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Macroeconomics

As the upcoming presidential race begins to dominate the airwaves, the candidates have begun to reveal their plans for the economy and so forth. What surely is to become a hotly debated topic is the government's fiscal policy, or more specifically, government spending and taxation. Americans generally want to know what tax cuts will be given, and how much is the government spending. These two government activities, tax cuts and spending, compose the budget deficit. The size of the budget deficit usually indicates how well the government's monetary and fiscal policies are faring.

The deficit in 2003 was $541.8 billion dollars. This was 12.7 percent larger than the highest the deficit had ever reached, $490.9 billion, in 2002. For 2004, it seems as though the government is intent on eclipsing the record levels reached in 2003. The government will invest an extremely large amount of money into building up the nation's defense. $380 billion will be spent on the Department of Defense. $9.1 billion will be spent on missile defense. Another $2.3 billion will help support foreign partners and allies. The United States government also seems to be intent on increasing domestic security. All federal homeland security programs and the Department of Homeland Security will receive a combined $71.2 billion. Approximately $14 billion will be devoted to the No Child Left Behind program which will aim to test all students in grades 3-8 by the 2005-6006 school year for proficiency in reading and mathematics (1). The same spending patterns in 2004 seem to apply to 2005. The government plans a 7 percent increase in spending for the Department of Defense. There will also be a 10% increase in homeland security spending. $11.1 billion will be spent for education, $1 billion more than last year, and a 75-percent increase since 2001. An increase in funding for faith-based initiatives will also happen in 2005. Approximately $2 billion will be given to these programs (2).

The government also plans to have an average tax cut of $1,083 for 92 million Americans, which in total approaches $100 billion for 2004.There was also a doubling of child tax credit from $500 to $1000 when compared to 2001 amounts (1). Death taxes were eliminated altogether. 25 million small business owners were provided with tax cuts averaging $3000. During this year, three major tax relief bills have been enacted. These bills aim to provide tax relief to the 109 million taxpayers in the U.S. and the removal of 5 million people from paying taxes altogether. Taxes were also reduced on capital gains. For 2005, there will be $1.98 billion in charitable tax incentives. Tax cuts may become permanent also (2).

It appears that the astronomically large deficit that the United States is facing can be attributed to domestic spending, along with tax cuts that benefit the rich. According to Paul Krugman, the decline in government revenue has come from taxes that are paid by the richest 5 percent of families. These taxes consist of personal income tax and corporate profits tax. What is alarming is that these taxes combined take a smaller share of nation income in any year after World War II. The government's tax cuts account for more than half of this year's projected deficit (5).

After the stock market bubble burst, the United State's Federal Reserve lowered interest rates to 1%. This is largely credited for saving the American economy from a deep recession and even a declination. It seems as though after the stock market fell, consumers borrowed more to keep spending and therefore, the American economy is now growing at a steady rate. There are now many reasons for the Federal Reserve to keep the interest rate at 1%. When job figures are interpreted in terms of employment instead of output, the U.S. has suffered a new low that hasn't been seen since the 1930s. In addition, the pace of rehiring has been dreadfully slow. Also, the core rate of inflation is only 1%. Given these factors and conditions, it seems as though the government is most comfortable and secure with keeping the interest rate at 1% (3).

Monetary aggregates are measures of a country's money supply. M1 is made up of funds that are readily available for spending such as cash. M2 consist of the M1 and savings or short-term deposits. M3 is the total of M1 and M2 plus the assets and liabilities of banks. M2 is the broadest measure of money supply. During 2003, the U.S. base M2 level was 6070.9 billion dollars. For the first month of 2004, the level was very similar at 6065.4 billion dollars. *[Professor Morley's note: the fall in M2 reflects seasonal factors in money supply. Seasonally adjusted M2 will have increased at a fast rate.]* Apparently, the government wants to keep the supply of money in the economy at a constant rate. This may help to rally the economy out of the recession that plagued it the last two years by providing a steady flow of funds (4).

In conclusion, it seems as though the government's fiscal policies are approaching a disaster. The budget is increasing at an alarming rate, while domestic spending is increasing. It also seems like more tax cuts are being implemented. These tax cuts usually benefit the rich and therefore cut the government's revenue by a large amount. On the other hand, the government's monetary policies seem to be providing a steady hand for the economy. The current interest rate level seems like it is helping to guide the economy out of its slight recession. Monetary aggregates have remained stable and constant. The government's fiscal policies seem to be failing the American people, while its monetary policies are helping to lift the economy out of its dreadful recession.

Works Cited

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