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## Why Obamanomics Has Failed

*Uncertainty about future taxes and regulations is enemy No. 1 of economic growth.*

By ALLAN H. MELTZER

The administration's stimulus program has failed. Growth is slow and unemployment remains high. The president, his friends and advisers talk endlessly about the circumstances they inherited as a way of avoiding responsibility for the 18 months for which they are responsible.

But they want new stimulus measures—which is convincing evidence that they too recognize that the earlier measures failed. And so the U.S. was odd-man out at the G-20 meeting over the weekend, continuing to call for more government spending in the face of European resistance.



The contrast with President Reagan's antirecession and pro-growth measures in 1981 is striking. Reagan reduced marginal and corporate tax rates and slowed the growth of nondefense spending. Recovery began about a year later. After 18 months, the economy grew more than 9% and it continued to expand above trend rates.

Two overarching reasons explain the failure of Obamanomics. First, administration economists and their outside supporters neglected the longer-term costs and consequences of their actions. Second, the administration and Congress have through

their deeds and words heightened uncertainty about the economic future. High uncertainty is the enemy of investment and growth.



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Martin Kozlowski

Most of the earlier spending was a very short-term response to long-term problems. One piece financed temporary tax cuts. This was a mistake, and ignores the role of expectations in the economy. Economic theory predicts that temporary tax cuts have little effect on spending. Unless tax cuts are expected to last, consumers save the proceeds and pay down debt. Experience with past temporary tax reductions, as in the Carter and first Bush presidencies, confirms this outcome.

Another large part of the stimulus went to relieve state and local governments of their budget deficits. Transferring a deficit from the state to the federal government changes very little. Some teachers and police got an additional year of employment, but their gain is temporary. Any benefits to them must be balanced against the negative effect of the increased public debt and the temporary nature of the transfer.

The Obama economic team ignored past history. The two most successful fiscal stimulus programs since World War II—under Kennedy-Johnson and Reagan—took the form of permanent reductions in corporate and marginal tax rates. Economist Arthur Okun, who had a major role in developing the Kennedy-Johnson program, later analyzed the effect of individual items. He concluded that corporate tax reduction was most effective.

Another defect of Obamanomics was that part of the increased spending authorized by the 2009 stimulus bill was held back. Remember the oft-repeated claim that the spending would go for "shovel ready" projects? That didn't happen, though spending will flow more rapidly now in an effort to lower unemployment and claim economic success during the fall election campaign.

In his January 2010 State of the Union address, President Obama recognized that the United States must increase exports. He was right, but he has done little to help, either by encouraging investment to increase productivity, or by supporting trade agreements, despite his promise to the Koreans that he repeated in Toronto. Export earnings are the only way to service our massive foreign borrowing. This should be a high priority. Isn't anyone in the government thinking about the future?

Mr. Obama has denied the cost burden on business from his health-care program, but business is aware that it is likely to be large. How large? That's part of the uncertainty that employers face if they hire additional labor.

The president asks for cap and trade. That's more cost and more uncertainty. Who will be forced to pay? What will it do to costs here compared to foreign producers? We should not expect businesses to invest in new, export-led growth when uncertainty about future costs is so large.

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Then there is Medicaid, the medical program for those with lower incomes. In the past, states paid about half of the cost, and they are responsible for 20% of the additional cost imposed by the program's expansion. But almost all the states must

balance their budgets, and the new Medicaid spending mandated by ObamaCare comes at a time when states face large deficits and even larger unfunded liabilities for pensions. All this only adds to uncertainty about taxes and spending.

Other aspects of the Obama economic program are equally problematic. The auto bailouts ran roughshod over the rule of law. Chrysler bondholders were given short shrift in order to benefit the auto workers union. By weakening the rule of law, the president opened the way to great mischief and increased investors' and producers' uncertainty. That's not the way to get more investment and employment.

Almost daily, Mr. Obama uses his rhetorical skill to castigate businessmen who have the audacity to hope for profitable opportunities. No president since Franklin Roosevelt has taken that route. President Roosevelt slowed recovery in 1938-40 until the war by creating uncertainty about his objectives. It was harmful then, and it's harmful now.

In 1980, I had the privilege of advising Prime Minister Margaret Thatcher to ignore the demands of 360 British economists who made the outrageous claim that Britain would never (yes, never) recover from her decision to reduce government spending during a severe recession. They wanted more spending. She responded with a speech promising to stay with her tight budget. She kept a sustained focus on long-term problems. Expectations about the economy's future improved, and the recovery soon began.

That's what the U.S. needs now. Not major cuts in current spending, but a credible plan showing that authorities will not wait for a fiscal crisis but begin to act prudently and continue until deficits disappear, and the debt is below 60% of GDP. Rep. Paul Ryan (R., Wisc.) offered a plan, but the administration and Congress ignored it.

The country does not need more of the same. Successful leaders give the public reason to believe that they have a long-term program to bring a better tomorrow. Let's plan our way out of our explosive deficits and our hesitant and jobless recovery by reducing uncertainty and encouraging growth.

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