

ISSUE BRIEF

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Obama Could Prevent a Made-in-Washington Recession

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The Congressional Budget Office (CBO) forecasts a recession for 2013. Forecasters rarely anticipate a recession. Almost by definition, recessions surprise. Some *unexpected* force or forces conspire to so disrupt the economy that it contracts.

What makes this recession different, and predictable, is that the disruptive force is Washington policies and, even more, Washington behaviors—policies and behaviors for which the nation can thank the Congress and especially President Obama. The policy is Taxmageddon. The behavior is intentional, insistent inaction. The consequence is recession. The response should and will be outrage.

This recession is not yet inevitable. Though Congress has recessed until mid-November, President Obama could and should immediately call it back to finish its bare

minimum tasks for the year. At no time this year has President Obama made the resolution of Taxmageddon a priority, and in this he has joined with Congress in a conspiracy of inertia. But time remains to change course, to prevent the recession-ary job loss and wealth destruction threatening the nation. If a slow-down or even a recession unfolds as CBO predicts, the blame will lie with President Obama. As he said in his recent *60 Minutes* interview, “I think that, you know, as President I bear responsibility for everything, to some degree.” Absolutely.

Mainstream Forecasters Rarely See Recessions Coming.

Economic forecasters almost never forecast recessions. Those few who do forecast recessions do so with great frequency and belong to the doom-and-gloom school of economics. Like a broken clock, these forecasters are occasionally right—not from analysis but merely by dint of repetition.

CBO is not one of these. Like most mainstream forecasters, CBO has forecasts that tend to show the economy moving toward its trend growth path. The difference among forecasters is typically with respect to the speed at which the economy returns to full employment. The bold

have the economy recovering sooner; the more pessimistic have the economy reaching full employment later. There are also typically minor differences in forecasts of inflation and interest rates.

For most, forecasting a recession is entirely out of character. Yet CBO forecasts the economy to slow from 2.2 percent growth in the second half of 2012 to a –0.3 percent contraction for all of 2013. Why? Taxmageddon and the fiscal cliff. As the *Financial Times* noted in its editorial of September 22 of this year, “Despite an increasingly anaemic labour market, Congress is failing to stimulate the economy and address the ‘fiscal cliff’ of expiring tax measures and planned spending cuts, *which could plunge the U.S. back into recession.*”¹

Taxmageddon is the nearly \$500 billion tax hike set to strike on January 1, 2013. It is comprised of the expiring 2001/2003 tax cuts (lower income tax rates, doubled child tax credit, etc.), plus the expiration of the 2 percentage point payroll tax rate reduction, plus some smaller items. The fiscal cliff combines Taxmageddon with massive spending cuts already scheduled to take effect, including huge cuts to national defense under the sequestration provision left over from the farcically

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failed super-committee effort in 2011, plus delayed deep cuts to Medicare providers (the “doc fix”) and some smaller items.

The Drag of Uncertainty: A Downturn Comes Early. As CBO models these policies, Taxmageddon and the rest of the fiscal cliff strike an economy growing at a moderate pace on January 1, and recession ensues. This is not quite right.

Congress has now left Washington, intending to return to conduct business in a lame-duck session in mid-November at the earliest. And there are other scenarios under which the Congress and President Obama will, by choice or by default, leave Taxmageddon and the fiscal cliff issues for 2013. Uncertainty over fiscal policy has increasingly dragged on the economy throughout the year. This uncertainty now grows rapidly—and, with it, the economic drag. Individuals and business, increasingly concerned about a jump in their own tax burdens and the economy’s poor prospects into next year, are reluctant to hire or invest more than is absolutely necessary.²

Consequently, the slowdown resulting from Taxmageddon is

already underway and will worsen as December approaches. Even if President Obama and Congress manage to avoid this calamity by defusing Taxmageddon in a lame-duck session, much damage to the economy will have already been done, leaving 2013 to start with a severe growth slump in any event. In truth, the President and Congress already bought the ticket to a slowdown. If they wait until November or later to act, the only question is how long and how deep the slowdown will go.

Obama’s Last Chance to Prevent Recession. President Obama should demand that Congress return and defuse Taxmageddon. In a similar circumstance, he relented once before, in 2010, arguing that the economy was too weak to sustain a major tax hike. He was right then and would be right again in so saying.

A permanent extension would be best, but in fairness, that is too much to expect from a Congress that has fulfilled precious few of its legislative obligations this year. Instead, Obama could argue for a one-year extension, and lawmakers can decide what happens a year from now after New Year’s.

Surely Obama knows about the economic slump that is assured if Congress waits until after the election to act—and the recession that CBO predicts if Congress does not act at all. His own economic advisers have doubtless confirmed these predictions. And surely Obama does not want to see his second term (if he wins re-election) torpedoed by yet another recession, this one effectively and clearly of his own making.

Not Too Late for President Obama to Lead. President Obama should demand that Congress return to defuse Taxmageddon, and Congress should immediately heed his call. The job need only take a few days away from their campaigning. The electorate would likely consider Members’ returning to do their job a responsible act, demonstrating that in a pinch, when the chips are down and the stakes high and clear, Washington can complete the nation’s business. It could be the most popular thing they do all year.

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1. Editorial, “Bernanke’s Gamble Is No Free Lunch,” *Financial Times*, September 21, 2012, <http://www.ft.com/intl/cms/s/0/deb36148-03eb-11e2-9322-00144feabdc0.html#axzz27a92PQnv> (accessed September 26, 2012). Emphasis added.

2. Curtis S. Dubay, “Taxmageddon Is Slowing the Economy Now,” The Heritage Foundation, *The Foundry*, June 20, 2012, <http://blog.heritage.org/2012/06/20/taxmageddon-is-slowing-the-economy-now/>.