Why the US can't afford a Green New Deal

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As the list of Democratic presidential candidates grows, so do their promises. So far, the candidates have largely embraced the same policy focus: expanded entitlement spending to guarantee new welfare benefits.

Massachusetts Sen. Elizabeth Warren recently endorsed a universal federal provision of child care. Vermont Sen. Bernie Sanders has long supported "Medicare for All," and businessman Andrew Yang is perhaps best-known for his advocacy of a universal basic income. Meanwhile senators Cory Booker, Kamala Harris, Kirsten Gillibrand and others have all backed the Green New Deal, which promises to address climate change and inequality by providing universal health care and creating millions of jobs.

While reasonable people can disagree on some aspects of these proposals, one fact is uncontroversial: the United States cannot afford them.

Congressional Budget Office projections of the federal debt make this point compellingly. According to CBO projections, federal debt held by the public, currently at 78% of America's gross domestic product, or GDP, will approach 100% in the next decade and reach 152% by 2048. Cutting the debt-GDP ratio to its 1957-2007 average within 25 years would require policymakers to permanently reduce spending or increase taxes by 3.8% of GDP, which amounts to about $800 billion, or24% of federal revenue.

Distinguished economists have recently argued that debt may be less costly in the future because of low interest rates. This assumes we can forecast future rates. In reality, estimates of long-run interest rates differ widely and are highly uncertain. Rates have stayed low over the last decade due to a combination of factors, such as monetary policy, weak foreign demand and deleveraging in the wake of the 2008 recession. These forces are unlikely to play as important a role in the future.

More importantly, while low interest rates might permit running a long-term deficit that is stable relative to GDP, standard forecasts, such as those from CBO, project rising deficits.

Some Democrats have also claimed that federal debt is not a constraint by relying on "Modern Monetary Theory" (MMT), which argues that central banks can issue enough money to fund federal expenditures with little threat of inflation. But the stable inflation of recent years is precisely due to central banks' intentional pursuit of price stability as the primary objective of monetary policy. If monetary policy were to focus on funding government spending instead, the threat of inflation would increase rapidly.

Several Democrats have also advocated increasing taxes, but the revenue generated would not come close to funding their proposals. Warren has campaigned for two new wealth taxes that are estimated to increase federal revenue by about $210 billion annually. New York Rep. Alexandria Ocasio-Cortez supports a 70% marginal tax rate on income over $10 million, which is estimated to generate an additional $20 billion to $70 billion per year, assuming that wealthy Americans are not discouraged from working. Even if the US adopted all three of these new taxes, annual federal revenue would increase by at most $280 billion.

The additional revenue would hardly make a dent in the cost of Democrats' policy proposals. For example, Yang's plan for a universal basic income is estimated to cost $3.8 trillion annually, and the Green New Deal would likely cost upwards of $6.6 trillion per year. Revenue from all three tax increases would fund less than 10% of either of these programs, let alone help pay down existing debt.

Supporters claim that although Medicare for All would massively increase government spending, it would be offset by decreases in private spending that leave total health care expenditures unchanged. While this is plausible in the short run, little evidence suggests that public health care spending would grow more slowly than private spending in the future. Public health care spending in the US has grown faster than private spending over the past 30 years, and other countries with publicly-funded health care systems have continued to see increases in expenditures as a share of GDP. An aging US population is likely to increase health care costs in the future, regardless of whether those costs are paid by government.

Given that the US cannot afford its existing entitlement programs, adopting the massively expensive policies proposed by Democratic candidates would be foolish. Instead, the federal government should cut entitlement spending and look for cheaper ways to address problems like climate change.

Instead of the Green New Deal, the federal government could adopt a revenue-neutral carbon tax to decrease emissions without exacerbating the fiscal imbalance. Economists from across the political spectrum support carbon taxation as the most cost-effective way to address climate change. And a carbon tax would be most effective if uniformly adopted by other countries, too.

At a minimum, the US should slow the growth of entitlement spending to no more than the average growth of GDP. Reasonable approaches include increasing the age of eligibility for Social Security and Medicare, modifying the indexation of Social Security benefits or tightening eligibility requirements for disability insurance. These reforms would keep entitlement spending affordable, unlike current policy.

Reasonable people can disagree on the benefits of federal welfare programs, the appropriate level of redistribution or optimal cost-cutting reforms. But everyone should agree that restoring fiscal sanity in the United States requires significant cuts to federal entitlement spending. The policies advocated by Democratic candidates will only make things worse.

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