

[The micro alternative](#) [1]

Written by [Jan Boucek](#) [2] | Tuesday 9 August 2011



Financial markets are brutal task masters. Three years ago, they forced due recognition that housing and real estate were over-inflated and over-indebted. This past week, they did the same with western government finances. In both cases, the message from the markets has been clear ? we can?t go on like this anymore. Blame the markets for being rude about it but don?t blame them for being wrong. They should have blown the whistle sooner but at least they had a whistle, unlike the politicians and their attendant hangers-on.

This has been and will continue to be a tough one ? there?s just too much debt out there and it?s still growing for any simple one-button macro solution. G7 summits and spread-sheet driven Plan B?s aren?t going to make it. Even the Chinese last week fired off a warning that ?the US government has to come to terms with the painful fact that the good old days when it could just borrow its way out of messes of its own making are finally gone.? It?s a warning that applies equally well to most of Europe, including the UK.

Western governments didn?t get into this mess by any single policy that can be undone in one fell swoop. Rather, it was a series of policies that seemed innocuous, well-intentioned and even costless at the time but which slowly sapped economic growth potential. The list is endless and ASI fans can rattle them off easily. Here?s just three obvious ones for the UK:

High marginal tax rates are clearly counter-productive. This needs no explanation for friends of the ASI and our own Eamonn Butler elegantly [restated the case](#) [3] last week.

Extensive labour market regulations discourage employment. Minimum wage rates mean people are unemployed at £5.93 an hour rather than employed at below £5.93. Job security rules mean protection for vacancies that are never created. Ditto for working time and vacation regulations.

Absurd pricing regimes for ?green? energy and immoral subsidies for bio-fuels wildly distort investment from more productive purposes while raising the cost of energy and food for all.

It was curious to see Italy?s belated response last week to its fiscal crisis. Not only was there a macro proposal for a constitutional amendment to balance the budget but micro measures included liberalising closed professions, faster welfare reforms, overhauling the labour code and loosening up regulations on building a house or starting a business. Prime Minister Silvio Berlusconi?s credibility on this isn?t high after so many years in power but at least his heart seems to be in the right place ? finally.

As the markets continue to thrash the errant, don?t be fooled by siren macro solutions of just a bit more quantitative easing, Plan B or slower-and-shallower cuts. It took a couple of decades of endless tinkering with the economy to get us here and it?s going to take some time to undo the worst of it.

It?s the micro-economy, stupid!

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