglitz, Nobel Prize winner in Economics, November 2010, “Comment: To choose austerity is to bet it all on the confidence fairy: The mystical belief is that a smaller deficit will lead to an investment boom. What Britain really needs now is another stimulus,” <http://search.proquest.com/docview/759371294>)

Advocates of austerity believe that mystically, as the deficits come down, confidence in the economy will be restored and investment will boom. For 75 years there has been a contest between this theory and Keynesian theory, which argued that spending more now, especially on public investments (or tax cuts designed to encourage private investment) was more likely to restore growth, even though it increased the deficit. The two prescriptions could not have been more different. Thanks to the IMF, multiple experiments have been conducted - for instance, in east Asia in 1997-98 and a little later in Argentina - and almost all come to the same conclusion: the Keynesian prescription works. Austerity converts downturns into recessions, recessions into depressions. The confidence fairy that the austerity advocates claim will appear never does, partly perhaps because the downturns mean that the deficit reductions are always smaller than was hoped. Consumers and investors, knowing this and seeing the deteriorating competitive position, the depreciation of human capital and infrastructure, the country's worsening balance sheet, increasing social tensions, and recognising the inevitability of future tax increases to make up for losses as the economy stagnates, may even cut back on their consumption and investment, worsening the downward spiral. No business with a potential for making investments yielding high returns would pass up the opportunity to make these investments if it could get access to capital at very low interest rates. But this is what austerity means for the UK.

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Stop

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#### Deficit increase is the only way to stimulate investment

Malcolm Sawyer, Professor Emeritus of Economics at Leeds University Business School, May 2012, “Fiscal austerity: the cure that makes the patient worse,” <http://classonline.org.uk/docs/2012.05.20_Malcolm_Sawyer_-_the_cure_that_makes_the_patient_worse.pdf>

The present challenge is how to stimulate investment (and of the ‘right sort’) – the return of the ‘confidence fairy’ cannot be relied upon, nor can the false optimism of the OBR/Treasury macroeconometric forecasting. Low interest rates and quantitative easing have had little, if any, effect on investment. The direct way to stimulate investment is by the expansion of public investment – taken with the evidence that public investment can itself stimulate additional private investment⁷. Let us though be clear – the stimulation of investment, whether public or private, is likely to require effectively an increase in the budget deficit. The funding of the Green Investment Bank is a clear example of this. The increase can be masked by institutional and accounting practices which place the borrowing ‘off balance sheet’ – through, for example, creation of a State Investment Bank which borrows from the financial markets (along the lines of the European Investment Bank). But borrowing from a State backed institution is still needed. Insofar as the stimulation of investment is viewed as a boost to demand while the economy is recovering from recession and not a permanent increase in borrowing and in the budget deficit, it should not be included in the calculation of the structural budget deficit.

#### No risk that austerity improves confidence – spending is key

Paul Krugman, Nobel Prize Winner for Economics, Professor of Economics and International Affairs at Princeton, 7-1-10, “Myths of Austerity,” <http://www.nytimes.com/2010/07/02/opinion/02krugman.html?_r=1&ref=paulkrugman>

Which brings me to the subject of today’s column. For the last few months, I and others have watched, with amazement and horror, the emergence of a consensus in policy circles in favor of immediate fiscal austerity. That is, somehow it has become conventional wisdom that now is the time to slash spending, despite the fact that the world’s major economies remain deeply depressed. This conventional wisdom isn’t based on either evidence or careful analysis. Instead, it rests on what we might charitably call sheer speculation, and less charitably call figments of the policy elite’s imagination — specifically, on belief in what I’ve come to think of as the invisible bond vigilante and the confidence fairy. Bond vigilantes are investors who pull the plug on governments they perceive as unable or unwilling to pay their debts. Now there’s no question that countries can suffer crises of confidence (see Greece, debt of). But what the advocates of austerity claim is that (a) the bond vigilantes are about to attack America, and (b) spending anything more on stimulus will set them off. What reason do we have to believe that any of this is true? Yes, America has long-run budget problems, but what we do on stimulus over the next couple of years has almost no bearing on our ability to deal with these long-run problems. As Douglas Elmendorf, the director of the Congressional Budget Office, recently put it, “There is no intrinsic contradiction between providing additional fiscal stimulus today, while the unemployment rate is high and many factories and offices are underused, and imposing fiscal restraint several years from now, when output and employment will probably be close to their potential.” Nonetheless, every few months we’re told that the bond vigilantes have arrived, and we must impose austerity now now now to appease them. Three months ago, a slight uptick in long-term interest rates was greeted with near hysteria: “Debt Fears Send Rates Up,” was the headline at The Wall Street Journal, although there was no actual evidence of such fears, and Alan Greenspan pronounced the rise a “canary in the mine.” Since then, long-term rates have plunged again. Far from fleeing U.S. government debt, investors evidently see it as their safest bet in a stumbling economy. Yet the advocates of austerity still assure us that bond vigilantes will attack any day now if we don’t slash spending immediately. But don’t worry: spending cuts may hurt, but the confidence fairy will take away the pain. “The idea that austerity measures could trigger stagnation is incorrect,” declared Jean-Claude Trichet, the president of the European Central Bank, in a recent interview. Why? Because “confidence-inspiring policies will foster and not hamper economic recovery.” What’s the evidence for the belief that fiscal contraction is actually expansionary, because it improves confidence? (By the way, this is precisely the doctrine expounded by Herbert Hoover in 1932.) Well, there have been historical cases of spending cuts and tax increases followed by economic growth. But as far as I can tell, every one of those examples proves, on closer examination, to be a case in which the negative effects of austerity were offset by other factors, factors not likely to be relevant today. For example, Ireland’s era of austerity-with-growth in the 1980s depended on a drastic move from trade deficit to trade surplus, which isn’t a strategy everyone can pursue at the same time. And current examples of austerity are anything but encouraging. Ireland has been a good soldier in this crisis, grimly implementing savage spending cuts. Its reward has been a Depression-level slump — and financial markets continue to treat it as a serious default risk. Other good soldiers, like Latvia and Estonia, have done even worse — and all three nations have, believe it or not, had worse slumps in output and employment than Iceland, which was forced by the sheer scale of its financial crisis to adopt less orthodox policies. So the next time you hear serious-sounding people explaining the need for fiscal austerity, try to parse their argument. Almost surely, you’ll discover that what sounds like hardheaded realism actually rests on a foundation of fantasy, on the belief that invisible vigilantes will punish us if we’re bad and the confidence fairy will reward us if we’re good. And real-world policy — policy that will blight the lives of millions of working families — is being built on that foundation.

AT: Confidence

#### Investor confidence is resilient

Tymoigne 10 Eric Tymoigne, Ph.D. is Assistant Professor of Economics at Lewis and Clark College and Research Associate at The Levy Economics Institute, 7/30/10, “The CBO’s Misplaced Fear of a Looming Fiscal Crisis,” Wall Street Pit, http://wallstreetpit.com/37891-the-cbos-misplaced-fear-of-a-looming-fiscal-crisis

A government with a sovereign currency (i.e. one that creates its own currency by fiat, only issues securities denominated in its own currency and does not promise to convert its currency into a foreign currency under any condition) does not face any liquidity or solvency constraints. All spending and debt servicing is done by crediting the accounts of the bond holders (be they foreign or domestic) and a monetarily-sovereign government can do that at will by simply pushing a computer button to mark up the size of the bond holder’s account (see Bernanke attesting to this here). In the US, financial market participants (forget about the hopelessly misguided international “credit ratings”) recognize this implicitly by not rating Treasuries and related government-entities bonds like Fannie and Freddie. They know that the US government will always pay because it faces no operational constraint when it comes to making payments denominated in a sovereign currency. It can, quite literally, afford to buy anything for sale in its own unit of account. This, of course, as many of us have already stated, does not mean that the government should spend without restraint. It only means that it is incorrect to state that government will “run of out money” or “burden our grandchildren” with debt (which, after all, allows us to earn interest on a very safe security), arguments that are commonly used by those who wish to reduce government services. These arguments are not wholly without merit. That is, there may well be things that the government is currently doing that the private economy could or should be doing. But that is not the case being made by the CBO, the pundits or the politicians. They are focused on questions of “affordability” and “sustainability,” which have no place in the debate over the proper size and role for government (a debate we would prefer to have). So let us get to that debate by recognizing that there is no operational constraint – ever – for a monetarily sovereign government. Any financial commitments, be they for Social Security, Medicare, the war effort, etc., that come due today and into the infinite future can be made on time and in full. Of course, this means that there is no need for a lock box, a trust fund or any of other accounting gimmick, to help the government make payments in the future. We can simply recognize that every government payment is made through the general budget. Once this is understood, issues like Social Security, Medicare and other important problems can be analyzed properly: it is not a financial problem; it is a productivity/growth problem. Such an understanding would lead to very different policies than the one currently proposed by the CBO (see Randy’s post here).

### AT: Unsustainable

#### Stimulus is self-financing

Dennis Leech, Faculty, Department of Economics, University of Warwick, April 2012, “Fiscal Stimulus Improves Solvency in a Depressed Economy,” <http://www2.warwick.ac.uk/fac/soc/economics/staff/academic/leech/multiplier.pdf>

The Keynesian argument for a fiscal stimulus to a depressed economy either by an injection of government spending or a tax cut has been dismissed too readily by some on the grounds that it increases borrowing. We are told that the policy would simply make a bad debt problem worse: that the extra output induced by the stimulus will not yield sufficient additional tax revenue to pay for the extra government spending or to finance the tax cut because the multiplier effect described by Keynes in the *General Theory* is too weak.

However, this view is too pessimistic for two reasons. First, in general, what Is impor­tant is not the absolute level of debt but its level relative to gross domestic product: it is the debt/GDP ratio that is the key indicator of solvency. This means that in deciding on the efficacy or otherwise of a stimulus package it Is necessary to consider the magnitude of both components of this ratio and determine their net effect. When this is done, a different picture emerges. Secondly, in any case, there is growing evidence that the multiplier effect in a depressed economy might be more substantial than we sometimes allow. There are grounds for believing that the fiscal multipliers built into existing econometric models are underestimates for present conditions. There is even strong evidence to suggest that, with output well below capacity and interest rates near the zero lower bound, certain types of stimulus might be strong enough to be self-financing.

### AT: Downgrade

#### **Empirics prove – no impact to a downgrade**

Bloomberg 2012 (“Downgrade Anniversary Shows Investors Gained Buying U.S.,” 7/16/2012, <http://www.bloomberg.com/news/2012-07-16/downgrade-anniversary-shows-investors-gained-buying-u-s-.html> )hhs-ps

When [Standard & Poor’s](http://topics.bloomberg.com/standard-%26-poor%27s/) downgraded the U.S. government’s [credit rating](http://topics.bloomberg.com/credit-rating/) in August, predictions of serious fallout soon followed. Republican presidential candidate Mitt Romney described it as a “meltdown” reminiscent of the economic crises of[Jimmy Carter](http://topics.bloomberg.com/jimmy-carter/)’s presidency. He warned of higher long-term[interest rates](http://topics.bloomberg.com/interest-rates/) and damage to foreign investors’ confidence in the U.S. U.S. House Budget Committee Chairman [Paul Ryan](http://topics.bloomberg.com/paul-ryan/) said the government’s loss of its AAA rating would raise the cost of mortgages and car loans. Mohamed El-Erian, chief executive officer of Pacific Investment Management Co., said over time the standing of the dollar and U.S. financial markets would erode and credit costs rise “for virtually all American borrowers.” They were wrong. Almost a year later, [mortgage rates](http://topics.bloomberg.com/mortgage-rates/)have dropped to record lows, the government’s borrowing costs have eased, the dollar and the benchmark S&P stock index are up, and global investors’ enthusiasm for Treasury debt has strengthened. “The [U.S. Treasury](http://topics.bloomberg.com/u.s.-treasury/) is still the widest, deepest and most actively traded in the world,” said Jeffrey Caughron, a partner at Baker Group LP in Oklahoma City, which advises community banks on investments of more than $40 billion. “That becomes all the more important when you have signs of weakening global economic growth and continued problems in Europe.” Even in a slow recovery, the U.S. has unparalleled assets in the global market, including the size and resilience of its economy and the dollar’s standing as the world’s reserve currency. Low Treasury yields show that most investors think the U.S. government will meet its obligations, no matter how dysfunctional the political climate becomes in Washington.

#### Cuts cause downgrade – falling exports – and credit ratings are unreliable anyway

Malcolm Sawyer, Professor Emeritus of Economics at Leeds University Business School, May 2012, “Fiscal austerity: the cure that makes the patient worse,” <http://classonline.org.uk/docs/2012.05.20_Malcolm_Sawyer_-_the_cure_that_makes_the_patient_worse.pdf>

The ‘fear of the credit rating agencies’ argument is a convenient scare tactic and needs to be critically examined. It may first be noted that the credit rating of a government should be based on the ability of that government to service its debt. It is well-known that a government can always service debt provided that it is denominated in its own currency. At the limit the UK government can ‘print the money’ in order to service the debt: this would not take form of literally ‘printing money’ but rather the Central Bank being a willing purchaser of government debt in exchange for money. Second, the credibility of a programme designed to reduce a structural budget deficit cannot only be judged by the perceived commitment of the government to make public expenditure cuts and raise taxes. An achieved reduction of the budget deficit requires, as a matter of an accounting identity, some combination of a rise in the balance between private investment and savings and a rise in net exports (exports minus imports). Fiscal austerity threatens to bring that about through a decline in output and income which depresses savings and imports. The government’s hope (the return of the ‘confidence fairy’) is for a boom in investment and exports, which finds support in the forecasts of the Office for Budget Responsibility. But (as argued in Fontana and Sawyer, 2011, 2012) those forecasts are close to incredible. “The Office for Budget Responsibility's forecast of a return to growth next year, driven by a surge in investment and exports, has looked absurd for months. The idea that business investment will jump 40% by 2015/16, the biggest since 1945, is risible” (Hutton, 2012). Third the reputation and judgement of the credit rating agencies had been severely undermined by their roles in the build-up to the financial crisis. An oft-quoted example has been the degree to which triple A ratings were given to mortgage backed securities and credit default swaps. This would not deny that in the event of the credit ratings agencies downgrading government debt the government concerned could well be faced with higher interest charges and difficulties in borrowing, as funds are moved from that government’s debt to others. But what is questioned is the basis on which the ratings are made, and what actions by a government would lead to a downgrade.

#### No one trusts them – downgrade wouldn’t be perceived

Bloomberg News 6-18, <http://www.bloomberg.com/news/2012-06-18/austerity-doesn-t-pay-as-debt-markets-ignore-rating-cuts.html>

Moody’s and S&P were already controversial after they helped fuel a global housing bubble by awarding AAA scores to subprime mortgage investments, creating demand for the flawed issues, which led to more bad mortgages being made. The rating companies engaged in a “race to the bottom,” inflating credit grades to win business from Wall Street banks, a Senate panel reported last year. Thousands of these bonds plunged in value in 2008, which led to worst financial crisis since the Great Depression. Those soured securities were part of the reason the U.S. set up a $700 billion program in 2008 to bolster the financial industry. The crisis also spurred $787 billion of tax cuts and spending to help the [U.S. economy](http://topics.bloomberg.com/u.s.-economy/). The U.K. created a 500 billion pound package to rescue its banks, and the European Union started a 200 billion euro ($252 billion) stimulus program. Now, after governments widened their deficits to stem the crisis, their credit grades are under pressure from the same rating companies whose actions helped cause the financial turmoil. “How do you have any faith in them given they were part problem?” Blanchflower said.

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**Investors will still come to the US first –financial crisis in Europe makes US a safe zone for investments**

Bloomberg 2012 (“Downgrade Anniversary Shows Investors Gained Buying U.S.,” 7/16/2012, <http://www.bloomberg.com/news/2012-07-16/downgrade-anniversary-shows-investors-gained-buying-u-s-.html> )hhs-ps

We are a safe haven for now” for investors because of Europe’s debt crisis, Ryan said in an interview. Rates will rise, he predicted. “We just don’t know when, and I don’t want to tempt fate.” El-Erian of Newport Beach, California-based Pimco, which oversees the world’s biggest bond fund, didn’t respond to a request for comment. Terry Belton, global head of fixed-income and foreign- exchange research at JPMorgan Chase & Co. in New York, said on a July 26, 2011, conference call that a downgrade could boost Treasury yields by as much as 70 basis points in the intermediate term and increase the government’s borrowing costs by $100 billion a year. A basis point is 0.01 percentage point. Instead, the U.S. is on track to pay less interest this year. U.S. Treasury securities paid $454 billion of interest last year, [according](http://www.treasurydirect.gov/govt/reports/ir/ir_expense.htm) to the [Congressional Budget Office](http://topics.bloomberg.com/congressional-budget-office/). That’s projected to decline to $442 billion this year and won’t climb above the 2011 cost level until 2015, according to CBO forecasts. Credit Quality Weakening U.S. credit quality, such that the nation more resembles a AA rated borrower, is still likely to drive up 10- year yields by about 60 basis points over time, JPMorgan’s Belton said in a recent interview. “Yield changes during the last year had nothing to do with the downgrade, but it had to do with everything else pushing yields lower,” Belton said. “On the top of that list you have a massive flight to quality out of Europe, and the U.S. is a safe haven.” Investors outside the U.S. owned $5.16 trillion of U.S. government debt as of April 30, compared with $4.7 trillion at the end of July 2011 before the credit-rating cut. “The one thing the Treasury market has above any other government bond market is liquidity,” [Stuart Thomson](http://topics.bloomberg.com/stuart-thomson/), a money manager in Glasgow at Ignis Asset Management, which oversees the equivalent of $109 billion, said in a June 22 interview. “That liquidity premium is not going to disappear no matter how many downgrades Moody’s or S&P give to it.” Bidders offered $3.16 for each dollar of the $1.075 trillion of notes and bonds [auctioned](http://www.bloomberg.com/quote/USN10YBC:IND)by the Treasury Department this year as of July 2, as yields reached all-time lows, above the previous high of $3.04 in all of 2011, according to data compiled by Bloomberg. The so-called bid-to-cover ratio was 2.26 from 1998 to 2001 when the nation ran budget surpluses.

#### Downgrades have no effect

Jeff Poor, Daily Caller, 05/19/’12, [lKrauthammer: U.S. facing credit rating ‘downgrade’ if Obama reelected, <http://dailycaller.com/2012/05/19/krauthammer-u-s-facing-credit-rating-downgrade-if-obama-reelected/#ixzz21AfMp38X>] VN

In this weekend’s broadcast of “Inside Washington,” Washington Post columnist Charles Krauthammer explained the impact the upcoming presidential election will have on the country’s fiscal situation, particularly its credit rating. Last August, the United States lost its AAA credit rating from Standard & Poor’s and was downgraded to AA+, after Congress broke a stalemate and agreed to spending cuts that would reduce the debt by over $2 trillion. Krauthammer said the U.S. could suffer another downgrade if President Barack Obama is reelected. “No, but I think if we reelect Obama, we will have a downgrade, probably a default — something like a default, not a real default,” Krauthammer said. “But we’re going to head that way, obviously, because you can’t sustain trillion dollar deficits as far as the eye can see.” The Washington Post columnist went on to explain why the debt ceiling fight won’t be the cause of any such downgrade. “So a downgrade will come, but not over a debt ceiling thing, for the following reason: If Romney wins, this is a moot issue,” he said. “There’s not going to be a showdown. If Obama wins, it’s also a moot issue, because we’re going to be dealing with 18 other issues — the expiration of the Bush tax cuts, of the payroll tax, there’s going to be a tsunami of taxes and an increase in spending, as well. So, that’s going to be a minor issue. I think the reason [House Speaker John] Boehner raised it is to make it an issue. It’s a rhetorical issue. It’s only going to happen after Election Day, so it’s not going to have any effect on the real world.”

#### Downgrades have no effect

Mike Dorning, John Detrixhe and Ian Katz, Bloomberg Press, 07/16/’12, [Downgrade Anniversary Shows Investors Gained Buying U.S., <http://www.bloomberg.com/news/2012-07-16/downgrade-anniversary-shows-investors-gained-buying-u-s-.html>] VN

More Entrenched Because the consequences that had been forecast for a downgrade haven’t occurred, lawmakers may become more entrenched in their positions in the next standoff over fiscal policy, approaching at the end of the year. The threat of a downgrade has lost some of its power, said Steve Bell, a former Republican staff director for the Senate Budget Committee. “You cried wolf, and no wolf appeared,” said Bell, who’s now a senior director at the Bipartisan Policy Center in Washington. “It has persuaded a fair number of members of Congress that the effect of a downgrade is overstated and it will not lead to some serious economic or financial problem.”

AT: Downgrade

#### **Downgrade doesn’t affect consumer confidence or investments – consumer climate IMPROVED after the S&P downgrade**

Bloomberg 2012 (“Downgrade Anniversary Shows Investors Gained Buying U.S.,” 7/16/2012, <http://www.bloomberg.com/news/2012-07-16/downgrade-anniversary-shows-investors-gained-buying-u-s-.html> )hhs-ps

Standard & Poor’s lowered the U.S. credit rating after months of wrangling last year between President [Barack Obama](http://topics.bloomberg.com/barack-obama/) and congressional Republicans over whether to raise the federal debt limit. Though the impasse ended with Obama signing a [debt- ceiling](http://www.bloomberg.com/quote/PUBLDEBT:IND)increase on Aug. 2, S&P downgraded the U.S three days later, citing political gridlock in Washington and the nation’s long-term fiscal challenges. Treasuries responded by staging the biggest rally since December 2008, returning 2.8 percent that month as investors repudiated the decision. Yields on Treasuries due in 10 years have fallen 1.07 percentage point since the downgrade and have touched all-time lows, dropping to 1.44 percent on June 1. U.S. government bond prices, which move in inverse proportion to yields, have soared, such that the securities have gained 7 percent since Aug. 5 after returning 9.8 percent in 2011, their best performance since 2008, Bank of America Merrill Lynch index data show. Big Returns As a result, the naysayers would have earned about $8.59 million on a $100 million investment in Treasuries maturing in five to 10 years had they started a trade the day the U.S. was downgraded, according to the Merrill Lynch index data. Hedge funds worldwide have lost about 5.8 percent during that span, which would amount to a $5.8 million loss on a $100 million investment through the end of June, according to the Bloomberg Global Aggregate Hedge fund [index](http://www.bloomberg.com/quote/BBHFUNDS:IND). Almost half the time, yields on government bonds fall when a rating action by S&P and Moody’s suggests they should climb, according to data compiled by Bloomberg on 314 upgrades, downgrades and outlook changes going back as far as the 1970s. The rally showed the downgrade “was a mistake,” [Alan Blinder](http://topics.bloomberg.com/alan-blinder/), a [Princeton University](http://topics.bloomberg.com/princeton-university/)professor and former Federal Reserve Board vice chairman, said in a July 2 interview in New York. “The U.S. Treasury is still at the top of the heap.” Consumer Borrowing Consumer borrowing costs have also dropped. Home loan rates for 30-year U.S. mortgages on July 12 fell to a record low for a fourth straight week. The average rate for a 30-year fixed mortgage [declined](http://www.bloomberg.com/quote/NMCMFUS:IND) to 3.56 percent in the week ended July 12, the lowest in Freddie Mac records dating to 1971. In the week ended Aug. 4, 2011, immediately before the downgrade, the average rate was 4.39 percent. IntercontinentalExchange Inc.’s Dollar Index, which tracks the greenback against the currencies of six major U.S. trading partners, has climbed about 12 percent since S&P’s Aug. 5 downgrade, as of July 13. The S&P 500 stock index has [returned](http://www.bloomberg.com/quote/SPX:IND) 15.6 percent, including reinvested dividends. The U.S. attraction for global investors has strengthened. In May, 46 percent of international investors chose the U.S. as the market with the most potential during the next year, up from 31 percent a year earlier, according to a Bloomberg poll.

AT: Downgrade

#### Downgrade has no discernible effect on markets

Bloomberg News 6-18, <http://www.bloomberg.com/news/2012-06-18/austerity-doesn-t-pay-as-debt-markets-ignore-rating-cuts.html>

It’s not just Britain. After [Standard & Poor’s](http://topics.bloomberg.com/standard-%26-poor%27s/) stripped France and the U.S. of AAA grades, [interest rates](http://topics.bloomberg.com/interest-rates/) paid by the countries to finance their deficits dropped rather than rose. For investors and policy makers, predicting the consequences of a rating change by S&P or Moody’s -- the dominant issuers of debt scores -- may be little different from flipping a coin. (For an interactive graphic, click [here](http://go.bloomberg.com/multimedia/sovereign-debt-ratings/).) Almost half the time, government bond yields fall when a rating action suggests they should climb, or they increase even as a change signals a decline, according to data compiled by Bloomberg on 314 upgrades, downgrades and outlook changes going back as far as 38 years. The rates moved in the opposite direction 47 percent of the time for Moody’s and for S&P. The data measured yields after a month relative to U.S. Treasury debt, the global benchmark. The rating companies are still warning of downgrades while defending their assessments against critics. Moody’s said June 8 that all sovereign ratings in Europe would be reviewed, including Germany’s Aaa, if Greece leaves the region’s monetary union. The credit standings of Cyprus, Portugal, Ireland, Italy and Spain are deteriorating, the company said. The U.S. may have another downgrade by 2014, S&P said June 8.

### 2AC — AT: Crowdout

#### Their author concedes that infrastructure spending eventually boosts the private sector

Daniel Mitchell, Senior Fellow at the Cato Institute, 2-1-10, <http://www.cato.org/publications/commentary/spending-our-way-stagnation>

Interestingly, a large body of academic work attempts to measure the growth-optimizing level of government. This research is based on the notion there is not much prosperity in a state of anarchy. Governments solve this problem by imposing the rule of law (courts, police protection, etc). Those governmental functions cost money, but they yield big benefits. Moreover, government spending on "public goods" such as basic infrastructure also can facilitate the functioning of a market economy.

#### Spending expands demand – excess savings mean it doesn’t crowd out privates

Paul Krugman, Nobel Prize Winner for Economics, Professor of Economics and International Affairs at Princeton, 5-2-09, <http://krugman.blogs.nytimes.com/2009/05/02/liquidity-preference-loanable-funds-and-niall-ferguson-wonkish/>

In any case, I thought it might be useful to re-explain why our current predicament can be thought of as a global excess of desired savings — which means that fiscal deficits won’t drive up interest rates unless they also expand the economy. Here’s what I imagine Niall Ferguson was thinking: he was thinking of the interest rate as determined by the supply and demand for savings. This is the “loanable funds” model of the interest rate, which is in every textbook, mine included. It looks like this: where S is savings, I investment spending, and r the interest rate. What Keynes [pointed out](http://krugman.blogs.nytimes.com/2009/02/23/liquidity-preference-versus-loanable-funds-televised-wonkish-with-video/?scp=1&sq=keynes%20diagram&st=cse) was that this picture is incomplete if you allow for the possibility that the economy is not at full employment. Why? Because saving and investment depend on the level of GDP. Suppose GDP rises; some of this increase in income will be saved, pushing the savings schedule to the right. There may also be a rise in investment demand, but ordinarily we’d expect the savings rise to be larger, so that the interest rate falls: So supply and demand for funds doesn’t tell you what the interest rate is — not by itself. It tells you what the interest rate would be conditional on the level of GDP; or to put it another way, it defines a relationship between the interest rate and GDP, like this: This is the IS curve, taught in Econ 101. Now, we usually explain how this curve is derived in a different way: we say that given the interest rate, you can determine investment demand, and then through the multiplier process this determines GDP. What you’re supposed to understand, however, is that the derivation I’ve just given is just a different way of arriving at the same result. It’s just different presentations of the same model. So what determines the level of GDP, and hence also ties down the interest rate? The answer is that you need to add “liquidity preference”, the supply and demand for money. In the modern world, we often take a shortcut and just assume that the central bank adjusts the money supply so as to achieve a target interest rate, in effect choosing a point on the IS curve. Which brings us to the current state of affairs. Right now the interest rate that the Fed can choose is essentially zero, but that’s not enough to achieve full employment. As shown above, the interest rate the Fed would like to have is negative. That’s not just what I say, by the way: the FT reports that the [Fed’s own economists](http://www.ft.com/cms/s/0/23b62bfc-338b-11de-8f1b-00144feabdc0.html) estimate the desired Fed funds rate at -5 percent. What does this situation look like in terms of loanable funds? Draw the supply and demand for funds that would obtain if we were at full employment. They look like this: In effect, we have an incipient excess supply of savings even at a zero interest rate. And that’s our problem. So what does government borrowing do? It gives some of those excess savings a place to go — and in the process expands overall demand, and hence GDP. It does NOT crowd out private spending, at least not until the excess supply of savings has been sopped up, which is the same thing as saying not until the economy has escaped from the liquidity trap. Now, there are real problems with large-scale government borrowing — mainly, the effect on the government debt burden. I don’t want to minimize those problems; some countries, such as Ireland, are being forced into fiscal contraction even in the face of severe recession. But the fact remains that our current problem is, in effect, a problem of excess worldwide savings, looking for someplace to go.

AT: Crowdout

#### No crowd-out – their theory assumes full employment

Robert Skidelsky, Professor Emeritus of Political Economy at Warwick University, 11-22-10, “The relevance of Keynes,” *Cambridge Journal of Economics* Vol. 1, <http://www.relooney.info/0_New_8976.pdf>

Keynes riposted: ‘Mr. Baldwin has invented the formidable argument that you must not do anything because it means you will not be able to do anything else’. Yet the Treasury argument of 1929 was restated in 2009, in almost identical terms, by Professor John Cochrane of Chicago University: If money is not going to be printed, it has to come from somewhere. If the government borrows a dollar from you, that is a dollar that you do not spend, or that you do not lend to a company to spend on new investment. Every dollar of increased government spending must correspond to one less dollar of private spending. Jobs created by stimulus spending are offset by jobs from the decline of private spending. We can build roads instead of factories, but ﬁscal stimulus can’t help us to build more of both. (Cochrane, 2009) This is equivalent to saying that a market economy will be always be at full employment, i.e. that the multiplier is zero. The policy implication of this argument is that the ﬁscal stimulus was a mistake and should be withdrawn as soon as possible in order to create room for private spending. And this has been the almost unanimous theme of conservative politicians and commentators. The increasing pressure for ﬁscal retrenchment ignores the fact that enlarged government deﬁcits are an automatic consequence, not a cause, of a fall in aggregate demand and will shrink automatically (though not fully) as aggregate demand recovers. Government spending to put the unemployed to work is not taking away employment from those already in work: it is adding to the amount of employment. In 1932, Keynes wrote: ‘The voices which—in such a conjuncture—tell us that the path of escape is to be found in strict economy and in refraining, wherever possible, from utilizing the world’s potential production, are the voices of fools and madmen’ (Keynes, 1982, p. 61).

#### Austerity kills growth – that discourages the private sector

Malcolm Sawyer, Professor Emeritus of Economics at Leeds University Business School, May 2012, “Fiscal austerity: the cure that makes the patient worse,” <http://classonline.org.uk/docs/2012.05.20_Malcolm_Sawyer_-_the_cure_that_makes_the_patient_worse.pdf>

When we say austerity does not work, we mean that austerity does not lead to the reduction in budget deficit on the scale envisaged (as we indicate below, the reduction in budget deficit is likely to be of the order of at most one third of the reduction in public expenditure). Austerity does not cause a revival in the economy. Austerity will not bring growth, though growth will bring a lower budget deficit. If growth of private sector demand revives, then the budget deficit will decline. But austerity itself does nothing to bring about that revival of private demand, and indeed is more likely to hold it back. When Nick Clegg says that “Austerity alone does not create growth…It is a necessary but not sufficient step”², he is wrong – austerity kills growth, and is certainly not necessary.

### 2AC — AT: Map-21

Map-21 is just stopgap legislation

Rall and Hughes, 7/24 [2012, Chris and Richard “Guest Viewpoint: Transportation bill is step in the wrong direction” registerguard.com, http://www.registerguard.com/web/opinion/28417143-47/transportation-bill-oregon-funding-bridges.html.csp]

The Register-Guard is right to express disappointment in the federal transportation bill signed into law on July 6 (“At last, a highway bill: It’s flawed but buys time to create better policy,” editorial, July 3). Moving Ahead for Progress in the 21st Century, or MAP-21, is a misnomer for this stopgap legislation, which represents the last gasp of a 20th century approach. Traffic is declining nationally. The trend is stronger in Oregon and among young people and has continued through periods of economic growth and recession (since 2002 in Oregon). Lane County residents are driving 7 percent fewer miles total than they were 10 years ago, even as the population has grown by 9 percent. Transit ridership, biking and walking are all up, and cities are now growing faster than the exurbs. Young people today are the first generation less likely than their parents to have a driver’s license. That evidence all points to a structural shift in where we live and how we get around — a shift that calls for a change in transportation investments. We need to maintain roads and bridges rather than building expensive new ones. If we are going to invest, it should be in the gaps in our transportation system: better transit, more biking and walking routes, and rail. Instead, after three years of development and negotiations, this disappointing last-minute, closed-door deal does little more than avoid a shutdown. The Senate had produced a bipartisan, forward-looking bill with important reforms. However, it seems that Senate negotiators abandoned many reforms in favor of regressive House changes, simply to get a bill and keep Canada’s Keystone XL pipeline and coal ash regulation out of the final deal. For the first time since the program began in 1956, the House attempted to develop a purely partisan transportation bill, refusing to tap the expertise of leading Democratic transportation committee members ,such as Oregon Congressman Peter DeFazio. Because of the extreme provisions in its proposal, House Resolution 7, the House never was able to pass long-term legislation. Despite the fact that House negotiators came to the conference committee with nothing more than a three-month extension, they won major concessions from the Senate and inserted many HR 7 provisions — as if it actually had passed. The resulting transportation bill takes a major step backward on accountability in how transportation funding is spent. The deal hands states a blank check without proper assurances that roads will get safer, traffic congestion will improve, people can get to work or bridges will get fixed. The bill increases funding for major highways while eliminating dedicated funding for bridge and road repair, and it limits the ability of states to spend their highway funding on fixing roads and bridges that aren’t part of the national highway system. That will shift responsibility for fixing these roads and bridges to a smaller pot of flexible funding that could be used for transit, bicycle and pedestrian projects. Local communities now may face difficult choices about whether to spend their pots of funding on innovative projects or on a local bridge that in the past could have been fixed using the money given to the state for highways. The pressure is compounded by changes to the tiny sliver of funds that traditionally make biking and walking safer for school kids, commuters and older Americans. These dedicated funds for key safety projects — such as pedestrian crossings on deadly East Main Street in Springfield, the Alder Street Cycletrack in Eugene and safety education programs for kids — were cut by about 45 percent for Oregon. Despite the shortcomings of this new law, there is still a lot we can do to ensure that we make smart transportation investments in Oregon. We need to hold the Oregon Department of Transportation and other transportation decision-makers accountable to use the flexibility in the new bill to achieve Oregon’s goals: economic competitiveness, energy security, and safe and efficient movement of people and goods. Because this bill expires in September 2014, we will have the opportunity soon enough to support our delegation’s work for a transportation bill that re­al­ly does move us ahead. Chris Rall is an organizer with Transportation for America, a coalition working on transportation reform. Richard Hughes is president of Greater Eugene Area Riders, a group that promotes bicycling for transportation and recreation.

Map-21 continues existing funding – industry officials want more

Engineering News-Record, 7/9 [2012“Obama Signs $104B Highway-Transit Bill”] LexisNexis

Ending more than 33 months of transportation funding via stopgap bills, President Obama has signed into law a new $104-billion highway and transit authorization measure. With key lawmakers as well as construction and transportation group leaders in attendance, Obama signed the long-delayed bill on July 6 in a brief ceremony in the East Room of the White House. The measure—titled MAP-21, for Moving Ahead for Progress in the 21st Century—funds surface-transportation programs through September 2014. The new statute's roughly 27-month span gives state agencies and construction-industry companies more of the funding certainty they have sought to plan and launch road, bridge and transit projects. Final congressional approval of the bill came on June 29, when the House passed the measure on a 373-52 vote and, soon after that, the Senate cleared the bill, 74-19. To keep federal transportation funds flowing until the enactment date, the president on June 29 signed a one-week highway-transit authorization. It was the 10th in a series of extensions since Sept. 30, 2009, when the last long-term highway-transit statute lapsed. The latest stopgap was needed because the previous one was due to expire on June 30. Construction and transportation industry officials, who have lobbied hard since at least 2009 to get a long-term bill, hailed the bill's enactment. But already they are thinking ahead to further legislation. American Road &mp; Transportation Builders Association Chairman Paul Yarossi and the association's CEO, Peter Ruane, said they were forming an ARTBA task force to seek additional federal transportation funds, beyond the amount MAP-21 provides, in any comprehensive budget and tax measure Congress may take up. Yarossi also is president of design firm HNTB Holdings Ltd. MAP-21's path to passage was long and rough. The final version represents a compromise between the $109-billion, two-year bill that the Senate approved in March and the three-month bill—including significant non-transportation provisions—that the House passed in April. In the final negotiating push, the House agreed to drop the non-transportation items, including language to direct quick U.S. approval for the Keystone XL oil pipeline and a provision that would block the Environmental Protection Agency from regulating coal ash as a hazardous waste. The Senate agreed to drop language providing aid for the Land and Water Conservation Fund. Along with its highway and transit funding, the legislation includes provisions that mandate important changes in surface-transportation policy, including steps to accelerate highway and transit project approval and sharply reduce the number of federal surface-transportation programs and funding categories. MAP-21 also gives a huge funding boost to the Transportation Infrastructure Finance and Innovation Act (TIFIA) program, which provides loans and loan guarantees for major projects. Under the new bill, direct aid to TIFIA would climb to $750 million in fiscal 2013 and to $1 billion in 2014, up from $122 million a year now. TIFIA is attractive to states, localities and congressional lawmakers because each dollar of direct federal subsidy supports $10 in loan value. Thus, the $1-billion authorized for 2014 would back $10 billion in loans for projects. Project-approval «streamlining» provisions were in both the Senate- and House-passed bills. The final version moves closer to the House’s language, which was more favorable to industry. The changes are expected to halve the time for environmental and other reviews and permitting, a House GOP leadership aide says. One provision would have project reviews by multiple federal agencies done concurrently, rather than one after another. Stephen Sandherr, Associated General Contractors of America CEO, said the measure "provides the kind of serious and substantive reforms needed to make the federal program more cost-efficient and more effective at delivering needed transportation improvements." But environmental groups contended the project-review provisions go too far. Scott Slesinger, the Natural Resources Defense Council's legislative director, said the final version has "damaging and unnecessary concessions that weaken environmental reviews of highway projects—reducing public oversight and excluding some from review entirely." Another compromise came over transportation «enhancements,» such as bike paths and walkways, which have enjoyed a mandated share of highway funds. Republicans had pushed to pull back on enhancements, which, they argued, divert funds from mainstay highway and bridge projects. The final version retains the enhancements program, and renames it "transportation alternatives," but directs half the funds to local agencies. States would continue to determine how to use the other 50% of the money and have more flexibility in how to use it. Industry officials were happy and relieved to see the bill finally become law. But they also note that it does not provide a long-term prescription for fortifying the weakened Highway Trust Fund, the highway program's main federal funding source since 1956. The rise of more fuel-efficient vehicles and some slowdowns in miles traveled, because of the economic crunch, have put a crimp in the trust fund's gas-tax income.

### 2AC — AT: Fiscal Cliff

No impact to fiscal cliff

Nin-Hai Tseng, Staff Writer for CNN Money, 06/12/’12, [The fiscal cliff may look more like a fiscal slope, <http://finance.fortune.cnn.com/2012/06/12/fiscal-cliff-explainer/>] VN

Some think so. Chad Stone, chief economist at the non-partisan Center on Budget and Policy Priorities, says the fears are misplaced. In a paper released last week, he wrote that the economy won't immediately fall over a cliff and plunge into another Great Recession come January 1. Rather than rush negotiations and end up with potentially very bad policy, policymakers still have some (although limited) time to come up with a solid plan and therefore avoid another downturn. To be sure, Stone doesn't doubt the U.S. will slip into recession if lawmakers drag their feet for too long. The slated policy changes include an end to the temporary tax cuts enacted during the George W. Bush administration, as well as an end to the temporary Obama administration payroll tax reductions. If the slated changes take effect, the economy could contract by 1.3% during the first half of 2013 and grow by 2.3% during the second half, according to the Congressional Budget Office. That's scary stuff. However, it will take some time before the economy feels the weight of those changes. Stone offers a few examples, starting with the tax cuts: It's true that households might feel a pinch from an increase in taxes withheld from their weekly or monthly checks, "but taxpayers newly falling within the reach of the [Alternative Minimum Tax] in 2012 will not actually pay those higher taxes until they file their returns in subsequent months," he writes. So while the implications of a fiscal cliff are very real, it's more like a "fiscal slope," he adds. Stone's bigger point is that good policymaking takes time. If lawmakers go past the fiscal cliff by a few weeks or a month, the economy would be okay.

Fiscal cliff won’t make the economy any worse

Heidi N. Moore, Marketplace Economy Staff, 06/07/’12, [Is the U.S. headed off a fiscal cliff?, <http://www.marketplace.org/topics/economy/us-headed-fiscal-cliff>] VN

Ryssdal: So pick your geographic feature -- is it really a cliff, or a slope? I mean, what's it going to be? Moore: Yeah, you can call it a canyon, a gully, a ditch -- I mean, the question is: Are we going to bungee jump off this thing or what, right? The key problem, as you mentioned, is the spending cuts and the tax cuts that start at the beginning of 2013. So Congress has until basically the beginning of the year to deal with that. And the problem is, there's problems with calling it a cliff. We know it's happening in January, but look around: We already have problems, we have high unemployment, we have a weak economy. So it's not like we're falling from a really great height. And the economy doesn't run on our timetable; it's not as if like the New Year's ball is going to drop in Times Square -- Ryssdal: And boom! Moore: Right -- 'Recession! It's here!' That's not going to happen, there's going to be a lag. So I would say picture it more as a ski slope, it'll be gradually downward. Ryssdal: A bunny slope, if you will? Moore: A bunny slope, even. Except we're going to hit nothing but empty air if we don't get it right, which is more like a black diamond slope. Ryssdal: All right, well help me out then. Why was it that we've known about this cliff for a while, you look at the markets -- first of all, all day yesterday and then early today, up hundreds of points -- what's the disconnect between what's actually going to come and what Wall Street and that part of the economy thinks is happening? Moore: Sure, absolutely. Well what Wall Street wants to see is that lawmakers are paying attention. And from that montage we just heard, they definitely are -- they're obsessing about it, they're having secret meetings about it, that's really good. And the other thing that helps is that governments all over the world are thinking about a recession, and so we're not the only ones worried -- there's China, Australia, Brazil -- they all cut their interest rates. Europe has low interest rates. And people in the markets like to see that. So I talked to Gary Thayer, he's the chief macrostrategist for Wells Fargo Advisers. He said the fact that Congress is having all these secret meetings is a good sign.