The Romney Cure for Obama-Induced Economic Ills

By John B. Taylor

When my economics students ask me how Mitt Romney's program will improve the economy, I begin by stressing the basic problems and then address the usual counterpoints.

First is the obvious: The American economy is getting worse, not better. Real personal income fell by 3.8% at an annual rate in August. In the past two months, half a million Americans gave up looking for work, and the percentage of the working-age population with jobs is below, rather than above, what it was when the recovery began in July 2009. Unemployment has been stuck above 8%. Economic growth in the most recently reported second quarter was a minuscule 1.3%.

The Obama administration and its supporters counter with a rosier view, noting that, according to a Bureau of Labor Statistics survey of households, there are 2.3 million more jobs in the past 12 months. That may sound good, but over the same period the working-age population increased by four million. And in the past two months, the survey shows, employment declined.

The second basic problem is that the economic policies pursued by the Obama administration consist mainly of short-term interventions, such as the stimulus packages, cash-for-clunkers, and temporary payments to state governments and individuals. At best, these have produced only small, short-term economic blips.

Here, too, some administration defenders claim that at least the fiscal stimulus packages stopped the economic free fall. This is not what the data show. The American Recovery and Reinvestment Act was enacted in February 2009, but the sharp decline in retail sales, exports and new investment orders ended in December 2008 or January 2009.

Basic economics tells us that such temporary policies do little to restart growth. More lasting reforms are needed. Mr. Romney's economic plan will deliver these reforms. It promotes growth by focusing on five strategic areas: energy, education, trade, debt reduction and job creation.

Economists point to enormous opportunities for sustainable growth in energy. To capitalize on these opportunities, the federal government has to approve the necessary infrastructure—such as the Keystone XL pipeline—and permit states to manage energy development on federal lands within their borders. The Romney plan would provide the needed federal approvals.

The nation's troubled education system is a drag on long-term growth. To improve outcomes, Mr. Romney proposes to allow students in poorly performing schools to use existing federal funds (such as those in Title I, which are targeted to disadvantaged children and high-poverty districts) to attend other public schools including charters, private schools if their state allows it, and online-education programs. Research by economist Eric Hanushek shows that bringing U.S. education back to the top of international rankings would substantially increase GDP and eventually increase average incomes by 20%.

A more aggressive program for negotiating trade agreements to open markets for U.S. goods and reduce costs for American producers and consumers will raise real income. The current administration has not started and brought to completion even one trade agreement. Mr. Romney intends to move ahead on trade agreements and create global enterprise zones to remove barriers to trade.

The federal debt is exploding. With the administration's policy, the Congressional Budget Office projects a debt-to-GDP ratio of 80% in two years, double the amount at the end of 2008.

> Lower tax rates would offer incentives for more investment and hiring, especially by small business owners.

This policy is slowing economic growth by raising the likelihood of large future tax increases or another financial crisis. Mr. Romney puts a high priority on bringing the debt down as a share of GDP. Specifically, his plan is to reduce deficits by gradually bringing down spending as a share of GDP to 20% by 2016, which is where it was before the crisis in 2007. This reduction in federal spending is what any responsible family or business would do if they were borrowing at an unsustainable pace.

Mr. Romney's tax reforms are designed to foster more investment and jobs. For example, his proposal to lower marginal income-tax rates across the board by 20% will provide incentives for small businesses to expand and increase their hiring. Cutting the corporate-tax rate from to 25% from 35% and insisting on a cost-benefit approach to regulation—both part of the Romney plan—will enable American firms to be more competitive in the global market.

In response, former President Bill Clinton said at the Democratic National Convention that Mr. Romney would return to "the same old policies that got us in trouble in the first place." No, the Romney plan rejects such policies, including perpetual support of poorly regulated housing-finance agencies, such as Fannie Mae and Freddie Mac, which got us into the mess. Mr. Romney also argues against the easy-money policy by the Federal Reserve that helped lead to the crisis.

Critics complain that Mr. Romney's tax proposals favor the rich. Actually, he wants to eliminate or limit deductions from special provisions in the tax code for high-income Americans in exchange for lower marginal tax rates. We have not had a major tax reform since 1986, and the tax code has become notoriously cumbersome and a drag on growth.

His plan does not, as Mr. Clinton claimed at the convention, "get rid of those pesky financial regulations designed to prevent another crash and prohibit future bailouts." Rather, the plan bolsters capital requirements, repeals debilitating regulations in Dodd-Frank that had nothing to do with the crisis, and follows the rule of law, including the bankruptcy code, without giving favors to special interests. It thereby avoids both crises and bailouts—and puts the country on a sound path toward sustainable prosperity.

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