Commentary: Macroeconomic Policy and Long-Run Growth

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The Competitiveness Policy Council that I chair is a national commission created by the Congress to recommend action programs to improve America's performance in all the areas we are talking about at this conference. We basically define competitiveness as productivity and our effort is very deeply embedded in the framework of this discussion.

The commission has 12 members, four each appointed by the President, the Senate and the House. Each group of four comprises one corporate CEO, one labor union president, one top government official, and one public interest person. It's totally bipartisan. Unlike most commissions, it is quasi-permanent. Our hope is to be as successful as Alan Greenspan was when he chaired the Social Security Commission a decade ago.

When we did our unanimous first report to the Congress and President earlier this year, we took the view that the United States faces a very serious competitiveness problem. What the Japanese now call "the America problem" is not just slow growth and foreign catch-up. It's the fact that our productivity has expanded less than 1 percent per year for about 20 years and that our real wages are flat or down over that 20-year period. The attainment of our educational system is flat or, on some counts, worse than it was 20 years ago. (That, incidentally, raises questions about whether enrollment data are adequate proxies for measuring the output of our education system.)

We have had huge external deficits—nearly a trillion dollars over the last decade. This is significant, contrary to what Siebert implied, because the United States is now as open an economy as Japan or the European Community taken as a group. As Alan Greenspan said at the start of today's discussion, there is deep dissatisfaction in the American public concerning the state of our economy and our commission is trying to come up with suggestions on what to do about it.

Our first report echoed both the old and new growth theories. It echoed what Kumiharu Shigehara said earlier this morning: that one must have a broad-based effort. He and we call for a comprehensive competitive strategy for the United States. That strategy would include large macroeconomic policy changes, particularly to raise the low levels of savings and investment. Major structural reforms are needed in four key areas: education and training, health care costs, technology commercialization, and corporate governance/financial markets. We also need a new mechanism to develop thoughtful, sector-specific policies rather than reacting in the destructive and often protectionist way that we have in the past.

Our commission set up eight sub-councils which are now working out detailed blueprints in each of these areas. They include about 250 top people, many of whom are in this room. Our full council intends to submit a detailed competitiveness program to the President and Congress in early 1993.

To pick up on the discussion of a moment ago with Larry Summers, and some of the earlier papers, we are inclined to propose a very ambitious goal for the United States: doubling the rate of national productivity growth by the end of the century, from the 1 percent of the last few decades to 2 percent. "Doubling productivity growth sounds ambitious while "raising it by 1 percent" sounds less ambitious. But they amount to the same thing.

As Larry said in his paper, increased investment would have to be done in ways that have super-normal rates of return in order to get the kind of productivity increase we want. As we quantify our effort, we conclude that the actual investment rate would have to increase by something like 8 percent of GNP, as suggested in both Larry's paper and Alan Auerbach's paper.

In addition, we do not want to increase the external deficit. In fact, we would like to eliminate it. Hence, national savings would have to go up by more than 8 percent of GNP over the rest of the decade. So we will make a proposal that, over the remaining years of this decade/century and the next two presidential terms, the U.S. national saving and investment rates need to rise by about 1 percentage point per year to achieve the desired goal of doubling annual productivity growth.

Once we agree on such a goal, how do we achieve it? I don't pretend that we have a full program yet. The papers and discussions from this conference will help us enormously in doing that. I obviously haven't time to go through the entire program that we do have at the moment. But a big part of it, at the macro level, is the old faithful—converting the budget deficit not just into balance but into surplus. We would take it from the current level of deficit, 3 to 4 percent of GNP, to a surplus of 2 to 3 percent of GNP (including the trust funds). We would get a large part of the total increase in resources that we need with that kind of budget correction.

The rest of those resources would need to come from an increase in private saving. The key question, of course, is how to do that? We observe a structural change in the American economy in the 1980s. Historically, as you all know, there has been an inverse coalition between public and private saving in the United States. The national saving rate stayed more or less constant. Public saving went up when private saving went down and vice versa.

But both went down in the 1980s, undermining the availability of resources for productivity increases. That raises the question of whether the United States has become a nation of target savers. Are we aiming for a steady stream of investment income growth particularly as, on the institutional side, corporate pension plans come to dominate the saving picture and defined benefit plans become a major portion of saving by individuals? If we are a nation of target savers, then of course higher interest rates mean ***less*** saving. Better tax treatment of investment income means ***less*** saving. The result would be perverse in terms of the experience we have had in the past.

If that were true, then I find no other way to reverse the correlation of the 1980s than budget correction. This would take pressure off interest rates and boost private as well as public saving, helping to generate the resources that we need. There may be ways for policy to promote private saving directly as well, like mandating defined benefit pension plans for all companies.

The next and equally critical question is how to channel the investment that would then be available into high productivity and strategic payoffs. The obvious positive answer to Al Wojnilower's question is that the allocation of capital does make a difference. In our view, some of that needs to be done by the government itself with public infrastructure investment at a much higher rate than it has been.

Additional means to these ends would include much stronger education and training programs. Our view is that the fundamental problem of U.S. primary and secondary education is that the students have no incentives to work. Students can get into colleges and universities as long as they can pay, and in most cases even if they cannot pay. (They cannot get into Harvard or MIT but they can get into some college or university whatever their attainment in high school.) Their ability to get jobs also has very little to do with their attainment in secondary school. Therefore we want to create major new incentive systems based on national standards that are required for graduation from high school and entry to college. Federal funding of higher education should, in turn, be conditioned on application of those standards.

We have a number of ideas on commercialization of technology, and tax incentives to private investment. We agree with Larry Summers' paper, and with Alan Auerbach's paper, that the government can do better in promoting investment than in promoting saving. Marginal incentives pay off. Targeted marginal incentives pay off. A new equipment tax credit makes sense.

All this must be done consistently with bringing the budget into surplus over the time period I mentioned. Corrections in the budget position will have to total more than 100 percent of the current deficit level because a few new expenditures, including tax expenditures, will be needed. On the tax side itself we want to kill two birds with one stone: any new revenue increases ought to be achieved with tax measures that provide incentives to save and disincentives to consume. In our initial report, we already suggested the possibility of shifting from income-based taxation to consumption-based taxation--or at least going partly down that road to a value-added tax or a wide-based energy tax.

This is a very broad brush of a number of directions we are leaning toward to suggest how the United States can sharply improve its productivity performance and its competitiveness over the coming decade. Everything that I've mentioned sounds pretty ambitious. The question is whether it is doable. Our commission concluded there was no chance for extensive policy reform in election year 1992. Therefore, we did not present a detailed program or specific proposals for this year but rather laid out broad strategies and tried to help focus attention on the problem.

However, we concluded that there might be a chance of major policy action in 1993. We know that the U.S. government moves dramatically only in two circumstances. One is when there is a crisis. However, in some senses unfortunately, the competitiveness problem is not a crisis as much as "termites in the woodwork."

The other time the United States tends to move is in the first year of a new administration so we concluded that 1993 might be the year for action. Moreover, we know that the United States is in its fourth year of economic stagnation without much prospect of picking up sharply. We compare rather poorly with the rest of the world, as just suggested in the question by Stanley Fischer. There's not much prospect for early recovery, in part because the United States has no available policy tools. With the budget deficit at this level, we can't use fiscal policy. Nor is there much impact from monetary easing with the financial system still under strain, even with significant reductions in interest rates and all that the Federal Reserve has done to stimulate the monetary side.

As we look at the world, the prospect is for very sluggish and inadequate medium-term growth. The Germans are struggling with their version of Reaganomics and the European countries are all striving to bring their policies into conformity with the Maastricht standards for economic and monetary union—lower inflation, lower budget deficits, further disinflation. In addition, the seeming structural downshift in Japan presages slower economic growth in Asia as well.

So our conclusion is that the best, perhaps only, short-term strategy for now is to start coming to grips with the long-term fundamental underlying problems. It was fascinating that all members of our commission agreed that no quick fixes or jump-starts were possible. We had to begin an early attack on the underlying problems to get the American economy back on track. In the current political campaign, some of these issues are being discussed—but not the tough ones comprising saving and investment, the budget, and the like.

We have come to a final judgment that, when the new President wakes up on November 4 after having been elected, he really will have only two choices. One is to try to skate through the next four years without dealing with the fundamentals. Jimmy Carter did that in the late 1970s. George Bush has done that over the last four years. The result is stagnation, poor economic performance, and continued deterioration. The alternative is to take ambitious measures, recognizing they will require taking some political heat early. That's what Ronald Reagan did, taking a recession—the biggest since the 1930s—in his first year-and-a-half but with nobody remembering that recession when his re-election was approaching. A sweeping victory was the result.

So even in terms of short-term politics, there may be a case that correlates with dealing 'with the real problems of the economy. The fact that Paul Tsongas and Ross Perot did very well this year indicates to us that there is an enormous undercurrent of sentiment in the American public that would support an effort to deal with the fundamental problems, and a recognition that jump-starts and quick fixes aren't available and won't work. Thus we believe the time has come to try to deal with these issues.