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Pawlenty bets big on Reaganomics, but some economists say it won't work

By Derek Wallbank | Published Wed, Jun 8 2011 8:13 am

Tim Pawlenty

WASHINGTON — On a symbolic stage in Chicago, Tim Pawlenty doubled down on trickle-down Reaganomics, pitching a plan to dramatically overhaul the nation's spending with sweeping tax cuts and a fundamental re-think of how the federal government operates.

But for Pawlenty's very optimistic plan to work, experts say he'll have to engineer the greatest expansion of the U.S. economy in modern memory (by far). And many of his ideas, while they may sound good individually, coalesce into an economic plan that one economist said would put the country in "exactly the wrong direction."

The University of Chicago is known as a hub of free-market economic theory, and Pawlenty on Tuesday began by noting how appropriate that, for that reason, his speech was appropriate to be delivered there.

And it was there that Pawlenty offered up his own economic prescription. "We can fix our economy," he said. "Our people are ready to get back to work. We just need to give them to tools to get there. And get the government out of the way."

Unsaid, but understood by all, is the symbolism Pawlenty's location has to the Obama administration he hopes to evict.

The university sits in Hyde Park, a south side Chicago neighborhood that's also home to one Barack Obama. The first lady, Michelle Obama, had been a top leader at the school's medical center, and Obama's top economic adviser, Austan Goolsbee, came from that university (and, the day before Pawlenty spoke there, announced he'd be leaving to resume teaching there).

And while Pawlenty offered up a stinging rebuke of Obamanomics, experts say the numbers in his own plan don't really work.

"There are some good elements, but the basic thrust of Pawlenty's argument is exactly in wrong direction," said Charles Ballard, a political economist at Michigan State University. Pawlenty's plan, he said, would increase income gaps between the very top earners and everyone else.

"Basically, Pawlenty's policy proposal is trickle-down economics on steroids. In terms of generating increased inequality of income and wealth, it is an excellent set of policies. But it has rather little to offer for the bottom 90 percent of households."

Steve Smith, a Minnesotan who directs the Weidenbam Center on the

Economy, Government and Public Policy at Washington University in St. Louis, said Pawlenty's "substantive problem is the basic formula: lower taxes equals faster economic growth."

"The high growth periods that Pawlenty cites were periods in which marginal tax rates (and tax receipts as a percent of GDP) were higher than they are now. This formula works for Republicans, who, by and large, want taxes and spending cut in a way that leads to a balanced budget."

Simplified tax code with huge tax cuts
Pawlenty's tax plan starts with giant cuts, particularly for businesses and those in what's known as the investor class. Here's the blueprint:

- Corporate tax rates shrink to 15 percent, from 35 percent now.
- That cut will be offset somewhat by what Pawlenty says will be cuts to subsidies, like the ones on ethanol he's called for doing away with. "The tax code is littered with special interest handouts, carve-outs, subsidies and loopholes," he said. Exactly how deep he's going here is unknown (and I've asked, many times), so it's hard to estimate how much he'd get out of this.
- Individual tax rates shrink down to two: The first $50,000 ($100,000 for married couples) in income would be taxed at 10 percent. And income above that would be taxed at 25 percent — and companies that currently fall under individual income-tax guidelines could opt out and choose the lower corporate tax rate of 15 percent.
- Pawlenty does away with a host of taxes that benefit high-income earners and investors: Capital gains, dividend, estate and interest income taxes all go to zero.

"Once we unleash the creative energy of America's businesses, families and individuals, as we did in the eighties and nineties, a booming job market will reduce demand for government assistance," Pawlenty explained. "And rising incomes will increase federal revenues."

It's the classical cut-taxes-raise-revenues defense, but it's one that hasn't worked recently, as Slate's Dave Weigel pointed out. "Our experience since 1982 is that income tax cuts don't actually increase revenue. See: the decade between 2000 and 2009, which Pawlenty does not mention here."

Ballard doesn't follow Pawlenty's logic either. "I don't see a revenue estimate for Pawlenty's tax proposals, but my guess is that they would substantially reduce tax revenue, even below today's level, which is lower than it has been in the U.S. for decades, and far lower than in most other developed countries," he said.

"If we have even less tax revenue, and if we want to reduce deficits, we have to cut spending, dramatically. Pawlenty talks about cutting Amtrak and the Government Printing Office, but these are chump change. The big money is in Medicare, Medicaid, Social Security, national defense, and interest on the national debt."

Pawlenty's cuts to discretionary spending would be big. He looks for a freeze until there's a balanced budget, and wants additional presidential prerogative to demand across-the-board cuts if needed. There would be efficiency redesigns of federal agencies — think Six Sigma, which

Pawlenty cited specifically — that he estimated could save up to 20 percent of costs.

He calls for wholesale cuts to or privatization of any service that he feels could be duplicated by the private sector, citing the U.S. Postal Service, Amtrak and Fannie Mae/Freddie Mac (which underwrite much of the U.S. mortgage market) as examples.

But Medicare, as a word, didn't feature in Pawlenty's speech at all, though he's expected to roll out a plan for that in the weeks to months ahead. On Medicaid, Pawlenty said he'd support capping that spending and block-granting it to states, while he's called for means-testing Social Security cost-of-living increases and raising the retirement age for younger workers who haven't hit that benefit yet.

Pawlenty, to the great ire of the folks at the Cato institute who otherwise have praised him extensively, won't touch the Defense baseline spending at all.

Is this explosive growth realistic?

So where does Pawlenty achieve big savings? Sustained, explosive growth, to the tune of 5 percent a year.

"Five percent economic growth over 10 years would generate $3.8 trillion in new tax revenues," Pawlenty estimated. "With that, we would reduce projected deficits by 40 percent, all before we made a single budget cut."

Aiding that, he said, would be a streamlining or rollback of many federal regulations, doubling U.S. exports through additional free trade agreements and strengthening the dollar (the latter two policies are somewhat antagonistic, but not insurmountably so).

But the big fish here is regulatory reform. "The fact is, federal regulations will cost our economy $1.75 trillion this year alone," Pawlenty said. "It's a hidden tax on every American consumer, built into the price of every good and service in the economy."

Taking all that into consideration, tax cuts, spending cuts, reforms, all of it, Pawlenty projects 5 percent growth sustained over 10 years. And that, he says, will bring in a whopping $3.8 trillion in revenue.

Again, we haven't seen the specific projection breakdowns so I can't say if that growth equals that take-in (and at what estimation, given his overhauls).

But I can say with certitude that his asked-for amount of growth is staggering. To give a perspective on the sheer bigness of it, the last time the economy topped 5 percent year over year was 1984. And as for sustained growth of that level over 10 years? Pawlenty says it's been done before, but there's actually not an analogous time in recent memory.

The Washington Post's Ezra Klein was unyielding in his criticism: "This plan isn't optimistic. It isn't a bit vague. It's a joke. And I don't know which is worse: The thought that Pawlenty knows that and went forward with this pandering, fantasy-based proposal anyway, or the thought that he doesn't know it, and he really thinks this could work."

If Pawlenty's growth goal were lowered a little bit, however, then it's not so pie-in-the-sky.

"I think it would be more reasonable to set the bar a little lower, at four percent," Ballard said. "We have achieved 4 percent growth in 20 of the last 50 years." That's most of the Kennedy and Johnson administrations, a minority of the Nixon, Ford and Carter years, half of Reagan's time and a slim majority of the Clinton years.

'Reaganesque' say Republicans; 'Disaster' say Democrats
Political reaction predictably came down in two camps: Republicans seemed pleased with Pawlenty's approach, while Democrats scolded him for what they branded irresponsibility.

"I think it's great, I think he's right on the right track," said Art Laffler, a former economic adviser to Ronald Reagan, in an interview with Fox News' Neil Cavuto. "This type of growth agenda is exactly what's needed, and I think Tim Pawlenty's exactly on track with this proposal."

Larry Kudlow, a CNBC host who was also a Reagan economic adviser, loved it, tweeting that it was a "dynamite Reaganesque speech" by Pawlenty. His final assessment: "Wow."

Democrats used their rebuttals to tie Pawlenty to two Republicans: Paul Ryan and George W. Bush.

"It's basically kissing cousins with Paul Ryan's plan," said Bill Burton in an interview with MSNBC. Burton, a U alumnus who is co-founder of the liberal super PAC Priorities USA and former White House deputy press secretary in the Obama administration, did not mean that as a compliment.

"Tim Pawlenty's plan to extend and expand the Bush tax cuts, deeply slashing taxes paid by the wealthiest Americans and corporate America and sending our deficit soaring even higher, is not an economic plan, it's a prescription for economic disaster that would fall squarely on the backs of seniors and working families," said Debbie Wasserman Schultz, chair of the Democratic National Committee.

"Mr. Pawlenty would take the Republican policies of the last decade, which exploded our deficit and debt and nearly sank our economy into a second Great Depression, and inject them with steroids."

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