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CONGRESSIONAL TESTIMONY

Examining the Rise of American Earnings and Living Standards

Joint Economic Committee of Congress

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Chairman Paulsen, Vice Chairman Lee, Ranking Member Heinrich, and distinguished members of the committee, thank you for the opportunity to submit testimony on the rise of American earnings and living standards.

My name is Stephen Moore and I am the Distinguished Visiting Fellow in the Project for Economic Growth at The Heritage Foundation. The views I express in this testimony are my own, and should not be construed as representing any official position of The Heritage Foundation.

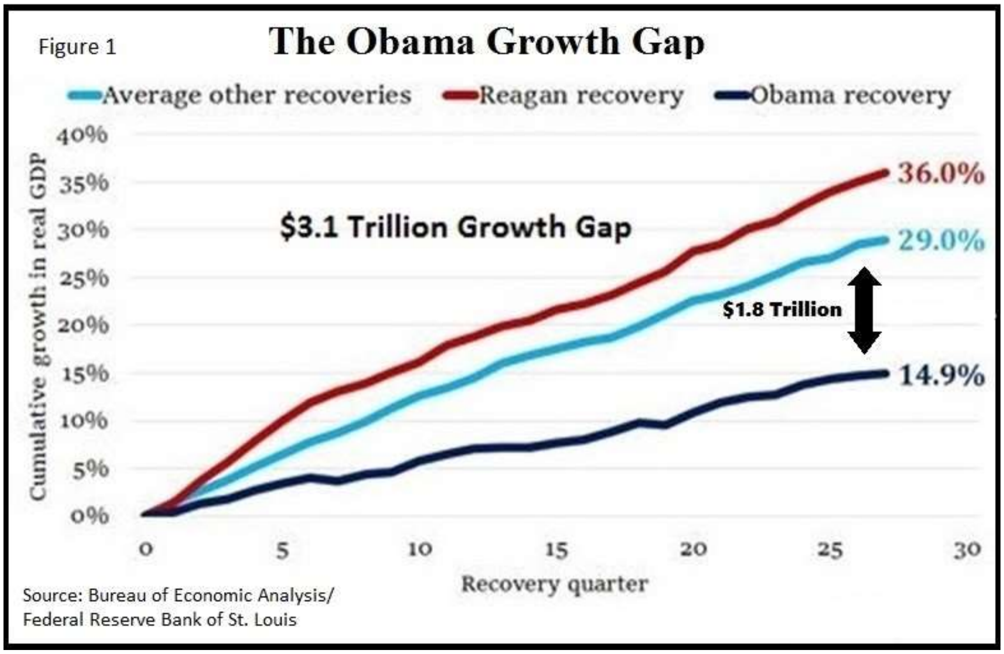
The great economic challenge of our time is how to maintain strong and persistent economic growth with rising living standards for all. Some economists on the left believe that an advanced industrial nation, such as the United States, can only hope to grow at about a maximum of 2 percent per year. This is called the "new normal," or what former Obama chief economist calls "secular stagnation."

As a senior economic advisor to Donald Trump during the presidential campaign, I can assure you that we flatly rejected this view - and no one more than Donald Trump himself.

One of the central tenets of Trumponomics is that there is no "limit to growth," and that nearly all of our socio-economic problems - from the budget deficit, to stagnant wages, to poverty alleviation, to funding Social Security and Medicare, to improving our schools and infrastructure - are more easy to solve when the economy grows at a faster pace. So fast growth is one of the primary goals of Trump's administration.

One reason that economists became convinced that faster growth was not achievable was that it hadn't happened for a decade. The defective thinking, as we saw it, wasn't that persistent growth of 3 to 4 percent was impossible, it was that the wrong-headed policies under Bush and then Obama after the financial crisis hit, inhibited growth and led to stagnation of middle incomes.

In particular, the Keynesian experiment of massive deficit spending, stimulus plans, minimum wage increases, Obamacare, more generous welfare benefits, and Fed policies of very low interest rates and $3 trillion of asset purchases, yielded the worst economic recovery from a recession since the Great Depression. **Figure 1** shows the widening cost of this "growth deficit" over time. GDP fell $2 trillion below the trend of an average recovery and $3 trillion below the trend of the Reagan recovery. This Committee issued a report in 2014 which found that per capita income would have been roughly $3,200 higher if the recovery had only been average. This was a significant blow to the living standards of middle and low income families.

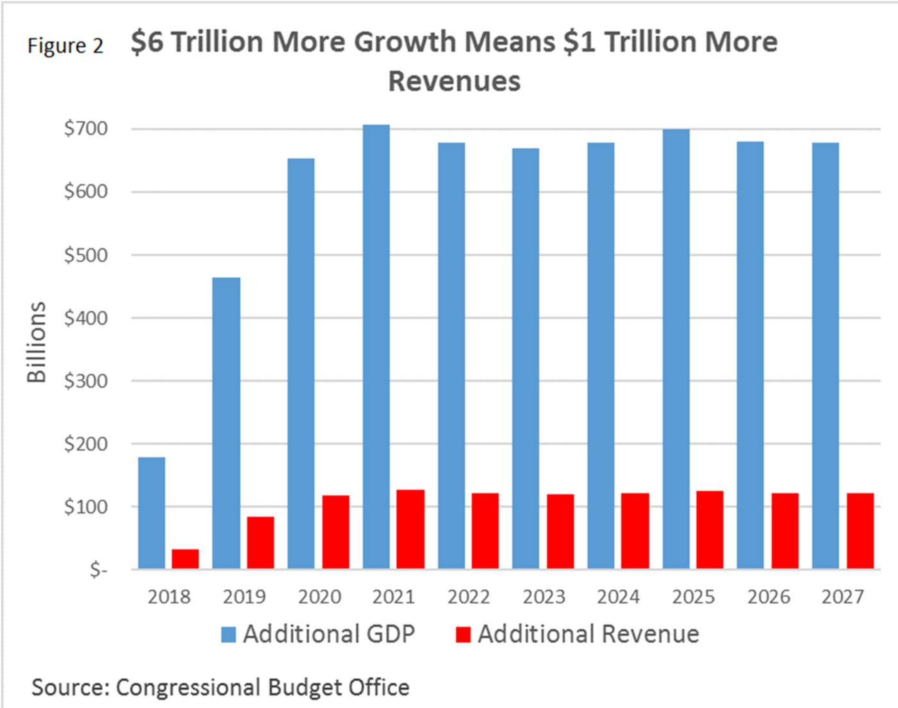


It is noteworthy that the biggest declines in family incomes in the Obama years (2009-15) was experienced by black households, Hispanics, and single women. It is also noteworthy that the standard liberal measure of income inequality - the Gini Coefficient - indicated a growing divide between rich and poor under the Obama presidency. The income redistribution policies not only failed to generate growth, they hurt minorities and the poor the most.

To his credit, Obama gave us a long and resilient recovery. What has happened over the last eighteen months is that this slow recovery that was running out of gas at the end of Obama's presidency in 2016, has now surged into an all-out economic boom.

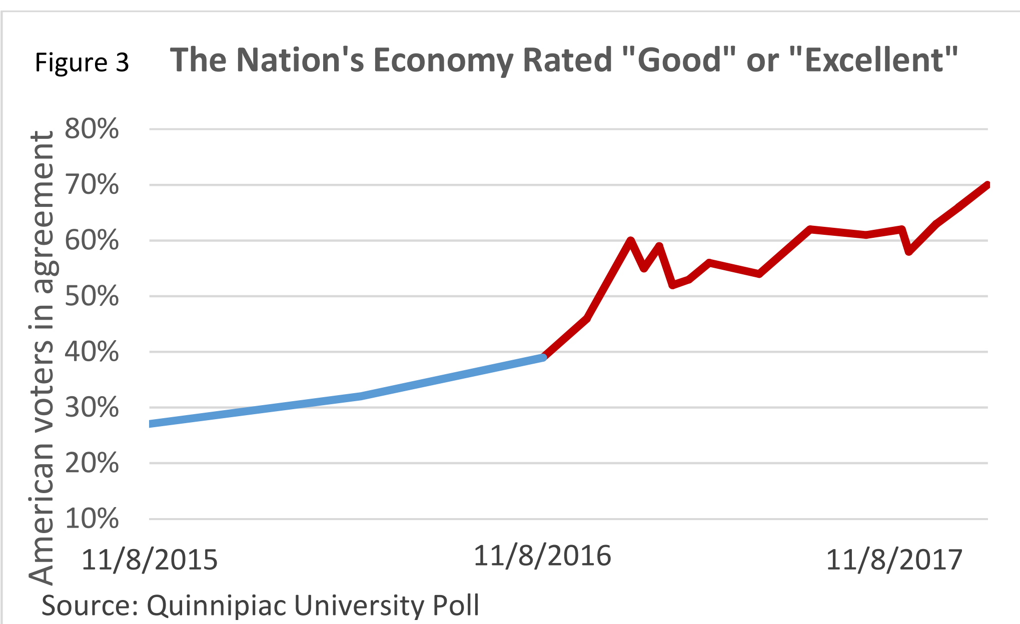
As one of the senior economic advisers to the Trump campaign, and with Larry Kudlow, one of the architects of the Trump tax plan, I can tell you that the growth revival has been larger than we expected in the wake of the tax cuts, deregulation, and energy production policies. Trump inherited an economy growing at 1.6 percent and now for the last five quarters we have 3 percent growth and for the past two quarters (Q2 and latest estimate for Q3) we have achieved over 4 percent growth. Again, this was something that many of the Obama economists believed was an impossibility.

Since the tax cut's passage in December 2017, as shown in **Figure 2**, the total increase in economic output, according to the Congressional Budget Office is $6.1 trillion higher over the 2018-27 ten year window. This will generate roughly $1.1 trillion more federal revenue and nearly $500 billion more windfall revenues for states and cities. The tax cut is getting pretty close to paying for itself already, if the CBO is correct.



It is worth noting that, by contrast, over the eight year Obama period, economic growth was *over*-estimated to the tune of roughly $2 trillion.

One remarkable indicator of how the American people have been impacted by the Trump policies is to examine how voters view the economy. Throughout the Obama years, at most about three of ten Americans rated the US economy as good or great. Today that number has rocketed to 7 of 10. See **Figure 3**. Americans can feel the improvement in their financial situation. Black and Hispanic unemployment rates have hit all-time lows.



How has this Trump boom affected the incomes of middle and lower income Americans? These numbers are harder to measure - in part because of the lag measurements from the Census Bureau - but we do know that in 2017 median real family income rose to above $60,000. A study by Sentier Research using the preliminary 2018 data indicates continued rises in median family income through the first half of the year.

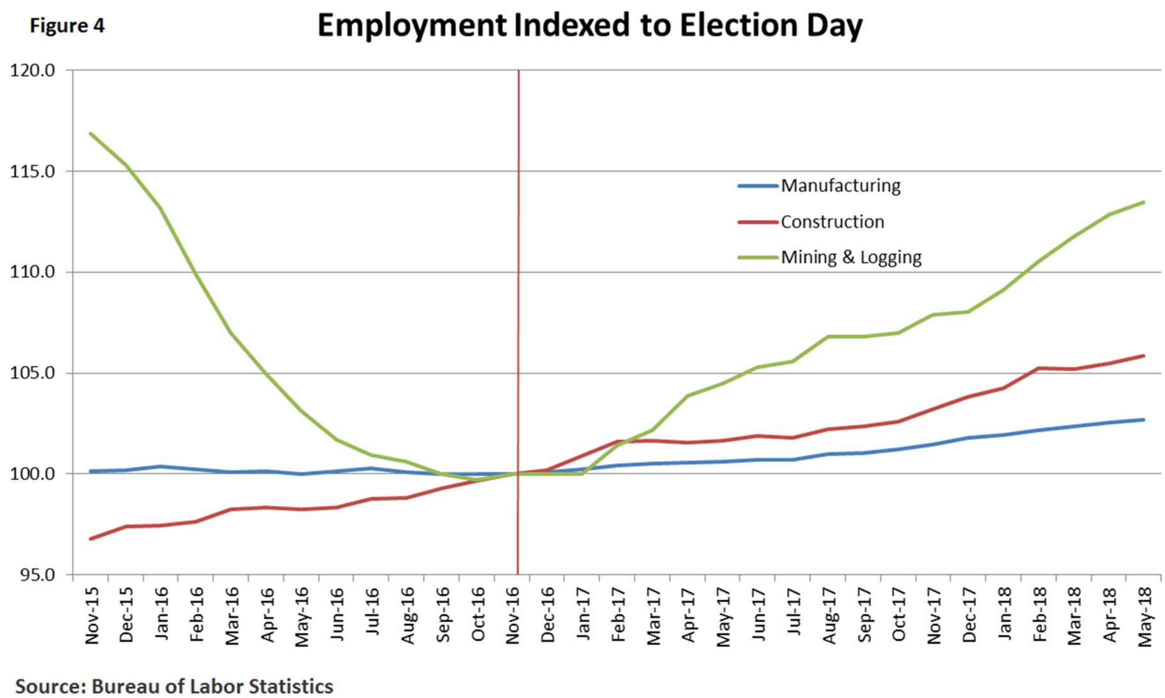
When counting bonuses, increased hours worked and overtime (due to the tight labor market), and increased fringe benefits, after-tax take home pay is rising for the middle class. The preliminary indications are that this 2017-18 rising tide really is lifting all boats. We also see this in very healthy consumer spending numbers. Americans are earning more, so they are clearly spending more.

The latest Bureau of Labor Statistics data show 6.5 million unfilled jobs and a shortage of workers to fill them. This is the very definition of a "tight labor market" and will likely lead to higher wages to come and bonuses to workers.

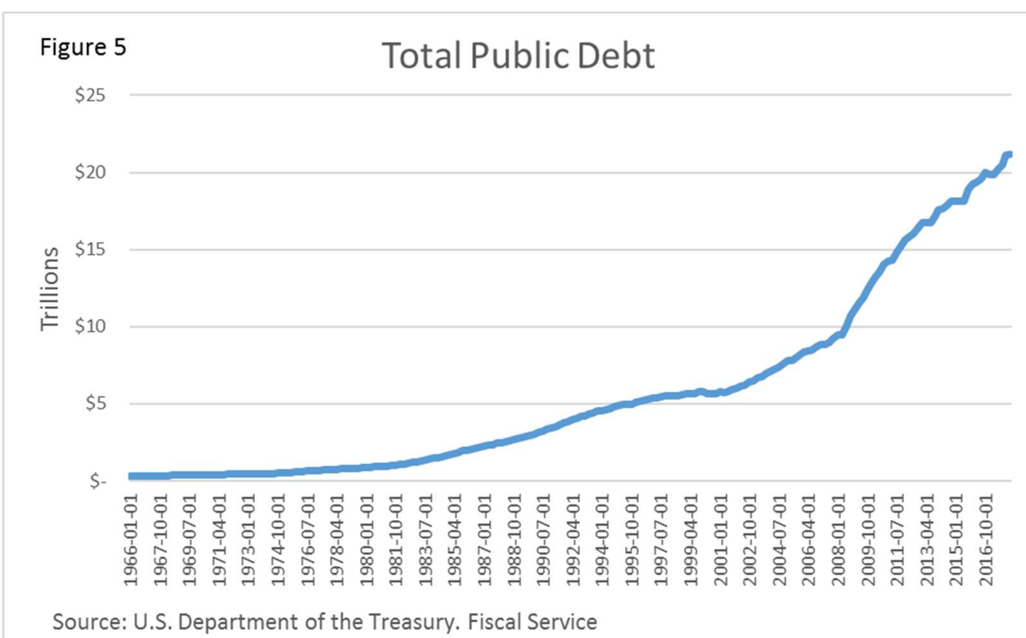
In some parts of the country, employers are now paying signing bonuses of up to $25,000 for welders, pipefitters, engineers and truck drivers. "We've probably never had a situation like we have today, where the demand [for workers] is strong and capacity is constrained," notes Bob Costello, chief economist of the American Trucking Associations (ATA).

Americans are also wealthier. The increase in the stock market under Obama since 2009 continues to rocket forward under Trump. Since the Trump election the value of all US stock holdings has risen by an estimated $8 trillion. Yes, this benefits the wealthy, but more than half of Americans own stock through their retirement plans, IRAs, and 401k plans. Most union pension plans and most state and local pension plans are also invested in the U.S. stock market.

Americans in the bottom 50 percent of income have also benefited from the surge in job openings. Since the end of 2016 through September of 2018, the American economy has created nearly one million blue-collar construction, manufacturing and mining jobs. See **Figure 4**. These are the desirable working class jobs that had been dwindling in the previous decade and that many economists thought would never come back to these shores. They are back. America is now in one of the greatest capital construction booms from coast to coast in American history. America is "making things" again.



So what is the lesson for this Committee and all Congress from the failure of Obamanomics and the early success of the Trump policies? Once again, we have learned the hard way the lesson that standard demand-side/Keynesian stimulus plans do not work. In the wake of the recession we spent hundreds of billions of dollars on unemployment insurance expansions, food stamps, Obamacare, solar energy subsidies, transit grants, tax credits, housing bail outs, and so on, but even according to the Obama administration's own numbers, unemployment was higher than if we had not spent the money at all. The only lasting effect has been the doubling of the national debt. See **Figure 5**

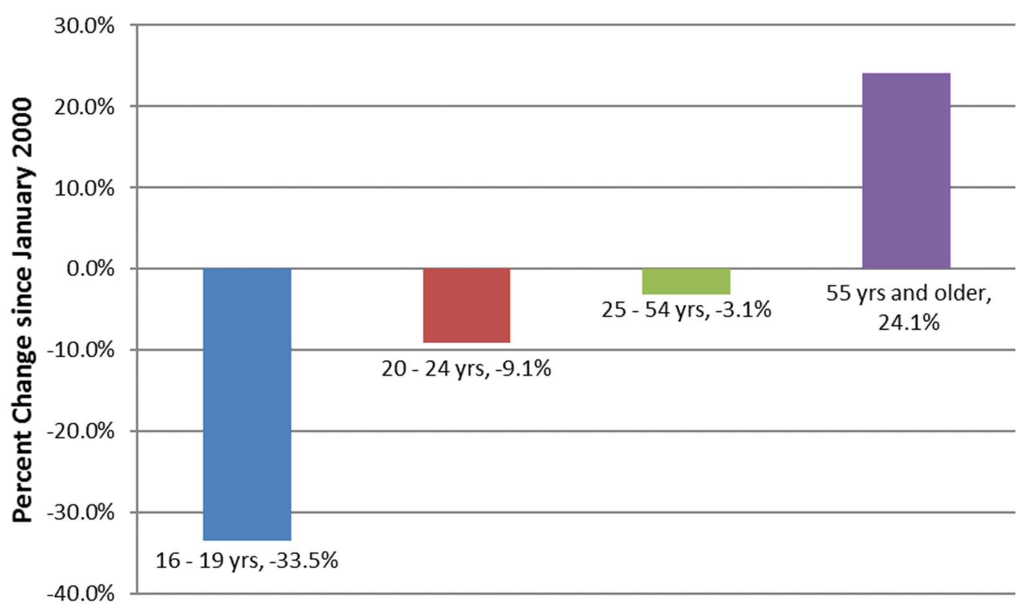


Trump borrowed from the Reagan supply-side formula of incentivizing business investment, startups, capital importation, work, and risk-taking through tax cuts and deregulation. We will have future economic downturns and stagnation, and hopefully Congress will have learned what works and what doesn't. As Milton Friedman taught us, when the government spends a dollar it has to come from the private market place and the cost to the economy of raising that dollar in most cases exceeds the benefit of the government spending.

Finally, I would like to address the issue of what can Congress do now to keep this expansion going strong with a special emphasis on incentivizing higher income gains for the middle class and poor.

As for the economic boom, to keep it going we will need more Americans working. The labor force participation rate for those 16+ dropped from 65.8 percent at the start of the Obama presidency to just 62.9 percent at the end of the Obama presidency and is now just creeping up again. **Figure 6** below shows that the biggest challenge is getting young people into the work force.

Figure 6 **Changes in Labor Force Participation since January 2000**



Source: Bureau of Labor Statistics

Older people are working more, and young people are working less. What is wrong with this picture? We need to get the younger than 25 Americans working full or at least part time.

A related point: the Fed has to stop believing that faster growth and higher wages are inflationary. When output rises, prices fall. As I look at the best measure of inflation, commodity prices, I don't see worrisome signs of inflation. Let's not let the Fed take away the punch bowl from this party just as it is starting to benefit the middle class.

So how do we make an overall great labor market picture even brighter? Here are six reforms that would help workers and grow the economy faster:

1) Reinstate the work for welfare requirements of 1996 that helped pull Americans out of welfare dependency and into the workforce. These helped reduce welfare caseloads in the late 1990s by half and those who moved into work. A seminal study by welfare expert Ron Haskins of the Brookings Institute, tracked down these welfare recipients who were moved in to work and found that most moved up the economic ladder. Welfare reform was one of the great bipartisan successes of the last 50 years, and now that we have a surplus of jobs, this is a very good time to require able-bodied Americans to work for benefits.

2) Lower the federal minimum wage for teenagers. This will encourage young workers to get job experience. One of the best predictors of future wages is the age at which people start working. Those who learn work skills early do better in life.

3) Encourage apprenticeship programs that would give young Americans a "college degree equivalent" for successfully learning a useful trade. This is something Presidents Obama and Trump agree on.

4) Make the Trump tax cuts permanent, especially the immediate expensing provisions that encourage business capital spending.

5) Allow employers to "opt out" of Obamacare mandates and requirements if they provide lower-cost health insurance coverage to their workers. Obamacare has corresponded to about a $3,000 rise in health insurance premium costs with more escalations expected in 2019 and 2020. These higher insurance costs to employers are crowding out pay raises for workers and thus reducing work incentives.

6) To help the lowest-income families, allow federally funded programs for children in the 20 percent worst performing school districts, so that poor parents can send their kids to public, private, or religious schools that work. These programs in cities like Washington, D.C. have increased test scores and parental satisfaction. More than 90 percent of the children's families helped are black or Hispanic. A mind really is a terrible thing to waste.

If we combine these policy changes with the course corrections that Donald Trump has already made, I believe that two to three more years of 3 to 4 percent growth is highly realistic.

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