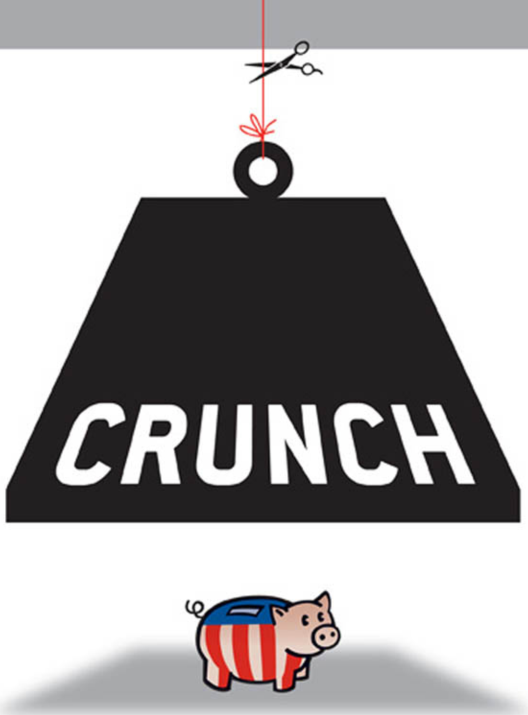

CRUNCH

WHY DO I FEEL SO SQUEEZED?

(AND OTHER UNSOLVED ECONOMIC MYSTERIES)

JARED BERNSTEIN

an excerpt from

Crunch
Why Do I Feel So Squeezed? (and Other Unsolved Economic Mysteries)
by Jared Bernstein

Published by Berrett-Koehler Publishers

Contents

3

Political Economy 202

4

The World Ain't Flat As All That

5

The Reconnection Agenda

Preface

My name is Jared and I am a practicing economist.

I made my first graph decades ago, and while it sure felt good to see the way the bars lined up, I figured I could control the impulse. After a while, I was making several graphs and tables per hour, and talking earnestly about inflation, supply and demand curves, and Federal Reserve policy. I still thought I could stop whenever I wanted to.

It hasn't worked out that way. In fact, it's gotten much worse. I now go on TV shows and have raging arguments about tax cuts, trade balances, the minimum wage, and unemployment. Maybe you've seen me while flipping through the channels. Maybe you've wondered, whatever's got this guy so wound up?

I'll tell you. Economics has been hijacked by the rich and powerful, and it has been forged into a tool that is being used against the rest of us. Far too often, economists justify things many of us know to be wrong while claiming the things we believe are critically important can't be done.

I can't tell you how many times I've seen smart people with good hearts crumble in the face of economic arguments. Many of us will defer to such arguments, no matter how nuts these arguments seem, because they come shrouded in the mysterious authority of science. You might want to argue that unemployed people need a safety net when they lose their job, for example, but you're prone to back off the minute some economist points out how that will lead to "European levels of unemployment" or how it will "kill the person's incentive to find a job."

Maybe you've wondered whether all the tax cuts targeted at wealthy investors are really so necessary, especially given that we're spending borrowed money, only to be reminded that these tax cuts will spur investment and growth. Don't you get it? the story goes: We can't afford *not* to cut taxes!

At most, you might muster the gumption to say, "Well, I'm not an economist, but that doesn't sound right to me."

Well, I am an economist, and if I may ironically borrow a phrase from Ronald Reagan, I'm here to help.[1] It doesn't sound right to me either, and that's because it's wrong.

I'm tired of being stuck in the studio engaging in rants with Darth Vaders with PhDs. Wouldn't it be more useful to have an open-ended, rant-free dialogue with real, everyday people about their economic questions?

Maybe you've been wondering, is Social Security really going bust, and what does that mean to me? If I hire an immigrant, am I hurting a native-born worker? How much can presidents affect economic outcomes? What does GDP measure and what does it leave out? How come child care workers make so little? What does the "Fed" do, anyway? What's the cost of ignoring global warming? What's a "living wage"? And what *is* up with all those high-end tax cuts?

And of course, one that looms particularly large in the pages that follow: Why do I feel so squeezed?

In the following pages, I answer these and other questions. Though I sometimes tweaked them a bit, I did not make these questions up, nor did I poll my wonky economist friends. The questions come from non-economists, mostly taken from e-mail questionnaires and the blogosphere, where I've been having entirely too much fun "talking" about progressive economics and trolling for good questions.

What's a "good question"? Good question. I've got one main criterion. A good question, in the *crunchian* sense, is one that comes out of your everyday life as you interact with the economy, like the "Why do I feel so squeezed?" example above. Sometimes these quesitons grow out of people's run-ins with policy matters that leave them perplexed. The other night, for example, when my wife and I were burning far too many brain cells trying to figure out my employer's new health care plan, she started peppering me with questions about why our health care system is such a mess (jeez, you'd think a guy could catch a break at home . . .). A question might involve a moral dilemma, like the predicament of the woman who wondered if she should worry about the incentives involved in giving a dollar to a homeless person.

And lots of people wanted to learn what to make of key economic statistics, like gross domestic product and unemployment figures. What are they telling us? What's left out? For example, why, asked a perplexed but observant questioner, does the stock market often rise when the unemployment rate goes up? Seems counterintuitive, no?

Think of this book as a chance to hang out with someone who likes to tackle questions like these and promises to try to answer them in an engaging, non-jargony way. Come on, what do you say? How about it? Hey, where are you going? Get back here! Lemme show you this graph—I'm just getting started!

Introduction: So What Is Economics, Anyway?

So a doctor tells this unfortunate woman that she has but six months to live. "Isn't there anything I can do?" she pleads. "Marry an economist," the doctor replies. "It won't cure the illness, but it will make the six months seem like five years."

We might as well start with the basics, and I promise this won't take anywhere near six months.

I recently completed my toughest speaking gig of the year: I taught an economics lesson to my first-grader's class. The goal was to teach them the fundamental concepts of needs versus wants, goods versus services, and scarcity. These distinctions are critical, because a good working definition of economics is the following:

The economy is the way we organize our society to best provide the goods and services that we need and want. Economics studies the best ways to do this.

They quickly got the needs/wants distinction, but they raised some fascinating questions. They got that housing is a need. But someone then asked, "What about a mansion?" (Just to be sure, I asked them if they knew what a mansion was. "A big house with lots of cobwebs," they said.) They discussed that and determined that a mansion is a "want," not a need. Smart kids, I thought.

Anyway, all I'm saying is that anybody of any age can get this stuff. In fact, to not get it, to give up because it's too obscure, is, as I will show, a profoundly important political act, one with damaging consequences.

The stakes are high, for ourselves and for those who come after us—too high to entrust to those whose agenda is to redistribute power and resources to themselves and their friends.

Am I really suggesting that evil people disguised as social scientists are out to rob us blind while we willingly sign on the dotted line because we don't get the math?

No, not at all, though many powerful political and corporate actors use economists and economic (il)logic to do just that.

It's just that there are countless ways to organize our society to "best provide the goods and services that we need and want." In other advanced economies—in those of Europe, Canada, Scandinavia—they answer this question quite differently from the way we do. For example, they take access to health care services "out of the market," based on the beliefs (a) that health care is a basic right in an advanced society, and (b) as discussed in some detail later, that there are special attributes of health care that make unregulated markets a particularly inefficient (read: wasteful) way to deliver and provide it. And you don't have to get on a plane to learn the lesson that there are different ways to organize the economy. In other periods within our own history, we organized things differently, too.

This question of how we organize the economy matters a lot. It determines how the benefits of growth are distributed. Even more important, it determines who gets the opportunity to realize their potential. If the best educational opportunities go to the haves, their position relative to the have-nots will become etched in stone, as economic mobility atrophies. If those in political power believe—and act on the belief—that labor standards, like minimum wages, overtime, or the right to collectively bargain, are harmful to economic growth, then the ability of some workers to bargain for their fair share of the growing economy will evaporate while that of others grows stronger. How we organize our economy determines how we structure our response to the challenges from environmental degradation, globalization, the lack of health coverage, and staggering wealth inequalities.

When answering the questions that follow, three unifying principles kept coming up. I'll come back to these often, as I found them to be useful navigational tools, providing the intellectual and moral guideposts needed to keep us moving in the right direction—toward an economy that works best for all.

BASIC PRINCIPLES OF CRUNCH-STYLE ECONOMICS

1. Economic outcomes are generally thought to be fair, in the sense that market forces dole out rewards to those who merit them. But that's not always the case. Power, whether it's based on political clout, wealth, class, race, or gender, is also a key determinant of who gets what.

2. Economic relationships often play out in surprising ways, contradicting both basic logic and textbook theory. The path to economic truth is paved with evidence, not assumptions.

3. Since economics is concerned with finite resources, economic decisions often invoke trade-offs: choosing one outcome over another. Though these trade-offs are usually thought of as the benign outcomes of rational discourse, it's not so: See #1.

As I hope these principles suggest to you, the goal of this book is not simply to help readers become better versed in economic discourse, though that's part of my goal. It's also to offer a new way to answer the question, how can we best organize our society to provide the things we want and need? America is a democracy, and in a democracy we all get to weigh in on biggies like this, not just the elites and their scholarly shock troops.

With that in mind, let's get to work.

Crunchpoint:* **Economics is not an objective, scientific discipline. It is a set of decisions about how to produce and distribute resources and opportunities. Understanding**

* *Each question and chapter in the book ends with a "crunchpoint," an allegedly snappy summary of the discussion.*

and evaluating the logic and rationales for those decisions, while recognizing whom those decisions favor or exclude, is a big part of what this book is about. To proceed with these insights foremost in our minds is the only way I know to rechannel the power of economic analysis back to the service of those who need it most: the ones in the vise grip of the crunch.

1

The Big Squeeze

Why do I feel so squeezed?

As I solicited questions for this book, the one above kept coming up, in one form or another. And while I'm not happy about that, it is affirming, because it is, in my view, the great, unanswered economics question of our time.

It's not that middle-class people are sliding into poverty, hunger, and homelessness, though in an economy as wealthy as ours, too many people do face those conditions. The sense I got from questioners, a sense I've tried to convey in the answers I offer below, is that something is "off" in the new economy. We hear great economic news about financial markets, prices, profits, growth, productivity, and globalization, yet many of us live with a weight of economic anxiety that our parents would not have recognized. Most of us are making progress as we age, but the path seems steeper than we might have expected, with deeper potholes along the way. For some of us, things we aspire to, like secure health care or the ability to send our kids to a good college without taking on a lot of debt, are still within our grasp, but we have to reach farther to grab them, and it's harder to hold on.

For others of us, a bit farther down the income scale, these aspirations are fading. To our surprise, we find ourselves without health coverage, or unable to afford the premiums and co-payments. We're stuck in a house and a neighborhood we thought we'd have grown out of by now, with a school to which we'd rather not send our kids. And while we're working as hard as ever, that paycheck is alarmingly thin after gas and groceries.

Not everyone feels that way. Raise the issue of the squeeze, and many economists and policymakers will excitedly (and correctly) remind you productivity is soaring! . . . unemployment's historically low! . . . inflation's down!

How do I know this? Because I'm a regular on CNBC's *Kudlow & Company*, a show that focuses largely on stock and bond markets. It's almost infectious, the way Larry Kudlow and his guests from the world of financial markets bubble over with effusive, heartfelt praise for all those positive trends just mentioned. To them, for example, globalization means a greater supply of capital and labor, "more global liquidity," lower prices, lower interest rates, and a lot more people with whom to make trades. To millions of others, globalization means greater wage competition and less job security. They're both right.

I'm fortunate that these financial market mavens will at least entertain a different perspective, but no matter how many times I point out that the typical working family's purchasing power—its inflation-adjusted income—is actually down over their beloved economic boom, they can't hear me.

Why not? Well, like they say, denial ain't just a river in Egypt. It's a place to which lots of economic elites retreat so that they can avoid the tough question, what's behind the divergence between the macroeconomy and the microeconomy, between stock portfolios and paychecks, between the view from Wall Street and the view from Main Street?

Let us begin by presenting some evidence, and then tackle that critical question.

The statistics behind the squeeze are embarrassingly easy to come by. Anybody with a mouse can stop puzzling over this after a precious few clicks.

- The economy grew by 15 percent between 2000 and 2006, but the inflation-adjusted weekly earnings of the typical, or median, worker were flat (down 0.7 percent; the *median* is the worker at the 50th percentile, right in the middle of the wage scale).[1]

- Partly due to the jobless recovery that lasted until mid-2003 (I discuss recessions and recoveries later on), the typical working-age household's income was down 5 percent, or $2,400, from 2000 to 2006.[2] Their income was down more than their wage because they found fewer available hours of work.

- After falling steeply in the latter 1990s, the share of the population that's officially poor rose from 11.3 percent in 2000 to 12.3 percent in 2006, the most recent available data point for poverty rates.[3]

- While inflation overall has been moderate since 2000, as I point out below, the costs of some of the key components of the middle-income market basket—health care, child care, college tuition, housing—have been growing much faster than the overall average of all prices taken together.[4]

That's a lot of numbers, but let's not gloss over them. Over the course of this highly touted economic expansion, poverty is up, working families' real incomes are down, and some key prices are growing a lot faster than the average.

Now, I know you don't hear about such numbers every day—instead, you hear about the stock market every hour. But these statistics are not secret.

It's obviously important to document the facts, but it's also useful to look beyond the statistics to people's own views about the economy. Such views jump around to some extent with highly visible indicators like gas or home prices, but in one weekly poll (ABC–*Washington Post*), more than half of respondents have registered negative impressions about the economy since the summer of 2001. Clearly, dissatisfaction with the Iraq War dominated the 2006 midterm elections, but the economy was next in line. According to the *New York Times* exit poll, two-thirds of voters in November 2006 reported that they were either just maintaining their living standards (51 percent) or falling behind (17 percent). By 2007, 44 percent said they lacked the money they needed "to make ends meet," up from 35 percent a few years earlier.[5]

Remember—this is a critical part of the story—the cheerleaders are right, in their own narrow way. While all these unsettling poll results were coming in, the economy was expanding at a good clip and generating stellar rates of productivity growth.[6] We were achieving efficiency gains at a rate that hadn't been seen in over 30 years. The unemployment rate was low in 2006–07, below 5 percent. The stock market took a dive in late 2000, but by the end of 2006 it was up 56 percent from its '03 trough. Five years into this recovery, corporate profits as a share of national income were at a 56-year high and were percolating along at a rate more than twice the average of past recoveries. Yet more than 4 in 10 told pollsters they were having trouble making ends meet.

What this barrage of percentages is telling us is that if you feel squeezed, chances are it's because you *are* squeezed. Most of the indicators that matter most to us in our everyday lives—jobs, wages, mid-level incomes, prices at the pump and the grocery store, health care, retirement security, college tuition—are coming in at stress-inducing levels, but gross domestic product (GDP), our broadest measure of the economy's health, explained later, keeps on truckin'.

Something's wrong, something fundamental. Not Third World–poverty fundamental, not blood in the streets, massive homelessness, or Great Depression fundamental. If the problem were that obvious, it would be less amorphous, less indecipherable, less of a head-scratcher.

The name of the problem is *economic inequality*, and it's been on the rise for decades. It's at the heart of the squeeze, and it's a sign that something important is broken: the set of economic mechanisms and forces that used to broadly and fairly distribute the benefits of growth. What "mechanisms" am I thinking of? They are unions, minimum wages, employer and firm loyalty, global competitiveness, full employment, the robust creation of quality jobs, safety nets, and social insurance, all of which are discussed in the following pages.

The belief that growth should be fairly distributed, that the bakers should get their slice, is a fundamental economic value in America. It is, of course, not one we have always lived up to, especially for the least advantaged among us. But it's always there, this sense that the rising tide should lift the rowboats and the houseboats, not just the yachts. When the lesser boats founder, people know it. And that's where we are today. Bill Clinton won an election appealing to those people in 1992, various senators and congresspeople did so in 2006, and, from what you could hear as the 2008 campaign season got under way (much too early for the taste of most of us), the Democratic presidential candidates were tapping directly into the same set of values.

Now, you won't hear this description of our economic challenges from most op-ed writers, any presidents, or central bankers. Their answer to the inequality question comes down to one, and only one, solution: more education. They believe that the reason the economy is passing so many folks by is that they don't have the smarts and skills to cash in on the opportunities we're creating.

The education mantra is a clever framing because (a) it rings true—you're always better off with more education, and (b) it subtly puts the burden on you. The message is, "The opportunities to get on the right side of the inequality tide are there, if you're smart enough." If you're not, well, then, either smarten up and join the parade or stop whining. As one U.S. Treasury official put it, "If the country . . . is going to undergo economic growth, then the population has to be able to take advantage of opportunities."[7] Or, as President George W. Bush elliptically put it, "We have an economy that increasingly rewards education and skills because of that education."[8]

Ten years ago, he would have been at least partly right. Today, education is neither the main cause of nor the main solution to the inequalities we face.

I deal with this in greater detail in a later chapter, but for now, I'll assert that inequality is no longer being driven by the highly skilled pulling away from the rest of the pack. Yes, you're far better off with a college education than without, but that degree won't insulate you from global competition. Especially if your work can be digitized and offshored, there are highly skilled but low-paid workers in other countries with whom you now compete. The real wages of American college grads rose less than 2 percent from 2000 to 2006.

Yet, while college grads are beginning to feel the same competitive pinch that the blue-collar workers have felt for years, the share of income going to the top 1 percent of households in 2005 was, at 22 percent, higher than in any year since 1929!

Therefore, a simple “big skills get big rewards” story just doesn’t cut it today. To understand what’s behind today’s inequality, something to which I devote considerable time in the coming pages, you’ve got to deal with principle #1: POWER. More so than in any recent period, those who hold a privileged position in the economic power hierarchy, the players who sit down at the poker table with a stack of chips reaching to the ceiling—the CEOs and the holders of large capital assets—are able to steer the bulk of growth their way. Then, using their political connections, they’re able to ice the cake with a nice bit of after-tax redistribution, as regressive changes in the tax code funnel even more resources their way.

The rest of us—those who sit down with a modest stack of chips—are left trying to figure out . . . well, like it says in the title, why do I feel so squeezed?

Crunchpoint: **You feel squeezed because you are squeezed. If this were just a growth problem, we could have a nice, polite discussion of ways to get productivity humming again, or how to bring down the unemployment rate. But productivity’s been great and unemployment’s low. The squeeze is on, and we won’t be able to call it off until we deal with our inequality problem.**

this material has been excerpted from

Crunch
Why Do I Feel So Squeezed? (and Other Unsolved Economic Mysteries)
by Jared Bernstein

Published by Berrett-Koehler Publishers
Copyright © 2008, All Rights Reserved.
For more information, or to purchase the book,
please visit our website
www.bkconnection.com