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Why Ronald Reagan cannot balance the federal budget

by Richard Freeman

President Reagan's Jan. 31 budget for fiscal year 1984 was a compromise between the most severe budget-cutting and "staying the course," i.e., doing nothing. As a result, the President ended up with a $200 billion deficit, further cuts in programs essential for the economy, and sharp cuts in the defense budget.

The Reagan budget was fashioned not with any concern toward the national interests of the United States, but rather as a result of the attempt of the President to placate the several voices in his administration who have been raising the line of the International Monetary Fund that only deeper and deeper cuts in the budget can allow the United States to ever get its budget into balance.

This has been the repeated chorus of a clownish group of Wall Street bankers and six former U.S. Treasury Secretaries—Simon, Connally, Dillon, Fowler, Kennedy and Blumenthal—who operate under the name of the Bipartisan Appeal on the Budget Crisis. On Jan. 20, just before the President was to release his State of the Union message, this group placed two full pages of ads in the *Washington Post,* urging $175 billion in budget cuts.

Reagan got the same advice from the Three Stooges in his cabinet—Treasury Secretary Regan, Budget Director Stockman and Secretary of State Shultz, a "former" board member of Morgan Guaranty Trust. The same message was also delivered to Reagan this week by former U.K. Chancellor of the Exchequer Geoffrey Howe, who predicted that unless the United States cut its budget deficit, there would be a world financial disaster.

Not having a strongly defined view of how to proceed, the President gave in to the IMF crowd to a point, and made significant cuts and raised taxes.

At this point the President is praying that he made the right decision and that somehow, some way his move would solve the budget problems.

A study just completed by the *EIR*'s LaRouche-Riemann model shows that the President really has no choice that will work as long as he works within a financial geometry defined by the IMF and Wall Street. The LaRouche-Riemann economic model is the only competent forecasting service operating in the United States, having predicted the course of the past three years' "double dip" depression collapse to the proverbial "t."

The model found that first, it is not the federal budget deficit which is out of control, but the entire U.S. economy. Second, it found that if the budget-cutting and tax hike "cure" is applied, it will either crash the U.S. economy toward zero overnight or guarantee *increasing* budget deficits up to $500 billion by 1990.

The LaRouche-Riemann forecast

The LaRouche-Riemann model study has found that the United States is shifting ever more rapidly from a manufacturing, farming and goods-producing economy to a "post-industrial society" junkshop of paper shuffling, video games, and "recreational" drugs. Unless that shift is stopped abruptly, the study showed, the economy's "overhead" costs will swamp its productive base. The federal budget, which merely reflects this shift, will simply grow more and more out of balance.

In fact, the model found that if the budget deficit passed $200 billion, as it is expected to do in fiscal years 1983 and 1984, the economy will go into a "self-feeding" tailspin in which attempts to narrow the budget gap will actually enlarge it to the $500 billion range, and more budget cutting attempts will only hasten the rate of industrial decline.

But if the budget is not cut, if nothing is done but to "stay the course" as President Reagan has been arguing, the Federal Reserve continues to print money to monetize the federal deficit, as Paul Volcker has done for the past few months, then the United States will experience hyperinflation—the "wheelbarrows-full-of-money-for-a-loaf-of-bread" type of

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collapse that hit Weimar Germany in the 1920s. This "heads-I-win, tails-you-lose" dilemma is only soluble outside the range of policies presently which are presently being offered to the President: only by the economic re-organization plan offered by Lyndon LaRouche.

Pandora's box

The way to approach this question is to consider the level of overhead than an economy can carry without collapsing. Most of the items on the U.S. budget are overhead, perhaps necessary overhead, like social security, or essential overhead, like portions of the defense budget, but overhead nonetheless. As the economy has shifted toward a post-industrial society, and workers have been thrown out of work, more and more of the cost of maintaining the population has been shifted onto the overhead cost of the government.

The fundamental shift is documented by the shift in the labor force. Whereas after World War II, 67 percent of the labor force was in goods production, and 33 percent in non-goods production (services, clerks, etc.), by 1979 that ratio had shifted to 34 percent in goods production, and 66 in non-goods production.

In 1979, this translated into two workers representing overhead for each productive worker. But by January 1983, in the space of three-and-one-half years of Volcker-led depression, this rose to three workers representing overhead for each productive worker. This means that each productive worker must support one additional person, something that can't be done with current collapsing levels of productivity.

This same shift was captured by the LaRouche-Riemann model when it found in its analysis last Dec. 29, that the overhead cost of the economy, called d was larger than the surplus generated by the economy, called S by a staggering $144 billion. When d exceeds S —the model calls this negative reinvestment or negative s'—the economy implodes inward on itself.

This unhealthy situation manifested itself last year, when for the first year in America's history since the depression, the increase in salaries and wages at $38 billion was exceeded by government transfer payments—unemployment benefits, Social Security payment increases, welfare and food stamps, veterans benefits, and so forth—at $60 billion. In fact, the manufacturing wages portion of the economy fell by $9 billion in 1982. It was only the salaries portion of the wages and salaries—white collar workers reflecting d overhead— that increased.

The transfer of costs from the productive sector of the economy to the government overhead (transfer payments) can be seen in the case of unemployment benefits, which soared from a level of less than $10 billion in 1979 to over $31 billion in December of last year.

Thus the economy, whose manufacturing base is being wiped out, is being led by transfer payments, and like it or not, defense spending. What happens if the Wall Street-IMF cabal's demand for cuts in Social Security, unemployment benefits and food stamps are heeded by President Reagan? The major source of personal income growth will be wiped out, thereby destroying purchasing power. What if defense spending is cut? The only industry growing at a 20 percent rate, and therefore one of the few sources of orders for steel, machine tools, cement and manpower, is eliminated. What if $60 billion in taxes per year are added on, especially regressive consumption taxes that hit the pocketbook of the wage-earner? That amount of purchasing power is taken out of the economy.

Thus, austerity measures, meant to balance the budget, reduce purchasing power further, which translates into fewer orders for steel, machine tools, and so on, which eventually leads to reduced production. This further contracts the tax revenue base, throwing the economy further and further into collapse.

If, on top of this, Volcker and the Fed raise interest rates, currently at 11 percent, that further contracts production—which deepens the deficit—and *leads to a deflationary collapse,* just as the IMF man predicted.

The danger of 'staying the course'

Austerity only deepens the budget crisis. But standing still and doing nothing—"staying the course," in the President's words—is equally dangerous. The United States will have $300 billion in borrowing needs this year, including an expected on-budget deficit of $190 billion, off-budget financing of $17 billion, and $90 billion in programs that get government credit guarantees. This amount is larger than U.S. savings, at $220 billion. To finance such a need—plus an additional $450 billion in outstanding Treasury debt that must be rolled over, the Federal Reserve would have to run the printing presses overtime. That does nothing to improve the economy, or therefore increase revenues or close the budget gap, but it does lead to a *hyper-inflationary explosion.* Thus, within the IMF world financial geometry, the United States must either have a deflationary or inflationary collapse.

Operating within this geometry, Reagan and the U.S. Republic are as good as gone. The only solution the President has is to reach outside his own circle of advisers and the IMF to heed the suggestions offered by Lyndon LaRouche. Federalize the Fed, and have it operate to finance a New World Economic Order. The Fed then generates two to three percent interest-rate loans, through the private banking system, to bankroll industry, farmers, mining, construction and scientific research. Instead of bailing out the IMF, the Fed would save the productive base of the United States, in order to also save the Third World. If this program were combined with a crash development beam-weapon defense program, which would provide a high-technology jolt to the moribund industrial base, the United States would generate hundreds of billions of tax revenue dollars, and close the budget gap. Without adopting such an approach, President Reagan is doomed to enlarging the budget deficit to a point that the U.S. government, and the economy, are bankrupt.