The Washington Post

A sturdier US economy can withstand automatic spending cuts resulting from budget standoff

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February 28, 2013

WASHINGTON — As economic policy goes, experts say, the automatic spending cuts that kick in Friday are — to use a technical term — bone-headed.

Fortunately, the self-inflicted wound isn't going to leave a deep scar on an economy that is otherwise looking pretty good. It's a fiscal speed-bump on the road to economic recovery, which is why the stock market is nearing an all-time high despite Washington's latest display of legislative paralysis.

That's a marked change from the past two years, when budget battles rattled consumer and business confidence and triggered big selloffs.

"Businesses and consumers have begun to look away from the histrionics and the battles going on in Washington," says **Bernard Baumohl, chief global economist at the Economic Outlook Group.** "They're beginning to realize that organic growth in the private economy is beginning to pick up speed."

From Wall Street to Main Street, Americans are too busy spending, hiring and investing to panic over Washington's latest budgetary melodrama.

They've seen this movie before. And this time, the ending doesn't scare them.

Even with Friday's trigger date for the cuts drawing near, Americans have been pouring money into the stock market. The Dow Jones industrial average has jumped nearly 8 percent this year and is approaching a record high.

Consumers are also growing more confident. And last month, orders for U.S. factory goods that reflect companies' investment plans surged by the most in more than a year. It showed that more businesses have become more upbeat about their prospects.

Only 27 percent of Americans surveyed for a Pew Research Center/USA Today poll last week said they had heard a lot about the looming spending cuts. And according to a Washington Post poll conducted late last month, less than a third of Americans said they thought the cuts would have a big impact on their own finances.

Why less concern this time?

The stakes aren't nearly as high as they were two months ago, when lawmakers engaged in a budget standoff over the so-called fiscal cliff. Economists had warned that the cliff's tax increases and spending cuts would send the economy back into recession if they remained in place for much of 2013.

By contrast, no one is talking about a recession this time, no matter what Congress does or doesn't do. The financial squeeze will be milder. And it will be delayed.

For one thing, the cuts are smaller than they seem: Actual spending will likely drop $44 billion in the budget year that ends Sept. 30, according to the Congressional Budget. That's only slightly more than 1 percent of federal spending.

Of that, about 80 percent will come from discretionary programs, which includes everything from environmental protection to defense spending. The rest will come from Medicare and other entitlement programs.

What's more, federal agencies must give workers a month's notice before imposing furloughs, which will likely force many to take one day a week of unpaid leave indefinitely. So the pay and spending power of government workers and many contractors won't be affected until April at the earliest.

Perhaps more important, the delay gives lawmakers time to seek a deal that might retroactively reverse the spending cuts before they could do much damage to the economy.

"If it lasts a matter of a few weeks or a few months, I don't think it will have any measurable impact on growth," **Baumohl** says.

Scott Anderson, chief economist at the Bank of the West, estimates that if the budget cuts lasted only through March, economic growth would drop just 0.1 percentage point in 2013. That change would reduce his estimate of growth for the year from 1.8 percent to 1.7 percent.

Not that the spending cuts won't hurt many workers and consumers. And

the longer the cuts are in place, the more they will slow growth, depress hiring and keep unemployment stranded at high levels.

If the automatic spending cuts aren't reversed, they would reduce economic growth in 2013 to 2 percent from 2.6 percent, wipe out 700,000 jobs and keep unemployment at 7.4 percent or higher through 2014, according to calculations by Macroeconomic Advisers, a forecasting firm.

Growth would rebound to 3.4 percent in 2014, the firm says. In part, that's because the Federal Reserve is expected to keep short-term interest rates near zero to blunt the economic damage from the spending cuts.

The spending cuts are taking effect just as the economy shows its most sustained improvement since the recession officially ended in June 2009.

The housing market, which had helped slow the economy's growth from the housing bust in 2006 until last year, is finally recovering. Sales of new homes rose last month to the highest level in 4½ years. Home prices rose in December from a year earlier by the most in more than six years.

The Commerce Department reported Thursday that business investment in buildings, machines and software rose at an 11.2 percent annual pace the last three months of 2012.

Companies are hiring more, too: Private employers added an average of 208,000 jobs a month in November, December and January, up from an average 155,000 from August through October.

That job growth is giving more people money to spend. After stagnating since the recession ended, hourly pay has risen faster than inflation the past three months. Families have reduced their debts and are in a better position to spend — although they did get pinched when a Social Security tax cut expired in January, raising the annual tax bill of someone earning $100,000 a year by $2,000.

Without the political dysfunction, **Baumohl** says, the economy would be growing at a healthy 3 percent annual pace.

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