THE WORLD ECONOMY'S PROBLEM IS TOO MUCH GOVERNMENT

This past week, the International Monetary Fund again lowered its global economic forecast for 2015.

From 2003 to 2007, real global growth in gross domestic product averaged more than 5 percent, but during the last five years it has averaged less than 3 percent.

During the last six years of both the Reagan and Clinton administrations, real GDP growth averaged more than 4 percent in the United States, but growth has averaged only a little over 2 percent since the recession bottomed out in 2009.

The Federal Reserve had forecast the U.S. economy to grow about 4 percent near the beginning of each year for the last five years. But during each year, the Fed was forced to reduce its forecast until it got to the actual number of approximately 2 percent. Other government agencies have been making equally bad forecasts.

These mammoth errors clearly show that the forecast models the official agencies use are mis-specified and contain incorrect assumptions.

One private economic forecaster who has been much closer to the mark is former Reagan administration Treasury official David Malpass. He has been arguing that the reason the IMF has been making such major forecasting errors is that it still has a major misunderstanding of global monetary policy.

Last week, Mr. Malpass wrote:

> "Monetary policies in the U.S., Europe, and Japan are contractionary and disinflationary, not stimulative, yet the central banks and the IMF believe they are stimulative and imbed that in their forecasts. The Fed has been consistently overestimating U.S. growth and inflation.
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> When it [quantitative easing] started, Japan began seriously overestimating its growth and inflation outlook. Europe is now following the same pattern, thinking that its bond-buying will add to growth and inflation even as interest rates are moving more deeply into negative territory."

Mr. Malpass further observed that the near-zero interest rates in the United States, and now negative interest rates in Europe, "distort the flow of credit, harming growth and investment."

Government economic policymakers have been trying to solve a problem of too much government spending, taxing and regulation by inappropriately using monetary policy, which has not and cannot solve the fundamental problems. It is like using a hammer rather than a shovel to dig a hole.

The major central banks have been holding down interest rates, which is actually a massive indirect tax levied on the world's savers. Historically, savers would receive about 3 percent interest above the rate of inflation on their safest investments, but now interest rates often do not cover even the low inflation that is occurring in the developed countries. In effect, responsible people (those who save for retirement or emergencies) have been giving the government interest-free loans.

Many economists expected savers to save less and consume more as a result of low or even negative interest rates, which they believed would stimulate the economy. Instead what is happening, particularly in Japan, is that many citizens and businesses are increasing their saving and even hoarding cash.

Why are they doing this? Global uncertainty has risen. All can see that most big governments are increasing their debt to such levels that it is unlikely they will be able to pay it back without inflating their currency.

Among the large economies, only China, India and Germany are likely not to increase their debt-to-GDP ratio this year. When businesses and individuals look at the world debt situation and the increased chances of another financial collapse, their rational response is to increase "precautionary" savings, even though they are not receiving interest on them.

As the Japanese situation illustrates, the deeper the government goes into debt the more individuals and businesses save out of fear, thus reducing consumption and further slowing economic growth. It can become an almost endless downward spiral.

Many politicians and officials of organizations like the IMF call for tax increases to reduce the level of debt. The problem is that most of the world's people are taxed out, and higher tax rates or more tax enforcement will only discourage productive work, saving and investment, most often leading to less growth -- with its higher demands on government -- rather than more growth.

Greece is Exhibit No. 1 at the moment.

The debt burden will continue to suck the vitality out of the global economy. *The only solution is to revive growth, and that can only be done by tax rate reductions, not tax increases, getting rid of non-productive government regulations, and radically cutting government spending.*

There is no other non-destructive way out.

Yet, the Organization for Economic Cooperation and Development and its big-government allies (e.g., the Obama administration) continue to try to jack up world tax rates and add increasingly destructive global financial regulations, which impede capital flows, reduce individual liberty, and increase the global stock of misery.

Or maybe the political class could just make it illegal to be unemployed and poor, as President Alexander Lukashenko of Belarus did last week, to prevent "social parasitism," meaning those who do not pay income taxes.

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