

Economic Austerity or Debt Default: Choose Your Poison

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Currently the US is now over \$15 trillion in debt. [1] The national debt has now gotten to the point where it is larger than US GDP and is now unpayable. In response to this crisis, many in government have been arguing for austerity measures, yet they have not been using that actual term, rather there has been an argument for deep cuts in social spending, with one example being Paul Ryan's budget proposal which targets mainly the poor and elderly. The debt crisis may very well lead the US to being forced to choose from two poisons, austerity on one hand and default on the other.

Austerity measures are currently being pushed by the intellectual elite. Niall Ferguson argues that the main problem in Western democracies "is the huge debts we have managed to accumulate in recent decades, which – unlike in the past – cannot largely be blamed on wars" and poses the question "[W]ould young people be wise to encourage politicians to pay-off national debts now to avoid an even more miserable financial future?" [2]

In the US, Pacific Investment Management Co.'s Neel Kashkari, states that the US should "stop kicking 'the can down the road' and implement fiscal austerity measures so the economy can fully recover from the financial crisis." [3] While Ferguson states that the debt "cannot be blamed on large wars," the facts prove him to be incorrect as during the Clinton Administration there began a decrease in the national debt and ended with the US being in the black. [4] When President Bush came in, the US went back deeply into debt and this debt increase can be blamed mainly on the Afghanistan and Iraq wars.

The arguments for austerity, while they may be many, are nullified by the fact that the International Monetary Fund, the biggest advocate of austerity for so-called third world countries (and increasingly for many first-world European countries), has admitted that austerity only hurts income and worsens long-term unemployment. [5] In other words, austerity only makes a bad economic situation worse. Yet, this begs the question, if austerity doesn't work, then why are people arguing in favor of it? This question can be understood by examining the situation from the perspective of the banks. Austerity measures result in large amounts of privatization and thus allow for banks to buy up essential services such as water and electricity systems for dirt-cheap prices and then the banks can make large amounts of money from the perpetuity of state assets. Thus, the banks that gave the loans will then be able to recoup the amount of the loan and then make much more money.

Yet, austerity has more effects than just those the IMF listed. Austerity also produces "falling wages and a broadly recessionary environment that can last for decades," [6] and can result

in the near or total economic destruction of a nation. In addition to this, one only need to look at Greece which used austerity measures to see just how ineffective they are. “[T]hose massive cuts in spending have caused the Greek economy to contract, reducing its ability to pay off its debt.” [7] Thus, there is no hope that austerity will work to aid America’s current debt woes as it will only create an even worse situation where it is that much harder to lower the debt.

Concerning default, that would be even more catastrophic than austerity measures. While one may scoff at such a notion, the reality of the situation is not unrealistic as just last year the US almost defaulted while the House of Representatives battled over whether or not to raise the debt ceiling. [8] A default on US debt would have multiple, interlocking effects. Firstly, a default would trigger a high degree of risk among US treasury which would result in the disruption of many different types of contracts and all types of transactions as well as the destruction of private credit. [9] Such a crisis would force the Federal Reserve to either “step in and provide an enormous amount of credit directly to households and firms” or “stand by idly while GDP fell 20 to 30 percent.” On top of all of this, the US economy would be hit even harder by the fact that

With the private sector in free fall, consumption and investment would decline sharply. America’s ability to export would also be undermined, because foreign markets would likely be affected, and because, in any case, if export firms cannot get credit, they most likely cannot produce. [10]

Thus, default will only bring about a near or total collapse of the economy.

The US, if it wants to get its economy back on track, will have to reject both default and austerity. The first step it could take is by making the bankers pay for the economic crisis that they created rather than forcing the burden upon the populace.

notes

1: *US Debt Clock*, <http://www.usdebtclock.org/>

2: Niall Ferguson, “Viewpoint: why the younger generation should embrace austerity,” *BBC*, June 16, 2012
(<http://www.bbc.co.uk/news/world-18456131>)

3: Tom Keene, Catarina Saraiva, “U.S. Needs Austerity to Reset Economy, Pimco Official Says: Tom Keene,” *Bloomberg News*, June 8, 2012
(<http://www.bloomberg.com/news/2011-06-08/u-s-requires-austerity-to-reset-economy-pimco-s-kashkari-says-tom-keene.html>)

4: *US National Debt by Presidential Term: Per Capita and as Percentage of Gross Domestic Product*,
<http://www.skymachines.com/US-National-Debt-Per-Capita-Percent-of-GDP-and-by-Presidential-Term.htm>

5: Alexander Eichler, “IMF Report: Austerity Measures Hurt Income, Make Long-Term Unemployment Worse,” *Huffington Post*, September 13, 2011
(http://www.huffingtonpost.com/2011/09/13/imf-austerity_n_960199.html)

- 6: Rob Urie, "Who Benefits From Austerity Politics?," *Counterpunch*, November 18, 2011 (<http://www.counterpunch.org/2011/11/18/who-benefits-from-austerity-politics>)
- 7: "End of the line: What a Greek default means," *CNN Money*, June 17, 2012 (<http://finance.fortune.cnn.com/2011/06/17/end-of-the-line-what-a-greek-default-means>)
- 8: "US 'almost out of time' for debt deal: Obama," *Dawn*, July 30, 2011 (<http://dawn.com/2011/07/30/us-almost-out-of-time-for-debt-deal-obama>)
- 9: Simon Johnson, "What if the Government Defaults?," *Slate*, July, 18, 2011 (http://www.slate.com/articles/business/project_syndicate/2011/07/what_if_the_government_defaults.html)
- 10: *Slate*, July, 18, 2011

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