Outline

1. What is So Exciting About Economic Policy?
2. Do Economists Ever Agree on an Answer?
3. What Can Economists Do When the Answer is Not Known?
4. How Should Policymakers Handle Uncertainty?
1. What is So Exciting About Economic Policy?

Lets You Focus on the Big Questions—Like Slowing Income Growth

Real Median Family Income, 1948-2015

- 1948-1973: 3.0%/yr
- 1973-2015: 0.4%/yr

Source: Census Bureau; author's calculations.
And the Small Ones—Like Sufficient Broadband for Mobile Devices
Some Other Issues I Worked on in the Obama Administration

Preventing a second Great Depression
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Post Office restructuring
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- Preventing a second Great Depression
- Post Office restructuring
- Deficit reduction
- Financial crisis
- Wall Street Reform
- Business tax reform
- Affordable Care Act
- Health Delivery System Reform
- Minimum wage
- Overtime regulations
- Patent reform
- Trade
- Infrastructure
- College financing
- Defined-benefit pensions
- Climate change
- Renewable fuels regulations
- Air traffic control reform
- Competition policy
- Cell-phone unlocking
- Poverty
- Criminal justice reform
- Autonomous vehicles
- Artificial intelligence
- Immigration
- College financing
- Preschool
- Sanctions on Russia
- Chinese credit expansion
- Currency manipulation
- Inequality
- Retirement savings regulations

1. What is So Exciting About Economic Policy?
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Economics, Politics, and Combining the Two: The Example of Climate Change

**Pure Economic Answer:** Ask 10 economists, and they will likely all agree on a carbon tax.
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Combining Politics and Economics
2. Combine multiple policies to address concerns: E.g., carbon tax together with a rebate, eliminating regulations, and taxing imported carbon.
3. Adopt the nth best alternative—hopefully n is not too high!
1. What is So Exciting About Economic Policy?

## Economics Should Be *One Input* Into Decisions

### Illustrative Example: Alternative Stimulus Tax Cuts

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<th>Effectiveness (per economists)</th>
<th>Likelihood (per strategists)</th>
<th>Overall Score (per President)</th>
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<tr>
<td>Making Work Pay—Fully Refundable</td>
<td>100</td>
<td>5%</td>
<td>5</td>
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<tr>
<td>Making Work Pay—Not Refundable</td>
<td>30</td>
<td>100%</td>
<td>30</td>
</tr>
<tr>
<td>Payroll Tax Cut</td>
<td>80</td>
<td>80%</td>
<td>72</td>
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Barack's Best Idea Yet

Reported by USA Today:

Barack Obama, the presidential candidate of "change," told a town hall meeting recently that he'd "seriously consider" eliminating the penny if Lincoln's face could be placed on another coin.
Some Examples of Broad (Albeit Not Universal) Agreement…

**Micro**
Trade produces net gains but concentrated harms

Climate change can be mitigated most efficiently by a Pigouvian tax
Some Examples of Broad (Albeit Not Universal) Agreement…

**Micro**
Trade produces net gains but concentrated harms

Climate change can be mitigated most efficiently by a Pigouvian tax

**Macro**
In the long run the economy tends towards full employment, but there can be large deviations in the short run

Fiscal stimulus or lower interest rates expand aggregate demand, increasing output in the short run—but not in the long run
Do Tax Cuts Pay For Themselves?

- More progressive economists might argue that labor tax cuts only pay for about **5%** of themselves.

- More conservative economists might argue that labor tax cuts pay for about **20%** of themselves.

- All economists would agree that the details matter—for example, how and potentially when the tax cuts are paid for.
a. Data Description—Example of the Macroeconomy


Gross Domestic Product: 2.1%
a. Data Description—Example of the Macroeconomy


Gross Domestic Product: 2.1%
Gross Domestic Income: 1.0%
a. Data Description—Example of the Macroeconomy


Gross Domestic Product: 2.1%
Gross Domestic Income: 1.0%

BEST GUESS: “Gross Domestic Output”: 1.5%
3. What Can Economists Do When the Answer is Not Known?

a. Data Description—Example of the Macroeconomy (cont.)

Alternative Measures of Similar Concepts:
Job Growth in March 2017

Nonfarm payroll employment increased 98,000
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BEST GUESS: 98,000
Alternative Measures of Similar Concepts:
Job Growth in March 2017

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BEST GUESS: 98,000 (or maybe 92%/8% so 128,000)
Alternative Measures of Similar Concepts:
How Is the Economy Doing Now?

Employment growth in Q1: 1.5%
GDP growth in Q1 (Atlanta Fed GDP NOW): 0.5%
a. Data Description—Example of the Macroeconomy (cont.)

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“Soft data”: ISM manufacturing: +2.7 from Dec to Mar
“Hard data”: IP manufacturing: +0.3% from Dec to Mar
3. What Can Economists Do When the Answer is Not Known?

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Alternative Measures of Similar Concepts:
How Is the Economy Doing Now?

Employment growth in Q1: 1.5%
GDP growth in Q1 (Atlanta Fed GDP NOW): 0.5%

“Soft data”: ISM manufacturing: +3.2 from Dec to Mar
“Hard data”: IP manufacturing: +0.3% from Dec to Mar

BEST GUESS: Reasonably strong Q1
a. Data Description—Sources of Median Income Slowdown

Bottom 90 Percent Share of Income, 1948-2015

Source: World Wealth and Income Database.
3. What Can Economists Do When the Answer is Not Known?

a. Data Description—Sources of Median Income Slowdown (cont.)

Labor Productivity Growth, Nonfarm Business Sector
Percent Change, Annual Rate

- **1948-1973**: 2.8%
- **1973-2015**: 1.8%

3. What Can Economists Do When the Answer is Not Known?

a. Data Description—Sources of Median Income Slowdown (cont.)

Real Median Family Income, 1948-2015

2015 Dollars (Log Scale)

Continuation of 1948-1973 Trend
No Inequality Increase
$10,000 (15%)

Actual

Source: Census Bureau; Bureau of Labor Statistics; author’s calculations.
3. What Can Economists Do When the Answer is Not Known?

a. Data Description—Sources of Median Income Slowdown (cont.)

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b. Economic Theory—Example of Gains from Trade from Two-Sided Spectrum Auctions

Television broadcasters received free rights to spectrum—in some cases broadcasting to as few as 10,000s of viewers.

Wireless broadband providers were willing to pay large amounts for this spectrum to serve millions of customers.

But coordination issues prevented a simple market solution. Patchworks of spectrum less valuable than contiguous spectrum.
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**Solution:** (i) government buys spectrum from willing sellers; (ii) moves some existing broadcasters and pays them compensation; and (iii) auctions off spectrum to willing buyers.

**Win, Win, Win, Win:** 84 MHz of spectrum reallocated. Winners include broadcasters who sold spectrum, providers who bought spectrum, consumers who use spectrum, and taxpayers who received $5 billion.
Incomplete Information

- Purchasers of insurance know more about their health status than sellers of insurance.
- Potential solutions include public provision or mandated purchase.

Behavioral Economics

- Encouraging savings with incentives or defaults?
- Auto-enrollment for public programs?
3. What Can Economists Do When the Answer is Not Known?

c. Causal Evidence—Example of Taxes on Tobacco Products

[Graph showing sales of selected tobacco products from 2002 to 2016, comparing roll-your-own and pipe tobacco, and small and large cigars. The graph illustrates a decrease in sales after a tobacco tax increase in April 2009.]
3. What Can Economists Do When the Answer is Not Known?

d. Building Models to Simulate Alternatives

<table>
<thead>
<tr>
<th>Income Class</th>
<th>Percent of Families</th>
<th>Static</th>
<th></th>
<th>Dynamic</th>
<th></th>
<th>Percent Change in Utility (Consumption Equivalent)¹</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Percent Change in After-Tax Income</td>
<td>Without Financing</td>
<td>With Financing</td>
<td>Percent Change in Pre-Tax Income</td>
<td>Percent Change in After-Tax Income</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Bottom Quintile</td>
<td>20.0</td>
<td>2.9</td>
<td>-12.3</td>
<td>1.0</td>
<td>-11.4</td>
<td>-22.4</td>
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<tr>
<td>Second Quintile</td>
<td>20.0</td>
<td>2.7</td>
<td>-3.2</td>
<td>0.9</td>
<td>-2.3</td>
<td>-2.9</td>
</tr>
<tr>
<td>Middle Quintile</td>
<td>20.0</td>
<td>2.5</td>
<td>-0.9</td>
<td>0.8</td>
<td>-0.1</td>
<td>-0.6</td>
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<tr>
<td>Fourth Quintile</td>
<td>20.0</td>
<td>2.4</td>
<td>0.3</td>
<td>0.8</td>
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<tr>
<td>All</td>
<td>100.0</td>
<td>2.3</td>
<td>0.3</td>
<td>0.9</td>
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Table 3
Economic Effects of Shifting from a Hypothetical 25% Proportional Income Tax to a 22.5% Labor Income Tax, 25% Capital Income Tax, and $900 Lump-Sum Tax
Some Lessons About Policymaking Under Uncertainty

1. Be clear about your uncertainty—and present a range of views.
4. How Should Policymakers Handle Uncertainty?

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5. Not every problem has a solution.
The Schelling Lecture: U.S. Economic Outlook and Policymaking

Jason Furman
Senior Fellow, PIIE

University of Maryland School of Public Policy
College Park, MD
April 19, 2017