Are We Going Over a Cliff?

By: John C. Goodman **May 26, 2012**

Did you know the economy is going to fall back into another recession in the first half of next year? That's the sad news coming from the Congressional Budget Office (CBO), in a **report** released this week.

If current law remains unchanged, on January 1, 2013 American taxpayers will be hit with a whopping tax increase (mainly the expiration of the Bush tax cuts) and a major decrease in government spending (the result of last year's budget deal) as well.

All told, we're looking at a $500 billion double whammy. But aren't economists recommending the opposite medicine? Won't higher taxes and reduced spending dampen economic activity and slow down the current recovery? Exactly. You can think of the January 1st fiscal tsunami as a New Year's Day "anti-stimulus" package. The CBO is predicting that the price we will pay for that package is a "double dip" recession.

But here is something even more disturbing. It turns out that uncertainty – not knowing what Washington is going to do about all this is worse than the reality. Will President Obama and the Congress agree to put off the tax increases? Will they agree to delay the spending cuts? Not knowing the answers to those questions appears to have more impact on the decisions of businesses and consumers than if everyone simply agreed to go ahead and let the bad things happen.

Historically, "uncertainty" has been a slippery concept in the vocabulary of economists. Everyone kind of knows what it means. But a precise definition has been impossible. Until now.

Economists at Stanford University and the University of Chicago have actually created an **uncertainty index** and they have tracked it over time for several decades.

Here's what they found. Their measure of uncertainty **soared during the Obama years**, where it has been at its highest levels over the past 30 years. It's not just uncertainty about what will happen next January that's a problem. In many ways, the entire Obama presidency is the problem. Public policy uncertainty alone is the apparent cause of a peak decline of 2.2% in real GDP, a 13% decline in private investment and the loss of 2.5 million jobs over the past five years.

Put yourself in the position of a small business owner who is considering hiring additional employees. And remember: hiring full-time employees is not a short-term decision. You'll

probably lose money on them for the first 6 to 8 months (while they are in training) and hope to make it back over the following 2 to 3 years.

So peer down the economic landscape for the next few years and what do you see? For starters, you have no idea what your labor costs are going to be. You know that Obama Care will force you to buy expensive health insurance for you employees. But you have no idea what will be required or how expensive it will be. And because the Democrats in Congress were so sloppy in drafting the legislation, the entire health reform bill may be declared unconstitutional.

You have no idea what you non-labor costs of production will be because of another Obama legacy – regulatory agencies pushing the envelope to exceed the authority previous regulators thought they had. Environmental regulations deserve a special uncertainty category of their own. (We still don't know if the Keystone pipeline will ever be approved.)

If you need a loan to help finance new equipment to provide to your newly hired workers, you have no idea if, or when, you will ever get it because Dodd/Frank financial regulations are putting a damper on business loans almost everywhere. And since those regulations are not even finalized, expect mattes to get worse, not better.

As for your cost of capital, do you know what the tax rate on dividends or interest income or corporate profits will be next year? No? Well, no one else knows either.

As for your personal tax rate, there is a lot to worry about there too. Democratic politicians almost never make a speech about the economy these days without mentioning the need for higher taxes. And the likely targets of this quest for more government revenue? Job creators, of course.

More than one commentator has noticed that our current "recovery" has been one of the slowest on record. Going back 60 years, we have had 11 recessions. The one we are in is at the bottom in terms of the speed at which we are getting back to normalcy.

Barack Obama doesn't deserve all the blame for public policy uncertainty, of course. He has to deal with recalcitrant Republicans and unreliable Democratic allies in Congress. Still, I would give the president an "F" on his stewardship of the economy.