Is the U.S. Budget in Crisis?

A Q&A with Brookings Institution Economist Bill Gale

By Sachin Waikar

As the U.S. heads toward unprecedented public debt and deficits, Kellogg hosted Bill Gale, Arjay and Frances Miller Chair in Federal Economic Policy at the Brookings Institution and a top national expert on fiscal policy. On October 17, 2019, Gale, author of the new book *Fiscal Therapy: Curing America's Debt Addiction and Investing in the Future*, was interviewed by Kellogg Associate Professor Strategy Amanda Starc, and took questions from faculty and students in attendance.

Here, we present select questions and answers from the event.

Are we in a crisis?

While the "crisis" debt scenario is dramatic to talk about, I don't think it holds much water. An old colleague said, "Deficits are the termites in the woodwork, not the wolf at the door." It's about a gradual eating away at the financial foundation.

Interest rates aren't rising. But we're financing the debt with capital inflows and will have to pay that back eventually. So whether the deficit raises interest rates or capital inflows, our future national income will go down if national saving goes down.

Congress does things only when they *have to*. So they've continued to put off dealing with the deficit.

What should the goal of fiscal policy be? What are the tradeoffs?

Policy's end should be a strong, more equitable economy in terms of distribution of income and opportunity across classes and generations.

There are very few areas without tradeoffs. One tradeoff-free area is investment in early childhood education, which produces positive outcomes for health, work, criminal behavior, and others.

Cutting social security costs, in contrast, has more tradeoffs, but it's the government's most popular program. A third of the elderly get 90% of their income from it. The fund won't run out of money until 2034. That's a long time in political years but short in terms of structuring a solution.

Healthcare spending—how to balance any cuts with ensuring access?

The problem isn't the government but the whole system.

Medicaid and Medicare operate relatively efficiently. Still, Medicare pays about 25% more for drugs than Medicaid and the VA system pay. If Medicare payments matched those of the others, we'd save over $500 billion per decade! That could save money without affecting people's benefits.

We're also seeing local healthcare monopolies expand, with large players buying up smaller ones. The only way to deal with that is rate-setting—just telling hospitals what they can charge, like other countries do.

Where can we expand spending?

The proposal that I made in the book was~~has been~~ to increase spending on social and safety-net programs~~, including for infrastructure,~~ by about 1% of GDP—an enormous increase relative to existing amounts. In addition, I propose substantial increase in infrastructure. N~~But the n~~et federal investment in infrastructure has been close to zero for the past 25 years. In 20 localities, Domino's pizza has given money to local government so their drivers can deliver pizza more safely. We shouldn't depend on Domino's for infrastructure!

How can we think about equity across generations and geography?

Debt creates burdens across generations: the younger generation is asked to pay for the older one, with the assumption that productivity and living standards will rise.

But that can lead to a cavalier attitude about the next generation's welfare. Economist Raj Chetty studied whether kids have more income than their parents, by generation. About 90% of children born in the WWII era ended up better off than their parents; only about half of those born in the 1980s did, despite a strong economic expansion over that period. ~~.~~

Equity across geography is very challenging. A study by Summer and Glaeser showed enormous differences in growth rates across regions~~metro areas~~—Northern Virginia versus rural Ohio, for example. But the only solution offered was boosting the Earned Income Tax Credit for people in slower-growth areas. And they are two of our smartest economists. It's very hard to figure out ~~hwo~~how to solve this problem.~~.~~

What critiques do you hear from the political right?

Taxes.

They feel I~~we~~ got the problem right: deficits. But the solution, they say, should be cutting spending, because raising taxes destroys the economy. But r~~R~~esearch shows that other G7 countries' taxes have been higher than ours over the past 40+ years, yet~~but~~ per capita growth rates have been identical. So it's possible to raise taxes without hurting growth.

How should businesses think about potential changes in the tax code or on the fiscal landscape overall?

First, read~~listen to~~ JPMorgan Chase CEO Jamie Dimon's speeches; he's a corporate leader who embraces the bigger picture.

Second, recognize that the corporate tax lobbyists I have met are the most narrow-minded people I have run across. ~~possible.~~ They don't care about the economy or industry or even the company they represent—just the taxes paid. If you offer them policies that reduce the company's taxes paid but hurt the company overall, many of them would ~~they'll~~ take it. They need to understand that a good economy is good for their company.

How can we preserve the social safety net when technological advancement is changing the labor market quickly?

We need to embrace technology-driven changes but also support a more aggressive spending program. The government has to step in, due to all the externalities involved.

But I'm not a fan of Universal Basic Income. It's enormously expensive. Even if we cut all spending programs other than Social Security and Medicare, we could only afford a UBI of about $2000 per person per year. And it's wrong to think it would eradicate demand for food stamps or other programs. We'd just be starting from a different place.

What do you think about the reality that the current tax code subsidizes health insurance and home ownership?

Reform ~~With health insurance~~should tax ~~, the idea is to impose some tax, either on~~ generous health insurance plans or the health insurance of ~~on~~ people with high incomes.

The mortgage-interest deduction is a disastrous policy. It may actually discourage home ownership because it boosts the value of land to high-income/high-tax payers who buy property and rent out to low income/tax payers and effectively share the tax savings. We should replace with a first-time homebuyer tax subsidy, which would cost less and encourage home ownership better.

Why do we lack the political will to solve obvious market failures? What has to change?

People are not accepting that there are problems and that we need to consider all of the ~~solutioons~~solutions. Lots of people still don't believe in climate change, for one. There's also the "no new taxes" pledge that many Republicans have signed, which makes it hard to negotiate anything on the budget issue.

Debates about taxes are less about the policies than how the revenues will be used. It gets caught up in ~~these~~ ideological wars. Both Democrats and Republicans ~~both~~ may propose a Value Added Tax, but conservatives want it to do away with corporate taxes and liberals want to use it to fund healthcare and other social policies. Earmarking taxes for specific purposes may help.

Congress usually responds to public opinion, so framing is key. And ~~Congresspeople~~Congress people need air cover from the White House, for the President to publicly support them on reaching a compromise. Then they can debate and discuss the issue.