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Fiscal Cliff: Republicans in Crisis

Fiscal Cliff: Last week, Treasury Secretary Geithner proposed \$600 billion in spending cuts for \$1.6 trillion in tax increases, which would include closing loopholes, limiting deductions and raising tax rates on the wealthiest Americans. Predictably, Speaker Boehner unveiled the GOP's counteroffer yesterday, calling for \$1.4 trillion in spending cuts and \$800 billion in tax increases through loopholes and deductions, not rate increases. Both sides will continue haggling during the next four weeks to reach a deal somewhere in the middle regarding the degree and nature of spending cuts and tax increases. The deal will most likely be reached around Christmas.

Secretary Geithner made it clear that the math to achieve enough tax revenues will not work unless tax rates for the highest income earners rise. It's a position that will be hard for him to backpedal from. We believe that Republicans will swallow the bitter pill of rate increases in exchange for more spending cuts to entitlement programs, namely Medicare. While such a scenario will be positive in that it avoids the fiscal cliff, it will worsen the economic outlook in 2013, arguably limiting GDP growth to 2%.

Republicans in Crisis: While no one really wants to see the fiscal cliff occur on January 1 because taxes will jump for almost all Americans, the current state of negotiations in Washington is deeply disappointing and foreboding. Democrats do not believe in lower taxes to incentivize Americans with the most capital (the rich) to reinvigorate growth, and Republicans are losing politically because while they defend tax cuts, they continue to threaten the social safety net during an economic crisis.

The Wanniskian political-economic model posits that the collective wisdom of the electorate knows the optimal policy solution, and it chooses the candidates/Party that comes closest to that solution. Today, the electorate doesn't want tax increases or spending cuts; for good reason. Tax increases, of course, disincentivize risk-taking capital, ultimately slowing production and growth. And the spending cuts being discussed will have a minimal impact on protecting the government programs that Republicans say they want to save. Accelerating economic growth by 0.1%, however, has 27 times the impact of reducing spending by 0.1%, [according to](#) the Club for Growth's Louis Woodhill.

Today, anti-rich tax-loving Democrats and Grinch Republicans are offering the American electorate what it doesn't want. Therefore, neither party has a mandate. **If there is any mandate, it is that both parties should work together and do as little as possible to upset the status quo, i.e. don't raise too many taxes and don't cut spending too much.**

For as poor as President Obama and the Democrats are on economic issues, a serious focus and criticism must be placed on Republicans. For as long as the economy remains weak and the GOP cannot offer a credible pro-growth solution, then Democrats who promise to protect the social safety net will have the political edge. This implies that if Republicans can get their act together to revitalize the economy, then elections will always be theirs to lose.

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Unfortunately, Republican Leadership is failing, allowing austerianism to infect the Party since 2010. Paul Ryan, who argues that growth will not solve the looming entitlement crisis, has been championing Medicare reform since then, even though Republicans never had a chance to pass it through the Senate. Not only was the maneuver politically imprudent, his assumption is wrong: the economy need only grow 3.5% consistently, and entitlement programs will be easily paid for by the federal government. Ryan's gambit effectively killed Republican political momentum since 2010. But Ryan won't quit; he is leading the campaign to demand relentless spending cuts as part of any fiscal cliff deal.

The Republican Party needs a Kempian renaissance, a reawakening to the ideas that made Jack Kemp beloved. The Party must heed Kemp's advice in his book, *An American Renaissance*, written in 1979, on how to politically balance the issue of economic growth and spending:

It seems to me the proper solution to the growing burden of social spending, then, is not to lower the safety net so far that it bounces against the ground, by slashing social-support programs. Instead, we must draw people out of the net by expanding attractive opportunities in the private sector. A vibrant economy can afford to leave the safety net in place and at the same time ensure that the net is as empty as possible.

Where is John Boehner or any other Republican, for that matter, promising to protect Americans during the economic crisis, while putting forth a better growth plan? Voters are always looking for peace and prosperity. Jude Wanniski, Jack Kemp's mentor, taught that one can only create prosperity with stable money, and peace with diplomacy as war is the failure of diplomacy. Can one have faith in the Republican Party as it stands today?

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