News from Senator

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Remarks of Senator Dole

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Economic advice is always blamed when things go badly, but the "dismal science" rarely gets its due when things go well. Public officials can't resist taking credit for what is right about our economy, but they like to have someone to take the fall when things get out of control. Economists are well advised to be cautious in giving advice, since all of their risks are on the downside.

Even so, we seem to pay more attention than ever to economics and economic projections. That is true not only for basic decisions as to fiscal, monetary, and trade policy, but considerations such as the economic consequences of specific spending programs, the incentives or disincentives associated with taxation and welfare policy, and many, many other areas. The emphasis on economic analysis is helpful but it gets confusing when you can generate a plausible economic argument, complete with charts and statistics, for almost any policy position. Valuable as it is, economic analysis seldom makes it any easier to forgoe a consensus on policy goals.

It is remarkable, then, to see economic opinion converge on the issue of the Federal budget deficit. It seems even more remarkable that, notwithstanding this unusual consensus, Congress seems determined to ignore the advice we are being given. Why this is so makes for a rather interesting story.

Deficit in Perspective

First we should understand why there is such strong agreement on the need to reduce the deficit. The general view is that as recovery proceeds, the size of these deficits--currently projected at around six percent of GNP--will either force us to monetize the debt, rekindling inflation, or will divert so much of our savings to financing the government that private investment will be choked off, thereby aborting recovery. In terms of our international financial relations, the deficits help keep interest rates high and the dollar strong, helping us finance the deficit but at the same time undermining our exports and the potential for growth through trade.

Even now, as recovery appears to be on track, the deficits are causing problems. Future risks cause present uncertainties, and that influences the behavior of financial markets, business planners, and the investment community. Having spent more than two years establishing a consistent anti-inflation, pro-growth policy, it would be tragic if all our gains--hard won in terms of economic cost and personal hardship for a number of Americans--were to be tossed aside because we decline to take the necessary steps to correct the severe imbalance in our fiscal policy.

Deadlock

The root causes of the budget deadlock are well known. Members differ sharply as to the merits of higher taxes, less defense spending, and less nondefense spending as a means of reducing the deficit. The President understands the need to move in each of those areas, despite his reluctance to change defense spending or taxes. Similarly, Congress is reluctant to cut nondefense spending. This is not a new situation: the same basic conflict existed in the last two budget years, yet we made progress. Furthermore, this year the budget problem is more acute than ever. Why then can't we make a bigger dent in that deficit? I would suggest that there are three basic reasons.

First, politics is a problem. Congress has taken serious steps to reduce the growth of domestic spending, but the prolonged recession has undermined our efforts. As a result, there is great reluctance in Congress to take another stab at nondefense spending, even though that lies at the heart of the problem. At the same time, there is strong opposition to significant tax increases. Even with the recession, revenues are projected at just under 19 percent of GNP. That is in line with recent history, so it is hard to contend that taxes are too low.

Finally, there is a strong consensus for boosting defense outlays, even though Congress prefers a smaller increase than the President. In each of these areas strong resistance to major changes prevents dramatic reduction of the deficit. Since the recession has deprived us of resources that might have eased the budget crunch, the 98th Congress must face squarely the new set of priorities established by President Reagan and the 97th Congress: higher defense spending, slower growth in domestic spending, and a lower, or at least stable, tax burden. At the moment of real choice, Congress balks at being too explicit about its priorities, lest one or another group be offended.

A second source of the budget crisis is, ironically, the hope for sustained recovery. Until we are confident of the pace and the strength of the economic recovery, there is real reluctance to undertake measures, particularly in taxes, that might slow recovery. Remember that our worst fears concern not the upcoming fiscal year, FY 1984, but primarily FY 1985 and FY 1986. It is difficult to say exactly what policies we will want to have in place that far ahead, because there is so much guesswork in the economic forecasts. All we can be sure of is that the deficit will have to be significantly lower: but that doesn't tell us the best <u>way</u> to reduce the deficit. So there is a significant "wait and see" attitude in the Congress.

Thirdly, we are finding that the budget process is being asked to carry too heavy a load. It simply is not adequate to the task of reconciling our sharp differences given the uncertainty about the course of the economy. That is not the fault of the able leaders of both budget committees, who have done their best to make the system work. But it is a reality we have to come to grips with if we are serious about the deficit problem.

Budget Process and Budget Reality

There is no doubt the budget process is in trouble. Both the House and the Senate budgets are like the fire department saving the lot after the house has burned down: they just go through the motions. The House resolution calls for $30 billion in new taxes in FY 1984 alone: an unrealistic figure, and one that certainly could not be raised without altering the third year of the President's tax cut. That tax cut takes effect July 1, and it is a bit late to be tampering with it. Not only has the President promised to veto any bill attacking the third year, but a broad consensus of economic opinion supports the view that the July tax cut is well-timed to aid the recovery.

For that matter, even the Senate revenue figure of $9 billion for FY 1984 is unlikely to be met. On the Senate floor 11 of the 20 members of the Finance Committee voted against the budget resolution that proposes this action. If the tax-writing committees cannot support the revenue target, there is very little prospect of finding the votes elsewhere in the chamber to get a tax bill through. But let's face it: this is a paper resolution. Even though it passed the Senate, I doubt more than half of the members who supported it would vote for the legislation needed to implement it.

If both budget resolutions stray from reality on taxes, they all too clearly reflect what seems to be the consensus on domestic spending: no more cuts. Far from cutting, the House resolution proposes $16 billion in additional nondefense spending in FY 1984. The Senate resolution does propose a modest $4 billion reduction in nondefense spending for 1984, but that is a small enough gesture in the context of $200 billion deficits. When we have programs growing at the rate of, say, Medicare--which was originally projected to cost $9 billion by 1990, and is now expected to cost $100 billion by that year--it is wrong to say that nondefense spending is untouchable. It must be touched, in concert with action to moderate the growth of defense spending and raise revenues to the extent necessary: preferably by continuing efforts to improve tax compliance and restrict tax preferences, rather than by tampering with the tax cut and indexing provisions that benefit working people more than any tax changes we have seen in years. The problem is that these resolutions put all the burden of deficit reduction on the revenue side: and even then they leave whopping deficits that could imperil recovery. In short, neither budget resolution is cause for celebration--not if we care about real results.

A New Approach

If our budget process is inadequate to our predicament, what is to be done? If we pass budget resolutions that cannot be implemented, we offer no real hope to the business or investment community, or to our allies and trading partners. As always, the problem is the failure of Congress to contend with the pleadings of special interests. But that has always been a fact of political life: what we need are procedures and institutions that cope more effectively with the multitude of demands placed on the Federal treasury. Let me suggest a few changes that might be helpful.

I have said on a number of occasions that the President should be more actively involved in the budget process, even though it is a Congressional procedure. In fact, I have long believed that a greater role for the President ought to be institutionalized in the form of a line-item veto power. The President has stated his intention to wield the veto pen freely this year, and that may prove to be one of the most effective budget control devices we have. A constitutional provision for a line-item veto, similar to the power most Governors have, would give the Chief Executive more leverage with Congress in restraining spending. What is more, it would force closer cooperation in setting budget goals between Congress and the President--and that could prevent the kind of impasse we are faced with.

Timing of the budget plan also is a problem. A two-year budget cycle has been proposed, and that idea may have merit in reducing the time spent each year on the budget blueprint. But the real answer may be to impose early, firm deadlines. This year we may not have a budget agreement until July or August--or we may not have one at all. That leaves too little time to carry out the complex legislative actions needed to implement a budget. The budget plan ought to be agreed on early in the year, in consultation with the executive. The notion of a Presidential budget being issued in January or February, followed by extensive analysis and political gamesmanship in Congress, has to be made a thing of the past. There is no excuse for a drawn-out process that sees every spending decision, however minor, made several times over--in budget debate, in legislative action, and in appropriations.

The budget process has been made to work, when we had the will to make it work. But our strength of will falls far short of what it ought to be, and we need a process that enforces a discipline on us even in our weaker moments. That is why the search for institutional restraints on fiscal decisions, particularly constitutional restraints, will continue. We may have made a mistake by relying on a complicated process to coordinate spending and taxing decisions, rather than adopting simple rules that are more likely to lead to budget restraint. One such rule might be to require annual review of spending levels in entitlement programs, perhaps by coordinated action of the authorizing committees and the Appropriations Committee. Another specific change that could help would be to set an overall budget limit, and make specific programmatic decisions within that limit. As it is, we have an aggregate budget figure and a breakdown by program and budget function: in practice, that means we make the program decisions, add up the figures, and present the bill to the Finance Committee--to be covered either by raising taxes or adding to the public debt.

The U.S. Budget and World Recovery

The Federal budget is just one part of the economic picture, and it is probably not the most important part. But there are very good reasons why the nation and the world are paying such close attention to our budget decisions and the effectiveness of our budget procedures. What is at stake is the credibility of our commitment to a return to noninflationary growth in the decades ahead.

The same fears that trouble domestic investors--that we will reflate our economy, or that we will choke off a promising expansion just as it gets underway--also disturb foreign investors. Because the world looks to us to lead recovery, and because of the important role of the dollar in international reserves, it is critical that we show a stable and consistent path for our economy. The deficit overhang restricts our ability to do so, that to that extent reduces the likelihood of a worldwide economic renaissance.

There is growing talk of greater economic coordination among nations, or stimulating growth by rolling back barriers to international trade, and of better communication concerning the economic fundamentals that the marketplace evaluates in determining foreign exchange rates. These are all worthy goals, and they share a common theme: broadening the movement toward larger world markets in order to unleash the tremendous potential of free and open economic decisionmaking on an international scale. But coordination is difficult given fundamental changes in the nature of the economy, upon which current trade rules are based, and when countries increasingly resort to government intervention to advance their trade goals.

This Congress will mark the 50th anniversary of the reciprocal trade agreements program. That program has guided U.S. trade policy since 1934, and is founded on three principles: (1) mutually reciprocal reductions in trade barriers; (2) enforcement of laws to workers and firms adversely affected by trade liberalization. The program has worked well: In the past three decades, total trade has increased from $26 billion to $500 billion, and tripled as a percent of our GNP.

Trade liberalization has served well as a job-creating policy. But the Finance Committee must reexamine whether the laws buttressing the reciprocal trade agreements program, and the international agreements such as GATT that were negotiated pursuant to it, adequ ly address current problems. We will look at the nature and effects of "industrial targeting" by other governments; agricultural and other subsidies; and the effects of increasing imports on our older workers, who may have difficulty being retrained. This review may suggest some alteration of current laws. In the meantime, the Committee will work on specific proposals to increase trade, particularly with developing countries. These include the Caribbean Basin Initiative; renewal of the Generalized System of Preferences, and a replacement for DISC.

But none of these efforts will succeed unless we can reduce uncertainties as to future inflation and flows of capital among nations. The transition to a noninflationary environment, with all its costs, has yet been managed with remarkable success so far. That success must be built on, without reneging on our commitments to a stable currency, reduced government interference in the domestic economy, and restraint on spending and taxes. Our failure to adequately address the spending issue has the potential to block a brilliant economic future, if we let it. That does not mean revenues will not play a role--the President agrees that they must, provided, that significant action is taken on spending. It does mean that we ought to keep our priorities straight.

We in government have to lead opinion and lead the nation in a revolt against the narrower interests that threaten our common goals. That means we must explain clearly and forcefully, and reiterate again and again, why the stakes are as high as they are. The public must understand that their jobs, their aspirations for theirselves and their families, are what is really at stake in the budget debate. When we get across the message that the quality of life in this nation--and abroad--must yield to the selfish interests that generate budget gridlock, then I believe we will succeed. The public is willing to support a campaign to cut the deficit if we do our job of explaining why their interests are best served by doing so, even at the cost of some program or tax preference favored by one or another group. The diversion of interests leading to political stalemate is a classic problem of democracy. It has been solved before by honesty, forthrightness, and leadership. We have no time to lose by solving it that way once more.

-30-