

The Schelling Lecture: U.S. Economic Outlook and Policymaking

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College Park, MD

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Outline

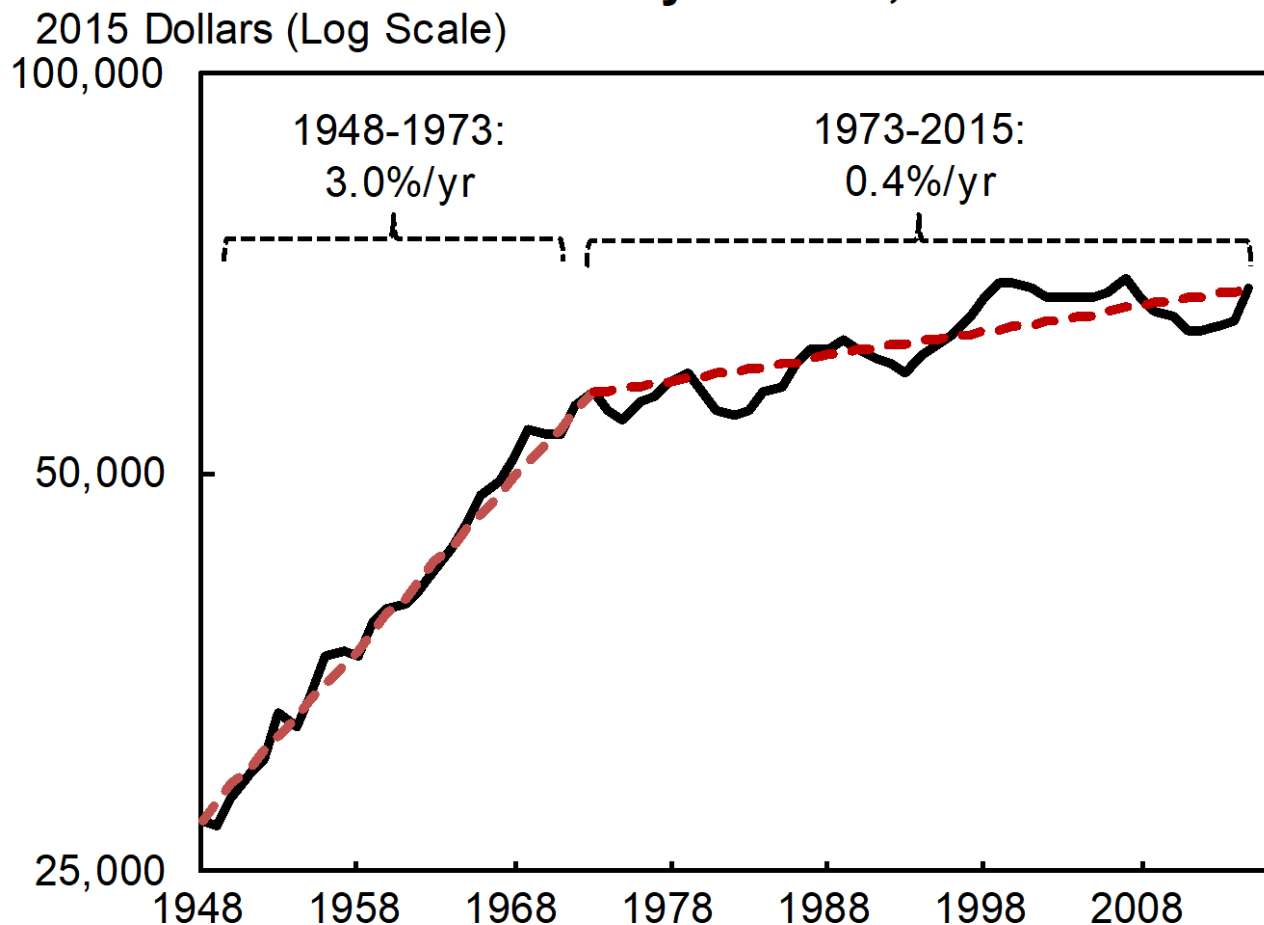


- 1. What is So Exciting About Economic Policy?**
- 2. Do Economists Ever Agree on an Answer?**
- 3. What Can Economists Do When the Answer is Not Known?**
- 4. How Should Policymakers Handle Uncertainty?**



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

Real Median Family Income, 1948-2015



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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Preventing a second Great Depression

Post Office restructuring

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

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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1. Better description of the best policy: maybe a “future fee” instead of a “carbon tax.”

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2. Combine multiple policies to address concerns: E.g., carbon tax together with a rebate, eliminating regulations, and taxing imported carbon.

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Combining Politics and Economics

1. Better description of the best policy: maybe a “future fee” instead of a “carbon tax.”
2. Combine multiple policies to address concerns: E.g., carbon tax together with a rebate, eliminating regulations, and taxing imported carbon.
3. Adopt the n th best alternative—hopefully n is not too high!



Economics Should Be *One Input* Into Decisions

Illustrative Example: Alternative Stimulus Tax Cuts

	Effectiveness (per economists)		
Making Work Pay—Fully Refundable	100		



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Illustrative Example: Alternative Stimulus Tax Cuts

	Effectiveness (per economists)	Likelihood (per strategists)	
Making Work Pay—Fully Refundable	100	5%	
Making Work Pay—Not Refundable	30	100%	
Payroll Tax Cut	80	80%	



Economics Should Be *One Input* Into Decisions

Illustrative Example: Alternative Stimulus Tax Cuts

	Effectiveness (per economists)	Likelihood (per strategists)	Overall Score (per President)
Making Work Pay—Fully Refundable	100	5%	5
Making Work Pay—Not Refundable	30	100%	30
Payroll Tax Cut	80	80%	72



Bipartisan Agreement in Economics

GREG MANKIW'S BLOG

Random Observations for Students of Economics

THURSDAY, MAY 22, 2008

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

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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

Debate Among Economists Is Often Narrower Than the Political Debate



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

Alternative Measures of the Identical Concept: Economic Growth in 2016:Q4

Gross Domestic Product: 2.1%



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Alternative Measures of the Identical Concept: Economic Growth in 2016:Q4

Gross Domestic Product: 2.1%

Gross Domestic Income: 1.0%

BEST GUESS: “Gross Domestic Output”: 1.5%



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 (or maybe 92%/8% so 128,000)



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

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%



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“Soft data”: ISM manufacturing: +2.7 from Dec to Mar

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



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

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

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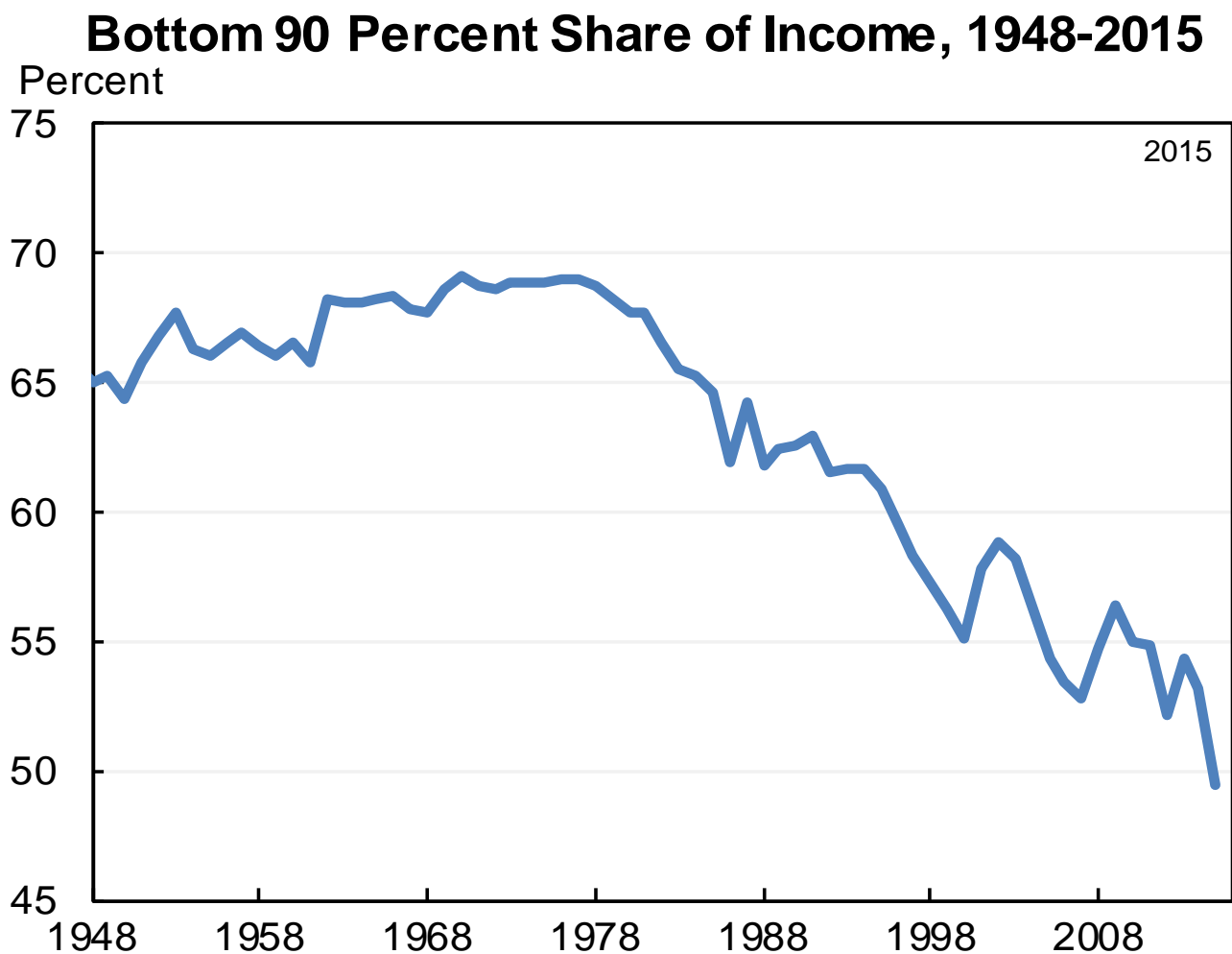
GDP growth in Q1 (Atlanta Fed GDP NOW): 0.5%

“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

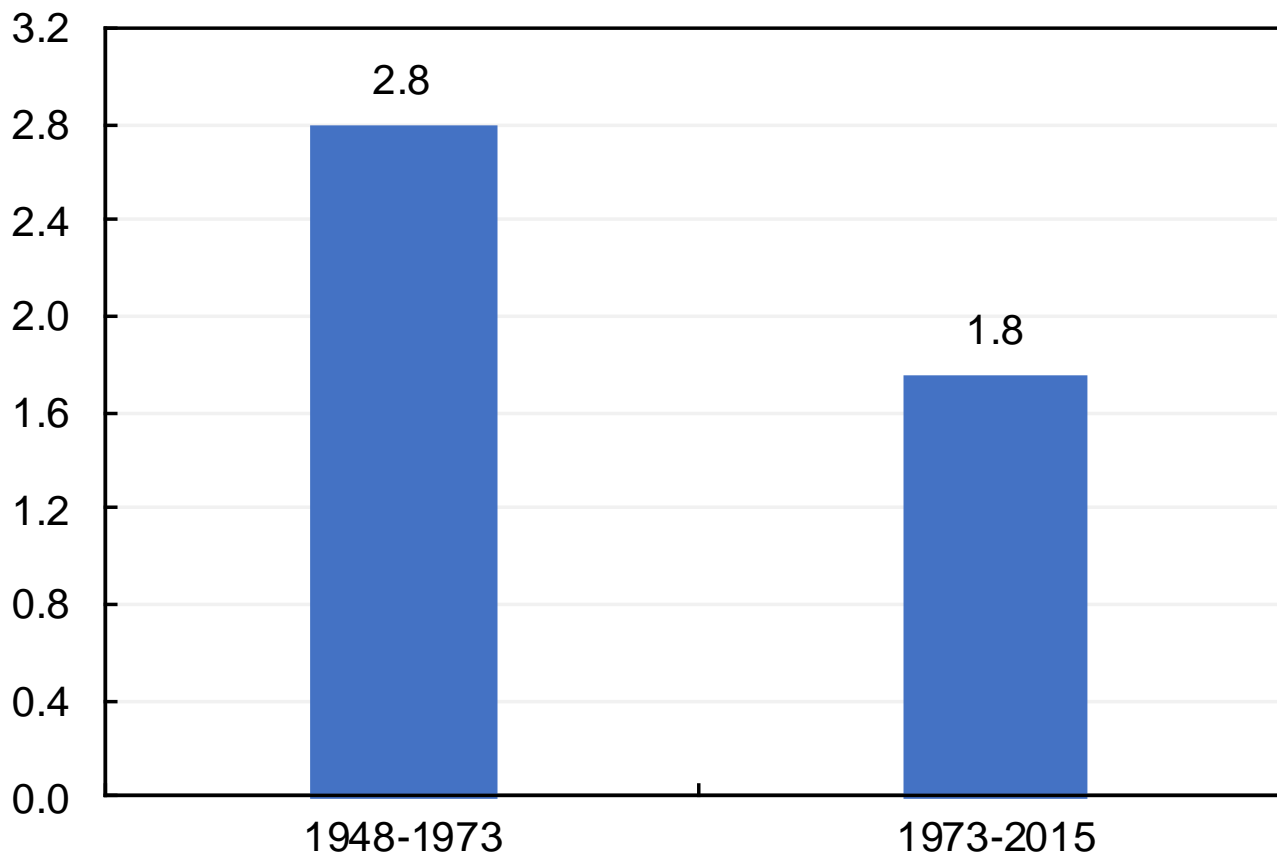


a. Data Description—Sources of Median Income Slowdown (cont.)



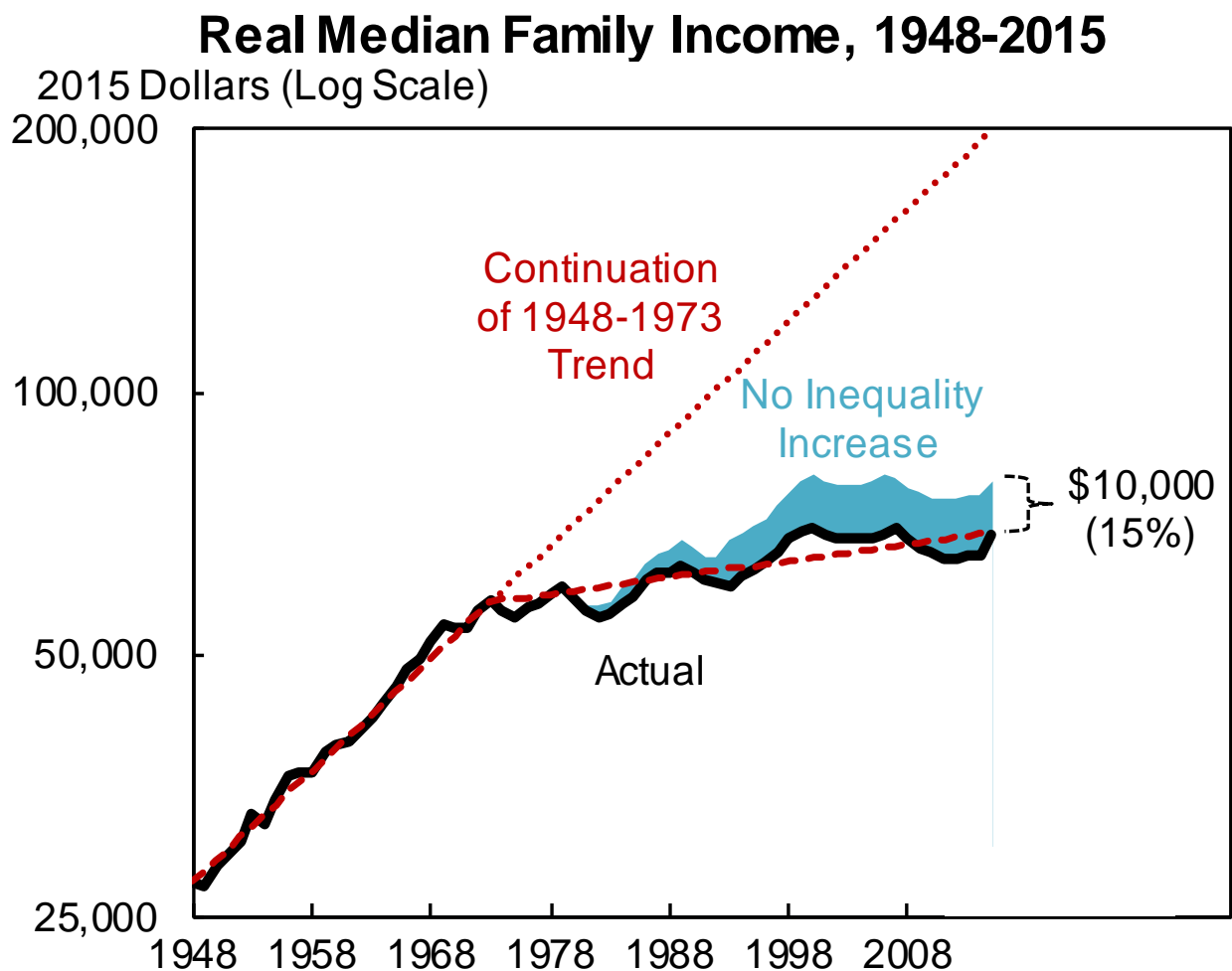
Labor Productivity Growth, Nonfarm Business Sector

Percent Change, Annual Rate



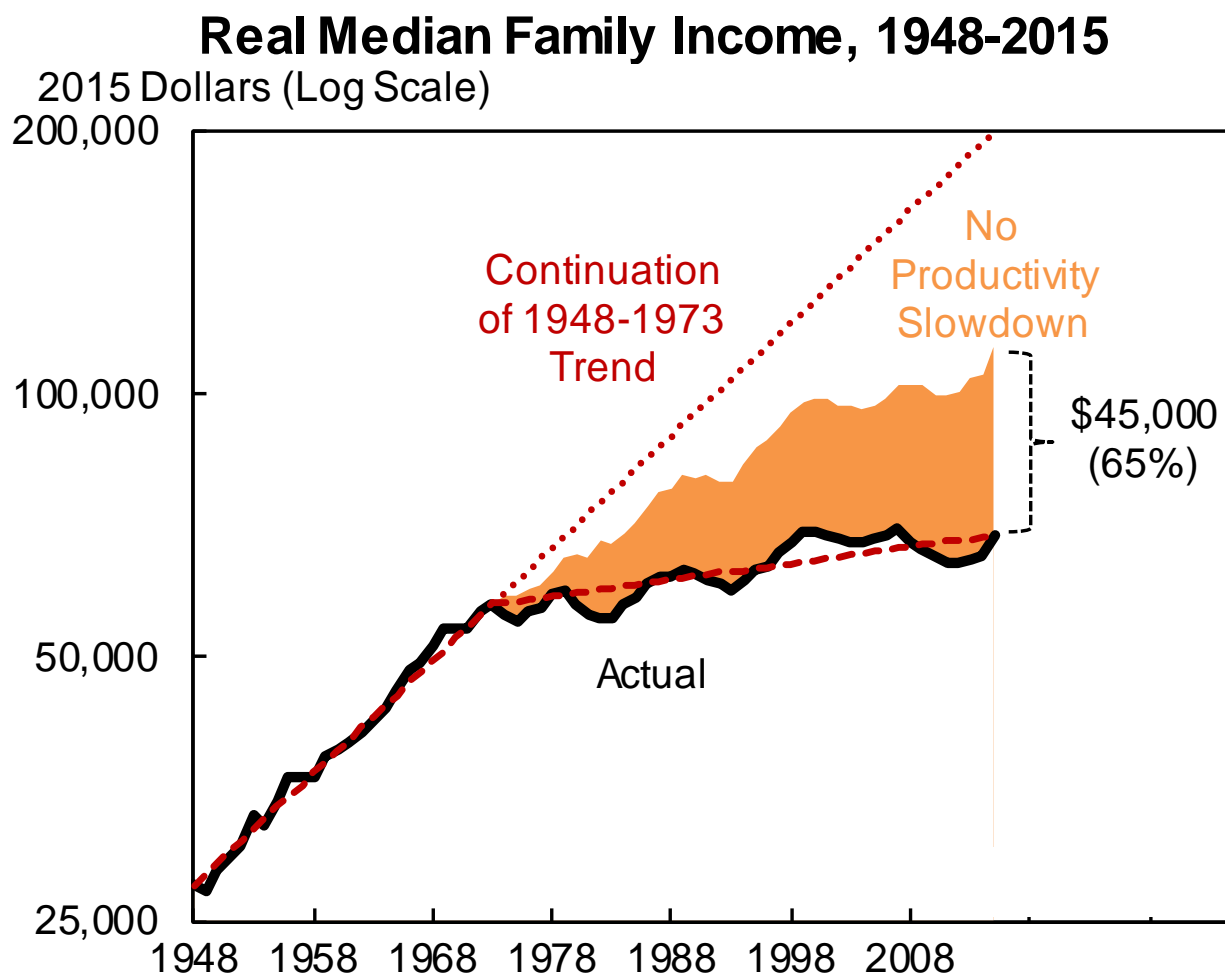


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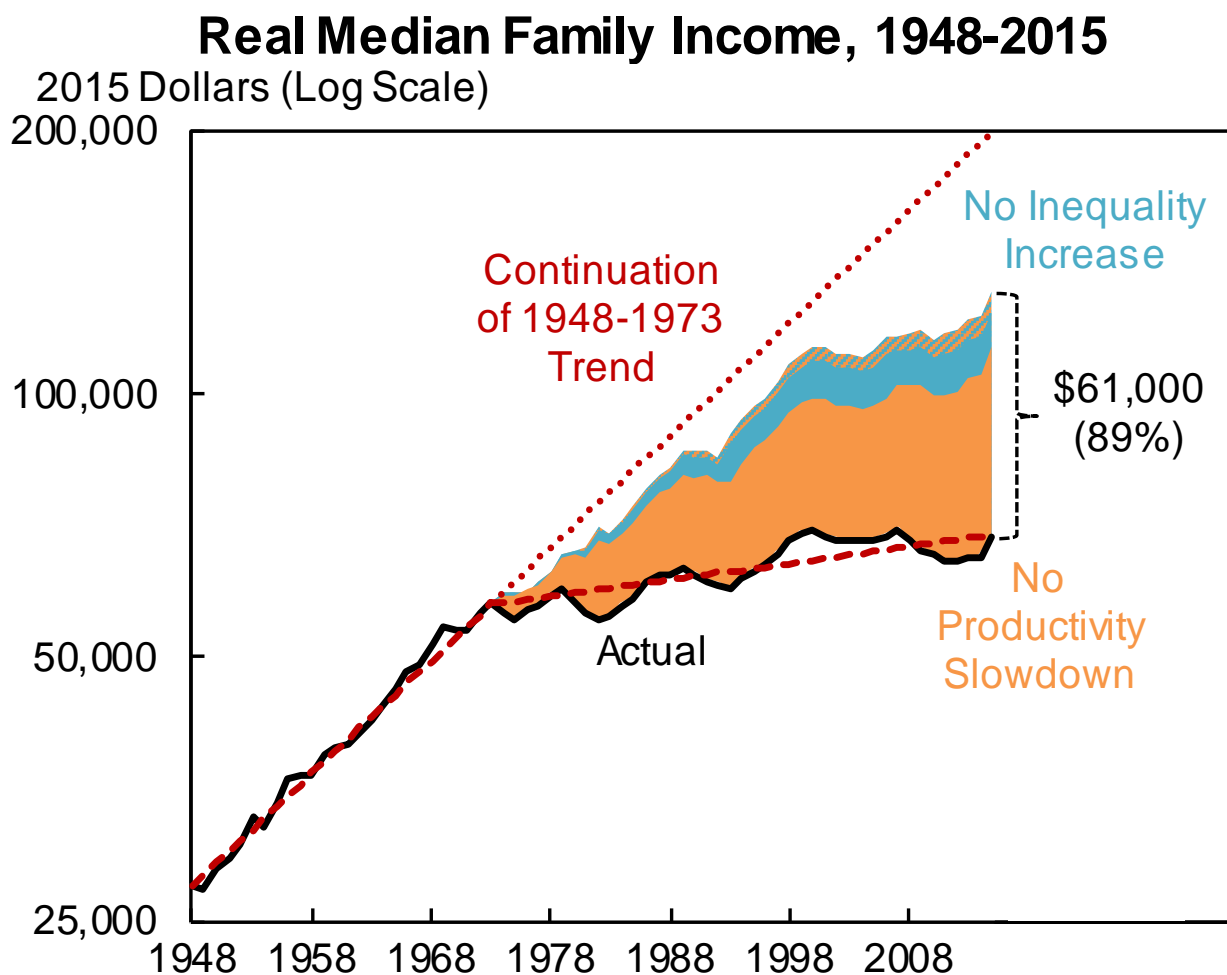


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b. Economic Theory—Example of Gains from Trade from Two-Sided Spectrum Auctions

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

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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.

b. Economic Theory—Departures from Simple Model



Incomplete Information

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

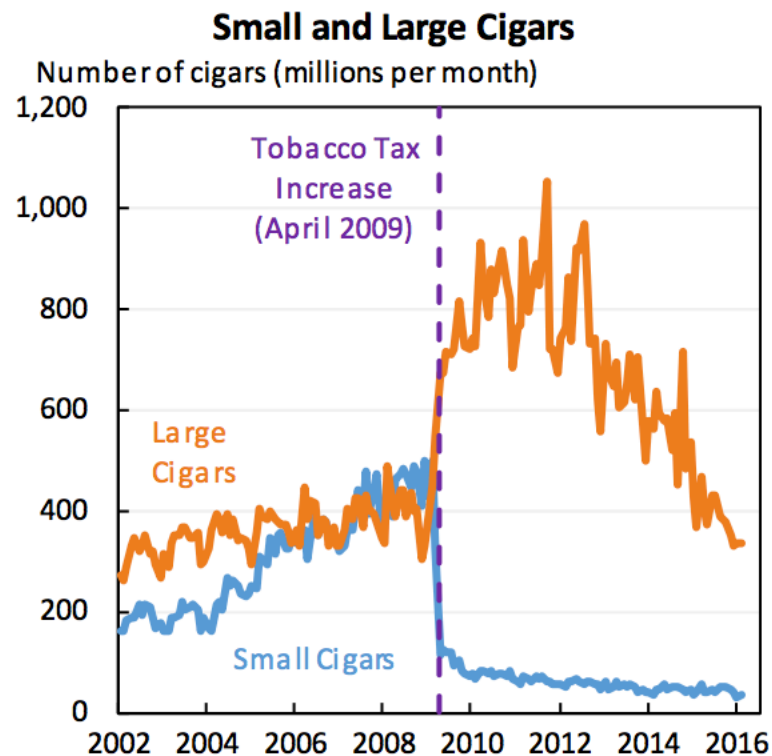
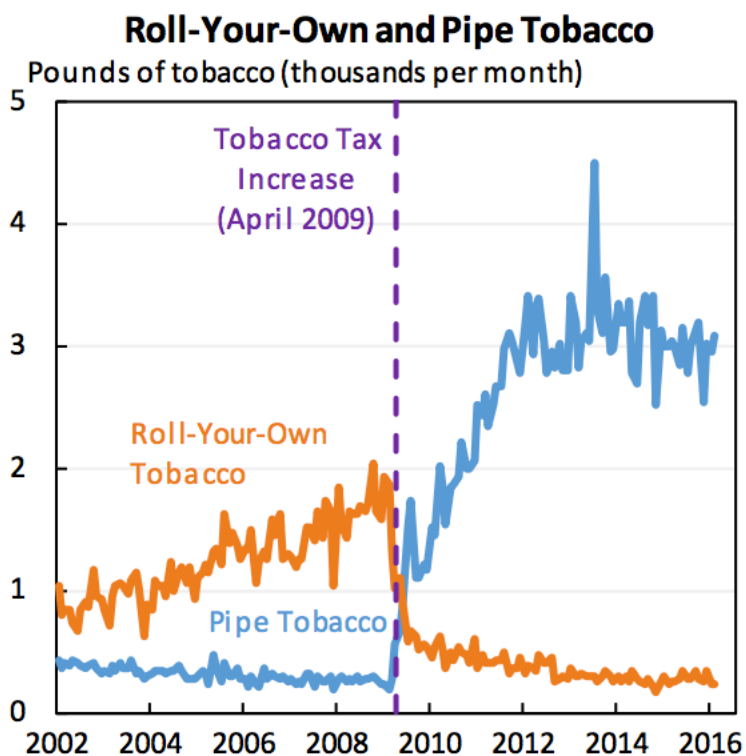
Behavioral Economics

- Encouraging savings with incentives or defaults?
- Auto-enrollment for public programs?



c. Causal Evidence—Example of Taxes on Tobacco Products

Sales of Selected Tobacco Products, 2002-2016





d. Building Models to Simulate Alternatives

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

Income Class	Percent of Families	Static		Dynamic		
		Percent Change in After-Tax Income		Percent Change in Pre-Tax Income	Percent Change in After-Tax Income	Percent Change in Utility (Consumption Equivalent) ¹
		Without Financing	With Financing			
Bottom Quintile	20.0	2.9	-12.3	1.0	-11.4	-22.4
Second Quintile	20.0	2.7	-3.2	0.9	-2.3	-2.9
Middle Quintile	20.0	2.5	-0.9	0.8	-0.1	-0.6
Fourth Quintile	20.0	2.4	0.3	0.8	1.1	0.7
Top Quintile	20.0	2.3	1.4	0.9	2.3	1.8
All	100.0	2.3	0.3	0.9	1.1	-4.7



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5. **Not every problem has a solution.**

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