The Daily Dish

Stimulus versus Structural Reform

DOUGLAS HOLTZ-EAKIN, PATRICK HEFFLINGER | AUGUST 22, 2016

The Food and Drug Administration (FDA) announced that it will delay its new salt guidelines and will extend the public comment period to October 17th. The new guidelines aim to reduce Americans' daily salt consumption to 3,000 milligrams a day. The guidelines are the first step toward a ten-year plan to reduce salt consumption to 2,300 milligrams a day and will encourage restaurants and food manufacturers to use less salt.

The Federal Emergency Management Agency (FEMA) has halted $30 million in grant payments to the state of Mississippi that were aimed to help the state rebuild post Hurricane Katrina. The agency said the payments have been halted after it was discovered the state has not been properly documenting where the money has been going. According to FEMA, the state of Mississippi has claimed to have spent $31.5 million of the grant money, yet only $957, 776 has been documented, leaving $30.5 million unaccounted for. FEMA said additional grant payments will be halted until the state of Mississippi is able to account for the missing money. According to The Hill, Mississippi has repaired 945 homes damaged by Hurricane Katrina using the FEMA grant money.

Eakinomics: Stimulus versus Structural Reform

There is no disagreement that U.S. economic growth is disappointingly slow. There is, however, a disagreement over the foundations of this poor growth and the appropriate policy response.

One leading line of thinking is that we are in an era of "secular stagnation," a concept popularized by former Treasury Secretary (Clinton) and National Economic Council Director (Obama). In his own words, "The key to understanding this situation lies in the concept of secular stagnation, first put forward by the economist Alvin Hansen in the 1930s. The economies of the industrial world, in this view, suffer from an imbalance resulting from an increasing propensity to save and a decreasing propensity to invest. The result is that excessive saving acts as a drag on demand, reducing growth and inflation, and the imbalance between savings and investment pulls down real interest rates." The policy mix dictated by secular stagnation is continued easy money (or at least little and slow normalization) as well as fiscal stimulus — government-centric increases in demand — particularly through infrastructure spending. This line of thinking is clearly reflected in the policy proposals of Hillary Clinton.

The alternative view is that the problem is not inadequate demand, but rather that demand has brought the economy back to its potential growth, and that this potential growth is simply too slow. This line of reasoning is apparently embedded in the recent remarks of Fed Vice Chair Stanley Fischer, who argued that with unemployment below 5 percent and inflation over 1.5 percent "we are close to our targets." He remarked that "The combination of strong job gains and mediocre GDP growth has resulted in exceptionally slow labor productivity growth."

He then focused on productivity growth: "Low-to-middling TFP [total factor productivity] growth might also reflect the downward trend in business dynamism, as evidenced by a notable slowdown in gross job creation and destruction. Diminished dynamism has been linked to a marked slowdown in the reallocation of labor and capital from low-productivity establishments and firms to high-productivity ones, especially in innovative

sectors like high tech. Both phenomena are closely related to the declining trend in new business creation."

The policy mix for fixing the supply side are permanent, structural changes that will improve incentives for saving, investment, innovation and productivity, as well as incentives for labor force growth. The former included tax reform, federal debt control, regulatory reform, and education reform. The latter included a work-friendly safety net and pro-growth immigration reform.

I am more sympathetic to the second view, but there is no question that resolving the debate is central to getting better economic performance in the United States.