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Government Can't Really Stimulate the Economy **by Sheldon Richman**

The money sluices are about to open wide on Capitol Hill. With a new Congress convened and a new president about to take office, we are likely to see record-shattering government expenditures. All inhibitions about deficit spending, as weak as they have been in recent years, are now dissolved. The motto among those in control is: Spend now!

Why? To “stimulate the economy.” Well, that’s a lousy reason. The economy doesn’t need stimulation. It needs freedom. More precisely, we need freedom — to pursue our ends through production and trade unmolested by know-nothing politicians in Washington and the 50 state capitals. Bureaucratic spending on infrastructure, food stamps, unemployment benefits, R&D, or whatever else the political (parasitic) class has in mind is precisely the opposite of what is needed.

Any statement about the economy that contains a mechanical metaphor is more than likely wrong. We’re told government must “jump start” the economy. How can it? Think about what happens when a car is jump started. Cables connected to a charged battery convey juice to a dead battery. Energy is injected into the broken-down car from outside.

Politicians and court economists want us think this is analogous to government’s jump starting the economy. But it cannot be. Since the government has no money lying around waiting to be spent, it will have to borrow close to a trillion dollars to carry out the program President-elect Obama and the congressional leadership are planning. But borrowing money for their pet projects injects nothing into the economy. It merely moves money from where it currently is in the economy to where politicians want it to be. How is that a stimulus?

Moreover, the debt will be covered (monetized) by the Federal Reserve by creating money out of thin air. That money will then be spent and “invested,” but notice the problem. Creating money is not the same as creating wealth. Imagine you were stranded on a desert island. Overhead you see a plane. It drops a large box down to you. Excitedly you tear open the box expecting to find food and water. But instead you find a printing press and a large supply of green paper. An instruction sheet states: “Print all the money you need.”

Are you better off?

All resources are scarce. A quantity of steel, for instance, can be used to make a washing machine or a machine to produce more steel. It can't make both at the same time. When the Fed creates money, it increases the demand for scarce resources — but no new resources. How can that be a path to prosperity? Rather, it's a path to higher prices and lower real incomes.

But it's more than that. Since the new money gets into some hands rather than others first, monetary expansion — that is, inflation — changes the pattern of prices and production that would have resulted from voluntary exchange under sound money. Among the prices distorted are interest rates. By doing so, inflation transfers resources from those who produce wealth to others.

Inflation, therefore, is one more government income-distribution program. The lucky early recipients of the fresh fiat money gain purchasing power — command over scarce resources — at the expense of everyone else. The market process is thereby corrupted. In the absence of inflation (and other government interference), it is a system in which entrepreneurs pursue profit by pleasing consumers. What makes this work amazingly well is the price system, which communicates to producers and consumers the relative scarcities of products and factors of production, the relative demands for such things, and the degree to which people prefer goods in the present to goods in the future. This permits production to be guided by consumers' preferences. Inflation distorts those relative prices, garbling the signals and ill-serving consumers. In the end society is poorer than it would have been. When the inflation is finally stopped, the economy suffers depression and mass unemployment as it corrects for the malinvestment. Or, if the inflation accelerates to hyperinflation, as it did in Germany in the 1920s and in Zimbabwe today, society will be thrown into chaos.

This is where the Obama-congressional “stimulus” plans will lead. Nothing is more dangerous than a politician who thinks he must “do something now.”

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