The package's problem is physics

By Don Wiggins
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Recently, the big news in the U.S. has been company failures, bailouts, falling stock and real estate prices, and stimulus packages. The government can supposedly "jump-start" the economy by company bailouts, infrastructure projects, "short-term" assistance programs, and otherwise spending money. People go to work, bridges get built, and the economy is stimulated.

The problem with this idea is basic physics. There are many similarities between physics and economics, particularly the laws of thermodynamics. The first law says that the increase in energy in a system is equal to the energy added from some source minus the amount lost in the transfer.

This has two implications for stimulus programs. First, energy added to a system, such as funding for make-work government programs, has to come from somewhere. Energy can't be created or destroyed, just moved around. The energy being added by stimulus programs comes from additional government spending, which can come from three sources.

One: current taxpayers. The government can raise current taxes to pay for programs. This is obviously a direct wealth transfer from U.S. taxpayers to the companies and individuals who receive money under the stimulus programs. The money is simply spent one place in the economy instead of another.

Two: inflation. The government can create money and cause inflation, which is a hidden current tax. Your money deteriorates in value, say 5 percent, and the government receives the value you lose. It's the same as the government directly taxing away 5 percent of your money.

Three: future taxpayers. The government can borrow and spend the money on stimulus programs, shifting the tax burden to future generations. My children have irritated me occasionally, but not to the extent that I want to put a massive obligation on them.

The money borrowed by the government is unavailable for other borrowers, such as companies or individuals. This governmental "crowding out" reduces economic activity somewhere else in the economy.

The first law of thermodynamics also says that the energy added is reduced by the amount lost in the transfer. In stimulus programs, part of the money is wasted by government bureaucracy costs and part by normal government inefficiency in running programs.
Ultimately, stimulus packages are simply a wealth transfer with a large efficiency loss. By stimulus logic, you could sail your sailboat by placing a big fan on the deck and pointing it towards the sail.

Another "benefit" often cited by advocates is that the packages inspire confidence because something is being done. In the sailboat example, the sail will billow out and look impressive, but the boat will only sit still in the water and burn electricity. Any confidence the billowing inspires will be short-lived.

Negative effects of the transfer loss can be reduced by spending on certain types of programs, such as bridges or roads rather than purely make-work programs. But it's still negative.

Next time we will talk about cooling your house by opening the refrigerator door.

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