Joint Economic Committee Democrats

Senator Jack Reed (D-RI) – Ranking Democrat

Background Material September 2005

Meeting America's Economic Challenges in the Wake of Hurricane Katrina

Highlights from the JEC Democrats/Democratic Policy Committee Forum

Robert Rubin
Former U.S. Treasury Secretary
Director and Chairman of the Executive Committee at Citigroup, Inc.

We are on the wrong track on many fronts. We urgently need a renewed commitment to facing our problems and to providing the foundations for a healthy economy, and we must act now.

Our fiscal deficits are particularly pernicious because they occur, uniquely to the U.S. amongst the industrial nations, in the context of large and increasing current account deficits, partly caused by our fiscal deficits, and a virtually zero personal savings rate combined with very high levels of household debt. And all of that greatly increases the far greater threat that both domestic and foreign markets begin to fear long-term fiscal disarray, and also become concerned about our currency because of that combination of fiscal deficits and current account deficits.

The 2001 and 2003 tax cuts have a 75-year actuarial cost of 11 trillion dollars, while the Social Security 75-year deficit is estimated at 4 trillion dollars. Returning to Clinton era tax rates on incomes over $200,000, plus retaining the estate tax, versus making the 2001 and 2003 tax cuts permanent plus AMT reform, would generate $1.1 trillion over 10 years and $4.0 trillion over 75 years.

In my view, the President and the leaders of both parties and both houses should come together and take joint accountability for making the extremely difficult decisions that must be made, with the focus on the most immediate problem, the projected deficits of the next ten years, and on laying the ground work for dealing with the largest problem, federal health care.

Alice Rivlin
Former Director of the Office of Management and Budget
Senior Fellow at the Brookings Institution and Visiting Professor at Georgetown University

Katrina spending could be seen as a temporary emergency that could be easily financed by borrowing were it not for two facts. First, we already have a deficit of worrisome proportions financed by foreign borrowing. Second, federal spending will certainly escalate dramatically as the boomers retire and the cost of medical care continues to rise. Medicare and Medicaid alone will eat up most of projected federal revenues, if per capita health care spending continues to rise at historical rates. Hard choices will be unavoidable in the next decade. We shouldn't undermine the strength of the economy or make the future choices harder by fiscal irresponsibility now.

To view a webcast of this forum, go to www.jec.senate.gov/democrats/hearings.htm

Bruce Bartlett
Former Deputy Assistant Secretary of the U.S. Treasury Department
Senior Fellow at the National Center for Policy Analysis

I testify as [a Republican] who is very disenchanted with his party's fiscal policy since 2001. Our fiscal situation is dire and growing worse by the day. My principal concern, however, is not with today's deficits—even if they are swollen by Katrina and Rita-related emergency spending. What worries me is the retirement of the baby boom, the first of which turns 62 in 2008.

Virtually 100 percent of all federal taxes, on a present value basis, do nothing but pay for Social Security and Medicare. Unless there are plans to abolish the rest of the federal government, large tax increases are inevitable. Let me be clear that I am no advocate of higher taxes. Sadly, unified government has led to an utter lack of restraint by my party that is simply inexcusable.

I believe that the fiscal hole is now so large that it is unrealistic to think that we can just tinker with the tax system. And under the circumstances, I have no faith whatsoever that spending will be significantly restrained—at least not by my side. Since my party won't do it, yours is going to have to.

Like it or not, we must travel the same route taken by the Europeans, who…all imposed a broad-based consumption tax called the value-added tax as an add-on tax to all the others. I think it is only a matter of time before we are forced to do the same thing and the longer we wait the more painful it will be when it is finally done.

Roger Altman
Former Deputy Secretary of the U.S. Treasury Department
Chairman, CEO and Co-Founder of Evercore Partners

The tragedy of Hurricane Katrina has dramatically exposed a series of societal and governmental weaknesses. The following is a list of the policies which Katrina should impel our nation to take:

We must adopt and fully fund the Council on Foreign Relations' 2003 list of first responder preparations. Many of these preparations, in terms of equipment and training, should occur at the federal level. It is not practical to expect municipal or state governments to be primarily responsible for responding to mass catastrophes. We should properly expand our Army and Special Forces manpower levels by 100,000 - 200,000. Currently, there are insufficient military forces to intervene in the immediate aftermath of such events, while pursuing our current foreign involvements.

We should drop any proposals for further tax cuts for upper income Americans. They should not be put on the back burner, as Secretary Snow just suggested, they should be dropped. In light of these first responder and military needs and our existing and projected deficits, America cannot afford them. We should roll back the cuts in the two top marginal rates which have occurred since 2000. This is not only necessary to finance investments in emergency preparedness, but also to prepare for the giant Medicare and social security deficits which our children will face.

Finally, one of America's bedrock principles is its generational promise, that each generation will make the investments and the sacrifices to ensure that its successor generation experiences a safer nation and a better standard of living. We followed this principle unwaveringly for over 200 years. But, today, by ignoring these necessary investments for the sake of a foolish fiscal policy, we are unforgivably violating it.

Cecilia Elena Rouse
Former Special Assistant to President Clinton for Economic Policy
Professor of Economics and Public Affairs, Princeton University

Education is the primary route for upward mobility in our society. A prominent feature of the most vulnerable among our population is a lack of a high school degree, and this has a very high economic cost to our society. Not only does the lack of skills affect the current generation, but it also affects the next one, too.

Most of the individuals displaced due to the events of the Gulf Coast – particularly those in New Orleans – were among the most vulnerable in our population. Thus, a large fraction of them lack valuable labor market skills which will make it difficult for them to get reestablished in new areas, particularly since many of them likely relied on extended family in a multitude of ways.

Increasing the schooling of high school drop-outs even by one year could increase lifetime income for one cohort by about $72 billion and the gains in federal and state income taxes would be about $16 billion; if we add in Social Security taxes that gain would increase to about $27 billion. These are large numbers, especially when aggregated over multiple cohorts. Clearly, there are large social and economic losses to individuals not completing high school.

We know how to address inadequate education, but the most effective interventions (e.g. pre-school, smaller class sizes, and job training) are expensive. However, evidence shows that these interventions have a big social return and pay for themselves in the long run (e.g. higher incomes, greater tax revenue, lower crime rates).

Alan Blinder
Former Vice Chairman of the Federal Reserve
Professor of Economics at Princeton University

Rising income inequality has been with us for so long that I fear we may be becoming inured to it. The basic story is that *earnings from work* have grown vastly more unequal over the last quarter-century. The one notable exception was the boom years of the late 1990s, when labor markets were extraordinarily tight. The main culprit is *not* the government but the marketplace. Starting sometime in the late 1970s, the market turned ferociously against the less skilled and the less well educated. As natural market forces turned against the middle class and the poor, the federal government piled on by enacting tax cuts for the rich while either permitting or causing large holes to appear in the social safety net. It's a policy direction that, in my view, needs to be changed. The first step would be to stop piling on.

A job security issue whose present importance has been greatly exaggerated, but whose future importance, ironically, appears to be underappreciated is offshoring. Only a minority of American workers—including almost all manufacturing workers—have historically faced job competition from abroad. The share of American jobs that is vulnerable to offshoring is certain to rise as the technology improves and as countries like India modernize and prosper. As this occurs, tens of millions of *additional* American workers will start to experience an element of job insecurity that has heretofore been reserved for manufacturing workers. It is predictable that they will not like it.

As I see it, the key labor-market distinction in the Information Age will not be high-skilled versus low-skilled, as in the recent past, but rather services that can be delivered electronically with little loss of quality versus those that cannot. The fraction of U.S. jobs that can be moved offshore is certain to rise inexorably as technology improves. Despite all the fuss, it is pretty low now. But it will eventually be quite high. These people will constitute a much larger, more vocal, and more politically-engaged group than the poor and uneducated. It seems unlikely that they will just sit there passively and take their medicine. Congress will hear from them. So Congress would be well advised to start thinking about this problem now.

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