

Excerpt from “IOUSA Not OK: An Analysis of the Deficit Disaster Story in the Film IOUSA” by Dean Baker and David Rosnick, CEPR, October 2008

IOUSA by the Clock

Time in Film – Claim being made

3:30 – Our current standard of living is unsustainable, barring drastic action.

The only real threat to future standards of living is our health care system, with its out of control costs. If we can contain health care costs in the same way that every other wealthy country has done, then we will be able to both keep our budget deficits under control and sustain a healthy rate of growth of income.

4:18 – The problem is described as “fiscal cancer, with catastrophic consequences.”

If we can contain health care costs in the same way that every other wealthy country has done, then we will be able to both keep our budget deficit under control and sustain a healthy rate of growth of income.

6:25 – Robert Bixby describes current fiscal policy as unsustainable and headed off a cliff.

If we contain health care costs in the same way that every other wealthy country has done, then we will be able to both keep our budget deficit under control and sustain a healthy rate of growth of income.

7:00 – Robert Bixby compares the size of the 1988 budget document to the size of the 2008 budget documents, noting that the 2008 budget has several volumes.

The main reason for the increase in the size of the budget documents is that there are more requests for details and analysis from people like Robert Bixby.

8:40 – The fiscal wake-up tour “spans the political spectrum.”

Actually, it has a representative from the Heritage Foundation, a conservative think tank, and people from the Brookings Institution, a centrist think tank. It does not include anyone from a clearly identifiable liberal or progressive think tank.

11:00 – The large military and social spending of the 60s were two key factors that led to a downturn at the end of the 70s.

Actually, there is serious debate among economists about why productivity growth slowed in the 70s. It is not at clear that the budget deficits of the 60s were important factors. The slowdown of productivity growth in the 70s was almost certainly the most important factor behind the economic difficulties of the decade.

13:00 – In 1992, 22 percent of the budget was financed through borrowing and passed on to our children and grandchildren.

It is true that 22 percent of the budget in 1992 was financed by borrowing, but it is misleading to claim that it was passed on to our children and grandchildren. The economy was still recovering from a recession in 1992. If the government had either cut spending or raised taxes to reduce the deficit, then the unemployment rate would have been higher and growth would have been slower. As a result of the large deficit in 1992 the economy recovered more quickly and therefore created more wealth to pass on to our children and grandchildren.

15:10 – The film refers to ways to balance the budget, implying that this should be a target for fiscal policy.

In fact the government can run deficits forever, as long as the growth of debt does not exceed the growth in GDP. The essential condition for fiscal stability is that the ratio of debt to GDP does not rise over time.

16:00 – The films refers to deficits of \$200-\$300 billion as not doing well.

In fact, the government could sustain deficits of this size forever. With deficits at these levels, the ratio of debt to GDP would be falling.

16:29 – These deficits are described as being unsustainable over the long run.

Deficits in the range of \$200 billion to \$300 billion can be sustained indefinitely. If the U.S. government ran a deficit of \$300 billion annually for the next hundred years, then the ratio of debt to GDP would fall to less than 4 percent.

17:10 – The film reports the 2008 deficit as \$410 billion.

It doesn't note the fact that the recession was a major factor increasing the size of the deficit in 2008.

17:31 – The film refers to the fact that the U.S. government had just 5 surpluses in the last 40 years.

It would have been worth noting that the deficits were sufficiently small so that the debt to GDP ratio fell consistently from the end of World War II to the 1982. The ratio of gross public debt to GDP fell from 121.7 percent at the end of the war to 32.5 percent in 1982.

18:08 – In less than 10 years, Social Security will pay out more than the program takes in taxes.

This fact is completely meaningless from the standpoint of Social Security. The program is projected to hold more than \$5 trillion in government bonds at that point. The Congressional Budget Office projects that these bonds, together with annual tax revenue, will be sufficient to keep the program fully solvent until 2049 with no changes whatsoever.

The fact that Social Security will pay out more than it collects in taxes in ten years also has no meaning for the budget as a whole. Once the annual surplus of tax revenue over spending peaks and begins to decline, Social Security imposes a strain on the rest of the budget in the sense that it is lending less money each year than it did in the prior year. The peak was hit in the 2008 fiscal year.

18:59 – Senator Judd Gregg says the debt absolutely guarantees that our children will have a worse quality of life than we do.

None of the standard projections from the Congressional Budget Office, the Office of Management and Budget or any other authoritative source supports Senator Gregg's assertion.

19:40 – Alice Rivlin blames just 3 programs (Medicare, Medicaid and Social Security) for most of the deficit problem.

The problem with Medicare and Medicaid is the broken U.S. health care system. Social Security will be fully financed from its designated tax until 2049. Therefore, it makes no sense to blame Social Security for the budget problem. The projected increase in its outlays over the next four decades is covered by taxes already collected or that will be collected.

22:22 – The film shows a young woman complaining that government debt is like her parents incurring serious credit card debt and expecting her to pay it off.

Actually, this woman will inherit a much wealthier country than her parents did. In fact, she may even inherit a claim to some of this debt if her parents pass on government bonds to her.

27:00 – Robert Rubin says that there are very difficult trade offs in cutting spending or raising taxes.

It would have been worth mentioning reforming the health care system as a third possible way to deal with excessive deficits.

27:37 – The film talks about projections of government surpluses long into the future at the end of the 90s.

A substantial portion of the surpluses in the late 90s and the projected surpluses for future years was attributable to capital gains tax revenue associated with the stock bubble. The fiscal picture would not have appeared so bright in the absence of the bubble.

30:30 – The film complains about families spending more than they earn.

It would have been appropriate to mention the extent to which the ephemeral wealth of the stock bubble in the 90s and the housing bubble of the current decade led people to consume more and save less. Those who were concerned about insufficient savings should have been warning about these bubbles.

31:30 – The film complains about easy credit and a consumption oriented society.

See comment above.

32:50 – Representative Ron Paul complains about inflation.

This is a peculiar comment since the rate of inflation had remained remarkably low through most of the period in question. There was an increase in the rate of inflation in 2007 and in the first half of this year, but this appears to have dissipated quickly.

37:30 – Former Federal Reserve Board Chairman Paul Volcker tells viewers that the lesson of the 70s is “don’t let inflation get started.”

As noted above, this experience seems not to apply to the current decade, since inflationary pressures have quickly dissipated.

38:00 – The late Tim Russert is shown saying “prices are sky-high.”

As noted above, this experience seems not to apply to the current decade, since inflationary pressures have quickly dissipated.

38:20 – The film shows the headline: “fiscal crisis looming.”

It is not clear to what this is meant to refer.

43:00 – The film asserts that inflation most hurts those who are least well off.

It is not clear what evidence the film has for this claim. Some less well off people, for example Social Security beneficiaries, are protected against inflation because their benefits rise in step with the rate of inflation. In general, borrowers – such as people with mortgage debt – are benefited by inflation, while lenders are harmed.

43:30 – Greenspan asserts that the Federal Reserve Board’s monetary policy can’t affect saving.

This is not true. Under Greenspan, the Fed allowed the growth of first a stock bubble in the 90s and then a housing bubble in the current decade. Families increased their consumption believing that this bubble-generated wealth was permanent. If the Fed had pursued policies to burst these bubbles then the saving rate would have been higher.

44:00 – The movie asserts that “money must hold its value for people to save.”

Actually, the savings rate was fairly high in the 70s, the decade when the country experienced its worst period of inflation in the post World War II period.

45:50 – The movie ranks countries by the size of the trade deficit.

The United States has the largest economy in the world. It would not be surprising that it would have the largest trade deficit, if it were running a budget deficit. The proper way to make international comparisons is to show the deficit as a share of GDP.

47:45 – Warren Buffet comments that the U.S. has consumed considerably more than it produces for the last 6-8 years.

This is due to the over-valued dollar.

51:00 – The film asserts that we are dependent on foreign countries to finance the budget deficit.

This reverses causation. If foreign countries chose not to buy U.S. government bonds, then the dollar would fall. This would reduce the size of the trade deficit, thereby increasing domestic savings. With higher domestic saving, the United States could finance its own budget deficit.

54:55 – The film reports that China’s money is invested in Treasury bonds that could be pulled out.

What matters is that China is investing in U.S. financial assets, not that they are investing in U.S. Treasury bonds. While it is unlikely that China would maliciously sell its dollar holdings, it would cause the United States economy just as much trouble if China suddenly sold \$1.5 trillion of stock as if its sold \$1.5 trillion of government bonds.

57:00 – The film shows a news announcement reporting that China is holding treasury bonds that it could threaten to unload.

See comment above.

60:00 – Warren Buffet says that in 20 to 30 years, if 2 or 3 percent of GDP goes to service the foreign debt, then it would lead to political instability.

There is no obvious basis for this assertion. There are countries that devote a larger share of GDP to foreign debt service (e.g. New Zealand) without any apparent problem.

62:30 – The film presents a person commenting that “hopefully we will be able to turn deficit clock backward.”

While it is essential that the debt to GDP ratio be kept at a manageable level, there is no obvious reason that paying off the national debt should be a goal.

63:50 – The film notes the shift from surpluses in 2000 to deficits.

This discussion neglects to mention the impact of the stock crash and recession on the deficit.

69:03 – Former Defense Secretary Donald Rumsfeld is shown saying we can’t track \$2.3 trillion of transactions.

There is no context or explanation for this comment. For example, viewers have no idea if this refers to decades of transactions or just a relatively small number of years. We also don't know if it means that we have no idea how the money was spent (this is very unlikely), or just that we don't have full accounting for these transactions.

71:20 – The film adds the current debt plus projected future spending on Social Security, Medicare, and Medicaid over the next six decades to get a deficit of \$53 trillion.

It is unlikely that any viewers would have any idea of where this number comes from or what it means, although it is no doubt very scary. The bulk of this debt figure stems from the projected explosion of private sector health costs.

71:40 – The film asserts that if current trends continue, we would just have enough money to pay interest and some Social Security payments or we could double federal taxes.

Alternatively, it could have reported, “if we don't fix the private health care system, we would just have enough money to pay interest and some Social Security payments or we could double federal taxes.”

72:00 – Bush tax cuts are just 10% of the problem, the Iraq War just 3 percent.

These problems are small compared to the projected cost of Medicare and Medicaid, due to the projected explosion of private sector health care costs.

73:00 – When baby boomers retire there will be a tidal wave of spending.

There is projected to be a tidal wave of spending because of the projected explosion of private sector health care costs. If the health care costs follow their projected path, there would be a tidal wave of spending even if we did not have a large number of retiring baby boomers.

75:00 – Robert Rubin tells viewers that there is no free lunch.

Actually, eliminating waste in the health care system by reducing payments to drug companies and highly paid medical specialists, and adopting a more efficient health insurance system, would seem like a free lunch to almost any one who does not derive their income from these sectors.

81:00 – The film tells viewers that debt of \$56 trillion is \$184,000 for every American.

Most viewers have no idea of where this \$56 trillion figure comes from, as noted above. Most of this debt is attributable to higher Medicare and Medicaid costs due to the projected explosion of private sector health care costs. It would also be helpful to tell viewers that this debt is equal to approximately 7 percent of projected income. This would be far more informative.