Economics for the Election Year

Robert J. Gordon
Stanley G. Harris Professor
Northwestern University
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Agenda of Economic Issues: #1 Recession and Recovery

- The Recession and Recovery
  - When did it happen?
  - Why did it occur?
    - (How much blame on Clinton vs. Bush vs. neither)
  - How Bad was it by Historical Standards?
  - Why was it so Mild?
  - Was it “Jobless” or not?
  - The “disguised unemployed”
  - What happened to wages and incomes?
Income Distribution and Social Security

■ #2 Income Distribution: the Fundamental Difference
  ■ What has happened to inequality?
  ■ Who is in the top 1%, top 0.01%?
  ■ Advantages of raising taxes on the rich
    ■ Reduce deficit, pay for health care

■ #3 Social Security
  ■ Is there a crisis? If so, when?
  ■ Bush, Kerry, and other solutions
The Biggest Issue: Medical Care

- The twisted and deformed U. S. medical care system
  - 45 million uninsured
  - Employer-based, not government-based
    - GM: not just current workers, also retirees
    - GM vs. Toyota

- Bush vs. Kerry
  - Bush: Health Saving Accounts
  - Kerry: Catastrophic Coverage by Government
Business Cycles: The Incredible Volatility of Real GDP Changes

[Graph showing actual real GDP growth and average real GDP growth over time from 1950 to 2000.]

- Actual real GDP growth
- Average real GDP growth
Why the Recession?

- Why not? Previous expansion was 10 years old (March 1991 to March 2001)
  - Politics of the dating (November 2000 vs. March 2001)
- What goes up must come down
  - Hi-tech and dot.com investment boom
  - Stock market: Irrational Exuberance
  - Accounting tricks and overstated profits
- Clinton Guilty? Greenspan Guilty?
Why Wasn’t the Recession Worse

- Greenspan’s Monetary Policy
  - Made possible zero-rate auto financing
  - Made possible housing refinance
- Loss in stock market wealth offset by gain in housing wealth
- Bush tax cuts
  - Total 2004 saving $269 billion
    - Bottom 80% $90 billion
    - Top 2 to 20% $90 billion (4.2x as much)
    - Top 1% $89 billion (80x as much)
The Government Budget with and without the Business Cycle

Actual Budget Surplus

Natural Employment Surplus

Percent of natural real GDP

Assessment of Bush Tax Cuts

- 2/3 went to top 20%, 1/3 to top 1%

- If the goal is to stimulate the economy, wrong
  - Top 1% save most of their incomes, spend almost none of the tax cut
  - Bottom 80% spend most of their incomes, spend almost all of the tax cut

- If the goal is to stimulate investment, wrong
  - Domestic Investment = Government Surplus + Private Saving + Foreign Borrowing
How U. S. Domestic Investment is Financed

Figure 5-11: Components of Net Saving and Investment, 1960-2003

- National Saving
- Private domestic saving
- Private domestic investment
- Government Budget Surplus
- Borrowing from abroad
A Jobless Recovery?

Employment as a percentage of 2001 value

Household survey
Payroll survey
Differences between the surveys

- **Changes January 2001 to September 2004**
  - **Payroll survey**
    - Total -821,000
    - Private -1,634,000
  - **Household survey**
    - Total +1,690,000

- **Why the Difference**
  - Less moonlighting
  - Missing new establishments
  - Former employees as self-employed consultants
The “Disguised Unemployed” and Changes in Incomes

- Labor Force = Employed + Unemployed
  - If you’re not looking, you’re not included
  - 2.6 million people have stopped looking
  - Adding the *INCREASE* in the disguised unemployed, the unemployment rate would be 7.2, not 5.4

- Incomes? Increasing slower than inflation 2003-04
  - 9.9 million people laid off in 2001-2003
  - Only 45% have found new full-time jobs
  - Of those, 52% of jobs are lower paid
  - Loss in manufacturing, gain in low-paying service jobs
Income Distribution

- Ratio top 20% to bottom 20%, last 25 years up from 9 to 14
- Top 1% earn 14% of total income, bottom 20% earn 4% \((20\times14/4 = 70)\)
- CEO pay / average worker pay
  - 1979 50, 2001 440
- Who is in top 1%, the theory of the “Four Michaels”
- Pure rents: what happens if you tax them more?
  - Kerry: go back to pre-2001 (33% to 39% marginal rate)
  - Me: go to at least 50% marginal rate
- This is the golden goose that can pay for health care
Social Security

- Why a “Crisis”? 
  - Baby Boomers (1947-64) shift from paying SS taxes to receiving SS benefits 
  - Huge trust fund begins to decline 2015, zero by 2045 

- Bush vs. pay-as-you-go 
  - Young people set money aside for themselves, don’t pay taxes to support today’s elderly 
  - Risk of bad investments, who will bail them out? 

- Solutions: slower increase in benefits, slow rise in taxes, index retirement age to life expectancy 

- Crisis overblown! They don’t understand immigration!
The U. S. Medical Care Debacle

- Most Countries Fund Medical Care through Government Taxes
  - No connection between funding and provision
  - Hospitals and doctors can be private/nonprofit, not government owned or government employees (UK the exception)

- U. S. Employer-based system distortions
  - 45m uninsured
  - Employers convert full-time to part-time jobs
  - Employers aren’t competitive with foreign firms
  - GM and other legacy firms, $1,400 per car
Bush vs. Kerry

- **Bush:** Health Savings Accounts
  - Tax-deductible contributions, spending on medical can be withdrawn tax-free, interest tax-free
  - Unpopular because tied to high deductibles
  - Like all such plans, provide greater benefits to those in the top tax brackets

- **Kerry:** government-funded catastrophic care
  - Would reduce medical care premiums
Neither Addresses Basic Problems

- Employer-based rather than a right of Citizenship
- Republicans love “competition” but look what it brings us in medical care
  - 3 to 4% of GDP on administrative costs
  - Julie’s mail vs. my lack of mail, “this is not a bill”
  - Promotes imports, favors new startups vs. legacy firms
- Universal care, higher co-pays, eliminate paperwork
- The drugs-from-Canada situation
  - U. S. households subsidize drug research for Rest of World
  - Bush legislation prohibits government wielding purchasing clout
  - Why does UK have five firms providing flu shots, U. S. only two?