

How Did We Get Into the Current Economic Mess?

When I was a kid, I played baseball in a park from which you could see Boston Harbor on a clear day. That was the site of the original Tea Party, of course. I witnessed the moment of birth of the new Tea Party, with Rick Santelli's 02/19/09 rant on CNBC. I cheered when I heard it. Looking back, it's worth remembering that Santelli was venting *only 30 days after Obama took office*, with the country in the grips of the greatest financial crisis since the Great Depression. Clearly, Obama didn't cause it, but what did cause it?

I regularly disagree with my friends on both the political left and right. My biggest concern is that our political system has been deeply corrupted for many years by rivers of bribes in the form of campaign contributions. Unfortunately, the volume of disinformation floating around, together with the political theatrics in Washington, leads me to doubt the prospects for improvement anytime soon - if ever. We desperately need a real national dialog on these matters, which the paid advocates in congress are not providing.

This brief document is an entry in that dialog. It is largely a chronology of key economic events. Except for the graph and the final anecdote, it was not copied from anywhere. All facts and figures are a matter of public record. I have little faith in either Obama or the Democratic Party, but they're not the target of the following, which was written with a polemical slant to counter the political right's shameless campaign to blame our substantial economic problems on "the welfare state", government in general, or Obama in particular.

For anyone interested in an appropriately contextualized account of how we reached this point, we need to look at some relevant history, beginning 30 years ago, which is when we started down this trail. This is indispensable if you're really interested in what's happening. As Santayana famously said, "Those who cannot remember the past are condemned to repeat it." It's quite clear from listening to recent political dialog that a lot of people have learned nothing from the 2008 crisis, but these issues are much too important for that. Understanding them is essential if we are to leave a healthy society to our children and grandchildren.

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The total national debt at the time Ronald Reagan took office in 1981 was around \$1 trillion. After two terms of Reagan and one of George H.W. Bush, it had more than quadrupled to over \$4 trillion. This had been predicted in many quarters as a consequence of Reagan's "supply side economics", also known as "Reaganomics", which G.H.W. Bush had referred to as "voodoo economics" when he ran against Reagan in 1980. Those years were the beginning of what I call "credit card prosperity." While predictably blaming Democrats for "tax and spend" behavior, the "borrow and spend" Republicans ran up the bills to unprecedented levels.

Of course, some people will immediately say that the Democratic congress was responsible for this. Nope: Reagan's proposed budgets were, on average, **larger** than the ones finally approved by congress. Not only that, but for the first six years of Reagan, the Republicans controlled the Senate. What is more, Reagan got Southern Democrats to vote with him regularly, so he also had effective control of the House. Congress wasn't the problem.

As a sad anecdote to this, remember how George H. W. Bush lost the 1992 election because he violated his, "Read my lips, 'no new taxes'" pledge? Bush had begun to understand that unless taxes were raised, we would incur potentially dangerous levels of national debt (sound familiar?). For the good of the country, he raised taxes, which led to lower deficits. In doing this, he committed political suicide. Free lunch politicians, of which we currently have far too many, don't act that way.

When Bill Clinton proposed his first budget in 1993, every single Republican in both houses of Congress voted against it - twice. One after another they made passionate speeches predicting that Clinton's economic policies would ruin the American economy, mostly because it raised taxes, particularly on the wealthy. By the time Clinton left office almost 8 years later, over 22 million jobs had been created, the federal budget was running surpluses, and the national debt was **going down**, with trillion of dollars in **surpluses** being predicted. In recognition of this, the famous national debt clock was turned off, since it was thought that the debt problem had been solved. Prosperity was back. Look it up.

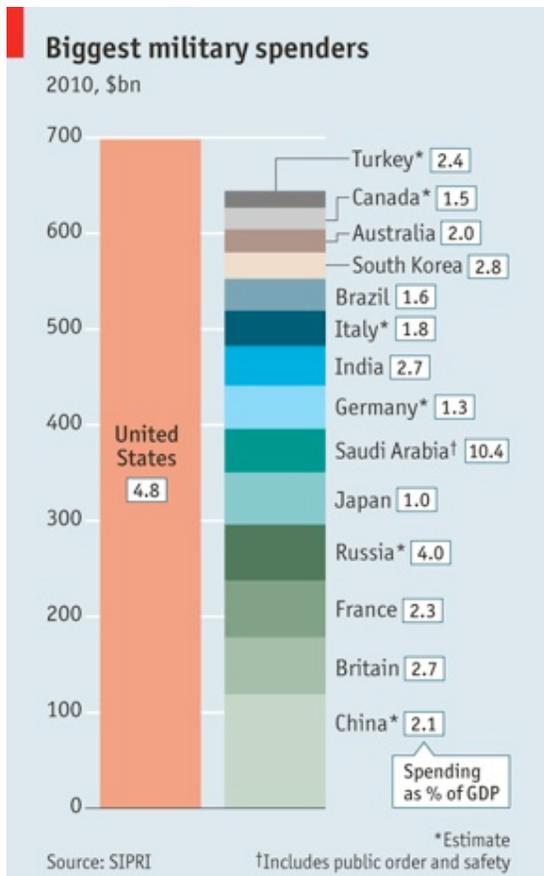
All that changed under George W. Bush. On the day he took office, the total national debt was around \$5.7 trillion. On the day he left office, the national debt had nearly doubled to 10.6 trillion. The country was also in the grips of the greatest financial crisis since the Great Depression. What is more, Bush had compiled "the worst track record for job creation since the government began keeping records" (Wall Street Journal), and his budget deficit for that fiscal year was \$1.2 trillion, which was far and away the worst in history.

Someone can respond to this by saying that 9/11 changed things. Certainly the first couple years of the war in Afghanistan were motivated by 9/11. On the other hand, the Bush administration misled the country into the Iraq War, while his prescription drug plan had nothing to do with 9/11 (but a lot to do with big pharmaceutical companies). Did

Bush raise taxes to pay for these? No, he gave two rounds of massive tax cuts to the wealthiest among us, all of which was put on the national credit card. And where are all the jobs that this \$1.7 trillion in tax cuts were supposed to create?

If anyone doubts the linkage of the Republican supply side economic theory mentioned earlier with the present mess, just remember this comment by former Vice President Dick Cheney: "Ronald Reagan proved that deficits don't matter." That is the essence of free lunch economic theory, and the Bush administration treated it as gospel.

Those on the political right in this country were pretty quiet for eight years about G.W. Bush's spending. Of course, they keep chanting the same slogans about waste, fraud, and abuse in government, as if it was all caused by Democrats. But have you heard Republicans demanding cuts from the \$700 billion per year "defense" budget? Of course not - military contractors faithfully make large campaign contributions to those who support this immense level of spending. But ask yourself - do we really need to spend almost as much money every year on the military as the rest of the world combined? Do we expect all of them to gang up on us? Here's a chart that compares U.S. military expenditures (in orange) to the next 14 largest military spenders.



This goes way beyond any credible defense needs. President Eisenhower (who is quite underrated) warned us about the dangers of the "military-industrial complex" in his farewell address. His fears have been realized by an immense, politically powerful industry that owns the Republicans, as well as a number of Democrats, in Washington. That's why they won't cut the military budget. They'd rather cut earned benefits for people who don't contribute significantly to their campaigns.

One of the best ideas I've heard in years is to require politicians to wear NASCAR suits, with the logos of all their sponsors (donors) showing clearly on them. That way we'll know just by looking at them who they are really working for - and it's not average folks. And by the way, Obama would be wearing a lot of Wall Street logos on his suit, which should be remembered not only by those who call him a socialist but by those who see him as a champion of the working and middle classes.

Now let's add another important dimension to the picture as it stood the day Obama took office.

In the near financial collapse of 2008, the Bush administration (with our tax money, of course) bailed out the banks to save them from the consequences of their own gambling debts (heads they win, tails we lose). This occurred in the wake of the deregulation of the financial services industry, which was driven primarily by Republican ideology ("government needs to get out of the way of business"), although plenty of Democrats were also bought by corporate money. This allowed Wall Street to run the biggest scam in history by building an empire of fantasy finance that was as unstable as a palace of cards. When this fraud was combined with the mounting federal debt problems, things went to hell in a hurry, partly because the government had to pay out mountains of unemployment benefits to those dislocated by the collapse. So, how many of those on Wall Street who were behind this fraud are now in jail

because of what they did? None. If you steal a couple hundred dollars from a convenience store, you will be put in jail when you're caught. If you run a multi-trillion dollar scam, you can just make large campaign contributions and it becomes de facto legal. Money not only talks in politics, it conducts a loud, uninterrupted monologue - and that's our biggest problem.

For those seeking some real understanding of what happened with the national debt, a good starter is "The Triumph of Politics" (1987) by David Stockman, who served the Reagan Administration as Director of the Office of Management and Budget from 1981 to 1985. If you read it, you will learn how our current financial mess began 30 years ago. Stockman has also been appearing on talk shows recently and his assessment of the current situation is more illuminative than anything else you'll hear on TV. A major goal of the Reaganites was to "starve" the government. They succeeded. Are they taking credit for achieving their goal? Of course not, they're blaming it on Democrats and "the welfare state." This is all part of what I call "the self-serving mythology of the looting class."

For a quick, but enlightening, introduction to what happened with the housing collapse and the subsequent bank bailout, see the movie "Inside Job" (2010). If you watch it, make sure you understand the following from it 1) how home loans

got disconnected from loan originators, 2) how Wall Street securitized (packaged as financial products) trillions of dollars in mortgages - many of them subprime junk loans - and got them labeled "AAA", 3) how they leveraged these "toxic assets" at up to 40-1 ratios and created an immensely more dangerous situation, 4) how this nearly crashed the world economy, and 5) how Wall Street executives got rich from this while Main Street got mugged.

With Republicans in Washington refusing to increase any taxes in response to the national economic mess that they created, let's have a quick look at the state of taxes on the wealthy in this country. Although tax increases on the wealthy by themselves won't completely cure our problems, they can certainly make the problems a lot more manageable. Consider some recent comments on income taxes by Warren Buffett, who has spent a number of years as the richest person in the world -

"...what I paid was only 17.4 percent of my taxable income - and that's actually a lower percentage than was paid by any of the other 20 people in our office. Their tax burdens ranged from 33 percent to 41 percent and averaged 36 percent." (These are mostly office assistants.)

"There's class warfare, all right, but it's my class, the rich class, that's making war, and we're winning."

"People invest to make money, and potential taxes have never scared them off."

Like Buffett (who should be a hero to the Occupiers), the top 400 income earners in this country last year paid an effective tax rate of only 17% on their earnings (IRS data) - they also possess more wealth than the bottom 150 million Americans.

Those who continue to believe Republican claims that higher taxes on the wealthy will ruin the economy (just as they said about Clinton's budget in 1993) should consider that when President Eisenhower left office 50 years ago the top tax rate was 91%. Would you say that we now enjoy a broader prosperity than back then?

President Kennedy lowered this rate (to around 70%), which stimulated the economy and tax revenues actually rose. So, lowering taxes can *sometimes* work, but if it *always* worked, lowering all rates to 0% would result in even higher tax revenues being collected and we would be *really* prosperous. Of course, without taxes there can be no tax revenues and no government - thus, no government services - not even a military, so that argument is only true when tax rates are inappropriately high. Tax rates *and* tax revenues are currently **very** low by historical standards.

Here's an anecdote for some perspective. Much of the income of hedge-fund managers is taxed as capital gains - at 15 percent - due to a loophole that Republican members of Congress have steadfastly guarded. If that single loophole were closed for only the top 13 hedge-fund managers, so that they had to pay the standard tax rate, would that really make much difference? You decide. Suppose their earnings were taxed as ordinary income. As an example, how many teachers do you think could be hired with the additional revenues generated by closing that one loophole? Here's a hint: last year, these 13 guys earned an average of \$1 billion each. One of them made \$5 billion. In fact, the additional revenue from them paying the standard tax rate would pay the salaries and benefits of 300,000 teachers. Three hundred thousand jobs, or a mountain of tax candy for those 13 guys - which would serve the country better right now? This might give you an idea of the staggering scale of the special treatment given to those who make large campaign contributions to our legislators. In fact, noted tax systems analyst David Cay Johnston refers to people at these stratospheric levels of wealth as the "political donor class." For each \$1 they give to politicians, they can generally expect to get back \$16 dollars in benefits, which could be anything from loosened regulations to special tax breaks. What a bargain our legislators are to big donors! The middle class and the poor don't provide such huge bribes, which is why their interests are largely ignored in D.C.

The Republicans would have you believe that these people are the job creators, so it's good for all of us when they receive tons of tax breaks. So tell me, if one of these hedge-fund managers, who merely arrange portfolio holdings for other rich people, buys his fifth Maserati, invests \$1 billion of his personal fortune in an Asian equity market, and buys an \$80 million Picasso, how many American jobs get created? And - one more time - where are all the jobs that the \$1.7 trillion in Bush tax cuts for the wealthy were going to create?