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Jeffrey Sachs: A New Direction for American Economic Policy

America remains mired in crisis because the mainstream economic prescriptions peddled by both parties are wrong. The Democrats want to jolt the economy back to prosperity through temporary stimulus. The Republicans want to slash government spending to make room for permanent tax cuts they claim are the key to economic growth. Moderates in the middle call for stimulus today followed by budget cuts in the future.

All three positions misread America's economic plight. Turning dials on stimulus and tax cuts won't solve the real problems. In my new book, The Price of Civilization, I suggest a new direction.

Washington Democrats (and White House economists) consider themselves to be the heirs of John Maynard Keynes. They view the economic downturn as a temporary shortfall of demand. The role of government is designed to boost demand for a year or two until the «animal spirits» of private investors once again are revved up. A short-term stimulus ostensibly serves two purposes: to bridge the period of low demand and to restore investor confidence in the long-term prospects of the economy.

Washington Republicans consider themselves to be the heirs of Adam Smith. They view the economic crisis as resulting from the lack of profitability of business investment and entrepreneurship caused by excessive taxation and regulation. The Republicans argue that any government spending must be covered by taxes, either now or in the future to pay off government debts. The key to low taxes, they note, is low spending in the first place.

A few self-styled moderates want to have it both ways: stimulate today and reduce the deficit in the future through planned cuts in spending. One obvious question arises in the moderate proposals. When does «today» end and the «future» begin? The stimulus in 2009 was followed by another round of temporary tax cuts at the end of 2010, and now by Obama's proposal for yet more temporary cuts in 2012.

In my opinion, all three positions miss the essential point. The U.S. economic crisis is structural, not cyclical. We are experiencing forces that have been at play for a generation, not a short-term drop of consumer demand that will quickly recover. The long era since the early 1980s has been characterized by low and falling tax collections, not a rising tax burden, but tax cuts have been to no avail. Something much more basic is missing from the diagnosis.

What is missing is the changing global economy. America has been hit by waves of technological and geopolitical change that have upended the old strategies for good jobs and middle-class incomes. The information revolution has knit together production networks that now span the globe. Apple may be an American company but it is employing up to 1 million Chinese workers to produce the iPads, iPhones, and other electronic wizardry that are the new staple products of our economy and culture.

America's challenge is not merely to create jobs. The key is to create good jobs at good wages. Such jobs cannot be created by a short-term jolt of government spending, or by cutting government investments in education, science, technology, and infrastructure. Adam Smith and John Maynard Keynes, who were both acutely aware of long-term productivity as the source of sustained economic wellbeing, would agree. And even as the guru of free markets, Smith

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had emphasized the importance of publicly financed education for the benefit of the whole society.

The key today is to raise American productivity sufficiently to restore the competitiveness of the American workforce in a tightly linked global marketplace.

Americans with a college degree are generally okay. Their unemployment rate is 4.3% and average incomes are above $60,000 per year. There are many help-wanted signs for talented computer programmers, engineers, and other high-skilled workers. Americans with a high-school diploma or less are falling into poverty, with unemployment of 10% and incomes averaging less than $30,000 per year. For these workers, the only help-wanted signs are for dead-end jobs that lead to poverty.

What is surprising and distressing is how few young people are finishing a four-year degree or an equivalent path to high job skills. The proportion of young people achieving a bachelor's degree has peaked at around 40%. Many more try college, but ended up dropping out because they can't meet tuitions and can't afford to be out of the labor market for the period of college study.

With America at the brink of financial collapse and class war, it is time for all sides to follow a new direction: a long-term effort to invest in skills and twenty-first-century infrastructure, paid for by increased taxes paid by cash-rich multinational companies, high net-worth individuals, and polluting industries. Rather than creating low-skilled and temporary jobs for our kids, we should be helping kids to stay in school until they have the skills to compete effectively in the new global economy.

The money to pay for this expanded effort can come largely from the top of the income distribution. The top 1% of households took home 10% of household income in 1980 but now take home roughly 23%. Along with this remarkable surge in income after 1980 came tax cuts and increasingly easy access of the rich to offshore tax havens.

It's time we insist that the rich do their part to help rescue America from decline. The tradeoff for America comes to this: fewer mega-yachts and other luxuries for the rich, and millions better educated children and young workers for society as a whole. America will recover when all Americans, especially those at the top of the heap, pay the price of civilization.

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