CONGRESS OF THE UNITED STATES

JOINT ECONOMIC COMMITTEE

CHAIRMAN JIM SAXTON

PRESS RELEASE

For Immediate Release
January 7, 2002

Press Release #107-59
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ECONOMIC FORCES DRIVE BUDGET CHANGES

WASHINGTON, D.C. – Recent statements made by critics of Administration economic policy exaggerate the short-term impact of fiscal policy on the economy, factually misstate the historical record with respect to interest rates, and ignore the important contribution of Federal Reserve policy to the long expansion of the 1990s, Chairman Jim Saxton of the Joint Economic Committee said today.

"The recent attacks on President Bush's economic policies made by Senator Daschle and others are misguided and factually unsound," Saxton said. "It will be recalled that changing economic conditions are the dominant force influencing budget revenues and outlays, not the reverse. The primary reason the budget surpluses have declined is that the economy has fallen into recession; meanwhile the response to terrorism has increased outlays. The long boom fostered by the Federal Reserve's monetary policy of price stability had led to a surge in revenue growth that wiped out the previous deficits much faster than official budget projections had forecast. With the onset of the economic slowdown, the revenue windfall has ended, and the surplus revenues have evaporated.

"The opposing point of view argues that the budget tail is wagging the economy dog. For example, in a recent speech, Senator Daschle repeated the Clinton Administration assertion that interest rates fell after what he calls the 'fiscal discipline,' or tax increase of 1993, propelling the economy forward.

"In his 2000 *Economic Report of the President,* former President Clinton had also suggested that interest rates fell after the tax increase of 1993, boosting the economy. **To the contrary, as his Council of Economic Advisers shows in tables and graphs published under the same cover, interest rates increased after this legislation was passed, and the Administration lowered its economic growth forecasts for 1993 and 1994.** This increase in interest rates is graphed on page 66 of the Administration report released in 2000.

"During most of 2001, long-term interest rates trended modestly downward, rising slightly in recent weeks with the expectation of economic recovery. It is difficult to understand the critics' complaints about long-term interest rates since they are currently at historically low levels. The recent levels of long-term interest rates have been low enough to foster a boom in mortgage refinancing that continues. In any event, no one should be surprised that the Fed's reduction of short-term interest rates has not reduced long-term interest rates commensurately, for the simple reason that the Federal Reserve does not directly control long-term interest rates.

"Nonetheless, during the 1990s the Federal Reserve succeeded in squeezing inflation out of the economy, improving the operation and efficiency of the economy, lowering inflation expectations, and thus leading to a reduction in long term interest rates over the course of the expansion. Unfortunately, this positive contribution of the Federal Reserve to the economic boom was noted neither in President Clinton's 2000 economic report nor in Senator Daschle's recent speech," Saxton concluded.

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