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The Rightness of Reaganomics

Almost every American President has suffered a loss of his own party's strength in Congress in the mid-term elections. The exception was Franklin D. Roosevelt elected in 1932; the Democrats increased their majorities in the Congressional elections of 1934. F.D.R. was able to keep his 1932 political momentum going and bring about a massive change in American political, economic and social trends.

The question is, can Ronald Reagan do likewise? Was the 1980 election a freak of timing, or is it the start of a new conservative era? Will conservative strength gain or fade in the 1982 elections? That question will be answered by the economy in general and by tax cuts in particular.

Ronald Reagan was elected with a mandate to cut taxes 10 percent a year for each of three years in order to stimulate the private enterprise economy and drastically cut the size of the Federal Government. Reagan's campaign promise was to enact Kemp-Roth tax cuts based on what is called "supply-side" economics. Simply put, that means: let incentives stimulate the economy, resulting in investment, capital formation, and creation of private-sector jobs. It means the fulfillment of Reagan's promise to "get America back to work again."

The Democrats in Congress have already forced Reagan to compromise his hope for a 30 percent tax cut (10 percent for each of three years) down to 25 percent over three years. Does that still sound like a big tax cut? It isn't really. The legacy of Jimmy Carter is that, even if Congress took no action at all, taxes would rise at about $100 billion a year (from inflation bracket creep, windfall profits, and Social Security taxes).

In the famous Reagan-Carter debate, Reagan asked Americans, Are you better off today than you were four years ago? The American voters answered NO to that question. The best way to fulfill Reagan's election mandate is to reduce the income tax. We've suffered long enough at the hands of the Keynesian borrow-and-spend, deficit-and-inflation economists. It's time to give the reins to "supply-side" economists.

Tax Cuts Essential Now

Although the Reagan budget cuts are essential to his economic program, the Reagan tax cuts are the heart of it. The tax cuts represent the innovative change, the real turning of the corner from the old, tired liberalism of the past, to the new conservative economics of the future.

The structure and rates of the current Federal income tax are the primary reason for the sluggish capital formation in the United States, which in turn restricts economic growth. High marginal tax rates discourage savings because they grab much income which would otherwise go into savings. To discourage savings means to discourage capital formation, which in turn means to discourage the creation of jobs.

The close relationship between savings and growth is reflected in the experience of other countries. Our big competitor, Japan, has a savings rate which is 4.4 times that of the United States, and a real Gross National Product growth rate which is more than ten times that of ours.

The United States also suffers by comparison with the savings and growth rates of Germany, France and Canada, although they are not as high as Japan's. These unhappy comparisons are despite the fact that we are about 60 percent self sufficient in oil, whereas Japan, Germany and France are almost totally dependent on oil imports.

Even though Congress has taken credit for voting a number of "tax cuts" since 1965, these have not been enough to cover the increases in real taxes caused by inflation. We have suffered a striking net increase in taxes due to tax bracket creep, the popular term for the effect of inflation in raising the rates on individual taxpayers by pushing them into higher tax brackets.

Look at how the jaws of the progressive income tax joined with inflation bit into and crushed the individual who had a $10,000 income in 1965. Between 1965 and 1979, his taxes were supposedly reduced $520 by legislative tax cuts, but actually inflation alone increased his taxes by $2,185. At the $40,000 income level, Congress supposedly reduced taxes $1,449, but inflation actually increased the individual's taxes by $18,999. It is obvious that inflation makes windfall profits for the government.

Inflation has made the progressive tax system become progressively more progressive even over the last five years. In 1973, one fifth of the taxpayers were paying 63.7 percent of federal income taxes. By 1978, one fifth of the taxpayers were paying 66.6 percent of the federal tax burden.

"Supply-Side" Means Incentives

Reagan's "supply-side" economics should be called "incentive" economics, because that's what it really means. Incentive is a word that any child can understand and relate to.

Incentive is a motivator that affects all people without discrimination. It moves rich and poor, black and white, male and female. Just as financial incentives may motivate a poor person to remain on welfare rather than take a low-paying job, financial incentives may motivate a rich person to relax and enjoy life rather than invest in a new enterprise.

Unfortunately, liberal economics and our present tax structure provide powerful incentives to idleness. When the poor person chooses idleness instead of work, society loses only the small amount of taxes he would otherwise pay (plus the cost of supporting him on welfare). However, when the rich man chooses idleness over work, society loses not only the large amount of taxes he would otherwise pay, but loses something far more valuable -- new jobs for other people.

The rich man, by definition, has more income than he needs to pay for the groceries and to meet the mortgage payments. When he makes more money than he can spend on himself and his family, he normally invests this excess income in other enterprises; and that's what creates new businesses, plant expansion, and more jobs.

Our present tax structure provides incentives to the rich to quit working, quit producing, quit investing; in other words, to become the "idle" rich instead of the productive rich. If the rich man is in the 60% tax bracket, for every additional dollar he earns, the tax collector gets 60c and he gets only 40c. Since he doesn't really need the money anyway, he decides that leisure is more appealing than extra work or risky investments.

Incentive economics focuses on the marginal tax rates, that is, the tax rate applying to the *next* dollar of income you receive. That's the point at which incentives or disincentives encourage you to earn more or to remain idle. Tax cuts provide incentives to the rich to withdraw from tax shelters, reject leisure, work overtime, forgo consumption, sell gold, buy stocks, start a business, and risk their savings in order to earn more.

Now suppose we cut the tax rates so the rich man can keep 60c from every additional dollar he earns, while paying the tax collector only 40c. All of a sudden, his leisure time costs him 50 percent more. The tax cut has given him an incentive to work harder and to invest more.

It matters a great deal whether the rich remain idle or go to work because, when the rich work overtime or invest in productive enterprises, they pay taxes -- lots of taxes. Rich people make more money for themselves, yet they pay a larger share of the national tax burden. Cutting the marginal tax rates will make the rich pay more taxes.

More important, their investments create more jobs, so more people move into the productive part of the economy. That means a healthier economy, more tax revenues, and less inflation because the nation moves closer to a balanced budget.

A productive economy depends on people working in jobs. If there are not enough jobs for the people who want to work (as now), what we need more than anything else is incentives to induce people with savings or extra income (i.e., rich people) to invest in businesses in a way that creates more jobs (called capital formation).

Incentive economics is the wave of the future which is destined to wash into oblivion the destructive economics of Lord Keynes which preached deficit spending and produced the politics of cynicism: tax and tax, spend and spend, elect and elect. The far-sighted "supply-siders" who have developed incentive economics include Paul Craig Roberts, Norman B. Ture, Arthur B. Laffer, George Gilder, Jack Kemp and William Roth.

Block Grants Vs. Categorical Grants

President Ronald Reagan's most far-reaching proposal is his plan to convert some "categorical" grants into "block" grants. The Reagan plan is imaginative, constructive, and would be a giant step forward for every economic, social, and political goal so devoutly sought by Reagan and by his enthusiastic followers.

The spectacular growth of Federal spending and regulatory power over the last decade has spawned a steady and increasing flow of tax dollars to a big variety of special-interest groups. These are called "categorical" grants; they go to particular categories of concerns, designated and regulated by Federal officials.

The Reagan Administration proposes to take some 83 of these categorical grants, divide them into six "blocks" which are designated for broad areas of purpose, cut overall funding by 25 percent, and then turn the money over to the states to spend among the 83 categories.

Just because funding for these programs would be cut 25 percent does not mean that there will be a 25 percent cut in services. The cost of unnecessary regulations, bureaucratic red tape, and Federal overhead is probably at least 25 percent.

The block grant proposal is an historic opportunity to do exactly what the voters elected Ronald Reagan to do: cut Federal spending, slash excessive Federal regulations, and return power, funds, and decision-making to the states. We would get better value for our tax dollars because the states would exert closer supervision over smaller amounts of money.

The Congressional debate on block grants has helped to educate the voters about the variety of special-interest programs on which our tax dollars have been spent. No wonder taxes on Middle Americans are so oppressive! Here are the proposed block grants:

1. The Social Service Block Grant would receive \$3.8 billion. This grant covers funding for Day Care, Child Abuse and Prevention, Adoption Assistance, Development Disabilities, Runaway and Homeless Youth, Community Services Administration, Rehabilitation Services, and the Legal Services Corporation.

2. The Energy and Emergency Assistance Grant would receive \$1.4 billion. This would cover programs of Home Energy Costs, Low-Cost Weatherization, Emergency Medical Care, and Emergency Social Services.

3. The Health Services Block Grant would be funded at \$1.1 billion. This block covers 15 categorical grants including Community Health Centers, Black Lung Clinics, Migrant Health, Home Health Services, Maternal and Child Health, Hemophelia, Sudden Infant Death, Mental Health Services, Drug Abuse, and Alcoholism.

4. The Preventive Health Service Block Grant would be funded at $242 million. This block would include High Blood Pressure Control, Health Incentive, Risk Reduction and Health Education, Venereal Disease, Fluoridation, Rat Control, Lead-Based Paint Poisoning Prevention, Genetic Disease, Family Planning Services, and Adolescent Health Services.

5. The Local Education Agency Block Grant would be funded with $3.6 billion. This block would include Elementary and Secondary Education Grants, plus grants for the Handicapped, Preschool Incentive, Adult Education, Bilingual Education, Basic Skills, and Emergency School Aid.

6. A second block grant of nearly $1 billion for education programs would give lesser amounts under the Elementary and Secondary Education Act, plus grants to Severely Handicapped Projects, Regional Resources Centers, Early Childhood Education, Gifted and Talented, Educational Television, Basic Skills Improvement, Arts in Education, Metric Education, Pre-College Science Teacher Training, Career Education Incentives, Consumer Education, and Women's Educational Equity. (This last has been receiving an annual budget of $10 million.)

Lobbying Against Reagan's Program

All the special interests are lobbying hard to keep funds flowing from Washington directly into their treasuries without the prying eyes of state and local officials and citizens. We would all be better off -- socially, politically, and financially -- if we reassert state and local supervision. Here is one example of tax-funded lobbying against the Reagan program.

The Federal agency called ACTION gave Federal tax funds to a "recipient organization" called the Institute for the Study of Civic Values. In March 1981, the Institute published a survey quiz for the stated purpose of helping citizens "assess the impact of President Reagan's Economic Recovery Program on their own communities or cities." Here is how this ACTION-funded document explains its unique methodology:

"The Cruelty Index is a measure of the hardship imposed upon a community or city by Ronald Reagan's proposed budget cuts in 1982. The Greed Index is a measure of the benefits that the taxpayers -- primarily wealthy taxpayers -- will receive under the President's Tax Reduction plan in 1982."

In case you didn't get the full import of the adroit choice of words "cruelty" and "greed", the document then purports to explain in more detail that the Reagan tax cuts would benefit the wealthy (called the "greedy"), and that the Reagan budget cuts would hurt the poor ("cruelly") by cutting their public services.

In order to spell this out in gruesome detail for those who cannot comprehend the concept of billions of dollars, the ACTION-funded quiz devised a point system to make its smear use of "cruelty" and "greed" more graphic. Each city and community is supposed to undertake its own analysis of the local impact of the Reagan program by assigning one point to every $10 million. For example, New York City was given a Cruelty Index of 53, Philadephia a Cruelty Index of 20.

In opening its investigation of this use of Federal funds, the General Accounting Office stated, "It is apparently a political document intended for wide distribution and would be useful in advocacy or lobbying campaigns." Indeed, it is.

If the Reagan economic program has a hard time getting through Congress, it will be because the American taxpaying public was outspent and outmaneuvered by Federal lobbyists using our tax dollars against us.

Reagan's Regulatory Relief

Regulatory relief for every segment of the economy is an essential part of Ronald Reagan's economic program. Under the capable command of Murray L. Weidenbaum, chairman of the President's Council of Economic Advisers, the Reagan Administration did 104 acts of deregulation in its first four months.

The number of final rules published in the Federal Register dropped by 47%. The number of proposed rules dropped by 54%. The number of published pages dropped by 60%.

Weidenbaum's goal is to reverse the intrusion of the Federal Government into the lives of citizens, into the decisions of businessmen, and into the choices faced by tens of thousands of state and local government officials and administrators. He doesn't think that workers, managers, investors or administrators need the Federal Government to make decisions for them on how to organize and run their daily lives and activities.

Look at the embattled auto industry. The liberal formula is to hamstring it with costly regulations (a burden that Japanese manufacturers don't have to bear), raise taxes, and give a federal subsidy or loan. The Reagan-Weidenbaum way is to rescind 34 specific regulations which, over a five-year period, will save the American motorist $9.3 billion in the cost of buying and operating cars and trucks.

This will also release $1.3 billion in company funds which can now go into capital improvement rather than down the drain of federally-mandated equipment, facilities, and compliance paperwork.

The regulations being lifted or lightened range from rules on bumper strength to exhaust emissions standards and certification procedures. The Administration will also propose that Congress amend the Clear Air Act by eliminating the requirement that all passenger cars meet 1984 emissions standards at higher altitudes.

Here is one example of how a simple change in an auto regulation will reduce costs greatly, allow consumers a wider range of choice, but have no adverse effect on clear air. The Reagan EPA will allow auto manufacturers to meet diesel exhaust emissions standards by using sales-weighted averages of the results from all their different model lines. Some can emit more pollution, some less, but the total of a manufacturer's emissions will be within the clean air standards.

The Reagan Administration has requested the D.C. Court of Appeals to remand to the Environmental Protection Agency for reconsideration a rule EPA previously issued which set noise emissions standards for garbage trucks. The costs, although not great by federal standards, are high in relation to the benefits sought.

More important, the Federal Government has no business being a busybody in the matter of garbage collection, which is a strictly local matter. If noise is a problem, municipalities could solve it better by altering truck routes to accommodate residential neighborhoods, rather than buying expensive sound-proof trucks to comply with EPA regulations.

The Reagan Administration withdrew the Department of Energy's proposed standards for the minimum energy efficiency of major household appliances, such as refrigerators and air conditioners. These unnecessary standards would have required the complete redesign of almost every appliance model by 1986. Appliance purchase prices would increase by $500 million a year, a cost that would never be recouped in saved energy costs, and which would bankrupt the smaller manufacturers that couldn't afford such rapid model changes.

The Secretary of Education withdrew proposed rules that would have required all school systems to offer a particular form of bilingual instruction to children whose primary language is other than English. The cost saving will be substantial and the lifting of this Federal harassment of local school curriculum is welcome.

The Department of Transportation delayed four regulations which would have imposed costly requirements on state and local governments, dictating how they conduct urban transportation planning, design traffic control devices, and rehabilitate or stockpile buses.

The Federal regulatory burden has simply risen way out of all reason. Between 1970 and 1981, Federal spending for regulatory activities alone rose from $0.9 billion to $7.1 billion. In constant dollars, that was an increase of 3½ times. The Reagan Administration is moving on schedule to try to stimulate a more productive economy.

The Productivity State

"What's in a name?" Shakespeare asked. "That which we call a rose by any other name would smell as sweet." But would it? American businesses spend millions of dollars to research and choose (or invent) a name before marketing a product. Publishers know that a book's title often makes or breaks its sale.

The rather unique economic system under which America, from a little band of immigrants who landed on our shores with only the clothes on their backs, grew into far-and-away the most prosperous and productive nation in the world is the greatest success story in history. But the people who enjoy its fruits don't seem to have much respect for the tree or know how to keep it producing.

The reason may be that the tree suffers from the handicap of not having a winning name. "Capitalism" (mistakenly, I believe) connotes *big* business to which most Americans do not relate with affection. "Free enterprise" and "private enterprise" have a hard time competing semantically and sentimentally with "the welfare state" or "the social welfare state," probably because more people relate to "welfare" than to "enterprise."

Yet the proven failure of the social welfare state and of socialism is just as dramatic as the success of capitalism/free enterprise. From Europe to Africa to the Caribbean to Asia, socialism is shown to be a congenitally diseased system which produces perennial shortages, food lines, black markets, political prisons, and people voting with their feet to escape to a capitalist country.

Even Sweden, long touted as the Perfect Experiment in democratic welfare statism, provides convincing evidence of its failure under the most advantageous circumstances: a homogeneous population, rich natural resources, and 150 years of avoidance of war.

With the government now consuming 64 percent of the Gross National Product, a typical Swedish industrial worker pays 50 to 60 percent of his wages in taxes, plus an additional 22.5 percent in value-added tax (VAT), a form of sales tax on all goods and services including food.

The United States may be rushing headlong down the same dead-end road. High taxes to make costly incentive-destroying, non-productive handouts have resulted in double-digit inflation, double-digit interest rates, high unemployment, and low savings and investment. Despite the proven success of the American economic experiment, Americans appear to lack understanding of and commitment to the system that produced our prosperity.

The uniqueness of our economic system has been its high level of capital formation -- the investment in plant and equipment which creates jobs, enables worker-plus-machine to produce more per manhour and thereby be paid higher wages. That's why it is accurate to call our system "capitalism."

However, in the 1980s the word "capitalism" inherits the semantic baggage of decades of leftwing smears. The word "capitalism" looks at the system through the eyes of the saver-investor-owner whom the worker-student-journalist-academician types have been taught to believe is the enemy. We need a new name to sell the successful American system. We need a name to which all participants in the economic process can relate personally.

I suggest we call our unique American economic system "The Productivity State." Productivity is a "good" word; whether we are workers, bosses, or journalists, we all understand that increased productivity (producing more per manhour of labor) brings a higher financial reward. Therefore, all types can relate to the goal: let's increase our productivity so we can labor less and enjoy it more.

The United States over the last decade has had the lowest employee productivity rate of any Western industrial nation. The auto industry, which has priced itself out of the world market, is only the most dramatic proof of our nationwide malaise.

Restoring our world leadership in productivity will require many things, starting with Federal budget cuts, which in turn will allow tax cuts, which in turn will allow increases in savings and investment, which in turn will cause more capital formation, which in turn will create more jobs and more productive jobs.

Calling the American economic system "The Productivity State" will give us a vision of a more prosperous future in which all individuals and groups have a vital stake, can work toward, and can taste their rewards. "The Productivity State" can dispose of the semantic problem so we can get on with more prosperity for more workers.

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