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The Role of Government in Growing a Strong Economy

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SPEECH

THE ROLE OF GOVERNMENT IN GROWING A STRONG ECONOMY†

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House of Representatives, Committee on the Budget, Chairman Ryan, Vice Chairman Garrett and Ranking Member Van Hollen, and Members of the Committee. Thank you for the opportunity to participate in this hearing. I want to thank the committee for its focus today on the state of our economy.

It is safe to say that the weak economy is the dominant concern for Americans today.[1] Americans can see with their own eyes and in their own communities that the economy is not growing like it should be. We are nearly three years past the end of the recession, and yet few Americans believe we have recovered from it,[2] nor has our economy begun to grow at a healthy and sustainable level.

The kind of snap-back we have seen in previous post-war recovery simply has not happened.[3] Many people who lost jobs in the last four years have not returned to the workforce—millions have given up trying altogether and have withdrawn from the labor market.[4] Business owners who retrenched and cut costs have been very slow to invest in the hopes of future growth.

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† Testimony to the House of Representatives Committee on the Budget, June 1, 2012.

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1. *See* Jennifer Agiesta & Tom Raum, *Poll Shows Americans' Pessimism on Economy Growing*, Real Clear Politics (May 11, 2012), http://www.realclearpolitics.com/articles/2012/05/11/poll_shows_americans_pessimism_on_economy_growing_114126.html.

2. *See* Matthew Philips, *Recovery—or Recession? Economists Debate*, Bloomberg BusinessWeek (July 19, 2012), *available at* http://www.businessweek.com/articles/2012-07-19/recovery-or-recession-economists-debate.

3. *See* Council on Foreign Relations, Quarterly Update: The U.S. Economic Recovery in Historical Context (2013) ("The economic expansion following the 2008 recession has been the weakest of the post-World War II era and remains an outlier among postwar recoveries along several dimension.").

4. *See* James Sherk, *Not Looking for Work: Why Labor Force Participation Has Fallen During the Recession*, The Heritage Found. (Aug. 30, 2012), *available at*

The housing market remains weak. Commercial real estate is still weak in many areas. What's worse: There is a strong sense in the business community that the economy is stalling again, and growing well below its historic potential.[5]

I recognize that the Members of this committee share a common awareness of the problems facing our economy. And you also share a common resolve to do your part to bring prosperity back to America.

The only question is how. What do we need to do in these chambers, or in state capitols, to improve the outlook for job creation, business expansion and overall prosperity?

I would urge you to look carefully at your primary responsibility—to manage the budgetary affairs of the U.S. government—as the place to start. At $3.8 trillion, the U.S. budget is a powerful force on the U.S. economy.[6] Its sheer size means that entire industries—whether heavily regulated or not—operate in constant awareness of what you do here.

When you combine this budgetary power with the separate powers of taxation and regulation, the federal government wields significant influence over the economy, both directly and indirectly. It is not an overstatement to say that right now, the U.S. economy operates significantly at the direction and behest of the U.S. government, not the other way around.

I can think of no better example of this trend than the economic growth of the Washington, D.C. area. The district and its surrounding area, is a picture of economic health and growth. Housing values within the Beltway have not fallen, as they have elsewhere.[7] There is a simple explanation for this: The near-constant growth of the main industry of this region—the federal government. And while the growth of the federal government is healthy for this area, one has to ask at what cost it occurs? Every dollar spent in this area was taxed from somewhere else—or borrowed, and therefore not used on some other productive activity.

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http://www.heritage.org/research/reports/2012/08/not-looking-for-work-why-labor-force-participation-has-fallen-during-the-recession.

5. *See* Philips, *supra* note 2.

6. *See* Tom Cohen, *President Obama Unveils $3.8 Trillion Budget*, CNN (Feb. 13, 2012), *available at* http://www.cnn.com/2012/02/13/politics/obama-congress-budget.

7. *See* Alice Rogers, *The Real Estate Market That Defies the Trends*, TIME, Jan. 5, 2012, http://business.time.com/2012/01/05/the-real-estate-market-that-defies-the-trends/.

Let me be clear: I do not believe in a zero-sum economy.[8] But I do believe that if the government gets bigger and more powerful, it largely does so at the expense of the rest of the economy, because government does not contribute to the economy the way the private sector does. A dollar spent on government services is not equivalent to a dollar of private sector investment.

Today's federal government did not emerge out of the blue three years ago. Far from it. But there is no doubt that the growth of the U.S. government, as a share of the U.S. economy, has risen sharply in the past three years.[9] Even when the economy began to grow, the government's share was growing faster.

In many cases, the government's growing size and influence was made possible by good intentions and hopeful policy ideas. Behind every spending program and every tax incentive and every regulation is an idea. It might sound good. It might in fact be a good idea. But those good ideas, as well as the not-so-good ones, add up. And the cost of everything you do here—every line item, every rule, every carve-out and phase-out and earmark—drains activity and investment and creative effort out of the private sector of the economy.

That is why my best advice to you is to perform a fundamental cost-benefit reconsideration of many programs in the federal budget. Please know that no matter your good intentions, the government creates unintended consequences when it acts.

What would a cost-benefit analysis show? I read recently of the forty-nine different federal job training programs—and that the number of such programs continues to grow.[10] I wonder about that number. What do we, as taxpayers, get from forty-nine job training programs that thirty-nine or twenty-nine or just nine could not accomplish? I wonder as well about the people who need the job training. How do they know which one is right for them? And who runs these training programs—are they being measured on the success with which they get people retrained?

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8. Under game theory, zero-sum games "are those in which everything gained by one player must have been lost by the other." David Crump, *Game Theory, Legislation, and the Multiple Meanings of Equality*, 38 HARV. J. ON LEGIS. 331, 361 (2001).

9. *See* Josh Barro, *Lessons from the Decades Long Upward March of Government Spending*, FORBES, Apr. 16, 2012, http://www.forbes.com/sites/joshbarro/2012/04/16/lessons-from-the-decades-long-upward-march-of-government-spending/.

10. *See The Job Training Mess: The Feds Have 49 Programs. Think There's Some Overlap?*, WALL ST. J., May 10, 2012, http://online.wsj.com/article/SB10001424052702304299304577348051965251164.html.

Do these forty-nine job-training programs operate with any sense that they could—and should be—closed if they fail? This is the daily worry of every business in America, but I would guess that not one of these programs ever worries that they will be put out of business by any of the other programs—or by their congressional funders. I wonder about what these job-training programs do, indirectly, to programs which are effective at providing focused skills training? Are we, by creating government programs, competing with those who actually do this work quite well in the private sector?

In this matter, the sheer size of congressional ambition is one problem. But there are other problems, too. The complexity of the programs. The failure to see whether taxpayer money is well-spent. The likelihood is great that by setting up these programs, government may be keeping someone else from doing their work. Someone who might do the job better than the government can, build a business from it, hire employees, pay taxes on profits, and so on.

In short: when you try to solve one problem, you may not only fail—you may create several others. Now if you multiply that one example across the economy, in multiple industries and multiple ways, it is hard to see what will happen, and has happened.

The government, by growing in influence and extending itself into all corners of the economy, makes it less likely that enterprising business people will address social needs through some kind of business idea or business plan. So it is not only that the government grows bigger through every program. Through the power of taxation and regulation, it also displaces the private economy—the innovators and inventors, the people who risk their own savings on a business idea, the established businesses who could grow but do not. The losses that follow are significant.

Someone recently asked a good question: what if the federal government tried to invent the mobile phone? What if Congress said: "People need to talk to each other and receive information while they are out and about, and we need to provide them that technology. So, let's fund a bunch of research, and get people the tool they need."

Well, you think, that did not happen and would not have happened. It sounds like an extreme example, but in reality, the federal government tries to invent solutions to people's problems all the time. Problems far more complex than mobile phone technology. Many well-meaning programs in the federal budget have this exact flaw: they try to accomplish through government fiat what would be better done by individuals and businesses who have a vested stake—through the profit motive—in achieving success.

We see this in spending programs, and we see it in taxing programs as well. Tax policies that advantage certain economic activities are usually just another form of government spending and subsidy. And while they grant an advantage to some companies and industries, they tend to disadvantage other companies and industries.[11]

There is a simple question of fairness that I pose to his committee: Why should a company pay taxes to support government subsidies for one of its competitors? I understand that there may be political support for specific industries and companies. But we know from recent experience that the government is not good at picking winners and losers in the economy. And fundamentally, it is not the job of government to pick winners and losers in the economy.

Again, I recognize why government tries to control the marketplace by sheer power and size. I recognize it because in my post-governorship life, I see it in the private sector as well. Big businesses often struggle at innovation because they wrap innovation in a heavy veil of bureaucracy and groupthink. Good ideas bubble up from time to time, but it takes a special organization to recognize how to let it breathe, how to invest in its growth slowly, and how to let it struggle before demanding it return a profit. There are countless examples of great companies who fail to move with the market, simply because a smaller and more nimble competitor arrives first with the winning solution.

But in the private sector, when a big company is beaten to the punch, it either learns fast or gets smaller fast. That's just how it is. Big companies routinely fail because they do not adapt.[12] And while we may bemoan the loss of capital and jobs that follows, we should remember that failure is a natural part of

11. *See, e.g.*, Jeff Johnson, *Long History of U.S. Energy Subsidies*, CHEM. & ENG'G NEWS, http://cen.acs.org/articles/89/i51/Long-History-US-Energy-Subsidies.htmlhttp://www.instituteforenergyresearch.org/2013/04/10/tax-preferences-for-renewables-is-17-times-more-than-fossil-fuels/ (last visited Apr. 21, 2013).

12. *See* Ned Smith, *Why Your Business Should Embrace Failure*, BUSINESSNEWS DAILY (July 9, 2011, 10:20 AM), http://www.businessnewsdaily.com/1182-adaptive-organizations-business-survival-failure-tolerance-trial-and-error.html; David Johnson, *2 Big Companies That Missed the Opportunity to Adapt to New Technology*, BUSINESS INSIDER (Nov. 28, 2011, 6:35 AM), http://www.businessinsider.com/overcome-by-change-the-failure-of-two-companies-to-seize-the-initiative-and-master-oncoming-change-2011-11.

a competitive market. More successful business leaders experienced failure at some point in their careers. And there is little shame attached to the experience, provided one learns from it and improves after it.

The problem here is that the U.S. government will not fail. None of us will allow the government to fail. Because the institutional bias within the U.S. government—especially the U.S. Congress—is not to punish policy failure, nothing is allowed to fail. What would occur in most private organizations and institutions—failure followed by defunding—simply does not happen here.

And so I urge this committee to look carefully at all proposals and to zero out programs that do not achieve their goals. A simple expectation—one that should not be terribly controversial. But I realize this will be a new concept to many federal programs.

I want to return to the rationale behind such a process. This is not simply about making government more efficient. Government efficiency and effectiveness is a worthwhile cause, and I applaud it. I am speaking of a much more fundamental goal, which is to apply a constant break to the size of the government. To make the government a smaller part of the economy.

The impulse to do something here in Washington, D.C., to resolve problems that exist in the country, is perfectly natural. But this impulse has only made government bigger, while the problems remain. We have to ask ourselves whether the status quo—an expensive and unaffordable status quo—is the best way to address the problems that the Congress has set for itself to solve.

I thank the Committee for its attention to these issues, and look forward to answering your questions.