

Economic Policy

Part 1 – Intro

Introduction

- Two types of economic policy:
- Fiscal policy – taxing and spending (simple, budgeting)
 - Families do this
- Economic policy – controlling inflation to determine the value of money (complicated, ??????? Magic?)
 - Families do not do this

Government, Politics, and the Economy

- “It’s the Economy, Stupid”: Voters, Politicians, and Economic Policy
 - Economic trends affect who voters vote for.
 - Economic conditions are the best predictor of voters’ evaluation of the president.
 - Republicans worry about inflation.
 - Democrats stress importance of unemployment.

Government, Politics, and the Economy

- Two Major Worries: Unemployment and Inflation
 - Unemployment Rate: measured by the Bureau of Labor Statistics (BLS), the proportion of the labor force actively seeking work, but unable to find jobs
 - Inflation: the rise in prices for consumer goods
 - Consumer Price Index: the key measure of inflation that relates the rise in prices over time

Good Times, Bad Times

- The U.S. economy experiences booms and busts. The busts are called recessions.
 - *Recession*, two or more successive quarters in which the economy shrinks instead of grows.
- Unemployment
 - Usually linked to the health of the economy
 - Today, its around 8%

How to get out of a recession: Keynesian Economics

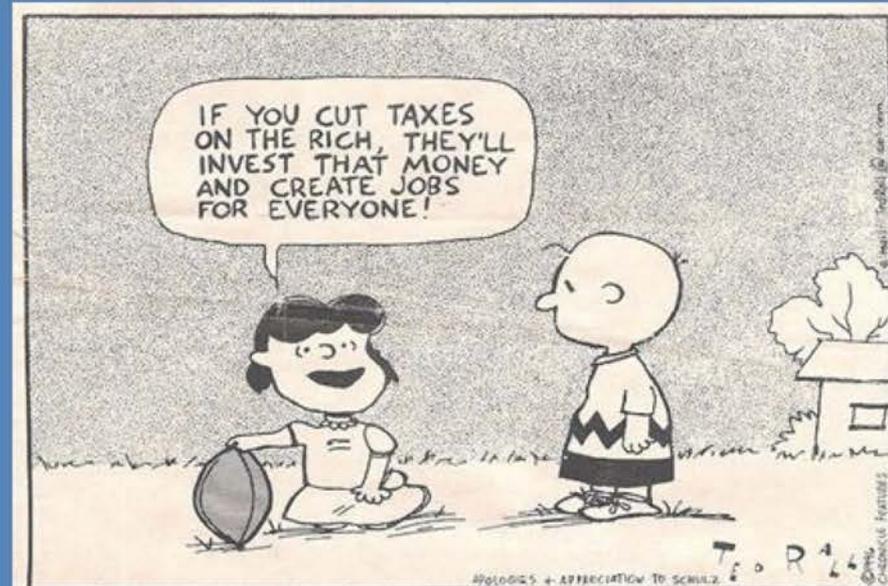
- John Maynard Keynes said:
- If we are in a recession, all we need to do is have the government spend lots of money to jumpstart the economy
- Major part of the New Deal
 - Highways, schools, TVA built
- Used by Bush 43 and Obama in “stimulus checks” mailed out to citizens after 2008 recession

Keynesian Economics and Debt

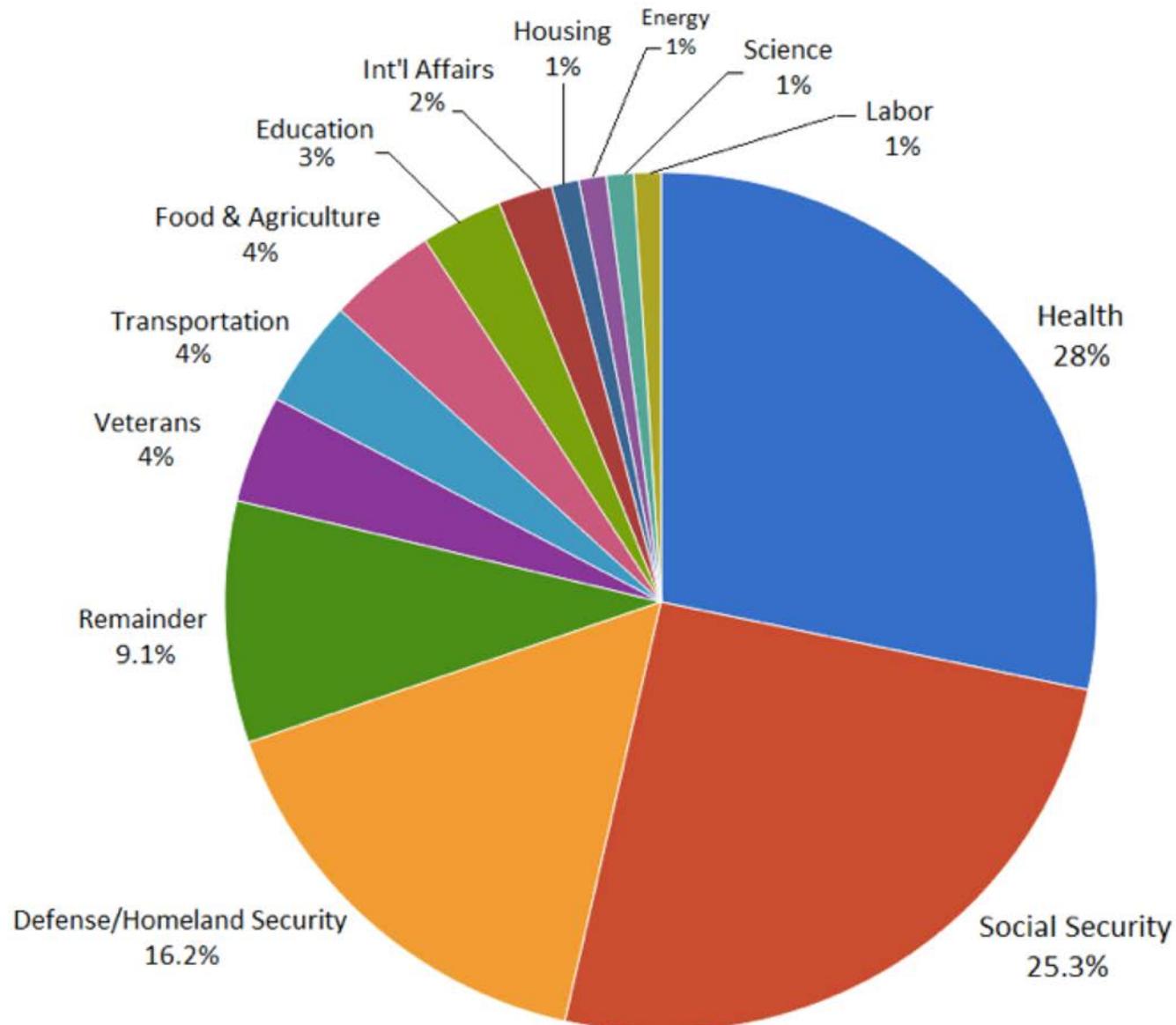
- We have to borrow the money to jumpstart the economy, not just raise taxes
 - If we raise taxes, we're just moving money around, not putting new money in
- This is why we are in such amazing debt
- Called “discretionary spending”
 - At the discretion of the government
 - Optional
 - Used to boost the economy

Reaganomics – Supply-Side Economics

- Provided businesses incentives to increase the supply of goods and services
- Lowered taxes
 - People saved more and invested their savings
 - Companies produced more and hired more workers
- Tax cuts benefited the rich more than the poor
 - Widened the gap between rich and poor



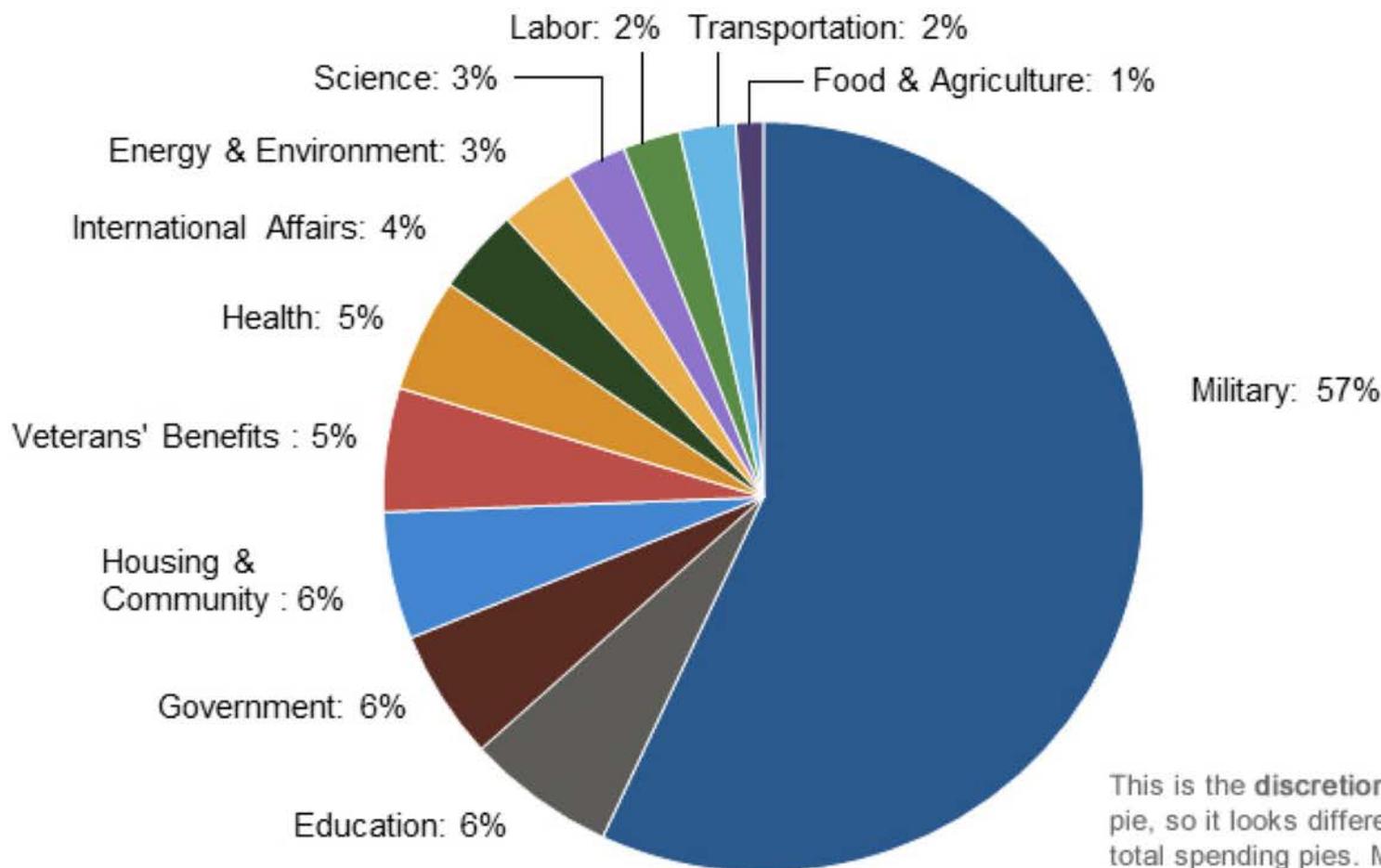
Percent of spending, including discretionary and mandatory



Discretionary Federal Spending Pie: \$1.15 trillion

This is President Obama's proposed discretionary budget for the coming fiscal year. The discretionary budget, which is only part of total federal spending, is set by lawmakers each year during the appropriations process.

More U.S. federal budget info at www.nationalpriorities.org



This is the **discretionary** federal spending pie, so it looks different than mandatory or total spending pies. More info and all spending pies: bit.ly/fedspending
How did we get these numbers?
bit.ly/nppsources

Federal Spending

2013 = \$3.5 Trillion

(Fiscal Year 2013: Oct 1, 2012 – Sept 30, 2013)

Your Priorities?

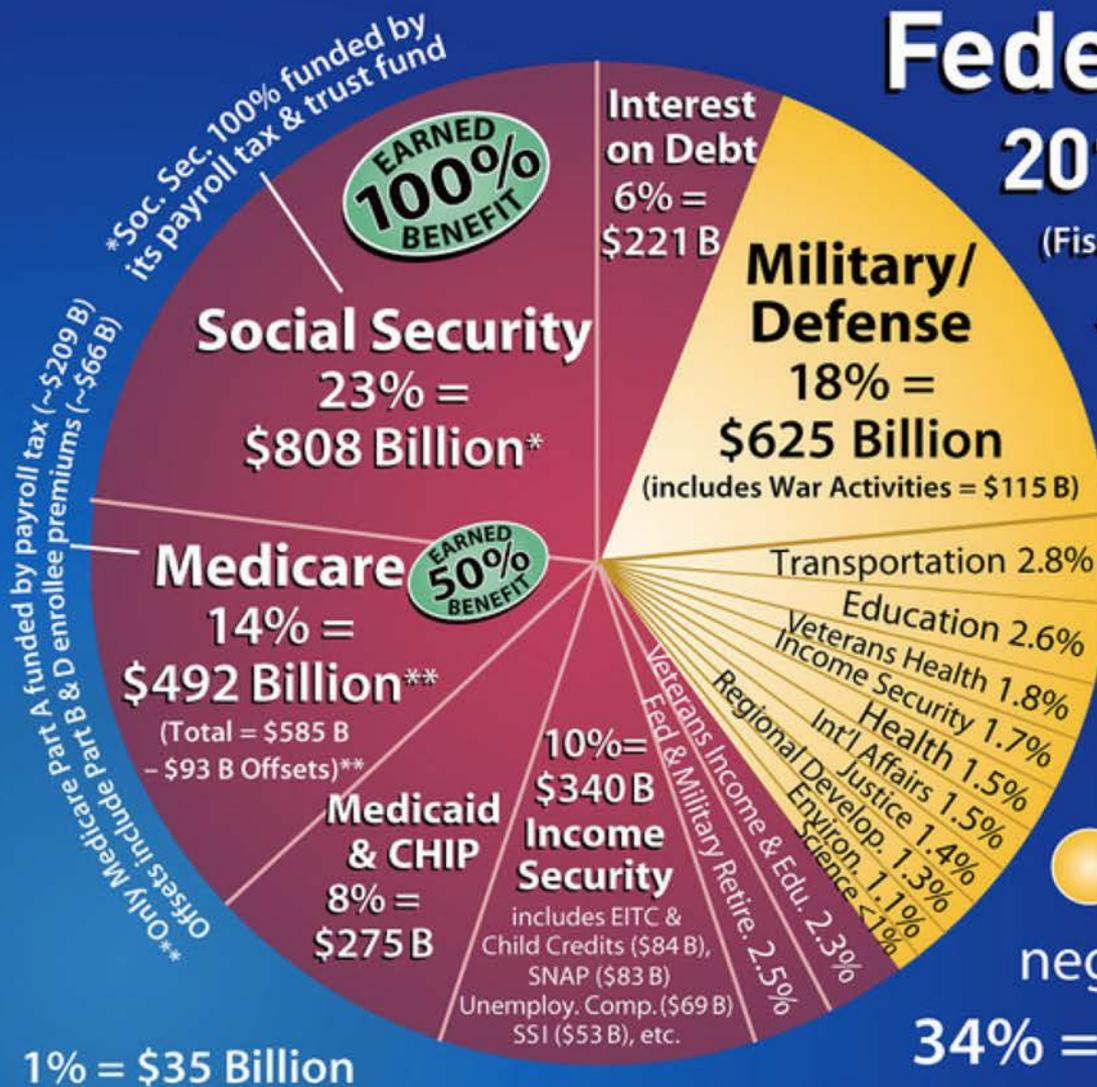
Mandatory
dictated by existing law
(or interest rate on debt)

66% = \$2.3 Trillion

Discretionary

negotiated each year

34% = \$1.2 Trillion



Source: Congressional Budget Office, "The Budget and Economic Outlook 2014-2024," Feb 2014 (www.cbo.gov)
2013 amounts in Tables 1-2 (pg 12), 3-2 (pgs 54-55), 3-5 (pg 72), 3-6 (pg 74), 4-2 (pg 85) & Box 3-2 (pg 68)

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quiz

1. What does discretionary spending mean?
2. Which economist promoted New Deal programs where the government "spent money to make money"?
3. What term means the economy has shrank for two consecutive quarters?

Part 2.1 – Monetary Policy and Taxes

Monetary Policy

- *Monetary policy*, the utilization of changes in the amount of money in circulation to alter credit markets, employment, and the rate of inflation.
- Determined by the Federal Reserve System

The Federal Reserve Board (The Fed)

Independent agency in the executive branch

Fed is designed to be non-political

The Fed controls interest rates for loans

When interest rates are lower, people purchase more (cars, homes)

Higher = more saving, less spending

The Balance of Trade and the Current Account Balance

- The *balance of trade*, or the difference between the value of a nation's exports of goods and its imports of goods. The U.S. balance of trade has been significantly negative for many years.
- If a country exports more than it imports, businesses will be more prosperous, right down to the workers. If it doesn't, everyone "pays" (see what I did there?)

Fiscal Policy

- The manner in which the government taxes and spends
- Each year the federal government creates a budget
 - The House Ways and Means Committee is where all tax policy begins (*tax bills must start in House*)
- The 16th Amendment (1913) allowed the government to tax citizens' income
 - The IRS oversees the collection process
 - Progressive tax system
- The government typically spends more than it takes in
- Currently \$19 trillion National Debt
- The deficit is the year-to-year difference between what gov't takes in versus what it spends

2.1 Quiz

1. What group in the federal government controls interest rates and inflation?
2. What type of economic policy is described in question 1?
3. If the government exports more to a country than it imports from it, the US has a _____ balance of trade.

2.2

Sources of Federal Revenue

- Article 1 Section 8 gives Congress the power to lay and collect taxes and to borrow money.
- The US has borrowed money throughout its history, and has been out of debt only once in its history.
- The 16th Amendment (1913) allows for the federal government to collect income tax from “whatever source derived.” Congress created the Internal Revenue Service (IRS) to oversee collection of these taxes.

Progressive Income Tax

- Progressive taxation means that the tax rate one pays increases, or progresses, as one's income increases. The highest tax rates have gradually lowered since the 1940s.
- 1940s - 94% top rate
- 1970s - 70% top rate
- 1980s - 30% top rate
- 2010s - 35% - 40% top rate

Individual Federal Income Tax Rates - 2010

Taxable Income	Federal Income Tax	Percent
25,000	3,331	13%
50,000	8,681	17%
100,000	21,709	28%
500,000	152,644	31%
1,000,000	327,644	33%

Source: Senate Committee on Finance, JCX-51-10, 2010

The Tax Code

- Congress has created a very complicated tax code, by using the power to tax it create incentives and punishments.
- Special interest groups push for loopholes in the tax code to favor certain people or groups.
- Congress has used the tax code as a way to draft social policy by encouraging certain behaviors and discouraging others.
- The corporate tax rate has varied between 10% - 35%. About 10% of all federal revenue comes from corporate taxes.

Trump's Tax Plan

- Made taxes simpler
- Closes some loopholes
- Tax cuts for everyone in the beginning
- Tax hikes for middle and lower class people in the next ten years
- Lowered corporate tax rate from 35% to 21%
- Tax cuts for upper class/corporations will lead to more jobs for poorer people

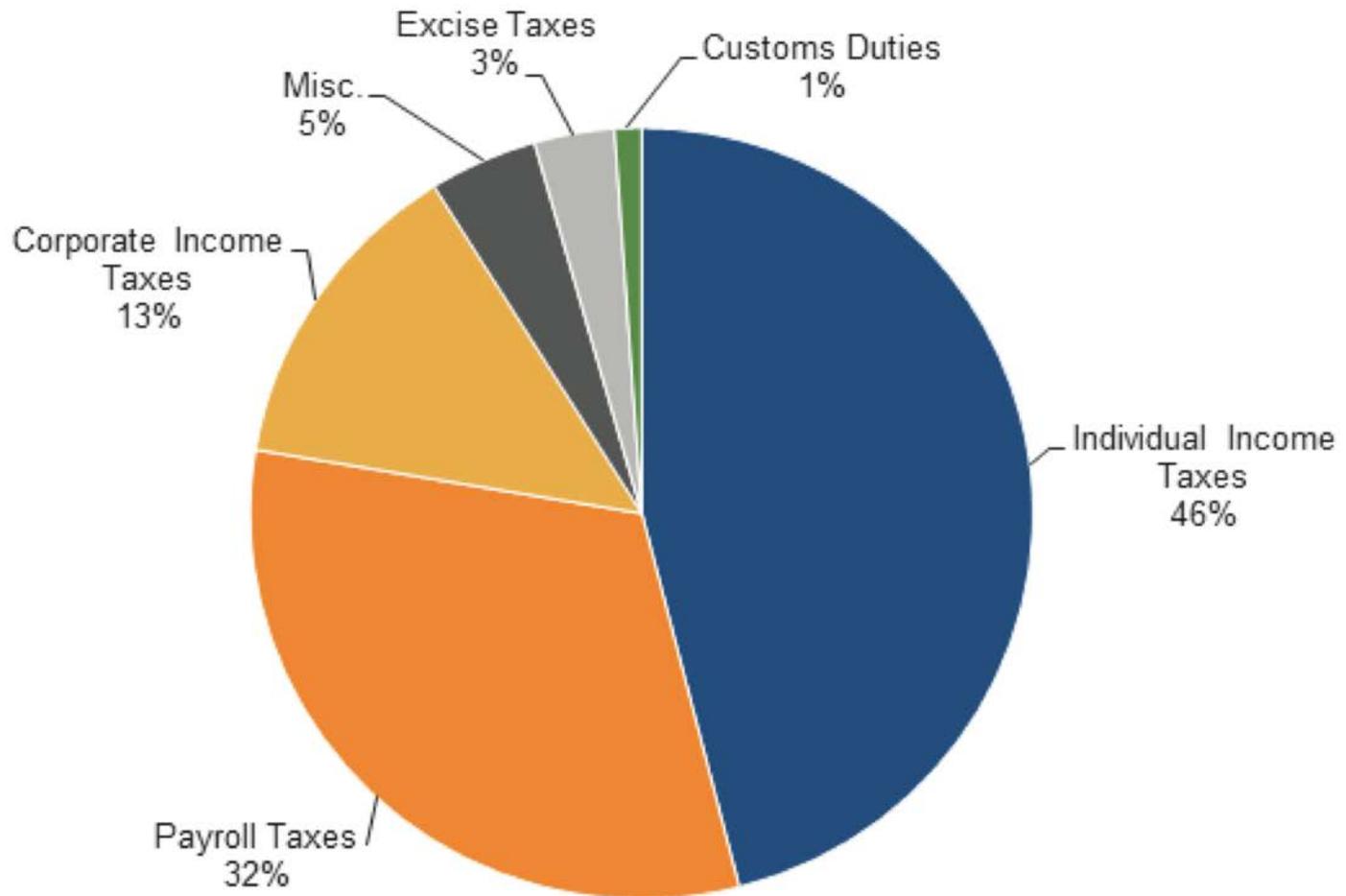


Income Tax Rate		Income Levels for Those Filing As:	
<u>2017</u>	2018-2025	Single	Married-Joint
10%	10%	\$0-\$9,525	\$0-\$19,050
15%	12%	\$9,525-\$38,700	\$19,050-\$77,400
25%	22%	\$38,700-\$82,500	\$77,400-\$165,000
28%	24%	\$82,500-\$157,500	\$165,000-\$315,000
33%	32%	\$157,500-\$200,000	\$315,000-\$400,000
33%-35%	35%	\$200,000-\$500,000	\$400,000-\$600,000
39.6%	37%	\$500,000+	\$600,000+

Other Revenue Sources

- Excise taxes are levied on particular goods or services, such as alcohol, tobacco, airline travel, and gasoline.
 - About 3% of federal revenue comes from excise taxes.
- States also can have their own income taxes, as well as sales taxes, additional taxes on hotels, alcohol, cigarettes, and other items.
- The overall tax burden in the US is lower than most industrialized nations.
 - US citizens pay 25.4% of their incomes in a combination of income, sales, and other taxes.

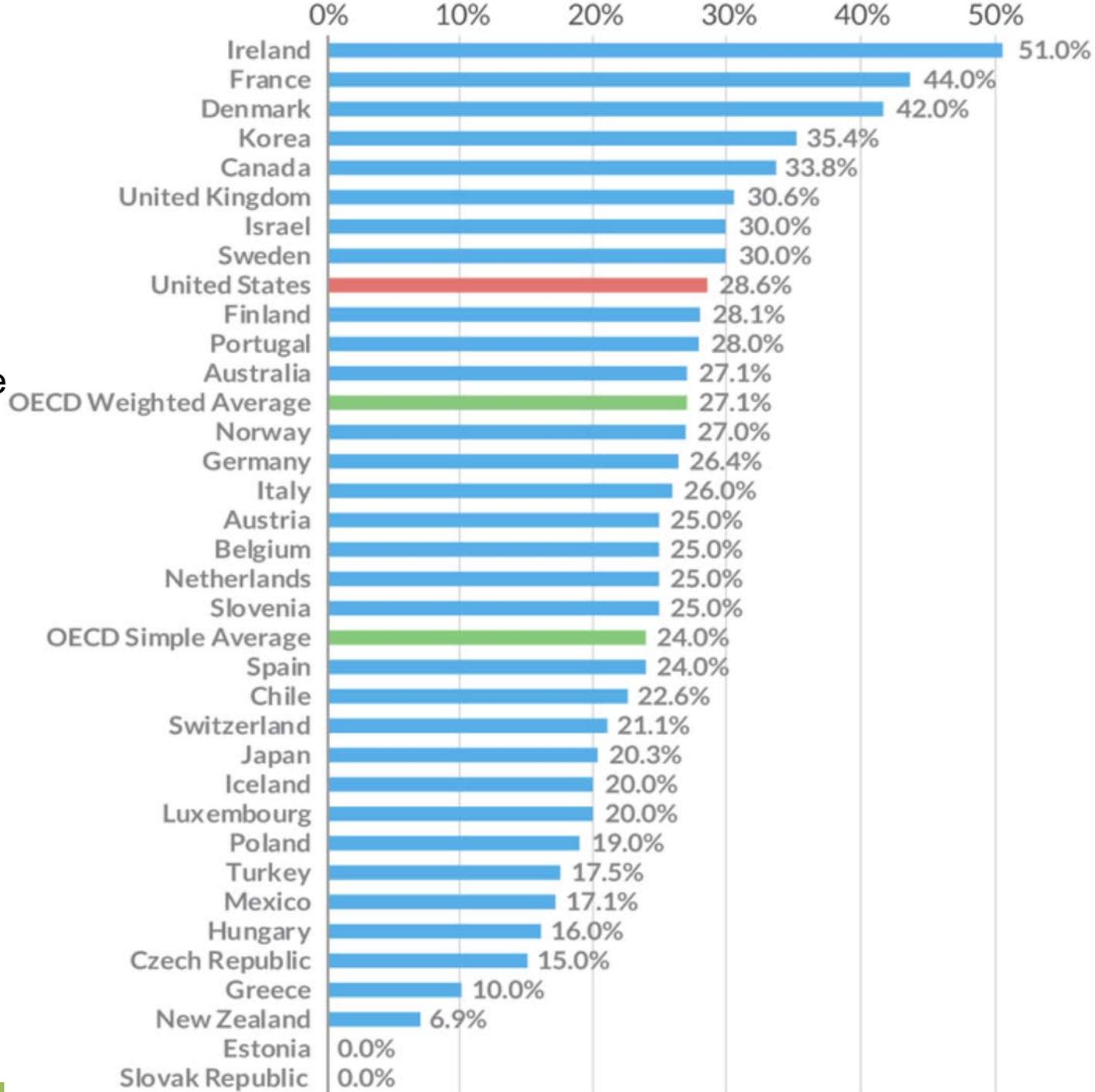
Projected Tax Revenue (Fiscal Year 2015)



Source: OMB
National Priorities Project



Percent of average income spent on taxes



2.2 Quiz

1. The government can get money from taxing and from _____.
2. Give one aspect of Trump's tax plan.
3. What is the percent corporations have to pay in taxes?

Part 3 – The Budget

Federal Budget Process

- The Constitution states “no money shall be drawn from the Treasury but in consequences of appropriations made by law.”
- Congress has the “power of the purse,” which means federal dollars cannot be spent unless Congress says so.
- The Congressional Budget and Impoundment Control Act, 1974, established the budgeting process which is used today.
 - It set budgeting guidelines, and created the
 - Office of Management and Budget (Executive)
 - and the Congressional Budget Office (Legislative).
-

Budget

- 2/3 of the Federal Budget is for Entitlement Spending
 - These are government services already promised by law to citizens (Social Security, Medicare, Food Stamps, etc)
 - Politicians usually too fearful to touch entitlements
- The remaining is “discretionary spending”
 - Most of this is spent on National Defense
- Some have argued for a “Balanced Budget Amendment” and the “Line Item Veto” to reign in wasteful spending
- Trade can impact the economy as well
 - Goal: to trade more than we buy
- NAFTA (North American Free Trade Agreement) – Free trade between U.S.A, Mexico and Canada

The President and the Budget

- President initiates the budget by submitting it to Congress
 - Does it with the help of the OMB
- Sends it specifically to the Senate and House Appropriations Committees
 - Appropriations means spending

Congress and the Budget

- 1974 – Congressional Budget and Impoundment Control Act:
 - Made to take control of the budget back from the president
 - Made a set budget calendar (must pass the budget by October 1st)
 - Created a budget committee in each house
 - Created the CBO (Congressional Budget Office) to advise Congress on the budget
- Goes from the president to the House and Senate Appropriations Committees
 - Then goes to the House Ways and Means Committee and the Senate Finance Committee
 - Ways and means to pay our bills

Deficit Spending and the Public Debt

- The government funds its deficit primarily by selling U.S. Treasury bonds.
- Sell \$100 bond today, pay back \$110 in 10 years
 - Like a loan, but not from a bank.
- Twenty years ago, only 15 percent of these bonds were held abroad.
 - Today the figure is 40 percent.
 - Mainly in China

Why are we debt?

- We spend more than we make
 - Spending on military and programs like Medicare and Medicaid (make up the majority of spending)
 - Making \$ from taxes and selling bonds
- Just like a family household, we are living outside our means

How can we get out of debt?

- Spend less on everything, especially on entitlement programs
 - Liberals don't want to do that
 - Say that those people are already living in poverty
- Raise taxes
 - Conservatives don't want to do that
 - Say that it will hurt businesses
- Compromise is needed, but probably won't happen.

Deficit Spending and the Public Debt

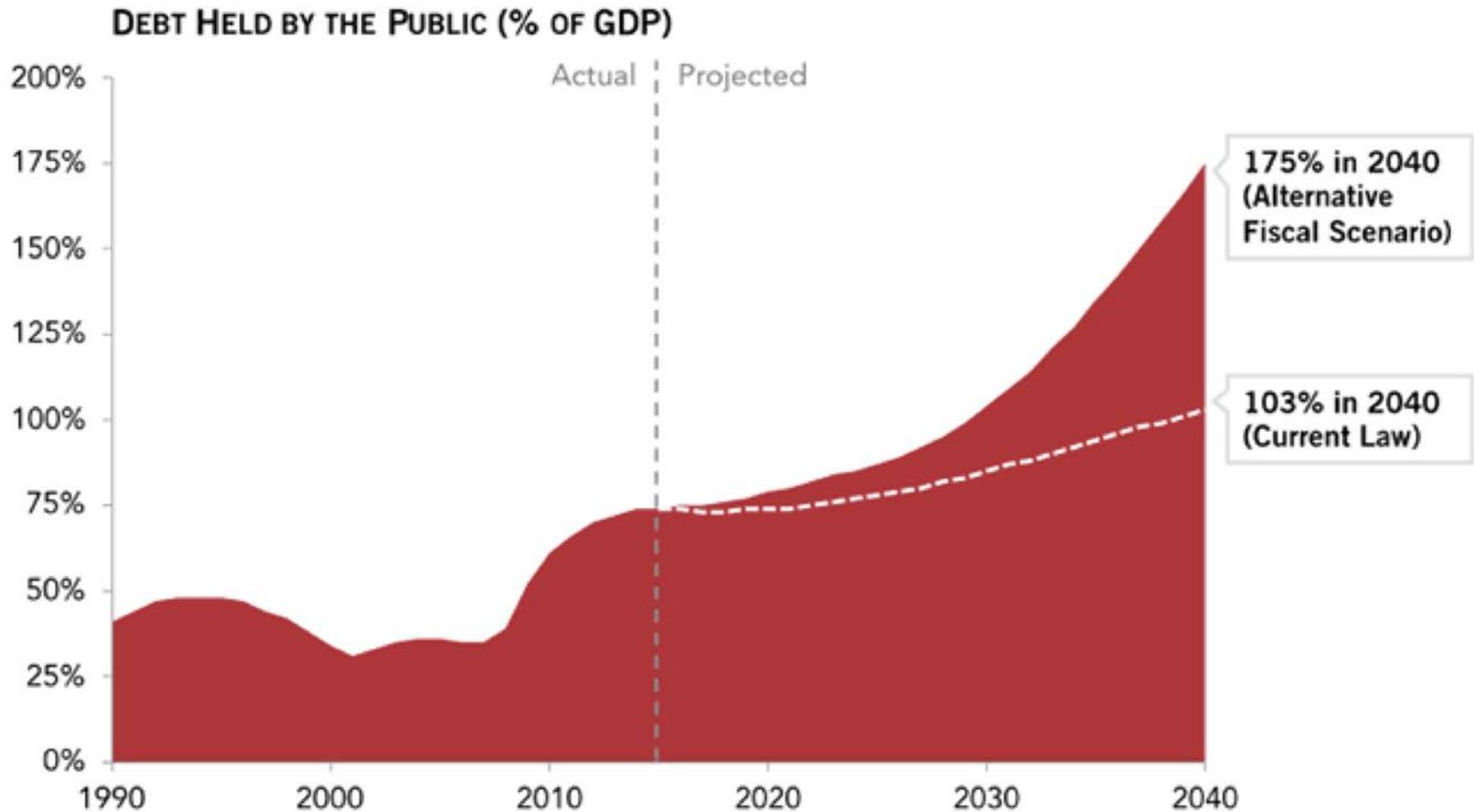
- *Net public debt*, the accumulation of all past federal government deficits; the total amount owed by the federal government to individuals, businesses, and foreigners.
- *Gross domestic product (GDP)*, the dollar value of all final goods and services produced in a one-year period.

1980 – 800 Billion
1990 – 3 Trillion
2000 – 5 Trillion
2008 – 9 Trillion
2016 – 19 Trillion
2020 – 21 Trillion

Net Public
Debt AKA
National Debt



U.S. debt held by the public is on an unsustainable path



SOURCE: Congressional Budget Office, *The 2015 Long-Term Budget Outlook*, July 2015. Compiled and calculated by PGPF.

NOTE: Current law projections are from CBO's extended baseline scenario. Data for the alternative fiscal scenario include economic feedback.

Quiz

- 1. What term means the sum value of all the things a country produces to sell?
- 2. How does the US “borrow” money?
- 3. Who proposes the budget?