The Global Debt Catastrophe

Governments world-wide are erecting towers of debt so high that they will, a decade from now, come crashing down in the next great financial crisis.

August 31, 2014

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Governments world-wide are erecting towers of debt so high that they will, a decade from now, come crashing down in the next great financial crisis. The debt problem was featured in a Cato Policy Report of May/June 2014, a review of the book, *The Government Debt Iceberg*.

The report states that “current generations have been consuming at the expense of future generations.” That is true in a financial sense, but not from an economic perspective. Today’s consumption comes from today’s production. We cannot today consume the future’s output. However, we do today live at the expense of the future in the excessive consumption of natural resources, such as the fish in the sea, and also in spoiling the natural environment. But that is a different topic from the government-debt problem.

The main problem with government debt is that promises are being made to the poor and the elderly, which cannot be kept. The present value of the funds promised to pay for medical care and retirement income are seven times greater than the present value of funds expected from taxation. There are various estimates of these unfunded liabilities, but for the USA they are in the order of $120 trillion dollars, seven times the amount of the official debt of 17 trillion dollars.

Today, the credit of the United States is still good. For the next several years, the USA will be able to borrow funds, but as the explicit debt becomes ever greater, US treasury bonds will no longer be regarded as safe from risk. The debt service will grow as a risk premium is added to the interest rate paid by the Treasury.

In *The Government Debt Iceberg*, published by the Institute of Economic Affairs, Jagadeesh Gokhale calculates that to close the fiscal gap, an extra nine percent of GDP in tax revenues would have to be levied each year. That would require more than doubling federal payroll taxes if the entitlement funds continue to come from that source. The debts of Europe and Japan are even worse. Gokhale proposes to have governments publish the real economic debt, forward-looking measurements that include all unfunded liabilities, so that the debt is no longer an iceberg, mostly hidden beneath the surface appearance.

There are four possible solutions to the towers of debt. The first and best is rapid growth, so that the ratio of national income to deficits rises. The only possible way to induce high economic growth is with an efficiency tax shift--replace market-hampering taxes with market-enhancing levies on pollution and land value, plus voluntary user fees.

The second alternative to avoid the catastrophic crash of government liabilities is to greatly reduce the obligations. But cutting medical and retirement benefits would create economic hardship and be politically infeasible. Governments will most likely reduce the growth of future liabilities by raising the eligibility ages, reducing the growth of benefits, and increasing co-payments. But that will still leave a large economic debt.

The third alternative is to greatly increase current tax rates, but that option would stifle growth and make workers even more dependent on entitlements. The fourth alternative is high inflation, which would reduce the value of the explicit debt, but if social security and medicare are indexed to inflation, that would not solve the problem of keeping the promises.

The only way to avoid economic catastrophe is to raise the income of workers by eliminating taxes on wages and goods, and using the economic surplus that is land rent to finance government. Workers would then be able to afford to pay for their own expenses. Unfortunately, neither the Cato review nor the IEA book even mention this efficiency tax shift.

Much of the funding for policy institutes derives from the profits of the landed interests, and that influences policy positions. These organizations believe in free markets, but are constrained by their lack of the ability to study the subsidies to land values. So we have to rely on geoist or Georgist organizations and scholars to analyze and publicize the most effective solutions. The world is stuck in poverty and debt, because the landed interests prevent the exposure of their subsidies.

The advocates of geoism or Georgism, the concept, promoted most prominently by Henry George, of equal rights to land rent, thus using land rent for public revenue and personal dividends, are a union of egalitarian advocates for justice, and individualist advocates for liberty. They hold the keys to the resolution of economic woes and political conflicts, but they are but a small remnant of today's progressive movements. Therefore the most effective solution to the debt will not even be discussed in the major media, and we will, once again as in 2008, be pushed by the currents of the river of deficits, towards an even greater financial waterfall.

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FRED E. FOLDVARY, Ph.D., (May 11, 1946 — June 5, 2021) was an economist who wrote weekly editorials for Progress.org since 1997. Foldvary’s commentaries are well respected for their currency, sound logic, wit, and consistent devotion to human freedom. He received his B.A. in economics from the University of California at Berkeley, and his M.A. and Ph.D. in economics from George Mason University. He taught economics at Virginia Tech, John F. Kennedy University, Santa Clara University, and San Jose State University.

Foldvary is the author of *The Soul of Liberty*, *Public Goods and Private Communities*, and *Dictionary of Free Market Economics*. He edited and contributed to *Beyond Neoclassical Economics* and, with Dan Klein, *The Half-Life of Policy Rationales*. Foldvary’s areas of research included public finance, governance, ethical philosophy, and land economics.

Foldvary is notably known for going on record in the *American Journal of Economics and Sociology* in 1997 to predict the exact timing of the 2008 economic depression—eleven years before the event occurred. He was able to do so due to his extensive knowledge of the real-estate cycle.