

**The End of Economic Growth  
And What To Do About It  
(The Key Problems,  
and a Menu of Solutions)**

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***Northwestern Continuing Education***

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# **Economic Issues Relevant to the Election Go Way Beyond Debate Sound Bytes**

- **Today we're going to delve deeply into America's economic problems that give people the feeling that "America is on the wrong path."**
- **The first part of the talk examines those signs of economic weakness that were already evident in 2007, before the recession**
- **Much of the policy discussion is related to these long-run issues, not just how to make the economy recover faster.**

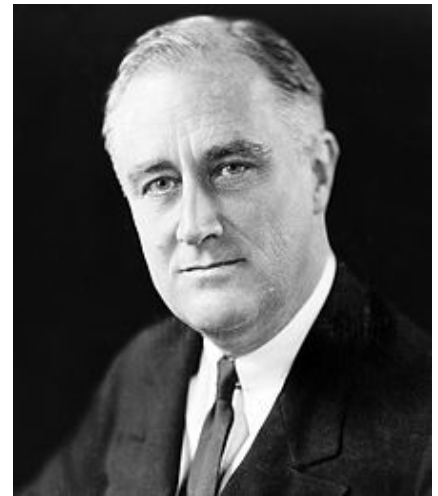
# **There's a Lot to Talk About**

- **Use your handout to follow along**
- **The outline of the talk is on the handout**
- **If you want to go back and look at the slides, they will be posted on my web site. How to find it? Look at your handout**
- **The handout also suggests three recent books if you're interested in following up on some of these topics through the library, bookstore, or Kindle download**

# Outline of the Next Two Hours

- **1. The Long Run, Why “American Economic Growth is Over”**
  - Not literally “over,” but much slower than 1891-2007
  - The media have exploded about this theme
  - For this group, the central issue about why your grandchildren face many more obstacles than you did
- **2. The Short Run, Why the American Economy is Operating Far Below Its Potential Output**
- **3. The Political Debate About the Short Run**
- **4. What to Do About the Long Run?**

# Preliminaries: Who Are You?



- I was born on September 3, 1940, the day that FDR surprised the world by signing a deal to send 50 “overaged” destroyers to the British in trade for rights to 8 “new world bases.”
- How many were born before 9/3/40? After?
- How many of you are retired?
- How many working full time? Part time?

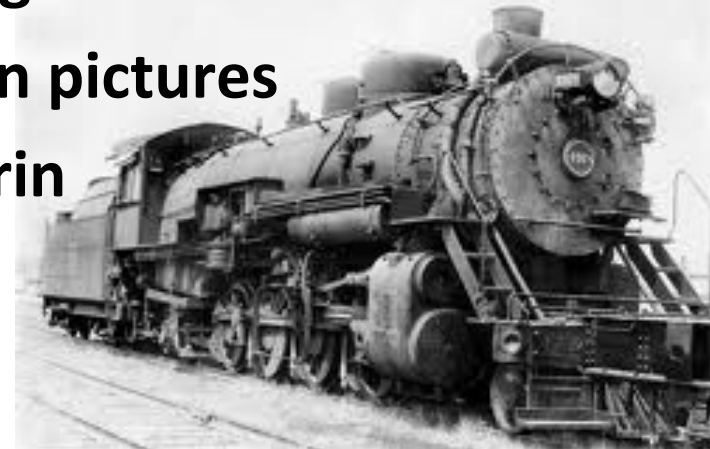
# What Am I Talking About???

## The End of Economic Growth?

- The central theme: technological change is not continuous. The Great Inventions of 1870-1910 involved a **one-time-only** set of changes. They were so important that it took the full century until 1970 to realize their full effect
- These included horses to trucks, outhouses to indoor plumbing, housewives carrying buckets to running water, and many more. The speed of travel increased from the horse to the Boeing 707 in 1958, but not beyond
- **Economic growth may not be a continuous long-run process but an artifact of a unique three-century period of human history. Will the next generation be better off?**

# Organizing Principle for History: The Three Industrial Revolutions

- **First Industrial Revolution (IR #1), 1770-1830**
  - Steam engine, cotton spinning, railroads, iron and steel
- **Second Industrial Revolution (IR #2), 1870-1910**
  - Electricity, elevators, power tools, electrified factories
  - Internal combustion engine: cars, trucks, busses, airplanes
  - Running water and indoor plumbing
  - Telegraph, telephone, radio, motion pictures
  - Chemicals, drugs starting with aspirin





# Third Industrial Revolution (IR #3)

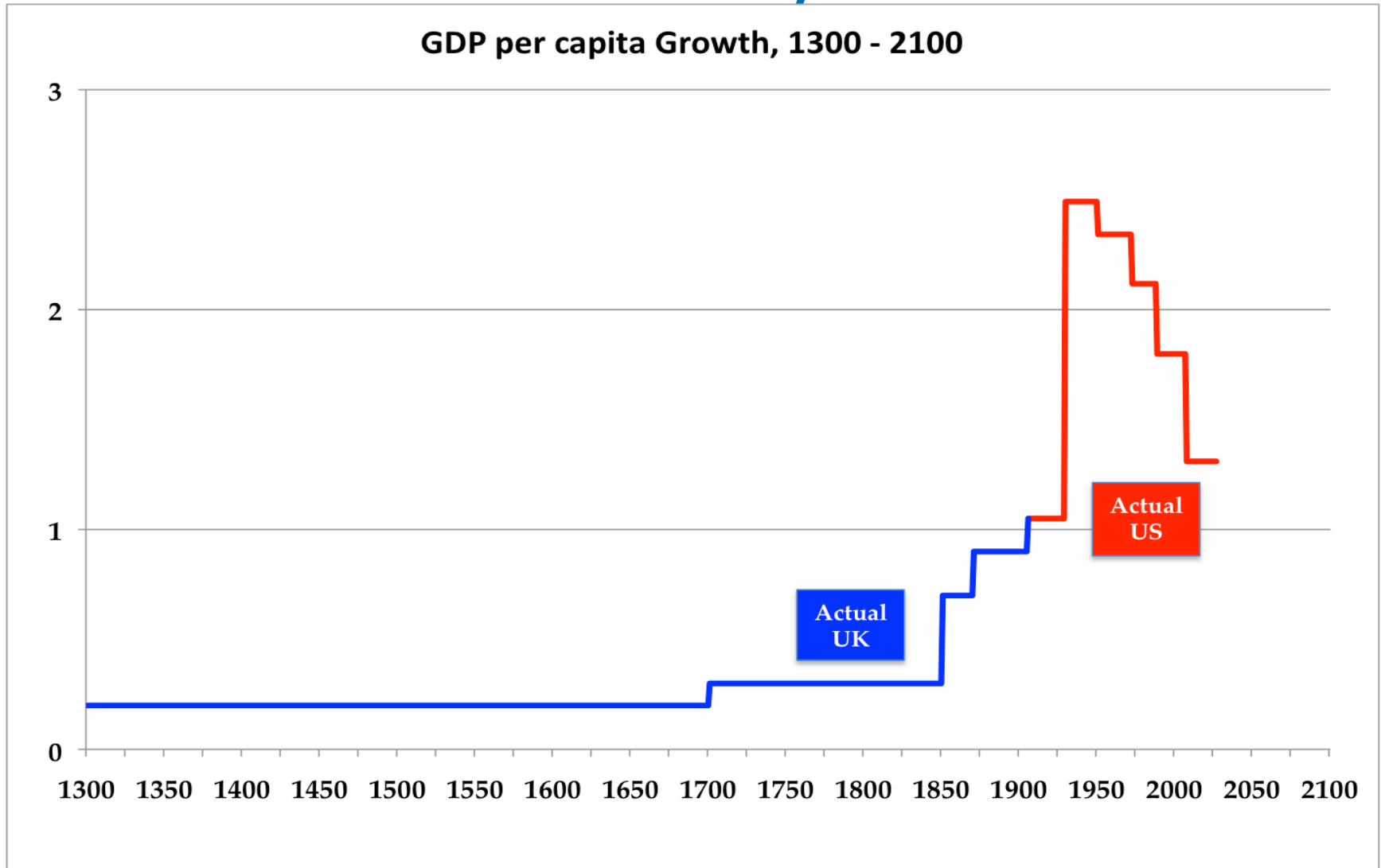
- **Computers and the Internet, 1960-2000**
  - Mainframes allowed computers rather than humans to churn out bank statements and telephone bills
  - Memory typewriters and early PCs eliminated repetitive typing
  - The ATM machine and bar code scanning became common 30 years ago
  - The world's information became available on your home screen more than ten years ago



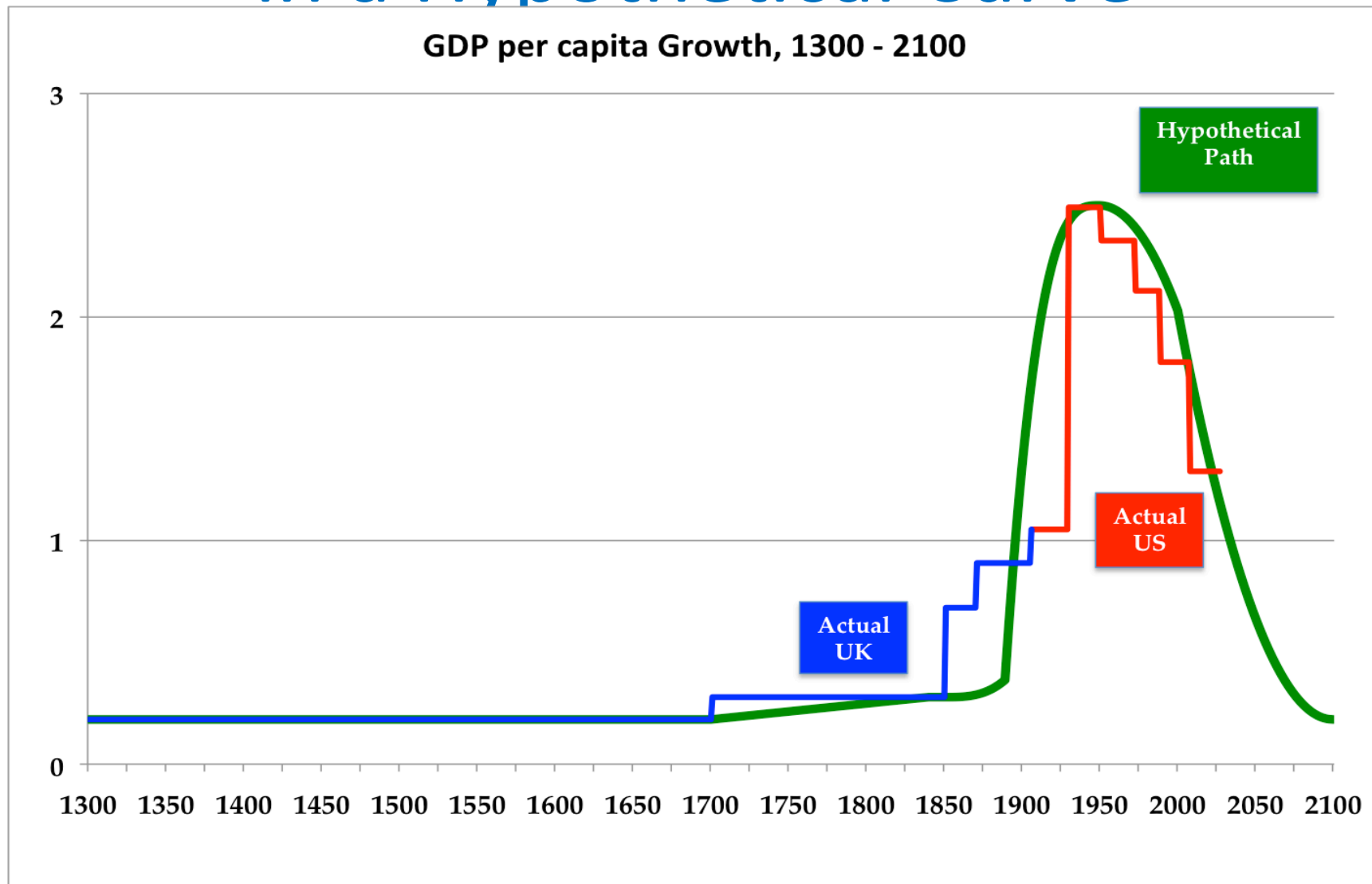
# Why the Great Inventions Are Behind Us: Outline

- UK-US economic growth in context, **1300-2050**
- Examples of low standard of living in 1870
  - Quantity/quality of consumption and of work
- Identifying the Great Inventions of IR#1 and IR#2.
- Which dimensions of human existence did the Great Inventions of IR #2 improve?
- Which dimensions of human existence has a broadly defined IR#3 improved, and when?
- **The seven headwinds, a SEPARATE ARGUMENT**
  - Even if innovation continues as in the last two decades, the headwinds will push growth down

# The Remarkable Three Centuries: Growth of the UK/US Frontier

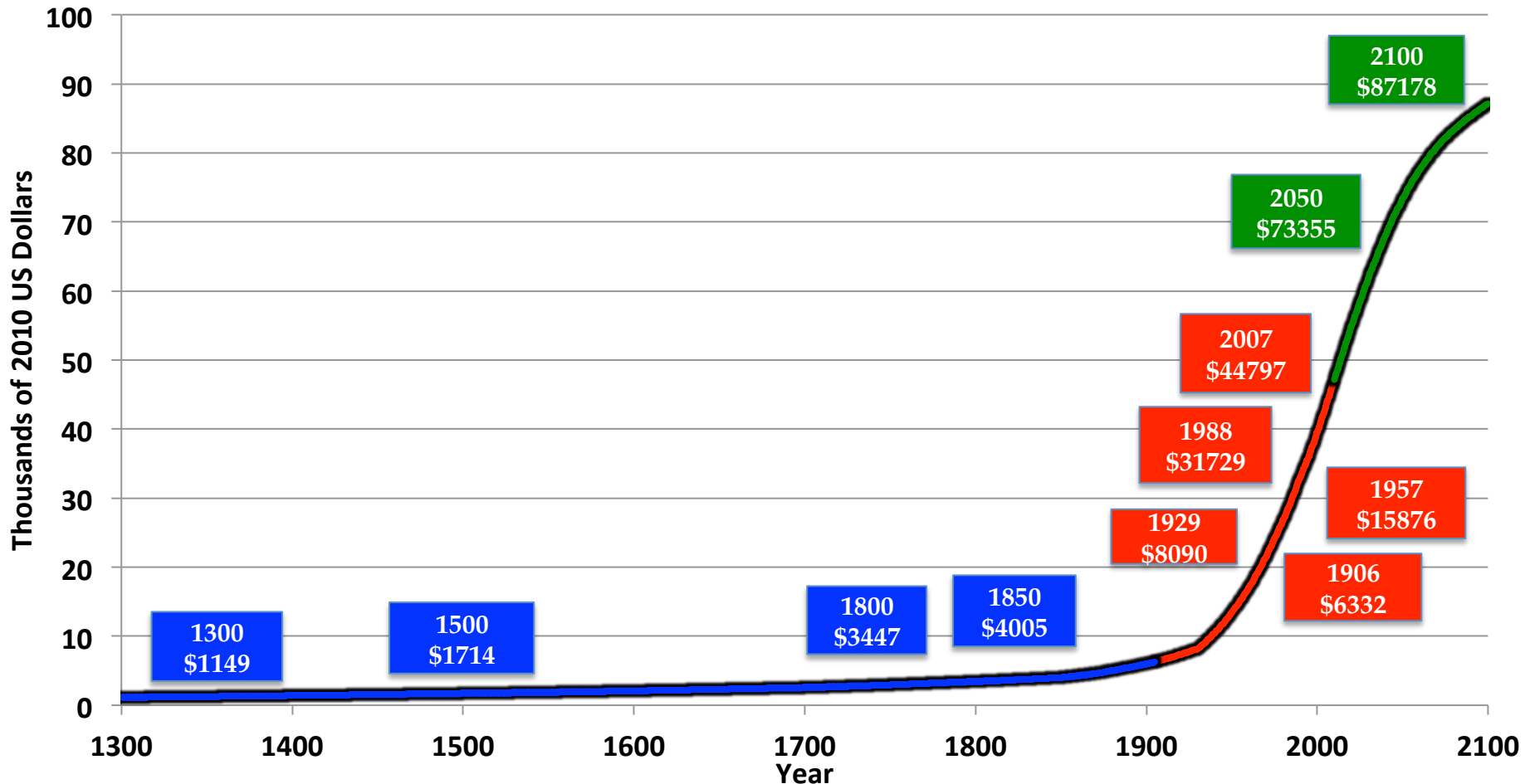


# Capturing the Actual Growth Rate in a Hypothetical Curve



# The *Level* of Historical and Future U.S. Real GDP per Person

Figure 3: Actual and Hypothetical Levels of GDP per Capita, 1300-2100



# Common Features of 1870 Housing, Rural and Urban: Smoke and darkness

- Lack of enclosed iron stoves that could control heat, invented after 1870. Housewives in 1870 **had only the open hearth**, with all its energy inefficiency that would curl the hair of the modern Sierra Club.
- Second, there was no electricity. Light for working and reading at night consisted of lamps fueled by kerosene or whale oil. “Air pollution inside the home”



# THE BIGGEST DEAL OF ALL: LACK OF RUNNING WATER

- Every drop of water for laundry, cooking, and indoor chamber pots had to be hauled in by the housewife, and the waste water hauled out.
- One source claims that the average North Carolina housewife in 1885 had to walk 148 miles per year while carrying 35 tons of water.
- Water in, water out. The water taken out was dirty and/or disgusting. Coal or wood in for fires, ashes out.
- *We all talked about “women’s lib” in our youth; nothing has liberated women more than running water in the period 1890-1930*
- Were summers better than winters in 1870?
  - Window screens had not been invented in 1870!



# Horses (and Pigs) on Every Urban Street

Urban America during 1870-1900 was utterly dependent on the horse. Horses required expenditures each year for food and maintenance equal to their capital cost

- Imagine if your \$30,000 car required every year \$30,000 additional for fuel and maintenance
- The average horse produced 20 to 50 pounds of manure and a gallon of urine daily, applied without restraint to stables and streets. The daily amount of manure worked out to between 5 and 10 tons per urban square mile, all of which required gruesome human labor to remove.





# Why Life Expectancy Was So Low in 1870

- **At birth life expectancy was only 45 years in 1870 compared to 79 years recently.**
  - **Causes in 1870: infant mortality resulting from poor sanitation, water-transmitted diseases, and contaminated milk.**
  - **The first attempts at urban sanitation infrastructure emptied waste not into cesspools but into nearby rivers with no filtration. The theory at the time was that “the rivers cleaned themselves.”**
- **Further causes: hard physical labor, injuries, RR deaths, polluted indoor air, violence, lynchings**
- ***A surprising fact about life expectancy***



# The Standard of Living Involves Not Just the Quality of Consumption but the Quality of Work



- We can rate the “quality of work” as “pleasant” and others as “unpleasant” for different occupations
- In 1870 87% of jobs were in “unpleasant” categories, only 22% in 2010 were in “unpleasant” categories
- And each given job in an “unpleasant” category, say farmers, has utterly changed
  - 1870: farmers pushed a plow behind a horse (see Spielberg’s “War Horse”)
  - 2011: Farmers drove in an air conditioned enclosed John Deere tractor that almost drove itself with GPS.

# Dimensions of Progress from IR #2

- **Replacing Animal Power by Motor Power**
  - Inefficiency of horses, need to maintain horses overnight, stench, need for yucky waste removal
- **Replacing Human Effort**
  - Running water, no more carrying water in and out. Oil and gas replaced coal and wood for fuel
  - Electric hand tools
  - Household appliances starting with washer and refrigerator





# Human Comfort and Convenience

- **Replace outhouse with indoor toilet**
- **Develop sewer systems to carry away the waste**
- **Replace open-hearth fire by central heating**
- **Replace candles and whale-oil lamps by electric lighting**
- **Replace coal as a source of polluted air**

# Speed and Comfort of Travel

- By 1870 RR had revolutionized inter-city travel but the horse still dominated intra-urban. RR speeds 3X 1870-1940.
- Increased speed electric street-car compared to horse-drawn streetcar, then motor bus



- Electric subway and elevated rapid transit
- Motor transit: from dirt roads to interstate highways in < 100 years
- Air travel, we haven't gone faster since (supersonic travel abandoned)

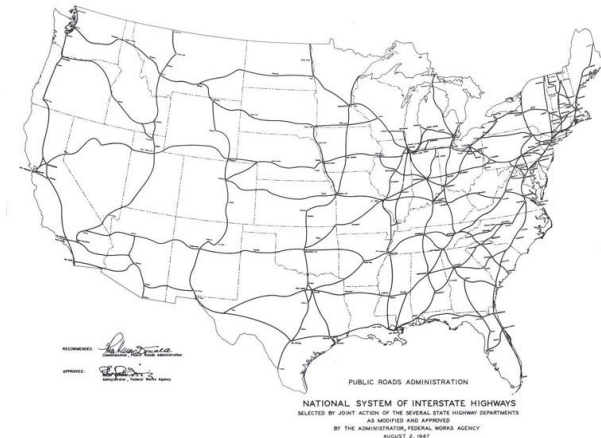
# Communication and Entertainment

- **Speed**
  - 1844 telegraph, one-way communication
  - 1876 telephone, two-way communication
- **Increasing the value of a leisure hour**
  - Phonograph, recorded music
  - Nickelodeon to silent movies to “Gone with the Wind” in 1939
  - 1920 radio, 1946 television



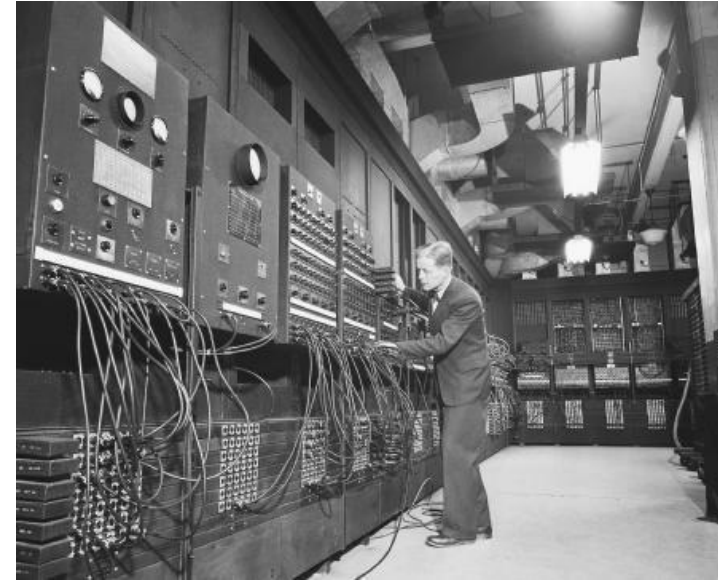
# Within One Century, Life had Utterly Changed

- **Break point, 1970: The Great Inventions of IR #2 had been fully absorbed**
  - Interstate highway system almost completed
  - Air conditioning universal in commerce and widespread in residential homes
  - Air travel completely converted to jet, no further increase in speed
  - Consumer appliances universal, only the microwave oven lay ahead
- **Post-1972 productivity growth slowdown: running out of ideas**

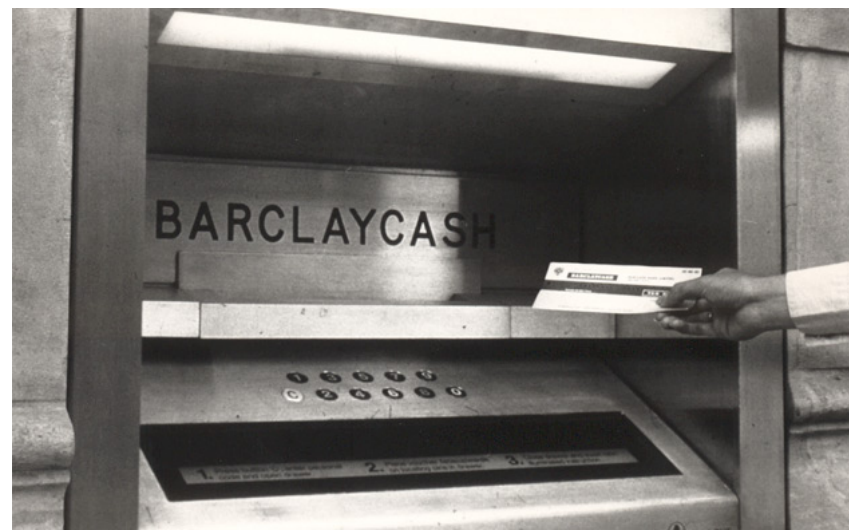


# IR #3, Big Benefits of Electronics Came Early

- Replacing human effort by machines
  - 1950s, elevator operators
  - 1961: industrial robot introduced by GM
  - 1960s, telephone operators
  - 1960s-70s, computer-generated bank statements and telephone bills eliminated tedious clerical labor
  - Credit cards, my AX card is stamped “1968”
  - 1970s, memory typewriters replaced boring retyping
  - 1970s, airline reservation systems



# Internet Revolution? How Long Ago did the Main Benefits Arrive?



- 1974: first bar-code scanner, 1980s ATMs
- 1980s. Word-processing, word-wrap, elimination of repetitive typing. Secretaries begin to disappear from Econ departments
- 1990s. E-mail, web, e-commerce
  - Electronic catalogs in libraries and auto parts
- **A qualitative difference in the importance of inventions since 2001**

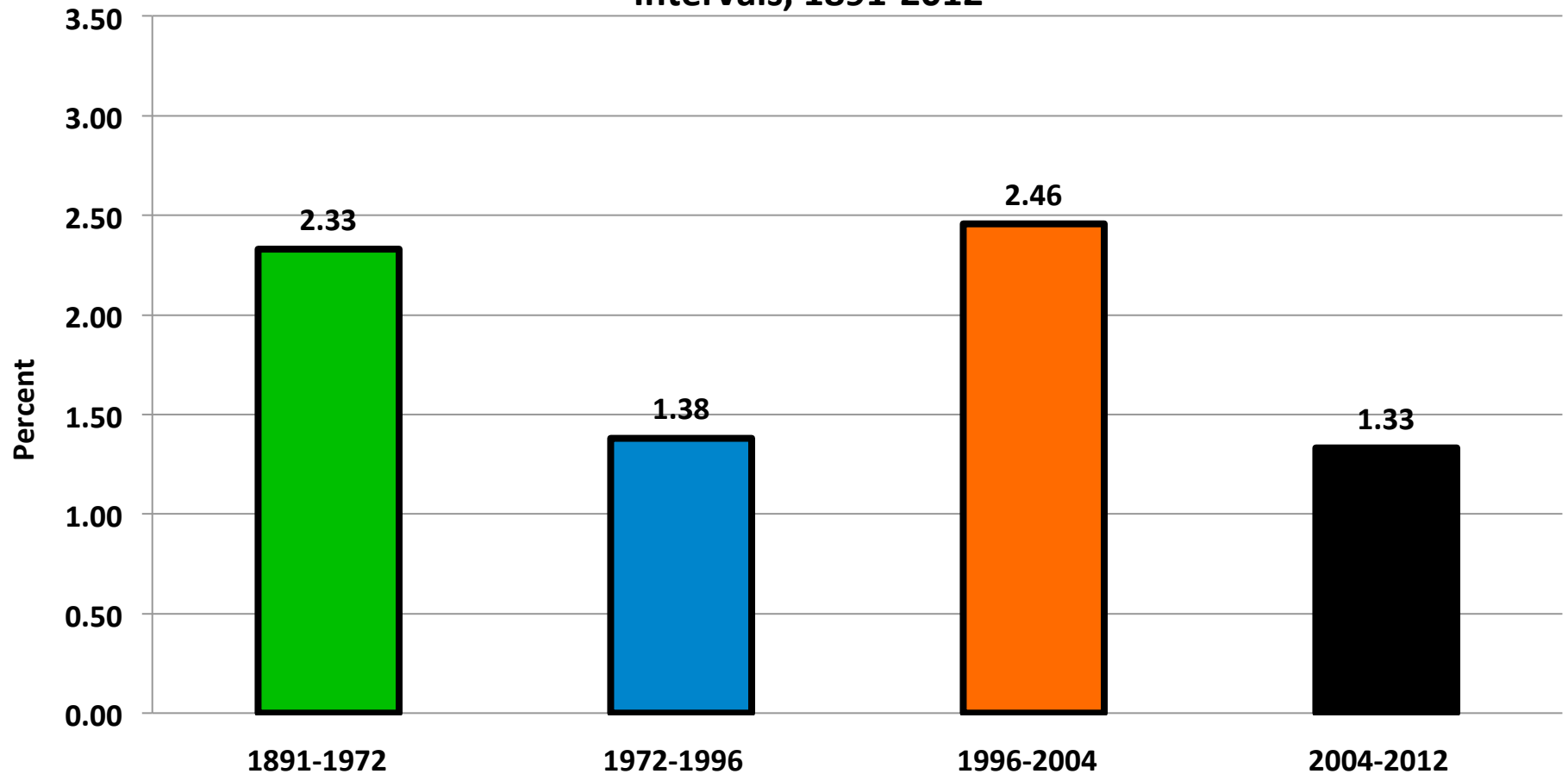


# Difference in Post-2001 Inventions

- **From 1960 to 2000, many IR #3 inventions involved the direct replacement of human labor by machine power**
  - From the earliest telephone bills & bank statements to replacement of paper catalogues by electronic catalogues
- **Since 2001 the most prominent inventions replace one form of entertainment or communication by another**
  - Walkman to iPod, cell phone to smart phone, laptop to ultrabook and iPad

# American Productivity Growth Since 1891

Figure 4: Average Growth Rates of US Labor Productivity Over Selected Intervals, 1891-2012



# How Important Were IR #3

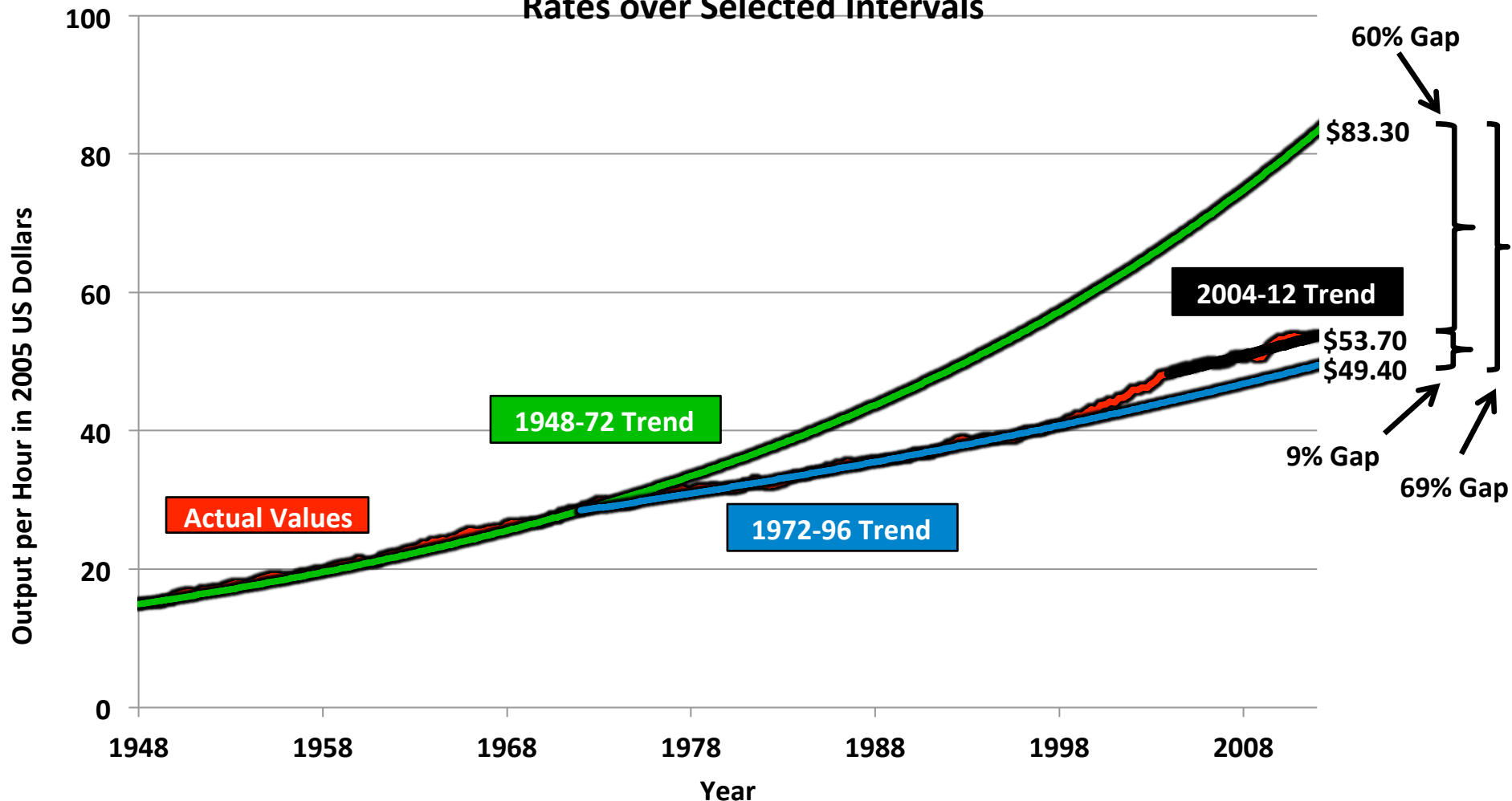
## Innovations during 2001 – 2011?

- A thought experiment: IR #2 vs. IR #3
- Choice A: You get 2002 electronic technology and get to keep running water and indoor toilets. But you can't use any electronic invention introduced since 2002. (You can have Wikipedia & Amazon)
- Choice B is that you get everything invented in the past decade, right up to Facebook, Twitter, and the iPad, but you have to give up running water and indoor toilets. There's no cheating, you have to do it. You have to take your iPad to the outhouse.
- Which do you choose?



# How Far Are We Behind the Growth Path of 1948-72?

Figure 5: US Labor Productivity from 1948:1 to 2012:1, with Trend Growth Rates over Selected Intervals



# Long-run Growth Prospects for U.S.

- While innovation continues at a frenetic pace, the effect of innovations on the basic quality of life and work is diminishing
- **We could do these things only once, not again**
  - Replace the horse with the motor car and truck
  - Replace back-breaking labor of housewives by consumer appliances and running water
  - Achieve an even 72° temperature year-round
  - Travel at 550 mph on a jet plane instead of at the speed of a horse

# But Let's Heed the Lessons from the Follies of Forecasting

- Let's *pretend* that the pace of innovation will continue at the same pace as in 1987-2007
- Maybe we really will all have personal airborne cars that vertically takeoff from our backyards.



# Ground Rules for the Exercise in Subtraction: The Seven Headwinds

- **First impediment to growth: new inventions aren't as important as the great old inventions.**
- **But assume that innovation continues unabated and continues to create important inventions**
- **We still face 7 headwinds. And some of them are uniquely American.**
- **If innovation slows down AND we face the 7 headwinds, then we're really in trouble**

# **We're Going to Start Optimistically and then Begin the “Exercise in Subtraction”**

- **I was not alone in making long-term growth forecasts around 2007, before the great recession.**
- **Like many others, I started at the 1.8% growth of 1987-2007 and subtracted two impediments (“headwinds”) that we already knew about back in 2007**
  - **Retirement of the baby boomers**
  - **The American “educational plateau”**



# Helpful Definitions

- Standard of Living is output per person
- Productivity is output per hour
- These can grow at different rates if there is a change in the economy's total ratio of hours per person
- A good change when people work more, a bad change when people work less
- **Good Change:** Increase in female participation in the labor force after 1965
- **Bad Change:** Baby-boom retirement

# The First Two Headwinds, incorporated into 2007 Forecast

- **#1. Demographic Dividend is Reversed**

- Growth of output per person from 1965 to 1990 was pushed by higher hours per person as females entered the labor force.
- Output per person will grow **slower** after 2011 due to Baby-Boom retirement. Lower hours, same population

- **#2. Plateau of Educational Attainment**

- Cost inflation in higher education, mounting student debt distorts life choices
- Poor math-science scores in OECD cross-country tests
- Achievement gap of black and hispanic minorities



# Four More Headwinds

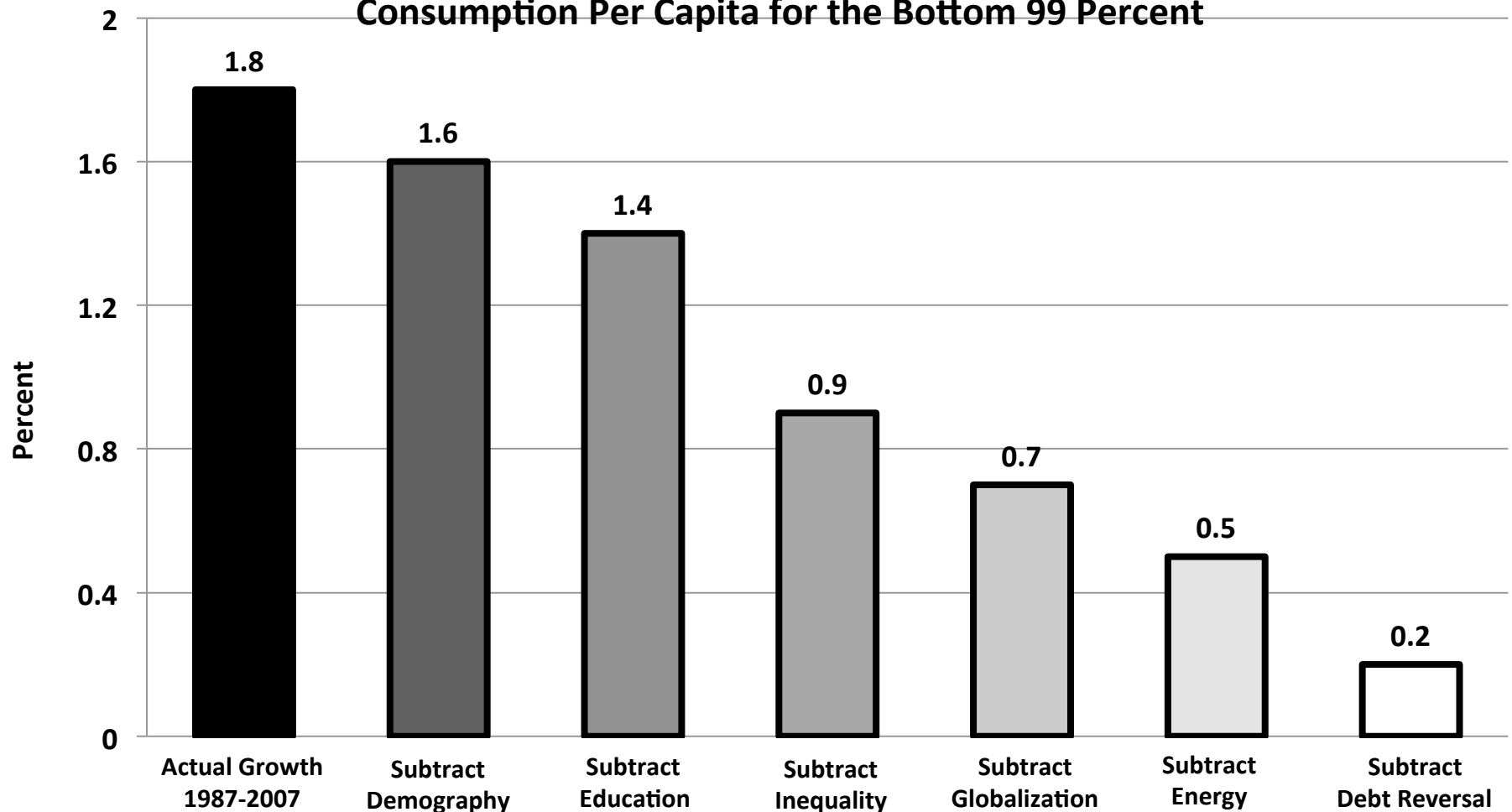
- **#3. Inequality: growth in median income is much slower than in statistical averages for income per capita**
  - 1993-2008. Growth of average real household income = 1.3%
  - Growth in bottom 99%, 0.75%. Top 1%, 3.9%
  - Top 1% captured 52% of income gains during 1993-2008

- **#4. Globalization linked with IT:** Hurts the leading nation more than others. Outsourcing and those radiologists in India.
- **#5. Environment:** Should we sacrifice so China can grow unimpeded? (is it fair?) 1901 full steam ahead, environment be damned
- **#6. Twin deficits: consumer and government debt overhang.** However slow is growth in production per capita, consumption per capita will grow slower.

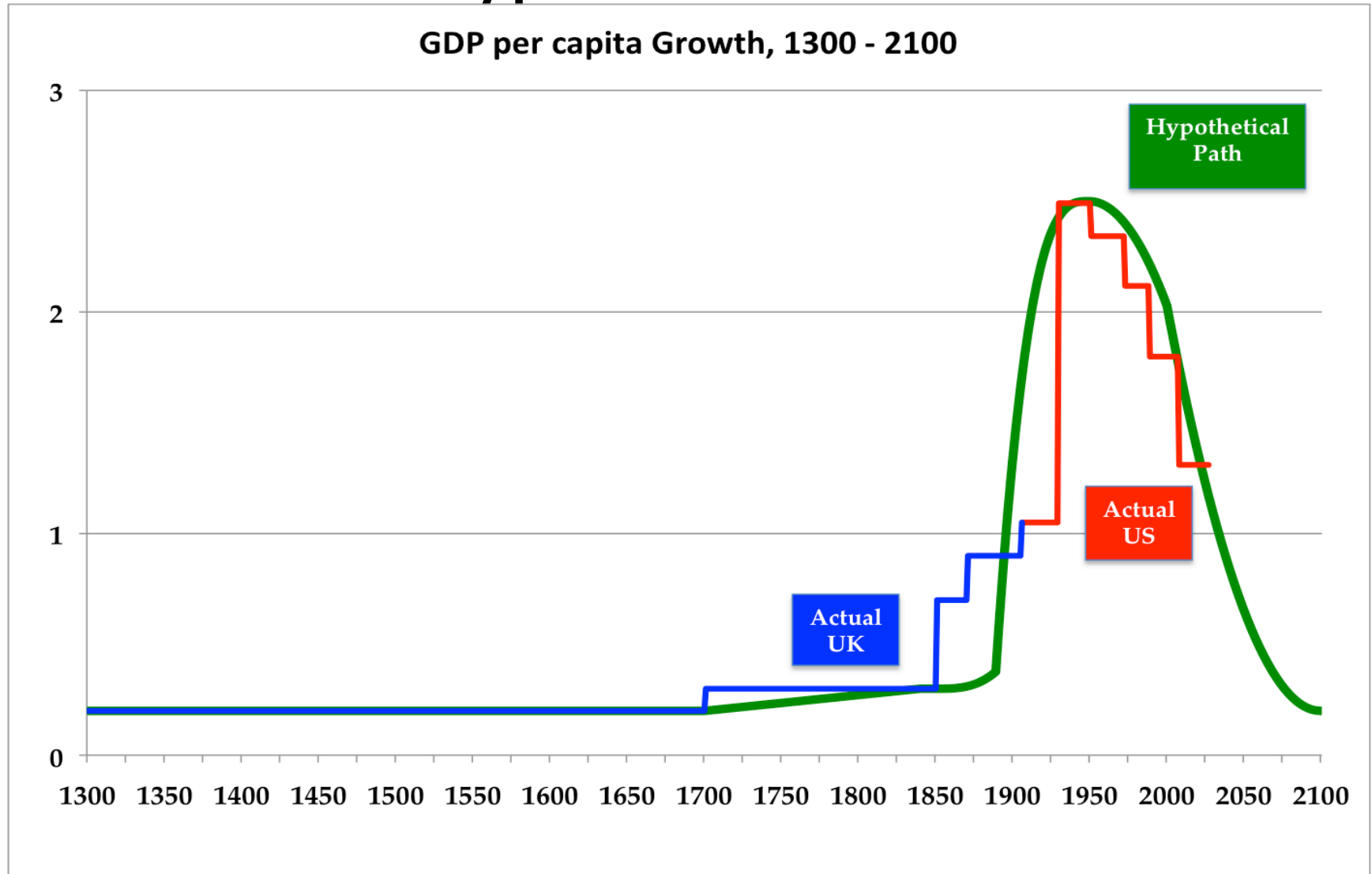


# An “Exercise in Subtraction” for the Six Headwinds

Figure 6: Components of the Exercise in Subtraction, from 1987-2007  
Growth in Per-capita Real GDP, To Hypothetical Future Growth in Real Consumption Per Capita for the Bottom 99 Percent



# Capturing the Actual Growth Rate in a Hypothetical Curve





# The 7<sup>th</sup> Headwind, Dysfunctional Medical Care System?



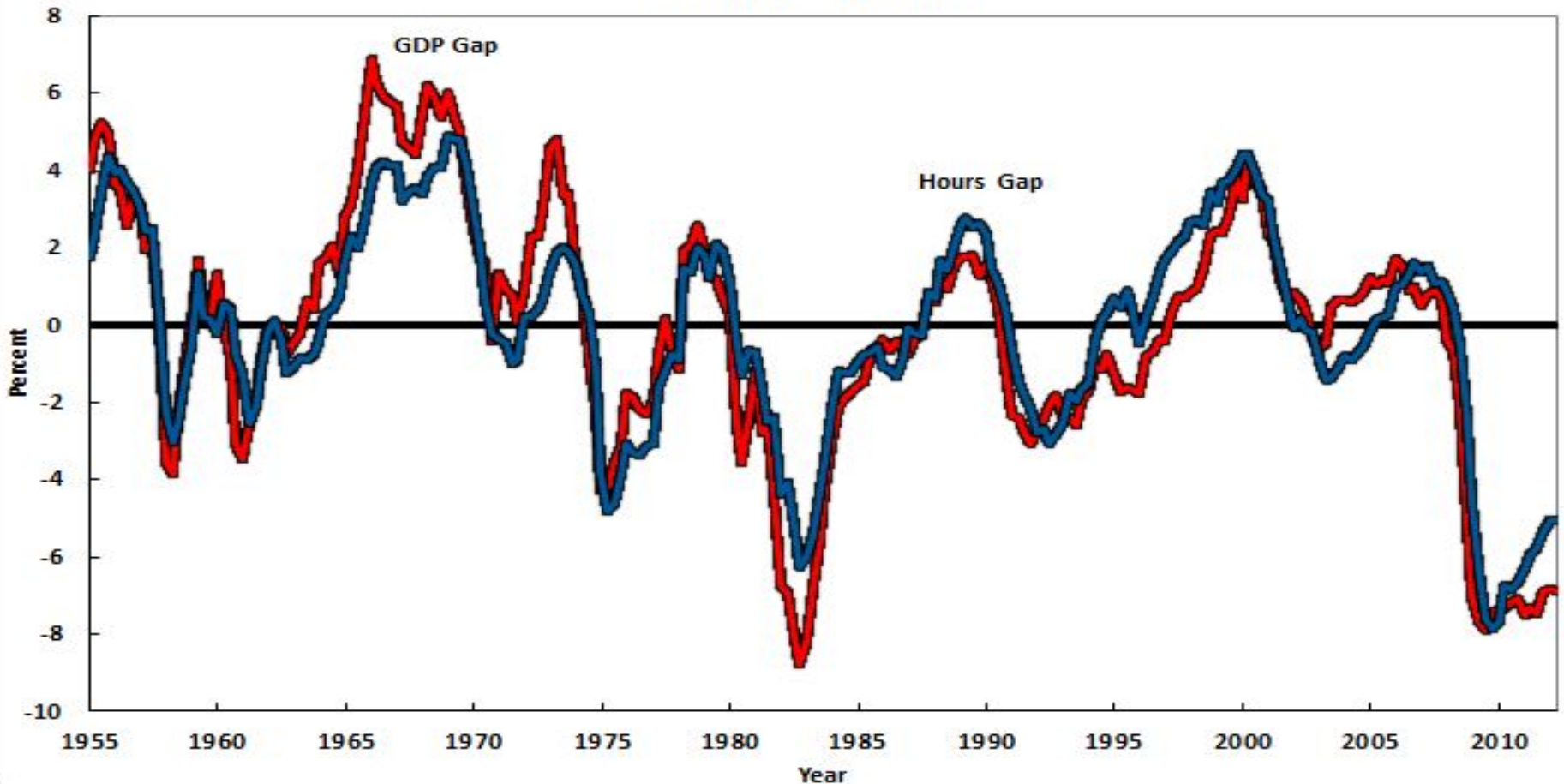
- Standard of living is about more than money
- It also includes how long we live and the **QUALITY OF LIFE YEAR (QALY)**, that is, how healthy we are while we're alive
- U. S. is #38 on a ranking of life expectancy
  - Japan 82.7, Israel 82.0, Italy 82.0, Canada 80.7, **US 78.2**
- U. S. #1 in health care spending as % of GDP
  - **US 15.2**, Japan 9.8, Israel 8.0, Italy 8.7, Canada 9.8

# **The Reality of Today's Economy: It Is Operating about 10% Below the Path Forecast in 2007**

- **Why Has the Economic Recovery Been So Weak?**
- **What Were the Impulses that Sent the Economy into the Tank?**
- **What Was Right or Wrong about the Obama Stimulus?**
- **What Policies Will Help? Which Will Not Help?**
- **Short-run Policies vs. Long-Run Policies**

# Output Gap vs. Gap in Aggregate Hours of Work

Conventional Output Gap vs Hours Gap,  
1955:Q1-2012:Q2



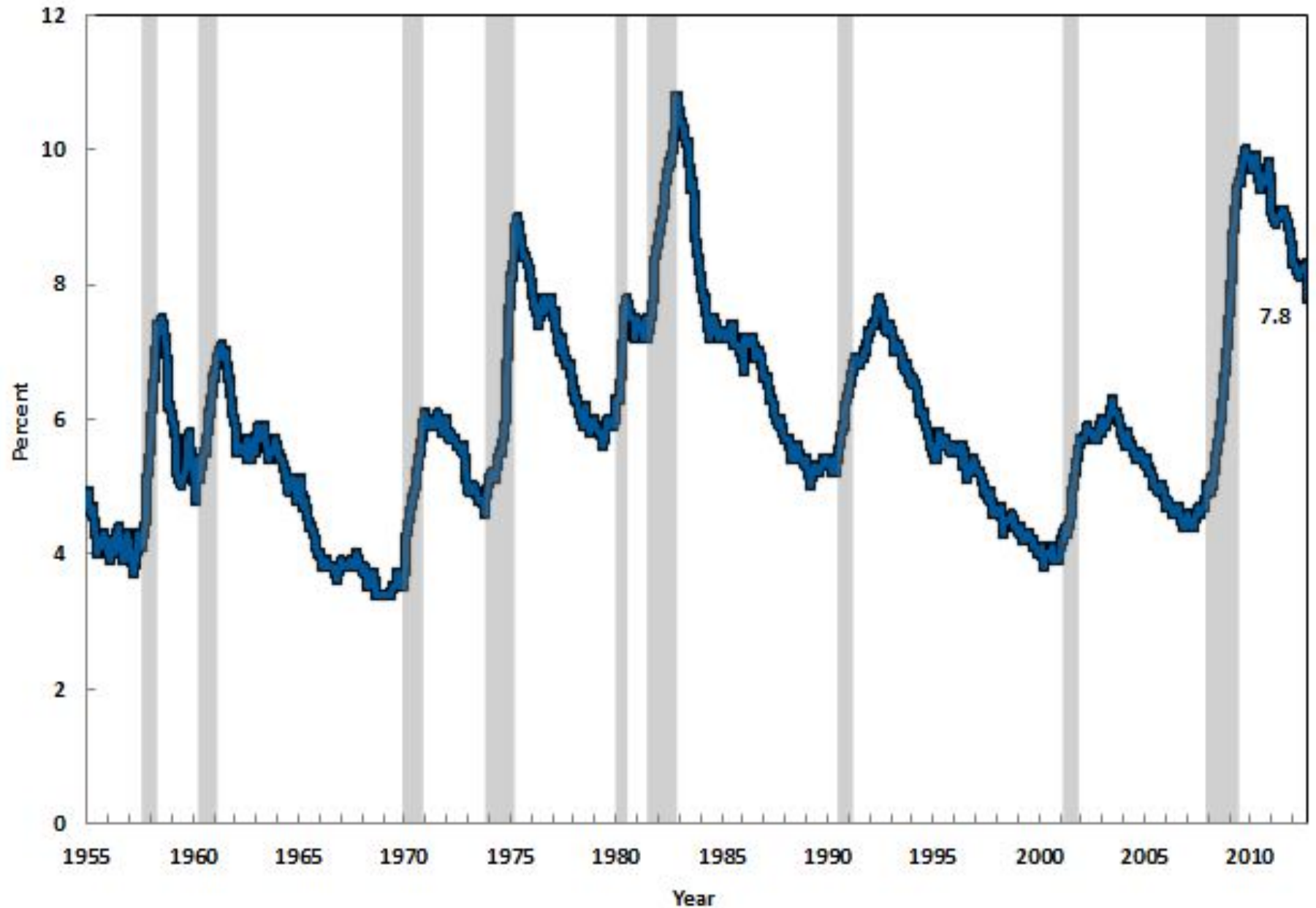


# Dimensions of Today's Economic Reality

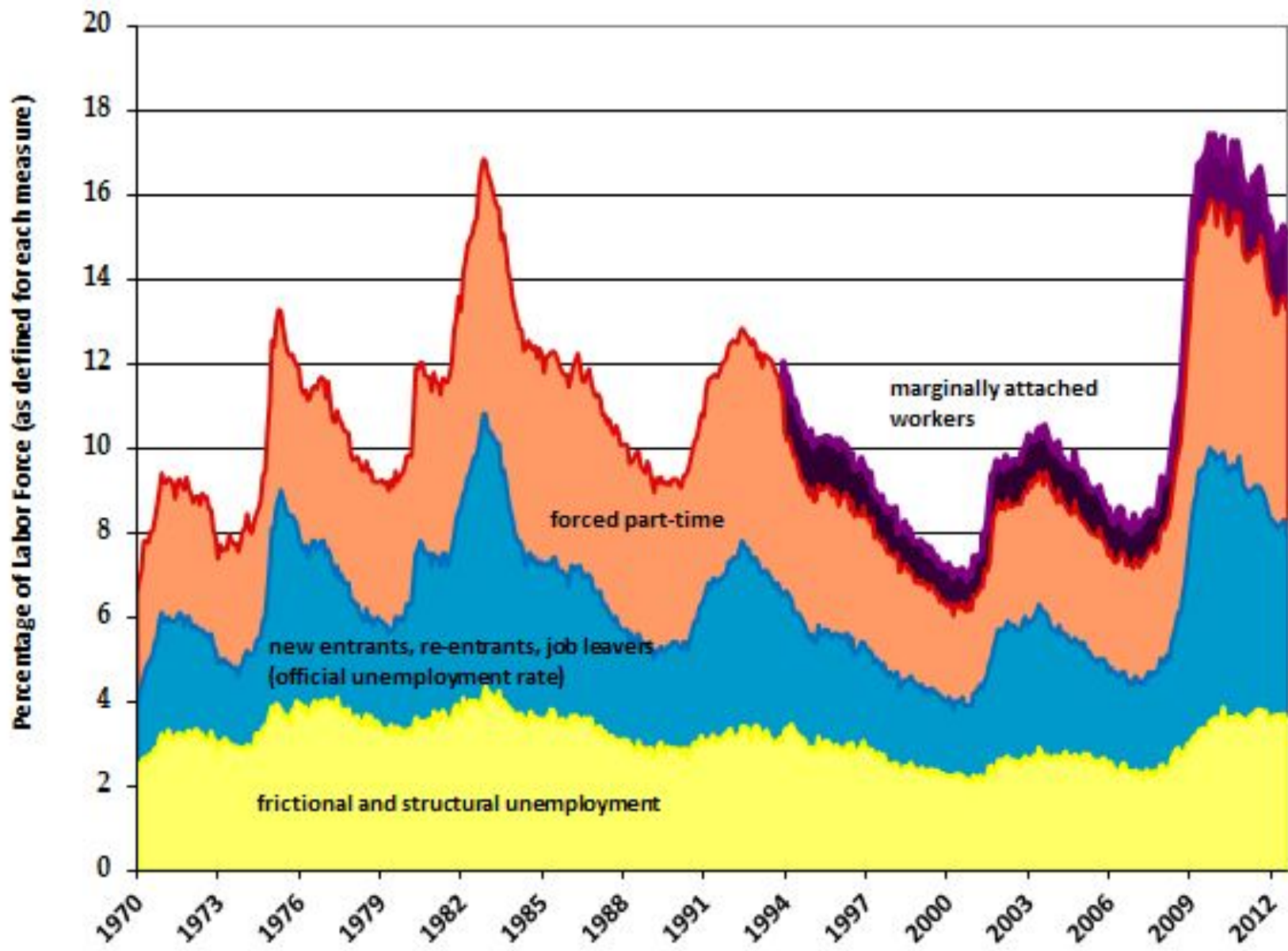
- Official Unemployment Rate (% unemployed divided by employed + unemployed). NOT the % of unemployed to population
- Add in those who've given up and who are forced to work part-time
- Comparison with past recessions and recoveries



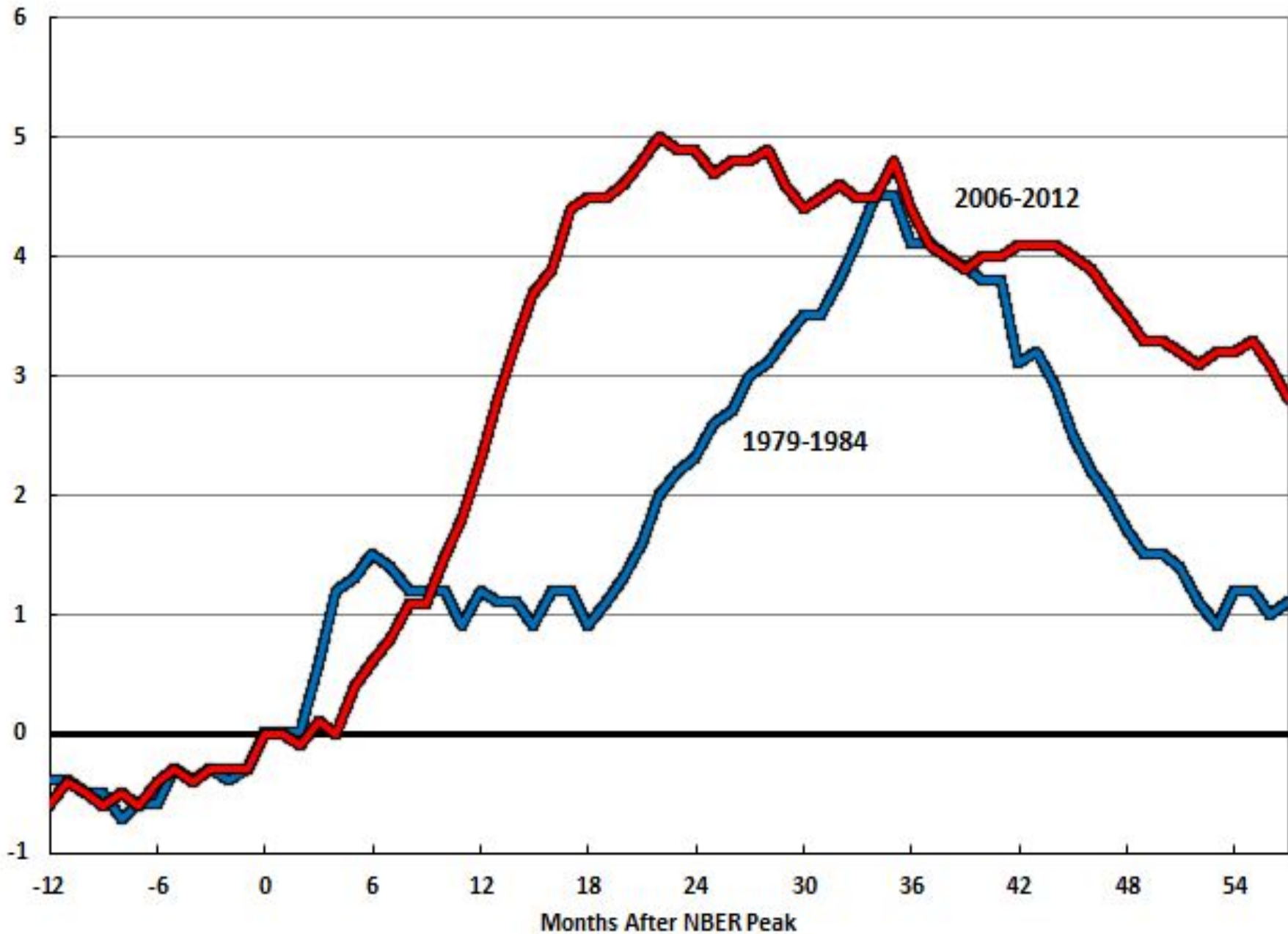
# Monthly Unemployment Rate, January 1955-September 2012



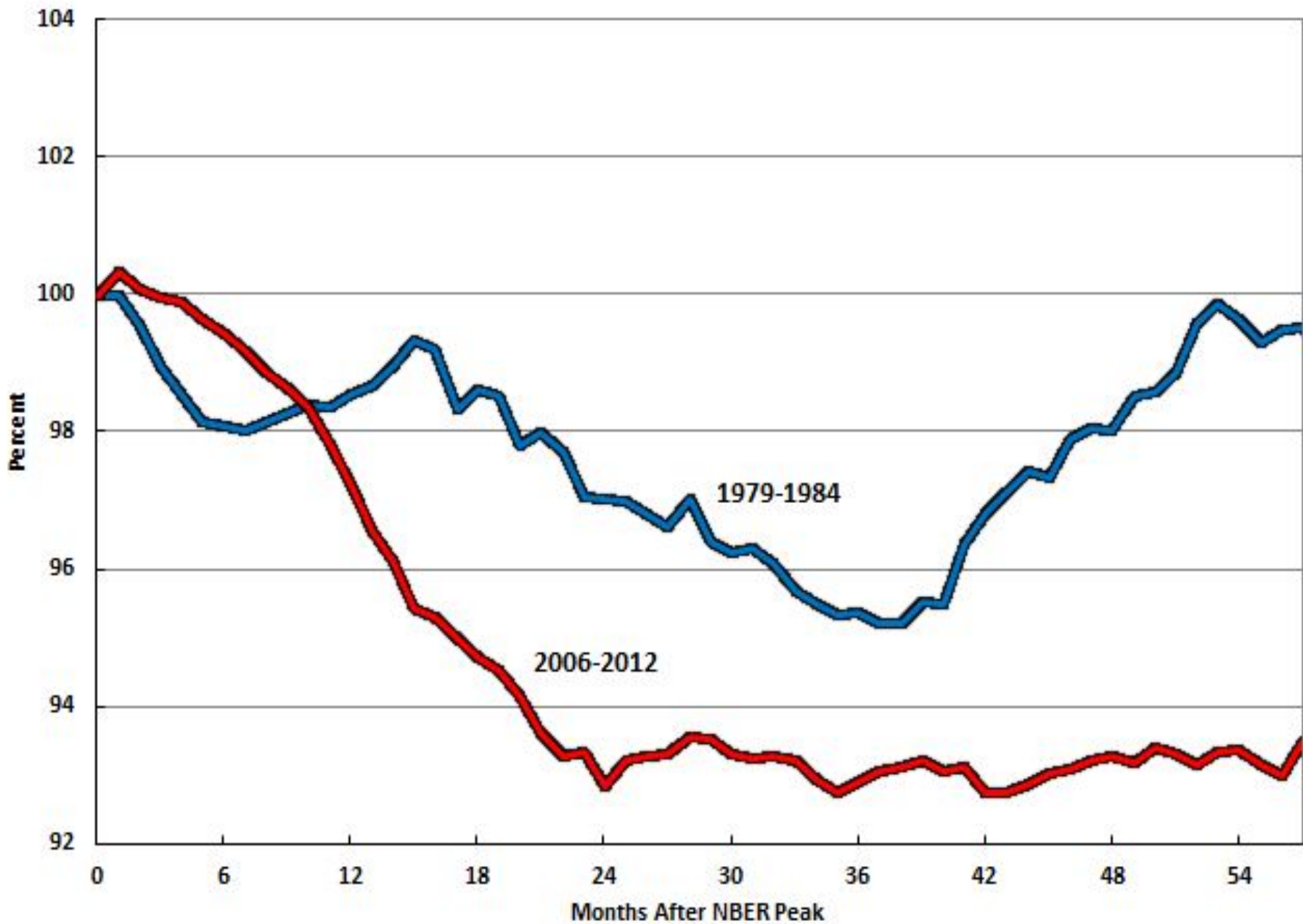
# Various Measures of Unemployment Rates from the BLS



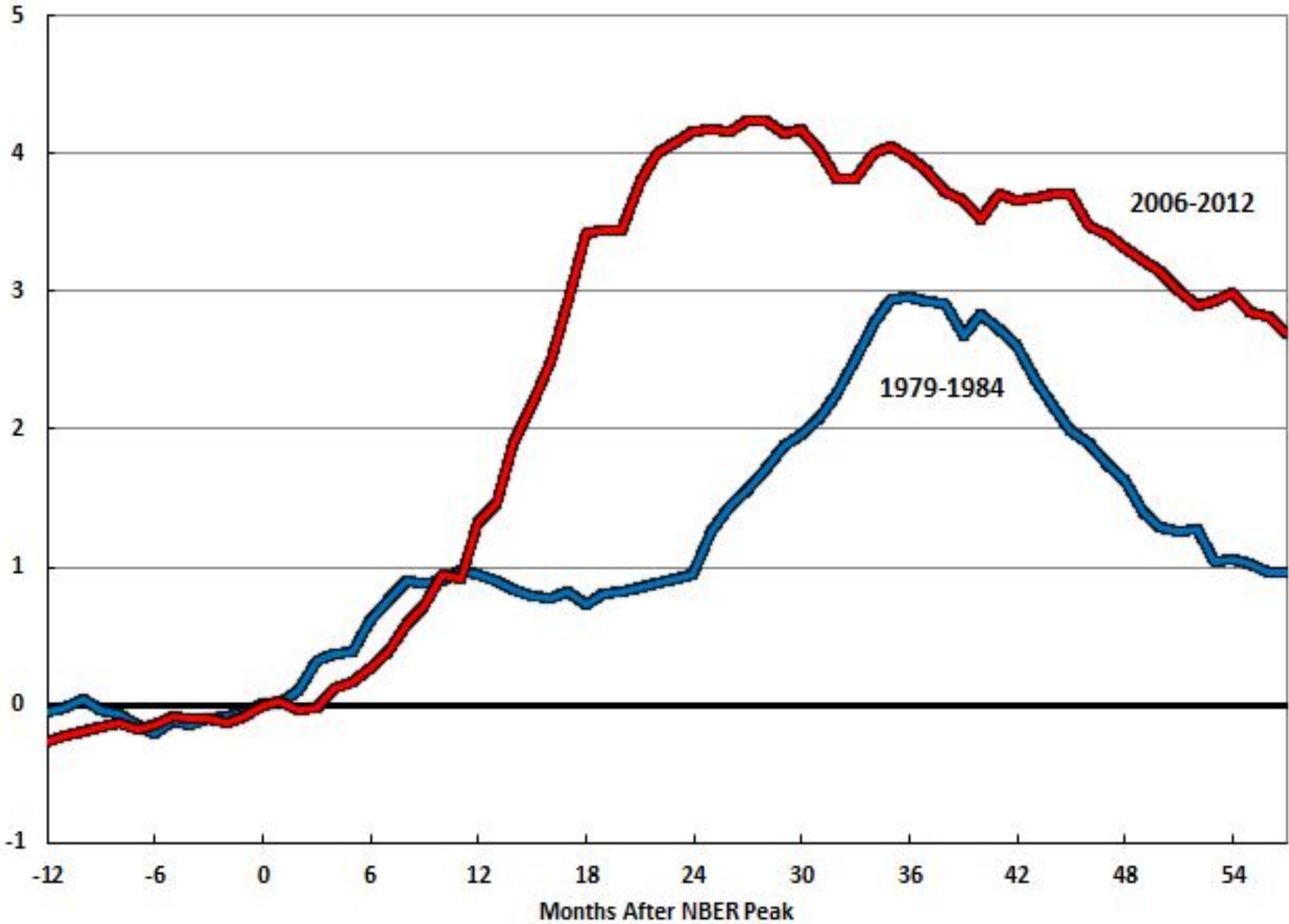
# Official Unemployment Rate as Difference from NBER Peak



# Employment as a Percentage of Peak-Level Employment



# Unemployment Over 15 Weeks Rate as Difference from NBER Peak



# Causes of the Financial Collapse, Recession, and Slow Recovery

- **New financial products were invented**
  - Commercial banks could also be investment banks (Clinton administration vs. FDR policy)
  - Mortgage-backed securities: your home-town bank no longer owns your mortgage so is less careful in lending standards (reversed now)
  - Billions of loans to low-income families
    - Tricked into loans they couldn't afford
    - Didn't understand adjustable rates, led to foreclosures
  - Wild west of finance caused housing price bubble
  - Irrational exuberance and Fed policy killed it



# **Consumption Boom of 2002-07 Depending on Housing Refinance**

- **Mortgage lenders and brokers were paid by originating mortgages, including refinance**
- **With house prices rising so much, this seemed a no-brainer**
- **Each new refinance raised the amount the borrower owed. The difference was taken as cash and used to finance consumption**
- **This support for spending immediately vanished when housing prices started to fall.**



# Why the Recession Was So Severe

- Finance industry froze up in fall 2008
- Banks wouldn't lend to each other, much less to consumers or businesses
- Business firms by 2001 had become more aggressive about preserving profits. No longer did they care about other "stakeholders"
- Unemployment went up far more relative to output's decline than in previous recessions or in comparison with Europe.

LEHMAN BROTHERS

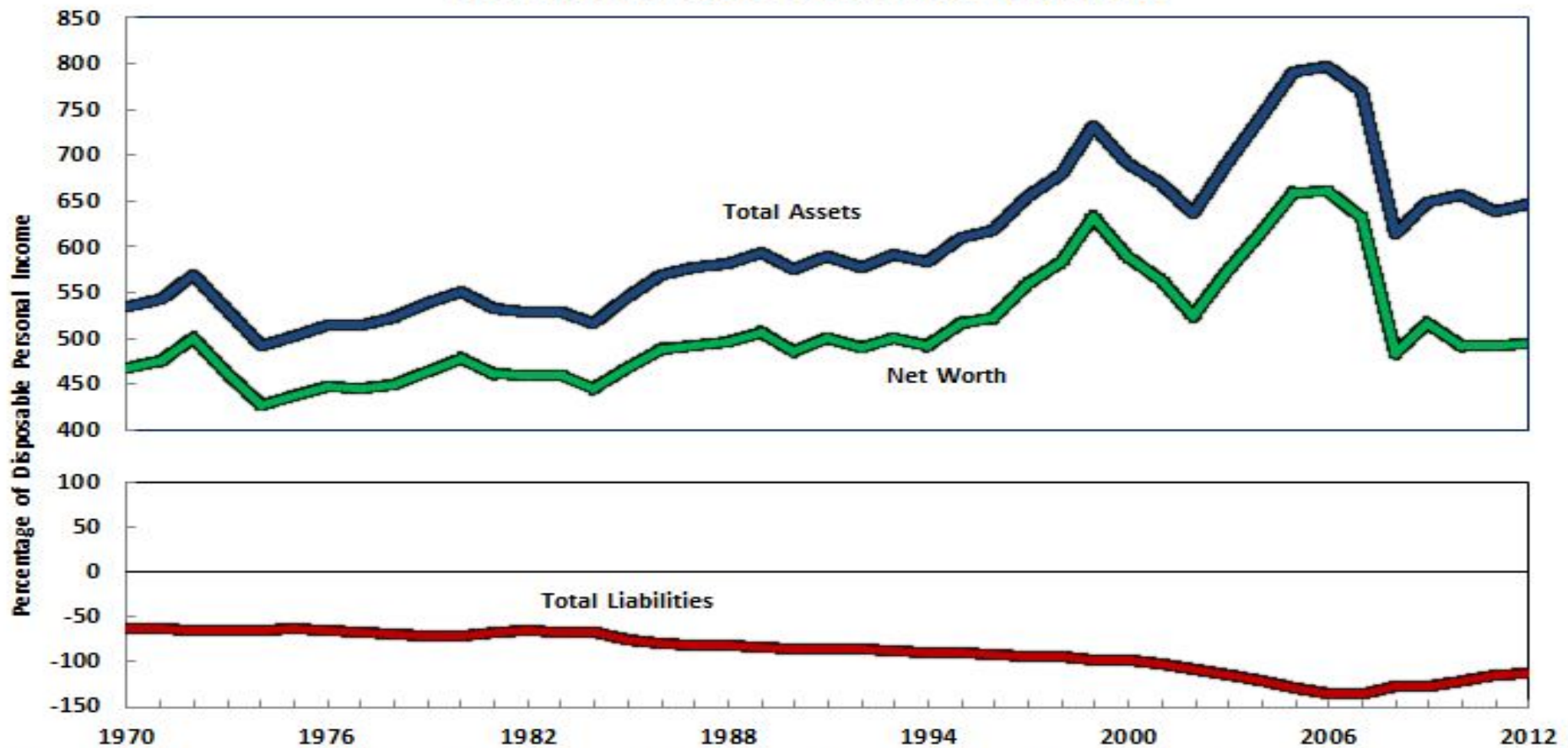
# Diagnosis of the Weak Recovery

- The “double hangover”
- Too many houses and condos were built, and many have not yet been sold (downtown Evanston)
- Each foreclosure raises the supply of housing by one unit but the victims add nothing to the demand for housing
- Consumer net worth collapsed (stock market, housing equity, too much borrowing)
- Paying back loans leaves less available for everyday consumption



# Consumption Problem: Household Balance Sheet

## The Twin Peaks of Household Net Worth



Sources: Federal Reserve Board *Flow of Funds Accounts* and Bureau of Economic Analysis *NIPA Tables*. Details in Appendix C-4.

# Instability in Housing Starts is Nothing New



# **Central Issue in the Election: The Vicious Circle**

- **Firms don't hire because consumers aren't buying enough**
- **Consumers aren't buying enough because firms won't hire them and because they have to pay off debt.**
- **Under-water mortgages and the end of refinance**
- **Credit tightness depends on under-water and your credit score (Chicago Fed paper)**

# **Polls Suggest Agreement that “The Country Is Headed in the Wrong Direction”**

- **This widespread feeling combines aspects of the long-run “end of growth” story and the “slow recovery” issues.**
- **After the intermission, we’ re going to look at play a new game called “Pretend I’m Dictator”. If I could do anything I wanted, could I fix all this stuff?**
- **Hint: No president can wave a magic wand and create an invention as important as electricity and the internal combustion engine!**

# INTERMISSION



# Now We're Going to Try to Fix the Economy

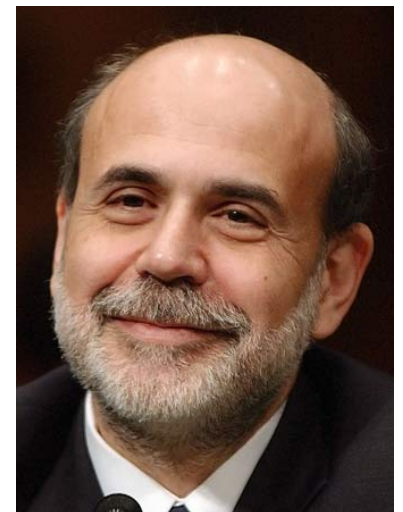
- The last hour will treat the short-term problems first, because that's what the election is about
- If time, some radical proposals will be suggested for the long-term problems. You may not like them, but they'll give you lots to talk about
- Here's the **RULE** for the last part of today's discussion. The "**BENEVOLENT DICTATOR**" can do anything he/she wants. It's a parliamentary system with a large majority. No filibusters, no vetoes.



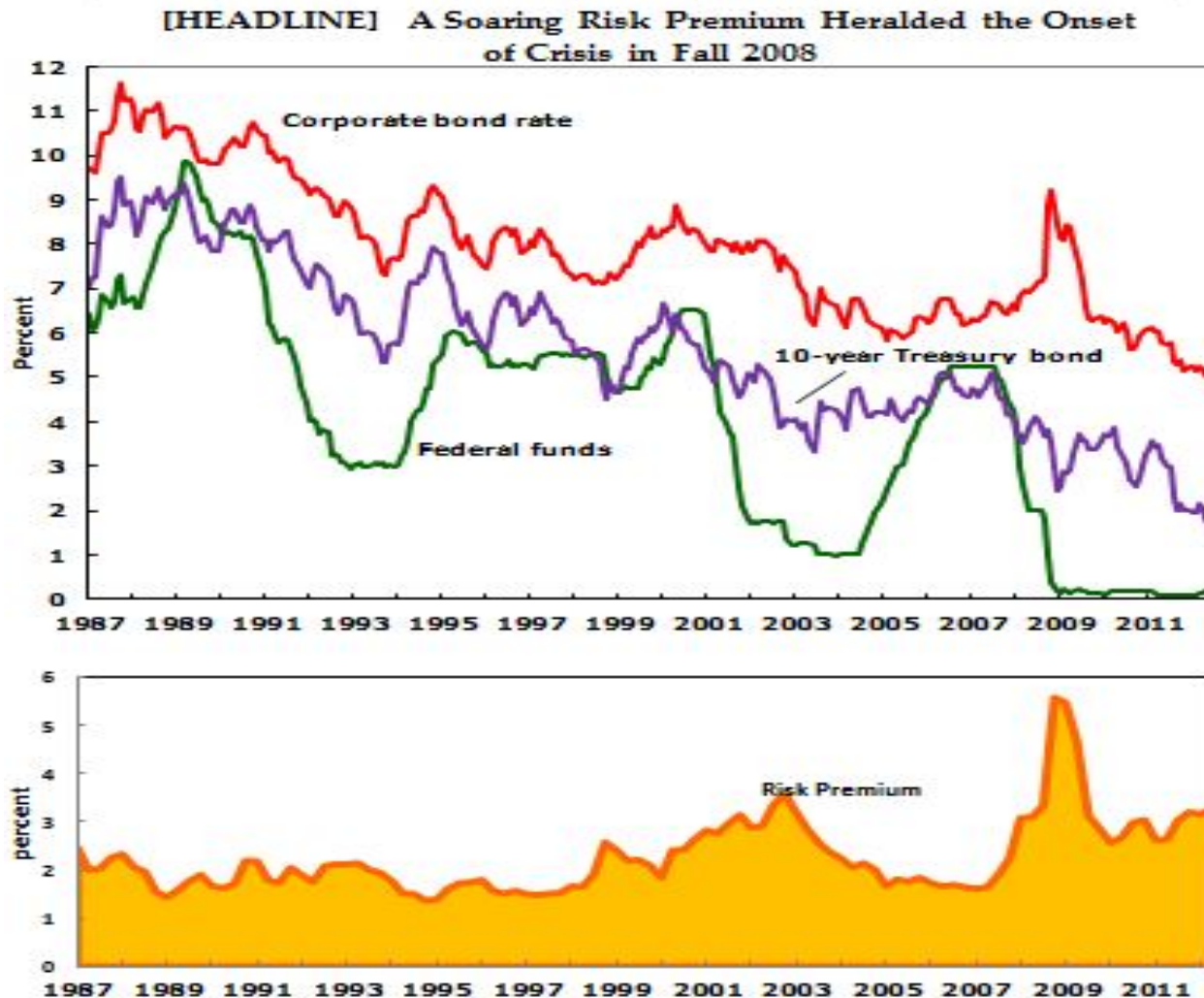
# Central Election Issue:

## What the Federal Government Can Do

- **Monetary Policy is run by the Federal Reserve**
  - They control short-term interest rates but not other interest rates, only indirectly
  - They can buy up assets, including a part of the government debt
  - They can make special loans to financial institutions
- **Review the recent history of interest rates (the “zero lower bound”)**
- **Fed can’t control cost of borrowing or force banks to lend**



# The Fed Can't Control the Cost of Business Borrowing



# The Other Traditional Policy: Fiscal (Expenditures and Taxes)

- Fiscal policy for the Federal Government requires approval by Congress and the President. States and localities also.
- Fiscal policy tools
  - Spending on goods and services (teachers)
  - Spending on transfer payments (food stamps, unemployment benefits, social security)
  - Tax rates
  - Tax rules (exemptions and deductions)
- Examples: Obama Stimulus and Obamacare
  - Auto bailouts



# **Our Agenda: the Economy is Operating Below Its Potential**

- Output is too low, unemployment is too high, a true vicious circle**
- Consumers do not have enough income to buy all that business firms can produce**
- Business firms cannot hire enough people and pay out enough income because consumer demand is so weak**
- Where can the money come from to kick-start the economy? Cut taxes or raise spending? But both increase the government deficit**

# **Let's Look at Three Big Economic Downturns, Differences and Outcomes**

- **Roaring 1920s followed by the dismal 1930s, with unemployment about 10 percent from 1930 to 1940. Cured by fiscal expansion, “WW2 Stimulus”**
- **The worst previous postwar recession, 1980-82. Caused by Fed, cured by Fed**
- **Housing and credit bubble of 2001-06 followed by collapse in 2008-09. Not caused by Fed, so Fed can't just turn a dial and cure it.**
- **Is there any hope?**

# Why Are There Business Cycles?



- **An Ancient Topic**
- **An alternation of too much spending and too little spending**
- **The roaring 20s followed by the depressed 30s**
  - **Partial explanation: the 20s were roaring too loud and could not continue**
  - **Analogy: the housing bubble of 2000-06 was roaring too loud and could not continue**

# **The 1920s Were Like 2000-06: Irrational Exuberance**



- **The Great Inventions**

- In the 1920s there was a stock market boom about radio companies, esp. RCA
- In the 1920s there was a land price boom, esp. in Florida
- In the 1920s there was a residential construction boom, the greatest of the 20<sup>th</sup> century, because the newly invented automobile opened up vast tracts of suburban land that were previously inaccessible by streetcar.
- But, as usual, they built too many houses, too many cars.

# Other Contributions to the Great Depression



- **The Stock Market Bubble of 1927-29**
  - It was like 1997-2000, but its collapse was more serious
  - Because ordinary people had been allowed to invest in stocks with 10% down payments, compared to 50% in recent decades
  - Helps us to understand the housing bubble, too many people were given mortgages with close to zero down payments. **LEVERAGE. HIGH DOWN PAYMENTS ARE GOOD. LOW DOWN PAYMENTS CREATE BUBBLES**
- **The financial chaos in Europe, caused by the aftermath of World War I**



# **The Key Mistakes in the 1930s: Bank Failures, Opposite from 2008-09**

- **The Fed adamantly refused to rescue banks, which was its basic mission when it was chartered in 1913-1914.**
- **The Hoover Administration compounded the problem by raising taxes in 1932**
- **The economy was allowed to collapse. That example shows how important were the Fed and Obama Administration actions in 2008-09 to save the economy. The bank and auto bailouts were essential (POLITICAL ISSUE)**

# The New Deal of 1933-40 Offers Many Lessons in What to Do and What Not to Do

- FDR didn't do enough. His government deficits were never nearly as large as Obama's.
- FDR overregulated business
- But FDR created two great programs that have left a permanent mark on America. The WPA and CCC. (Evanston Post Office and the Skokie Lagoons). Why not now?



# The Works Progress Administration Built and Built

- **Big things**
  - The Golden Gate Bridge
  - The Bay Bridge
  - The Hoover Dam
- **Little things**
  - The Evanston Post Office
  - The Berkeley Post Office





# The Civilian Conservation Corps (CCC)

- **Hundreds of thousands of young men were directly hired by the Federal government.**
- **They planted trees, built hotels and recreation centers at our national parks**
- **Here in our hometown, the CCC built the Skokie Lagoons. 1,000 young men working for the government dug it out by hand in 1939-40**

# **Ten Years Later in 1939, the Economy Was Still in a Slump**

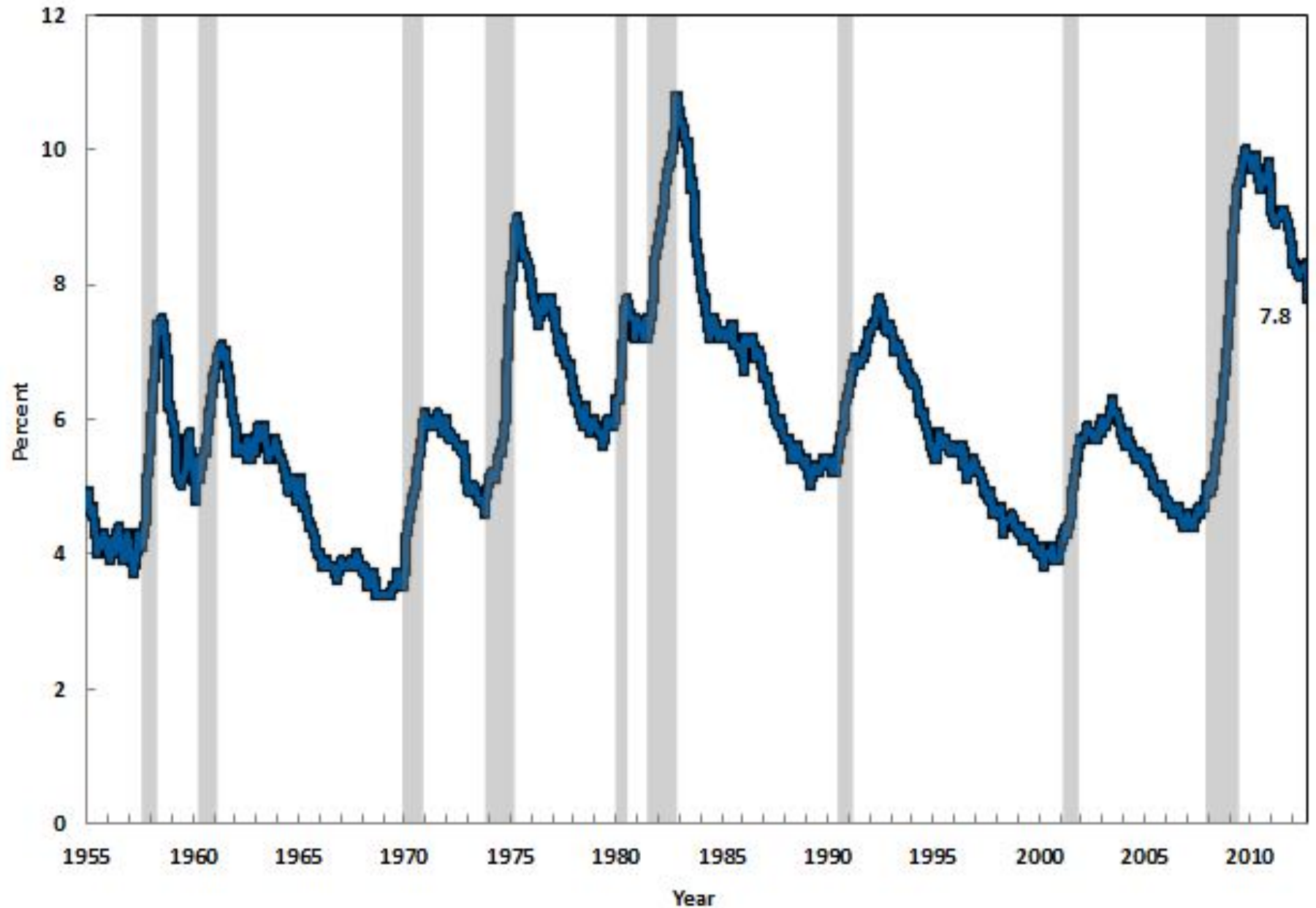
- **The Fed couldn't fix it. Interest rates were near zero.**
- **But Hitler did fix it, as he had fixed the German economy in 1934-37.**
- **Between 6/40 and 12/41 the share of government spending in GDP doubled.**
- **1940-41 is the key example of how rapidly output can recover when the government uses deficit spending to spend for purposes that directly create jobs**

# **Sometimes Monetary Policy Can Work to Cure Economic Slumps**



- **In 1982 the unemployment rate briefly hit 10.8 percent.**
- **But we all understood the cause. The Federal Reserve under Paul Volcker was determined to stop inflation (that had been started by higher oil prices in the 1970s)**
- **Interest rates went up to 19% on short-term government debt and up to 15% on mortgages**
- **It worked. Monetary policy deliberately created the recession and ended it quickly.**

# Monthly Unemployment Rate, January 1955-September 2012



# **Ben Bernanke, Academic Scholar of the Great Depression, in 2008**

- **He knew that the crucial step to prevent another Great Depression was to prevent the banks from failing**
- **Hence the bank bailouts of 2008**
- **The big mistake of Bernanke, the Fed, and Obama was not to devote equal hundreds of billions to bailing out under-water homeowners.**
- **This is not a reason to vote against Obama, because Romney is against any kind of government intervention to help solve problems.**

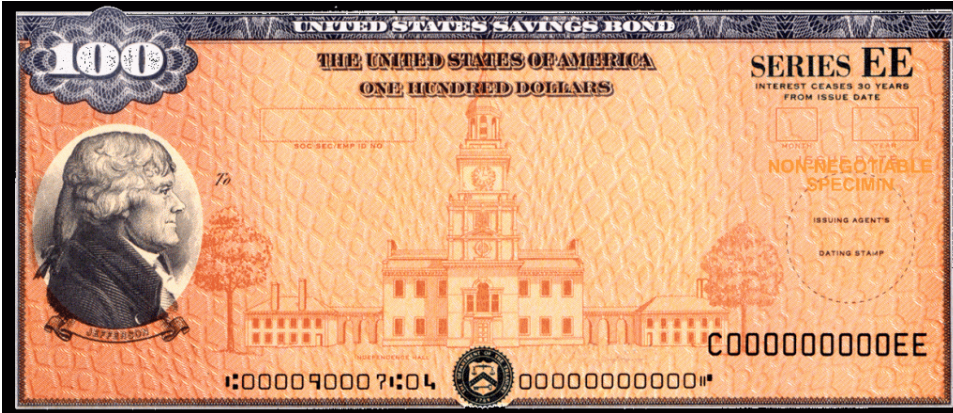


# What to Do Now? Fiscal Expansion with Fed Support



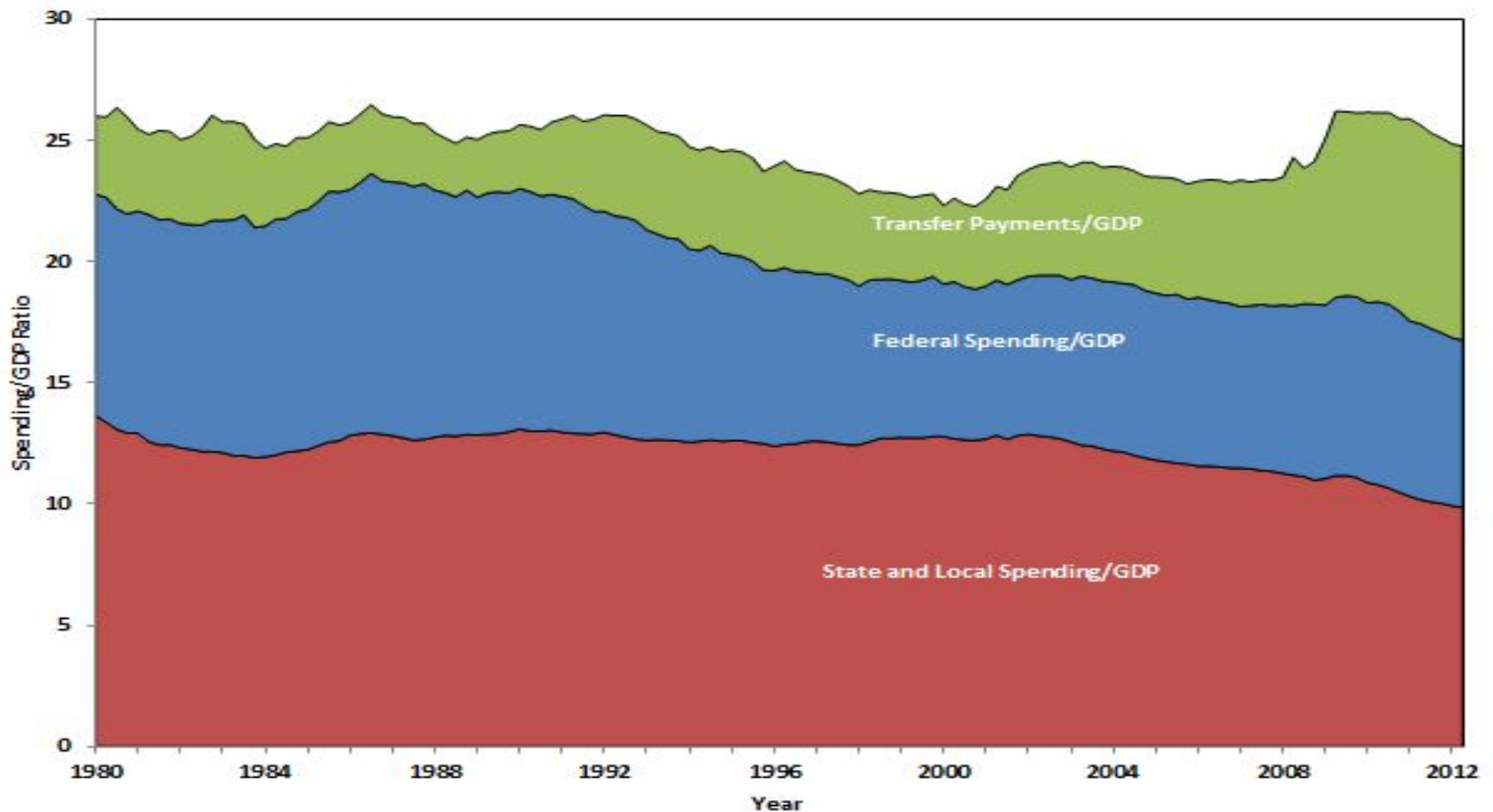
- Now is an ideal time to introduce another large fiscal stimulus
- It won't raise the debt held outside the government, because the Fed can buy the bonds
- Interest rates are so low the Federal government can borrow for free, the envy of the world
- But the new stimulus should learn the lessons about what was right and wrong with the Obama stimulus

# Obama Stimulus Lessons

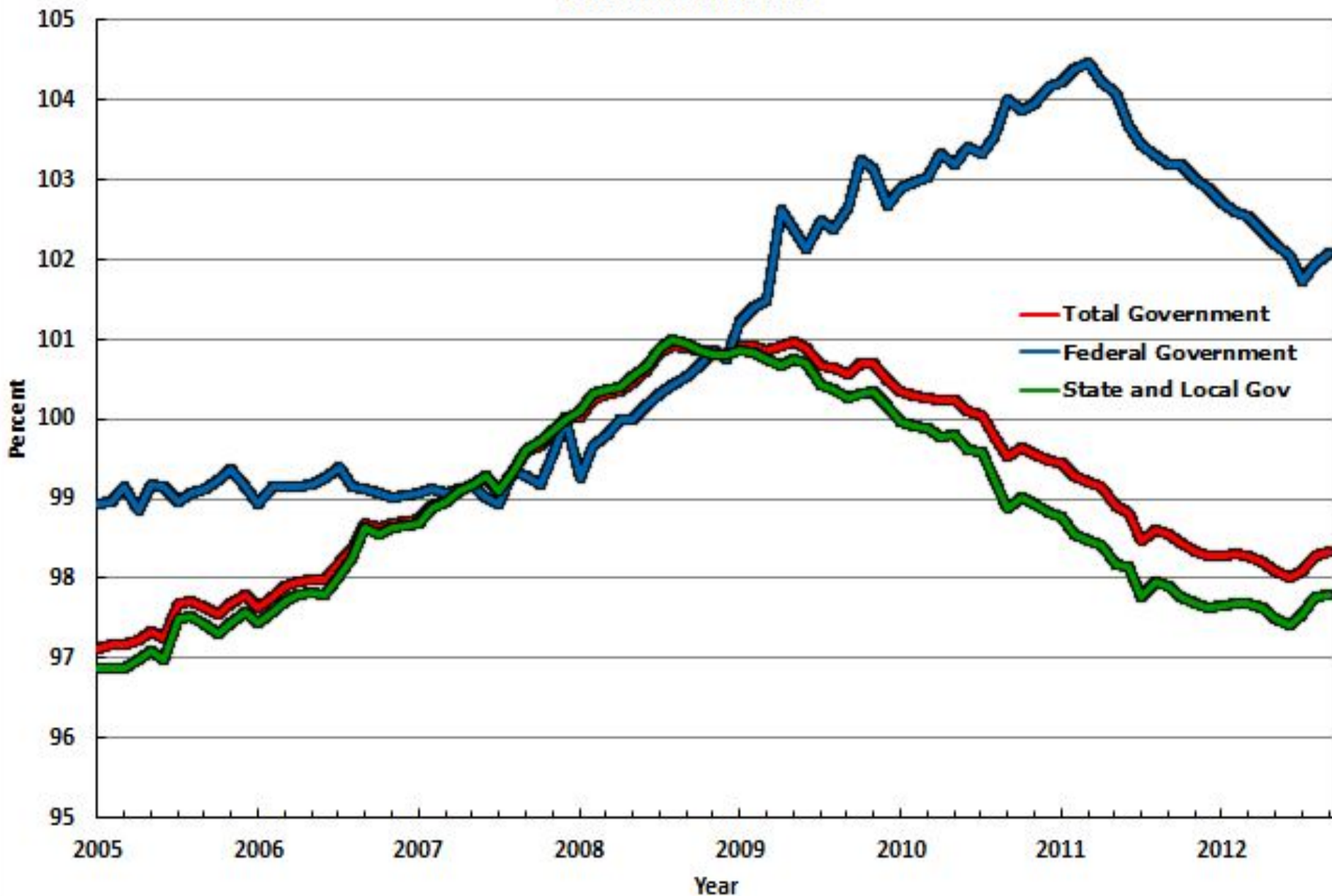


- Obama stimulus was too small.
- No priority to employment bang per buck.  
Sheridan Road in Evanston
- Job-creation took lower priority than everyone's favorite pet social policy
  - High Speed Rail
  - Subsidies to solar power start-ups (bankrupt Solyndra)
  - Arne Duncan's "Race to the Top"

# How Does the Obama Stimulus Measure Up?



Government, Federal, State and Local Employment, Excluding Census Workers,  
January 2005 - September 2012,  
December 2007=100



# **Last Section: Solutions to Long-run Problems, the 7 Headwinds**

- **Demography. Higher hours per person from increased female participation during 1965-90**
- **Now lower hours per person from retirement of baby boomers**
- **Solutions: (1) gradually raise the retirement age with life expectancy. (2) Listen to Steve Jobs and staple a green card. (3) Get rid of illegal immigration by making them legal!**

# The Education Headwind

- **Cost Inflation in Higher Education**
  - **NU: New Music Building, New Welcome Center for Undergrad Applicants, and new \$225 million Athletic Training Facility**
  - **Smart Podiums, just call 7-7666**
- **Candidates About Student Loans**
  - **Romney: get Federal Government out of it**
  - **Obama: get private profit-making banks out of it. Preserved the 3.5 percent interest rate when Republicans tried to double it to 7 percent**
- **Bankruptcy Law, Income-Contingent Loans**

# Ever-Rising Inequality

- **Previous: 1993-2008 top 1% earned 52% of all additional income (adjusted for inflation)**
  - **Top 1% own most of the stocks and bonds, enjoy a 14% tax on capital gains and dividends**
- Insert text here
- **The Buffett Rule (Obama yes)**
  - **Fast growth in Clinton years**
  - **No relation lower tax rates to Growth (Oprah, Tom Brady)**



# **Globalization Interacts with the Internet**

- **China and other emerging nations skip a whole century and adopt our technology developed painfully and slowly since 1800**
- **They can combine our technology with their low wages**
- **Manufacturing jobs in U.S. decline by 30% in the Bush years, 2001-07, BEFORE the crisis**
- **About 40% of those laid-off manufacturing workers have given up, dropped out of the labor force. Locational immobility**



# **Solution: Retraining**

- **But the technical demands of jobs keep increasing. Some manufacturing workers who've lost their jobs are not going to get new ones and will have to settle on lower paid jobs in the service sector.**
- **Globalization is tightly linked with inequality. The benefits of free trade go to consumers and to the highly educated.**

# Energy/Environment--Pollution in Beijing

- **Global Warming? We can't treat the US as an island. Taxing our people to cut their energy use will make us poorer.**
- **China and India want a free ride, exemption**



**They say, “the US and Europe grew without environmental regulation from 1870 to 1970. Why shouldn't we?”**

**We should encourage natural gas and nuclear, not subsidize wind and solar. And we should end subsidies to ethanol which drive up the worldwide price of corn and meat.**

# Consumer and Government Debt?

- **The government should have bailed out underwater homeowners by giving them a route to refinance at lower interest rates. This failure is a major impediment to recovery**
- **The government deficit? Not a high priority now when the borrow can borrow so cheaply and the Fed can buy government bonds**
- **Lives are being ruined by spending restraint. The Tea Party will decimate Federal and local government employment.**

# **7<sup>th</sup> Headwind: Medical Care**

- **US ranks #38 in life expectancy, way ahead at #1 in costs**
- **How could Americans develop something so inefficient?**
- **Fundamental principle of medical care everywhere: right of citizenship, not dependent on employment. Why attack the unemployed?**
- **Reliance on private insurance: they employ hawk-eyed bureaucrats to find everyone with a pre-existing condition to cut them out**

# More on Dysfunctional Medical Care

- **We have public insurance for the poor and the elderly over 65**
- **Why shouldn't we have public insurance for everyone?**
- **It would cost less than now because:**
  - **Convert from inefficient small doctor offices to group practices under hospital systems, like Evanston Northshore and Kaiser-Permanente**
  - **End fee per service**
  - **End doctors owning labs prescribing excessive tests**

# **Most Important, Keep the Poor and Uninsured Out of the ER!**

- **Our system is wasteful because uninsured people can't afford preventive care**
- **Instead of their stage 1 lung cancer or prostate cancer being caught by regular screening, they arrive at the ER with stage 4 cancer that is untreatable but uses up hospital resources**
- **The pathetic story in Sunday's NYT review section about Nicholas Kristoff's friend, who took a risk and did not buy insurance.**

# Evaluating the Candidates

- **Romney: He changes policies every day. Who could trust him?**
  - He invented Obamacare and implemented it in Massachusetts. But now he would repeal Obamacare
  - Why? Oh, this is a matter for states to decide
- **Is this the kind of country you want, where your move from state to state requires a completely different type of medical care?**
- **Folly of this attack on Federal government: when you leave things to the states you get the lowest common denominator. Rich win, poor lose**

# **More Romney Changes in Midstream (Romney = Bush or not?)**

- **Romney in the primaries: we' ll stimulate the economy by cutting taxes especially on the rich**
- **First debate. Oh, my tax cuts won' t raise deficits because I' ll take away all the deductions so my plan won' t raise the deficit**
- **But if you don' t cut taxes and give money to people, how can the economy revive?**
- **Do you really want to have your charitable deduction to your church, university, food shelter taken away as Romney now proposes?**



# **Solutions for Reviving the Economy's Weak Recovery**

- **More spending that creates jobs. More spending that goes to poor people and the unemployed who will spend every dollar and create a multiplier effect**
- **Pay for it two ways**
  - **Higher taxes on the rich. 36% above \$250K 40% above \$1 million. 45% above \$5 million. 50% above \$10 million**
  - **Let the Fed buy the bonds created by the extra deficits. The interest cost is zero. Fiscal stimulus is a free good**

# Other Comparisons

- **Immigration.** We need more, particularly high-skilled. Romney in primaries said: to hell with all those illegals, let them “self-deport”. In contrast Obama gave amnesty to children born in the US and should have fought harder for amnesty.
- **Education.** Neither has dealt seriously with college cost inflation but at least Obama prevented Republican congress from doubling interest rates on student loans

# Inequality

- **We can't tell NBC it can't pay Matt Lauer \$30 million a year**
- **But we can tell Matt Lauer that he's a very lucky guy and should pay 50% rather than 28% on his income**
- **How do tax cuts for Matt Lauer (Romney's plan) help the economy to recover?**
- **Some countries do it better. Canada's immigration policy, Canada's college completion rate, Canadian citizenship right to medical care**

# Medical Care

- **Romney: Repeal “Romneycare”. Oops, I meant Obamacare**
- **Don’ t prevent insurance companies from denying pre-existing conditions**
- **Don’ t allow children to age 26 to be covered under parents’ policies**
- **Deny coverage to the poor by drastically slashing Medicare**
- **Move ever further to a society in which 4<sup>th</sup> stage cancer winds up in the emergency room instead of being caught in the first stage by preventive care**

# Final Comment

- **People are finally waking up**
- **This is the most important election in a generation**
- **America suffers from flagging innovation that is nobody's fault: we've already invented a lot of great stuff**
- **But we can deal with some of the headwinds**
- **Today's talk has been about fundamentals. You judge yourself which candidate comes closest to proposing the necessary changes.**