10. ''Starving the Beast'' Will Not Work

> ***Congress should***
>
> - *not* expect a reduction of federal revenues to reduce federal spending and
> - continue to reduce the most distortive federal tax rates but accept the responsibility to reduce federal spending as a necessary complement to the reduction in tax revenues.

For nearly three decades, many conservatives and libertarians have argued that reducing federal tax rates, in addition to increasing long-term economic growth, would reduce the growth of federal spending by ''starving the beast.'' That position has been endorsed by, among others, Nobel laureates Milton Friedman and Gary Becker in *Wall Street Journal* columns in 2003.

Friedman summarized this perspective as follows:

> . . . how can we ever cut government down to size? I believe there is one and only one way: the way parents control spendthrift children, cutting their allowance. For governments, that means cutting taxes. Resulting deficits will be an effective—I would go as far as to say, the only effective—restraint on the spending propensities of the executive branch and the legislature. The public reaction will make that restraint effective.

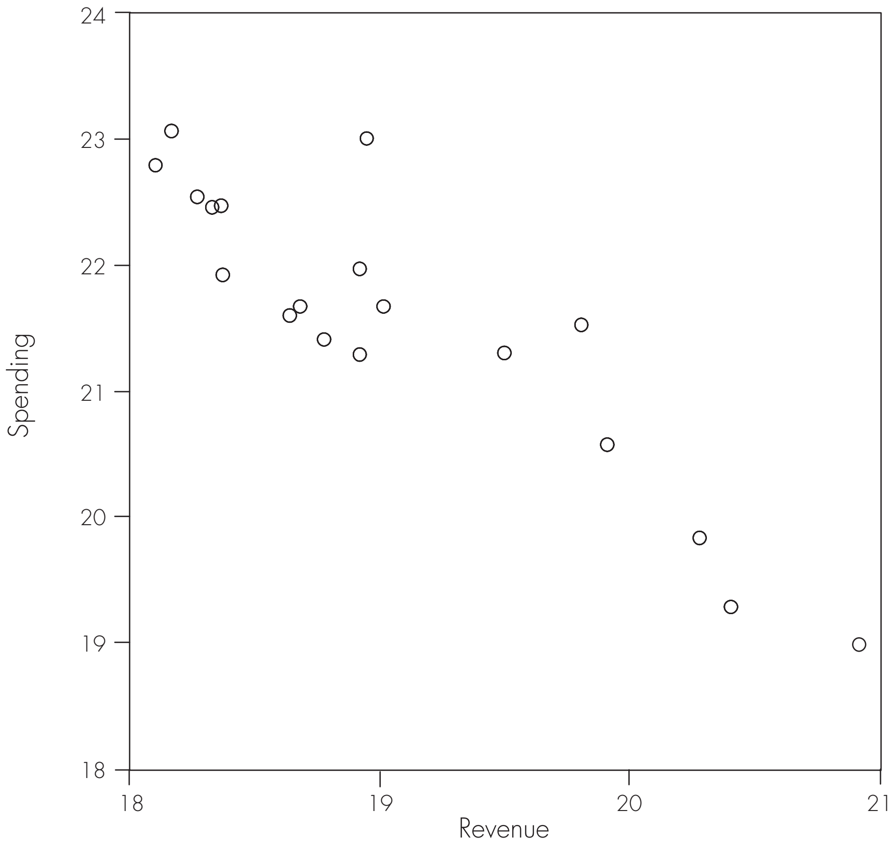
Becker and his colleagues describe this effect as ''The Double Benefit of Tax Cuts.''

There are two problems with this perspective. The first is that this perspective has *not* been consistent with the evidence, at least since the late 1970s.

In a brief note in a professional book that was published in 2002, I presented evidence that the relative level of federal spending from 1981 through 2000 was coincident with the relative level of the federal tax burden in the *opposite* direction; in other words, there was a strong *negative* relation between the concurrent relative levels of federal spending and tax revenues during this period, as illustrated by Figure 10.1. Controlling for the unemployment rate, the federal spending share of GDP *declined* by about 0.5 times the increase in the federal revenue share of GDP.

What is going on? The most direct interpretation of this relation is that it represents a demand curve—that the demand for federal spending by current voters declines with the amount of that spending financed by current taxes. Future voters will bear the burden of any resulting deficit but are apparently not effectively represented by those making the current fiscal choices.

Figure 10.1
Federal Spending and Revenue as a Percent of GDP
1981 through 2000



An update of this test confirms that there was a significant negative relation between the relative levels of federal spending and tax revenues (lagged one year) for the 25 years from 1979 through 2003, again controlling for the unemployment rate. An estimate of this equation for the prior 25 years from 1954 through 1978 also indicated a negative relation between the relative level of federal spending and tax revenues (again, lagged one year) but one that was not statistically significant. For no extended period did these estimates reveal a significant positive relation between the relative level of federal spending and tax revenues, the necessary condition for the ''starve the beast'' hypothesis to be confirmed.

At the limit, of course, the ''starve the beast'' hypothesis must be correct; there must be some maximum tolerable deficit that would force Congress to reduce spending by an amount equal to any reduction in tax revenues. The evidence of the above tests, however, is that there has been no such effective limit in the past 50 years.

The second problem is that the ''starve the beast'' perspective has led too many conservatives and libertarians to be casual about the sustained political discipline necessary to control federal spending directly, succumbing to the fantasy that tax cuts would solve this problem. President George W. Bush, for example, has proposed and won the approval of most congressional Republicans for large increases in federal spending for agriculture, defense, education, energy, homeland security, Medicare, and transportation, and he has yet to veto a single spending bill. As a consequence, real per capita federal spending during the Bush administration increased at the highest rate since the Johnson administration.

The political discipline necessary to control federal spending must involve a sustained commitment to principle. Members of the administration and Congress must increasingly ask *why* federal taxpayers should finance some program, rather than only how or how much. The necessary discipline requires that members of Congress address the following questions in both the authorizing and appropriation processes: Does the Constitution include explicit authority for the program or activity? Is the federal government better qualified to perform the activity than state and local governments or the private sector? Is the proposed federal activity the best of alternative ways to accomplish the shared goal? Is the marginal benefit of the federal activity higher than the marginal cost to the economy of the taxes necessary to finance the activity? A negative answer to any of those questions should be sufficient to reduce or eliminate the activity, whether it is among those already funded or those proposed. Other chapters

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of this *Cato Handbook* identify numerous current federal programs or activities that should be reduced or eliminated on the basis of one or more of these criteria. A focus on domestic discretionary spending other than for homeland security will not be enough; such spending is now only 18 percent of total outlays and includes much of the spending that benefits specific districts and is especially protected by members of Congress.

Conclusion

Above all, keep in mind that the size of government is best measured by the level of spending and regulation, not by the level of taxes. Reducing tax revenues without a commensurate reduction of federal spending only shifts part of the burden of current government spending to future generations—including *your* children and grandchildren.

Suggested Readings

Becker, Gary S., Edward O. Lazear, and Kevin M. Murphy. ‘‘The Double Benefit of Tax Cuts.’’ *Wall Street Journal*, October 7, 2003.

Edwards, Christopher. ‘‘Downsizing the Federal Government.’’ Cato Institute Policy Analysis no. 515, June 2, 2004.

Friedman, Milton. ‘‘What Every American Wants.’’ *Wall Street Journal*, January 2003.

Niskanen, William A. ‘‘Comment.’’ In *American Economic Policy in the 1990s.* Edited by Jeffrey A. Frankel and Peter R. Orszag. Cambridge, MA: MIT Press, 2002.

—Prepared by William A. Niskanen

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