Dennis Brack — Black Star

UNKINDEST CUT OF ALL

Gary Allen *is author of* None Dare Call It Conspiracy; The Rockefeller File; Kissinger; Jimmy Carter/Jimmy Carter; Tax Target: Washington; *and,* Ted Kennedy: In Over His Head. *He is an* AMERICAN OPINION *Contributing Editor.*

■ IN THE YEAR 1910 the total take of tax collectors in the United States was under $676 million, over half from excise taxes. The graduated income tax had not yet been instituted. As Dr. Gary North has quipped, "The old line seems true enough: *The golden age in American life was around 1910,* after indoor plumbing but before income taxes."

The level of taxation has since mushroomed like a hydrogen bomb. The Tax Foundation reports that the cost of federal, state, and local government will top $1.07 *trillion* this year! This is up 13.6 percent from last year's $942 billion in taxation by government at all levels. Two-thirds of this trillion-dollar burden is, of course, imposed out of Washington,

Tax and Budget cuts are still somewhere over the rainbow, while our standard of living is being crushed beneath the burden of deficit-fueled inflation, record interest rates, and taxes amounting to $18,712 for a family of four. The federal government will be taxing and spending $44 billion more this year than last.

D.C.; the rest by state and local governments. This comes to taxation amounting to $4,678 for every man, woman, and child in the nation — some $18,712 for a family of four! America is being suffocated by Big Government.

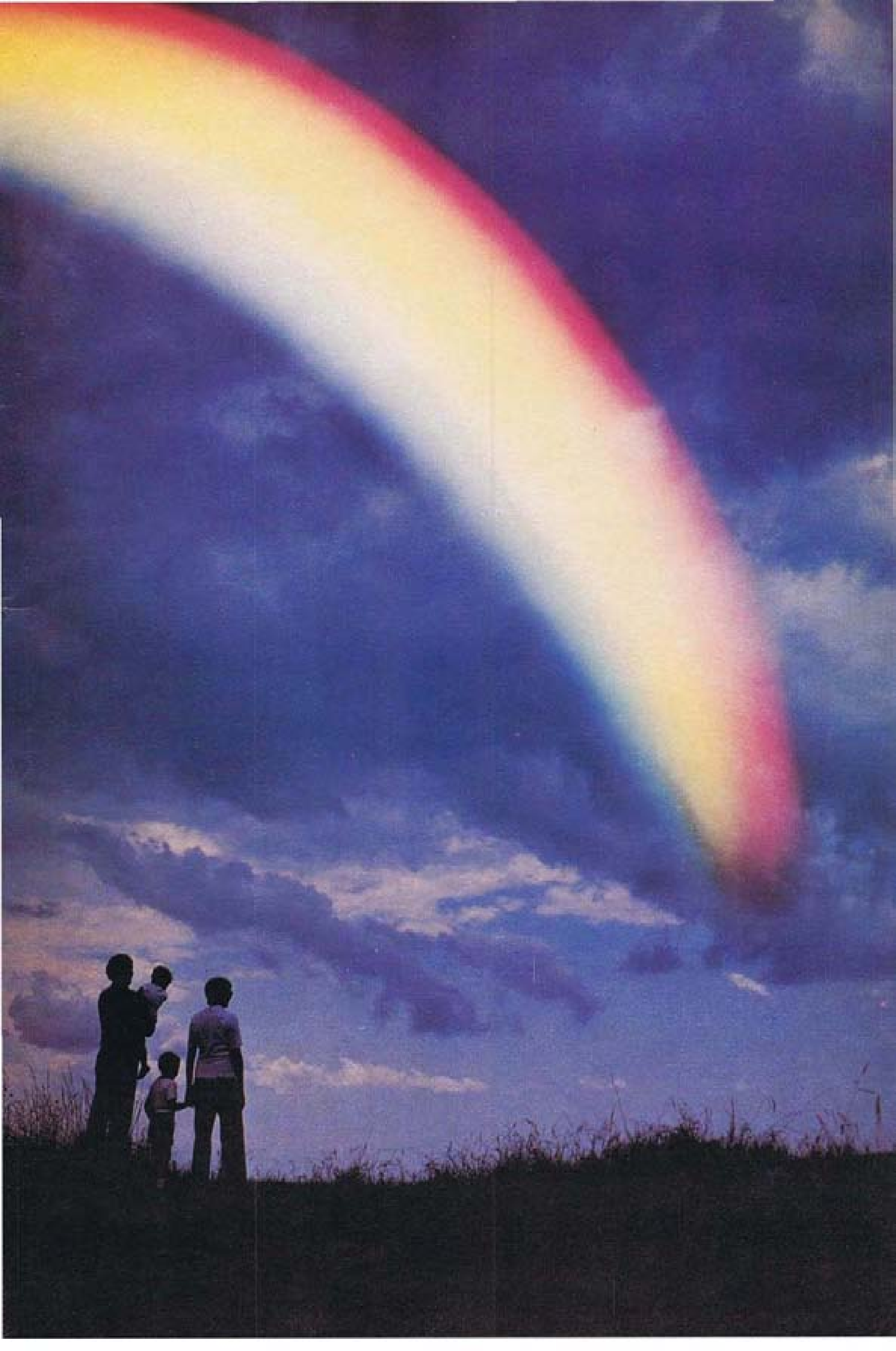
The question to consider is: Will Reaganomics and the new tax package passed by Congress reverse the trend toward ever bigger and more expensive government? I wouldn't bet my financial life on it.

The passage by Congress of the Administration-backed tax plan was hailed as an even greater political triumph for President Reagan than the victory he had achieved with the procedural vote a month earlier on the so-called spending cuts. As late as two days before the big vote on the tax bill, it looked as if the Reagan Administration would not have enough votes to assure passage. "Liberal" Democratic leaders like House Speaker Tip O'Neill and Ways and Means Chairman Dan Rostenkowski felt confident that, this time, Reagan would not get his way in the House. So the Administration brought out its big gun, Ronald Reagan himself, who went on national television to compare the advantages of his "bold" tax proposal to the "fearful and timid" one offered by the Democratic Leadership.

On the eve of the showdown, both sides were saying it was too close to call, but Reagan's eleventh-hour television address generated a wave of popular support for his plan and put considerable pressure on the Congress. This was accompanied by a Presidential blitz of personal lobbying among wavering Democrats. On July twenty-ninth the House approved the Reagan tax measure by a vote of 238 to 195 — with an even greater number of Democrats crossing party lines to back the Administration than had supported Reagan on the Budget reconciliation vote. Final details were soon worked out with the Senate and a victorious Ronald Reagan signed the bill into law on August thirteenth.

Reagan euphoria was epidemic among Conservatives. Senator Dan Quayle (R.-Indiana) exclaimed in elation that the Reagan tax program "will go down in history as the second American Revolution." Bitter "Liberal" Democrats opined that it was the end of Camelot. *Newsweek* for August tenth reported: "The age of conservative economics has arrived, and its implications for all Americans are immense. Not only did last week's tax bill reverse decades of social engineering to provide important new incentives for the rich, it also permanently reduced the gov-

H. Armstrong Roberts



Both total spending and taxing will increase because the new Administration decided that real spending and tax cuts would threaten the politics of envy and inflation. Supply-side economics does not challenge these forces. The actual Budget deficit for 1982 is therefore likely to be in the $80 billion to $100 billion range.

---

ernment's role in economic life."

All this talk of a "Reagan Revolution" that will "reverse decades of social engineering" is complete nonsense. There has been no Reagan Revolution because there has yet to be a move away from Big Government and enormous deficits. Ronald Reagan's leadership victories in the political arena may be impressive and glorious in the context of partisan politics, but all the sound and fury surrounding these political triumphs reflect nothing of certifiable substance.

Last month I explained that even though the media commentators speak of "massive Budget cuts," the federal government will spend more this year than ever before. Estimated total federal spending for Fiscal 1981 was $661.2 billion. The Reagan Budget for 1982 is estimated at $705 billion. Figure it out for yourself: The government will be spending $44 billion *more* this Fiscal year (1982) than it did last (1981). The so-called "cuts" are only out of the projected *increase* in federal spending estimated by the Carter Administration. And even the Reagan cuts in the Carter increase were reduced from $48.6 billion to $35 billion.

A real Budget cut would mean a reduction in spending from one year to the next — something not done since the G.O.P. controlled the Congress early in the Eisenhower Administration. Congress cut Eisenhower's first full year's Budget from $74.3 billion in Fiscal 1953 to $67.8 billion in Fiscal 1954 — a genuine cut of 8.7 percent. If Reagan were to cut the Budget by the same percentage his 1982 Budget would have to be $603.7 billion instead of $705 billion. This would be $57.5 billion less than the Budget for 1981 and about $135 billion less than what the Carter Administration proposed to spend. And, of course, the *actual* spending for 1982 will undoubtedly be much higher than the current $705 billion estimate, fueling further inflation with a deficit much greater than the projected $42.5 billion.

Just as there has been no cut in spending, so there has been no net cut in taxes. The Reagan Tax Cut is a cut in tax *rates*. The new law calls for a five percent reduction in personal income-tax rates on October first, a further cut of ten percent on July 1, 1982, and another ten percent cut on July 1, 1983. This amounts to a nominal tax-rate reduction of twenty-five percent over a period of thirty-three months. What we have here is a compromise version of the original thirty-percent rate cut (Kemp-Roth) supported by candidate Reagan, which was to have been retroactive to January first of 1981. But, as economist Murray Rothbard reports, the twenty-five percent rate reduction does not offset the built-in *increase* in the rate of taxation resulting from "bracket creep" and from Social Security tax hikes already scheduled.

The F.I.C.A. taxes that pay for Social Security benefits are set to increase to 6.70 percent next year from this year's rate of 6.65 percent, and the maximum covered wage will go up to $32,700 from this year's $29,700. By 1985 the rate will be 7.05 percent with a maximum covered wage of $43,500! These hikes were passed by Congress during the Carter Administration in 1977. Even now, many workers are paying more for Social Security than they do in federal income taxes! These taxes will continue to escalate. Since the Federal Pyramid Club faces collapse by 1984, taxes in some form are going to be raised to perpetuate this prototypical Ponzi scheme through a few more elections.

Bracket creep will add to this. As your income rises to keep pace with inflation you are automatically bumped up into a higher tax bracket. Heavily taxed brackets intended by Congress for the rich are now being imposed on poor and middle-income people.* Your federal tax bill will be higher next year than this year. About the only way you can expect to pay any less in taxes is to ask your boss to lower your wages!

So, there is no cut in spending and no cut in taxes. Should we not at least be grateful that the Reaganauts are slowing down the rate of growth in spending and taxation? "Perhaps," concedes *Birch Log* columnist John F. McManus. "But no more so than we should be pleased that the decrepit train carrying us toward a collapsed bridge has slowed from eighty to forty miles per hour. A far better development would see the train stopped and the railroad officials not only fixing the bridge, but also putting their bankrupt company back in decent financial shape."

We asked Free Market economist Murray Rothbard his opinion of the new tax package. Rothbard replied, "To me the only really important parts of the tax package were the two things the Southern Democrats forced on Reagan and which the Reagan people didn't want to take. One was indexing to prevent bracket creep. However, that will only start in 1985. God knows whether we will ever get to it. But at least that is very important — and something Reagan pledged to do in the campaign and then promptly forgot about. And the other important part is the cut at the top of the interest and dividends tax from seventy percent to fifty percent."

Under indexing, the level of income covered by a tax bracket would rise each year in accordance with the Consumer Price Index. A taxpayer whose income rose at the same rate as price inflation would continue to pay tax at the old rate instead of a higher rate as is now the case. One whose income doesn't keep up

(*Continued on page ninety-five.*)

*A taxpayer who moves from the $20,000 tax bracket to the $30,000 bracket does not simply pay one-third more in taxes. He may pay two to three or more times as much, depending on deductions and exemptions. This is the combined effect of inflation and the graduated income tax. In 1980 a family of four earning $20,000 paid $3,239 in federal income and Social Security taxes. With a ten percent rate of currency depreciation, that family will need at least $30,000 just to stay even by 1984. Even with the Reagan tax "cuts" this family's taxes would go up to $4,864 — a fifty percent increase!

From page six

THE UNKINDEST CUT

with inflation could fall into a lower tax-rate bracket. In addition, the personal exemption — now a thousand dollars — would also be indexed every year to the C.P.I. The standard deduction (the zero-bracket level), which is used by those who do not itemize their deductions, will also be linked to the cost of living. But all of this is at least four years away; and, politicians being what they are, Congress could in the meantime change its mind about indexing. It is not a solution to the problem of inflation, but the indexing of tax brackets to the Consumer Price Index might at least reverse the vested interest the government now has in inflation.*

The reduction of the rates on investment income (interest, dividends, and rents) — especially the cut in the maximum rate from seventy percent to fifty percent — is also significant. You can't have capitalism without capital, and you can't have capital without rewarding capitalists. This measure at least reduces the tax penalty on savings and investment for those who have money to save and invest. It will also have the effect of reducing the maximum rate on long-term capital gains (those on assets held for a year or more) from twenty-eight percent to twenty percent, retroactive to June 9, 1981.

The reason these measures are so important is that they might help Ronald Reagan buy a little time for his program of economic recovery. Our huge federal deficits have to be paid for either by increasing the money supply through the Fed (inflation) or by the government borrowing our savings in competition with businesses and individuals. The reason Japan can run large deficits and still not have much inflation is that it can borrow from its relatively larger pool of savings rather than monetize its red-ink expenditures. But the amount of savings (compared to G.N.P.) in the U.S. is much less than in Japan.† Because of our enormous deficits and low rate of saving, federal borrowing requirements are "crowding out" private borrowers from the credit markets, sopping up funds urgently needed for private businesses, many of which are already on the brink of bankruptcy. To prevent substantially more inflation, Reagan opted to use his political leadership quickly to induce a great deal more savings in our economy. It is hoped this will generate a sufficient pool of funds to accommodate the increasing federal borrowing without an even more deadly credit crunch.

Whether the new investment incentives will be sufficient to stimulate enough new savings to ease the credit crunch remains to be seen.

To the good, the new law permits much faster depreciation for vehi-

---

*Actually, federal revenues will still be going up with inflation after indexing begins in 1985, but the rate of increase in tax revenues will no longer be going up faster than the C.P.I., as is now the case. Because of the graduated nature of our Marxist tax system, for every one percent rise in the C.P.I., federal revenues now increase by 1.6 percent. In other words, if prices rise by ten percent, and personal incomes only keep pace with inflation by rising ten percent, taxes increase by sixteen percent because of bracket creep.

†According to former Treasury Secretary William Simon in his book *A Time For Action*, "Over the past two decades the United States has brought up the rear among industrial nations in percentage of Gross National Product held as personal savings. From 1973-77 other industrial nations were saving between 10 percent (Canada) and 25 percent (Japan) of GNP. During the same span, the United States saved only 6.7 percent, and in the past year the savings rate has fallen as low as 3.4 percent."

cles, plant, and equipment. In addition, there is a new investment tax credit of six percent for three-year write-off assets and a full ten percent for five-year depreciation. Professor Rothbard thinks these reforms don't go far enough either. He observes: "True, a more accelerated depreciation will now be permitted, and this is welcome relief. But the benefits will be concentrated on the old, highly capitalized industries with long-lived capital; the modern, new, and progressive industries which have the greatest potential for growth have already been depreciating at the new maximum rates. They *should* have been aided by the government, at long last, permitting *any* rate of depreciation that a firm deems to be appropriate."

Another disappointment was the tiny reduction in the corporate tax rate — from seventeen to sixteen percent in 1982 for the first $25,000 of income, and then only down to fifteen percent thereafter. For corporations earning profits between $25,000 and $50,000, the rates would be dropped from twenty percent to nineteen percent in 1982, and to eighteen percent in 1983. These infinitesimal reductions will hardly provide a real test of supply-side economics!

Then there are the new tax-free savings certificates permitted under the new game rules. Thrift institutions and banks are now loudly advertising interest-bearing certificates which are exempt from taxes up to a thousand dollars (two thousand for a joint return). They can, however, yield interest which is no greater than seventy percent of the Treasury Bill rate. Even so, these certificates will for some taxpayers prove competitive with money-market funds on an after-tax basis. This could temporarily help to ease the growing crisis in the Savings and Loan industry. James Christian, economist for the U.S. Savings & Loan League, says: "We expect the impact on S&L associations — deposits in general — to be substantial."

Another important part of the new tax legislation deals with retirement plans. Under the present law concerning Individual Retirement Accounts (I.R.A.s), only persons not already participating in a tax-qualified pension plan may deduct a contribution to an I.R.A. up to fifteen percent of their earnings. The new rules permit contributions up to two thousand dollars, and the maximum yearly Keogh Plan contribution increases from seventy-five hundred to fifteen thousand dollars. Unfortunately, there is a very bad kicker in this part of the Reagan tax law. At the last minute, a clause (314) was slipped into the tax bill which prohibits I.R.A.s, Keoghs, and self-directed pension funds from investing in such assets as stamps, jewelry, art, gems, gold, silver, coins — or any other asset that might be specified by the Secretary of the Treasury — without being taxed in the calendar year in which they are purchased! This is designed to stop money from flowing into hard assets and collectibles, and divert it back into money instruments. It is a frontal attack by the bankers on the hard-money community.

Economist Jane Bryant Quinn notes more changes in her *Newsweek* column for August seventeenth, observing: "Next year also brings a phased-in tax break for working couples, a bigger child-care credit for working parents, and a decisive drop in the top tax bracket from 70 percent to 50 percent. Naturally, none of this is easy. The complications have accountants and tax lawyers laughing all the way to the bank."

The theory behind these tax-rate changes and reductions is called supply-side economics. There is much of value in the supply-side theory — especially when contrasted with the intellectually and morally bankrupt and discredited notions of Keynesian (demand-side) economics. But there are some aspects of supply-side theory and application that are very controversial even among Free Market economists.

Supply-side economics involves the manipulation of tax rates to create fresh incentives for greater production and economic growth in order to maximize revenues to the government resulting from expansion of the tax base. The supply-siders contend that, if tax rates are cut sufficiently, economic growth will be so stimulated as to yield increased revenues for government even though tax *rates* have been lowered.

If all of this is true — and it is clearly based on observable propensities — the question to be asked is this: Why *should* our goal be the maximization of government revenue? The supply-siders want to find an optimum tax rate, one that least discourages production while maximizing government receipts. Many of us are concerned that while the supply-siders speak frequently about incentives and disincentives, they say little or nothing about the *moral* right of producers to manage and keep the fruits of their enterprise. That is, they ignore the basic issue of the proper role of government. We believe the market and not government should provide incentives. We think the interests of liberty require that definite limits be set on government; that its powers should be so circumscribed as to maximize individual rights; that the role of government is not to see how much revenue it might be possible to squeeze from its productive citizens. Our Constitution provides that producers should be liberated for their own sake — not just so they can produce more revenues for the government.

And, even though supply-side theory is correct in claiming that large cuts in tax rates are likely in time to expand the tax base, it remains to be seen whether the plan passed by Congress will provide enough cuts to produce enough revenue in time to make the Reagan Economic Recovery scheme work.

The context shapes the thing. Because of the lag time between the tax-rate cuts and the income they may generate, the President is embracing immediate and huge inflationary deficits. Eventually the revenues from the tax-rate reductions are *supposed* to bridge this gap and make possible a balanced Budget without cutting back on the Welfare State.

There are many uncertainties involved. For instance, what makes the Administration believe that the tax "cuts" will actually stimulate the consuming public to save more, and businesses to make significant capital expenditures, in view of the facts that consumers are up to their eyeballs in debt, Social Security taxes will increase, and the liquidity of many corporations is currently at dangerously low levels? With interest rates above twenty percent, who will borrow to expand plants? With bracket creep and inflation and Social Security increases eating up our income-tax rate reductions, who will be able to save more?

If the supply-siders are wrong, or if the Reagan tax package is not a real test of their theory, we have made a five-foot leap across a nine-foot ditch. Free Market economist

Henry Hazlitt ably summarizes: "Though 'supply-side economics' is a useful phrase, there are many questions that it cannot answer: Conceding that a cut in tax rates will encourage economic activity, will it encourage enough additional tax revenues so as not to increase the federal deficit? There is no way of calculating this in advance. And, if the deficit does grow, there are no assurances that the lower tax rates will generate enough savings and profits to provide the extra capital to meet government borrowing needs without more inflation of the money supply. Lower tax levels *can* promote an expanding economy. But they will not necessarily of themselves eliminate or substantially lower a deficit by reducing the need for government spending on welfare and unemployment compensation."

And there's the rub!

The Reagan people contend that the tax-rate cuts will permit the Warfare State to continue to operate and at the same time produce prosperity which will bail out the economy with increased production. Unfortunately, there is a Medfly in this ointment! Earlier I mentioned the plan to index income-tax brackets in 1985. The Medfly in the Reagan Economic Recovery Plan is the continuing indexing on the *spending side* of the federal Budgetary equation.

For several years, federal spending on various so-called "entitlement" programs, including Social Security, has been linked to the Consumer Price Index. When the inflation rate speeds up, this automatically triggers cost-of-living adjustments (C.O.L.A.s) which have been built into federal outlays. (And C.O.L.A.s are now a part of most major labor-union contracts in private industry.) Other benefits, such as workman's compensation, are also automatically increased when the unemployment rate rises. A full seventy-seven percent of the federal Budget has now been placed in this category of "uncontrollable" spending — outlays which are automatically triggered by cost-of-living increases and/or rises in the level of unemployment.

Everyone hopes that the tax incentives will stimulate economic growth — but everyone also knows that before these measures can produce a beneficial effect on the economy we face those huge federal deficits. The Reagan deficits will be handled either by more inflation or by an even worse credit crunch. Because of the C.O.L.A.s which Congress years ago wrote into the Welfare State spending programs, either price inflation or the increases in unemployment caused by interest rate hikes to borrow the money covering the enormous deficits will result in even *more* outlays and even *larger* deficits — leading to more inflation or to unemployment triggered by a credit crunch. It is a vicious circle.

As long as spending and benefits continue to be indexed, they will sabotage the Reagan plan for economic recovery. Revenues will chase outlays — never quite catching up with the automatically triggered C.O.L.A.s and the runaway deficits. In addition, if taxation is in fact indexed in 1985 to compensate for the effect of inflation, this will soon result in a further tax-rate cut. Even though revenues would still be increasing, they would not be going up as fast as they would without the indexing — and this will assure greater deficits and their consequences.

As syndicated columnist David S. Broder puts it: "Congress has yet to bite the bullet and reduce the major items of indexed benefits it inherited from its predecessors. Yet it seems blithely ready to forge for its successors a new set of fiscal handcuffs called tax indexing. A government in which benefits are indexed to rise with inflation while taxes are indexed to resist inflation would be a government on the way to bankruptcy, of course." Yea, verily.

The supply-siders have not taken into account the increase in federal spending due to the deficit-triggering of the C.O.L.A.s. Only now are they recognizing that this means federal spending will be much greater than they have been predicting. Revenues generated by the hoped-for economic growth might *never* catch up with spending. This means the Budget would never be balanced.

President Reagan has inherited a government with an upward bias in spending. As we pointed out here last month, federal spending is as out of control as a Roman orgy. Federal transfer payments account for half of all federal outlays — and 50.2 percent of the American people are now dependent on government as their primary source of income. None wants a pay cut. Because of the political implications of this, President Reagan probably could not have persuaded Congress to go along with deeper spending reductions. But as Congressman Phil Gramm (D.-Texas) has observed: "We must stick a finger in the dike of the entitlements before they blow up in our faces."

And not only do we have this horrific Social Welfare juggernaut, but President Reagan plans to spend at least $1.5 trillion on defense over the next five years. Military spending is now projected to be $200 billion in Fiscal 1982, $220-230 billion for 1983, $275-300 billion in 1984, $380-410 billion in 1985, and up to $400-430 billion by 1986. If you add the transfer payments and defense spending to the $100 billion in interest to be paid on the National Debt, you get a "bare-bones" Budget of back-breaking proportions.

Assuming that the Welfare State is not going to be liquidated, because Congress won't yet go along, the President's "supply-side" tax plan is perhaps the best gamble he could take. But it is a gamble. If the economy doesn't pick up significantly as a result of these measures, we will be drowning in massively larger deficits. Without big cuts in Social Welfare or national defense the Reagan deficits will be the largest in history.

How big will even that 1982 deficit turn out to be? No one knows, but it will be much more than the original $42.5 billion estimate of the Reagan economic team. New Reagan estimates predict the addition of another $20 billion. And that doesn't even include off-Budget outlays now conservatively estimated for 1982 at $18.2 billion. (They were in excess of $24 billion in Fiscal 1981.) The actual Budget deficit is likely to be in the $80-$100 billion range — maybe more! You can already hear the triggers pulling on the C.O.L.A.s!

The problem is political. It was decided by the new Administration that real spending and tax cuts would not be tolerated because they would threaten the politics of envy and inflation, both of which are deeply entrenched in the political system built up since F.D.R. The new gospel of supply-side economics does not challenge these forces, seeking to manage rather than liquidate them. And *that* is the trouble.

The "bible" of this "New Economics" is the much-touted book *Wealth And Poverty*, by George Gilder. Mr. Gilder is a longtime "Liberal" Republican whose schooling was paid for by David Rockefeller. M.S.

Forbes Jr. of *Forbes* magazine praises the book as "a first-rate analysis of the supply-side school of economics, whose practitioners will provide the cutting edge for economic policy in the Reagan Administration." And C.I.A. boss William J. Casey, a member of the Rockefeller C.F.R., applauds it as "a brilliant book that will serve as an inspiration and guide for the new Administration." So does William F. Buckley Jr.

But Gilder's alleged "defense" of Free Enterprise capitalism is thoroughly phony. He maintains that Free Enterprise is based on chronic uncertainty, sheer luck, blind faith, and self-sacrificial obligations to society on the part of producers. In contrast, he credits socialism with rational scientific planning. Indeed, Gilder clearly argues that Free Market entrepreneurs cannot plan rationally. While he offers some useful criticisms of the Welfare State, he does not reject its ethic. Gilder's criticism of the federal government is that it isn't efficient enough! He ignores the fact that if it gets any more efficient we will have no more freedom left!

George Gilder's attitude toward government power is essentially one of indifferent acceptance. He writes: "Big government is here to stay." He favors tax-rate cuts, but "the purpose of the cuts, it must be continually stressed, is to expand the tax base — to make the rich pay more taxes by inducing them to consume less and to work and invest more."

Ominously, this celebrated supply-sider tells us not to worry about deficits and inflation, asserting: "The fundamental problem of the U.S. economy is not inflation. It is collapsing productivity caused by declines in innovation and research, by a diversion of resources into real estate and collectibles, by steady expansion of the burden of government on every productive worker, by stagnant and misdirected business investment, by a booming tax-free underground economy of little long-run ability to generate technical progress, by the increasing age and obsolescence of plant and equipment, and by a 40 percent slowdown since 1973 in the rate of growth of capital stock per unit of labor. All these problems are either caused by or made much worse by a perverse and destructive pattern of taxation."

Is tax policy the *only* culprit? What about Budget deficits spun out in monetary expansion (inflation) and sucked up by government borrowing (high interest rates)? What about mammoth spending that has intruded government into every aspect of our lives? Dr. Gary North writes of George Gilder's supply-side approach in *Remnant Review* for August 7, 1981: "What kind of economic analysis is this? I'll tell you: analysis geared to selling a program of *continual deficits and massive inflation* . . . . If the program advocated by the supply-siders brought their analysis of high taxes and regulation into an overall program of reduced government spending, reduced regulation, and the establishment of a gold standard, I would have no objections. If they were to come out forthrightly for higher reserve requirements for banks, the reduction of the Federal debt to zero, the abolition of the Federal Reserve System, and the elimination of all price floors and wage floors, I would cheer. But then they wouldn't be supply-side economists. They would be traditional pre-Keynesian, or Austrian School, economists. They would also be out of office. That is the main fact to remember: their rhetoric is acceptable to the voters only so long as *no threat to the existing welfare system is posed by supply-side economics.*"

The goal of the supply-side tax-rate cuts is to stimulate the economy in order to *outproduce* the destructive effects of Big Government, deficits, and inflation! As Johnny Johnson remarked in the May 27, 1981, issue of his *Daily News Digest*: "Gilder explicitly accepts the idea of ever-increasing government spending and control, and opts only for tax cuts! In some magical way, government will then become more efficient, as if that weren't a contradiction in terms! And our solution is simply to produce more real goods than the government can print paper money! What a race to win!"

What this Rockefeller offspring advocates is not Free Enterprise at all, but a more efficient system of corporate statism. He speculates: "If the American government could make itself more productive than the private sector throughout the spectrum of needed economic activity, the public would gladly surrender its earnings to the state." George Gilder embraces the idea that the state should manage the productive affairs of the nation. There is a word for that, and the word is *fascism*. So much for the ethics of the Rockefeller wing of the supply-siders.

We must be fair to Ronald Reagan and note that he does not see high taxes as the only burden on our economy. What are the Reaganauts doing about regulations and controls? A headline above an article on page five of the August 13, 1981, issue of the *Wall Street Journal* says it all: "Dozens Of U.S. Regulations Are Targeted For Review, Probable Easing, Bush Says." Well, bless Mr. Bush's little heart! Of the hundreds of thousands of federal regulations choking us to our knees, *dozens* are targeted for *review*! Murray Rothbard comments:

"Actually, what they're doing is reducing only the rate of increase [*sound familiar?*] in regulation, and they haven't really cut much regulation. They're talking big but they haven't really done anything. Even their approach to the Davis-Bacon Act provides only a slight reduction. They've certainly done nothing about O.S.H.A. as far as I can see. Probably the second most hated government agency, after the I.R.S., it is still intact. While Interior Secretary James Watt may actually be trying to cut back, rather than just cut the rate of increase, look at all the flack he's getting! I think that's interesting. The only Reagan appointee the 'Liberals' really hate the guts of is trying to do what everybody thinks Reagan wants to do — namely, cut back government. Don't think Reagan's political seismographs aren't recording the message."

President Reagan's political strategists are also aware of unrest over high interest rates. Here he is facing a "Catch 22" situation. If rates are lowered, inflation will renew even stronger than before. If they are kept high, he faces a depression in the private sector that will increase Welfare State spending, expand deficits, and require higher interest rates or more inflation. Either way, he's in terrible political trouble. The situation might already be so completely out of hand that the Fed can no longer control interest rates anyway. Donald S. McAlvany writes in his *Gold And Monetary Report* for August:

"Although economic activity is already below peak levels, debts are still maturing at the incredible rate of approximately $100 billion per month or $1.2 trillion within the next twelve months. Debtors, having neither the income nor the cash to cover these debts, are being forced to borrow more (evidenced by the high Fed loan demand figures). But, lenders, fed up with inflation-related portfolio losses or concerned about borrower insolvency, are backing off, with the results that rates are moving higher *regardless* of monetary or fiscal policy. Business loan demand for short-term borrowings from banks and the commercial paper market grew at a *30% annual rate* in June and July. The government is continuing to 'crowd out' the private sector in the money markets, borrowing to cover the largest deficits in U.S. history at a seasonally-adjusted annual rate of $147 billion (source: Fed's Flow of Funds). This will continue with additional Treasury borrowing over the next nine months of nearly $70 billion."

So the growing money crunch is quickly coming to crisis. Market analyst Richard Russell offers the following scenario: "It's becoming obvious that the Reagan Administration (with Fed participation) is ready to take a 'short' recession in an attempt to bring down the inflation rate. My guess is that they are thinking like this: 'We'll squeeze this economy into late fall or into 1982, then ease up some during 1982 and into 1983. Then as we move into the 1984 election period we'll have the best of two worlds, low inflation and a rising economy." I have only one comment: It's a good plan, but remember that I've been saying that with $4.8 trillion in debt hanging over our heads, the U.S. must inflate or die. Rising inflation has been 'servicing' the U.S. debt. If the inflation rate turns into deflation, the debt will become unmanageable." (*Dow Theory Letter*, July 29, 1981.)

The idea is that, because of gargantuan federal deficits and enormous Treasury borrowing requirements, if interest rates do come down, the Fed will not be able to keep them down for more than a few months. If the government tries to borrow even more to cover its deficits, the resulting severe "crowding out" will force interest rates even higher and kill the economy. If the Fed resorts to a massive monetization of the Debt, this will certainly guarantee that interest rates will zoom into orbit as hyperinflation begins. Inflating the money supply eventually forces interest rates up just as it does other prices. So, no matter which way the government decides to fund its giant deficits, the long-term trend for interest rates is toward the stratosphere. And the "long term" is now just around the corner!

Economic recession will not reduce inflation — it will aggravate it. James Sibbet summarizes the point: "The reason is that the business depression will cut government revenue in half and increase relief expenses so much that the budget deficit will widen out to several hundred billion dollars." Then he warns: "The national debt has an average maturity of less than two years. Rolling it over at present T-bill rates will make the interest cost of this debt rise from $80 billion to $150 billion. That will increase the budget deficit by $70 billion." So, economist Sibbet concludes, "Under economic depression conditions and a fantastic budget deficit, government bonds will fail to sell. Then the Fed has to monetize the debt, and that is the root mechanical cause of excessive money supply and runaway monetary inflation." (*Let's Talk Silver & Gold*, August 27, 1981.)

Well, if recession brought on by excruciatingly high rates of interest will not stop inflation, what will it accomplish? It will let the *Insiders* in the banking system expand credit only to their big corporate cronies and allow them to buy up more of America's assets. Economist and investment advisor David E. Rhoads described to us how this is done through preferential credit rationing that favors some while bankrupting others:

"If you want to increase borrowing by the big borrowers (the friends of the Fed) by 25 percent — and you don't want to increase the money supply by 25 percent to do it — then you have to kill off those who are presently borrowing to get that extra 25 percent. If you don't lend to the little borrowers any more, then you can take the money that they had been borrowing and lend that to the big borrowers. Among the friends of the Fed, we have more lending going on from the banking system. Other areas of the economy — especially home mortgages and consumer credit — are getting much less credit. The collapse of these areas is intentionally engineered by the banks and the Fed, in order to make more credit available to their friends."

Rhoads, who predicts interest rates may peak by late October, with the prime possibly going as high as 24-25 percent, warned that many small- and medium-sized firms will be wiped out at that time. The Fed would only intervene with a bailout operation if its Establishment friends get into trouble. This weeding out process would result in a greater cartelization of the economy under *Insider* control — another fascist aspect of Reaganomics.

Unlike Rhoads, Jim Sibbet does not believe the smaller firms will be allowed to fold. He predicts, "They'll be bought up. They'll be merged. They will fold maybe as far as the stockholders are concerned, but the assets will be taken over." He pointed out that the big banks and corporations won't really need much extra money for these takeovers, because the equity of the firms forced into bankruptcy would be squeezed to almost nothing and cheap to buy.

And, despite the shakiness of their overseas loans, the major banks have actually improved their liquidity in the last couple of years. They have money to lend their friends for corporate takeovers and mergers. For example, besides Du Pont, three or four other big corporations participated in the bidding for Conoco — and borrowed about $24 billion for that purpose. They still have this borrowed money. We expect more Conoco-type deals soon.

Is there a way out? There is one and only one. What is needed is massive spending cuts to balance the Budget and reduce the real tax burden. President Reagan's political victories in Congress and current popularity give him a chance for the moment. He must take advantage of this opportunity by pressing for *real* Budget cuts, including reductions in federal loans, loan guarantees, and subsidies. To bring interest rates down and permit economic growth, the government must reduce its huge credit demands. That means taking apart the Welfare State and doing it now. ■ ■

CRACKER BARREL

■ The political talent of a multitude is nothing but confidence in leadership, noted Oswald Spengler.

■ A vast number of our social ills are the complicated products of the tinkering, muddling, and blundering of social doctors in the past.

■ Every man and woman in society has one big duty, emphasizes William Graham Sumner. That is, to take care of his or her own self. This is a social duty.