It Is Time to Remove the Debt Barrier to Economic Growth

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Out of habit, American economists worry about federal debt. But federal debt can be redeemed by the Federal Reserve printing the money with which to retire the bonds. The debt problem rests with individuals, companies, and state and local governments. They have no printing press.

We have explained that the indebtedness of the population means there is little discretionary income with which to drive the economy. The offshoring of middle class jobs lowered incomes, and after paying debt service—mortgage interest, car payments, credit card interest, student loan debt—Americans' pockets are empty.

This situation has been worsened by Covid lockdowns. In the US the federal government has sent out a few Covid payments to help keep people's heads above water as they face expenses without income. The financial press refers to these Covid checks as "fiscal stimulus," but there is no stimulus. The Covid checks do not come close to replacing the missing wages, salaries and business profits from lockdowns.

Corporations have indebted themselves and impaired their capitalization by borrowing money with which to repurchase their stock. This has built up their debt in the face of stagnant or declining consumer discretionary income.

We propose to deal with the debt crisis by forgiving debts as was done in ancient times. Our basic premise is that debts that cannot be paid won't be. Widespread foreclosures and evictions would further worsen the distribution of income and wealth and further contrain the ability of the economy to grow. Writing debt down to levels that can be serviced would clear the decks tor a real recovery. Income that would be siphoned off in debt service would instead be available to purchase new goods and services.

A few economists muttered that we were overlooking the "moral hazzard" of absolving people of their debts. But leaving the economy stagnated in debt is also a moral hazzard.

Policymakers did not endorse our proposal, but, in effect, policymakers adopted our policy. However, instead of forgiving the debt itself, they forgave payment of the debt service. Individuals and businesses who cannot pay their landlords or lenders cannot be evicted or foreclosed until June. This doesn't hurt the lenders or banks, because the loans are not in default, and their balance sheet is not impaired. The banks add the unpaid payments to their assets, and their balance sheets remain sound.

When June arrives, the prohibition against eviction and foreclosure will have to be extended as the accrued debt service cannot be paid. Extending the moratorium on foreclosures and evictions will just build up arrears. Is the implication a perpetual moratorium?

The question is: If policymakers are willing to forgive debt service, why not just forgive the debt. The latter is neater and clears the decks for an economic renewal.

The US economy has been financialized. Debt has been built up without a corresponding gain in productive capital investment in order to carry the mounting debt.

In financialized capitalism, the main purpose of bank loans is to refinance existing investments, not to expand productive capacity with which to service the debt. It is not possible to grow out of debt in a financialized economy, because too much income is used for debt service. The way to deal with this problem is to write down debts.

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