

Reich Takes on Simpson – And We Do the Fact Checking

October 27, 2016

by Robert Huebscher

This article is part of our Schwab IMPACT 2016 Special Coverage this week. More articles are listed [below](#).

Robert Reich, a prominent Democrat, and Alan Simpson, a distinguished Republican, engaged in a friendly debate to discuss issues that they said were not addressed during this campaign season. But on crucial subjects, both relied on out-of-date and inaccurate reasoning.

The debate, which took place yesterday, was a keynote presentation at the Schwab IMPACT conference, held in San Diego. It is the largest conference in the industry, attracting approximately 2,000 advisor attendees.

Reich is a political commentator, economist, professor and author. He served in the administrations of Presidents Gerald Ford and Jimmy Carter, and was Secretary of Labor under President Bill Clinton from 1993 to 1997. He is a professor at the University of California, Berkeley.

Simpson served from 1979 to 1997 as a Senator from Wyoming. In 2010, Simpson was appointed by President Obama to co-chair the National Commission on Fiscal Responsibility and Reform with Democrat co-chair Erskine Bowles of North Carolina.

I'll look at the positions they took on key issues and provide my own comments to highlight their factual errors.



Robert Reich



Alan Simpson

Budget deficits

Simpson claimed that the biggest unaddressed issue was the federal debt, and reminded the audience that he wrote a report with Erskine Bowles about how the country was “going broke and needed shared sacrifice to save itself.” The reaction to the Simpson-Bowles recommendations, he said, was that “everyone ran for the exits.” Simpson claimed that two-thirds of the American budget is not being addressed – it is the cost of healthcare and is “on autopilot and cannot be stopped.”

Reich agreed with Simpson on the dangers posed by the federal debt. He said that the U.S. debt-to-GDP ratio is about 75% - “that’s high but not as high as after WWII – and is being driven by aging baby boomers and healthcare costs.” When those two forces converge, he said, “there will be a debt explosion.”

Reich was a trustee of the Social Security and Medicare systems. He said that Medicare is the big problem, and that Social Security can be fixed “without dramatic changes.”

The view that the U.S. faces a debt crisis was popularized by Reinhart and Rogoff in their book, *This Time is Different*. But it is by no means the consensus view. At no time in history has a country with the reserve currency defaulted on its debt or faced a sovereign debt crisis. Both the U.S. (as Reich noted) and the U.K. (prior to the Industrial Revolution) have had much higher debt-to-GDP ratios than the U.S. does now, and in both cases periods of extraordinary growth ensued. Moreover, many prominent economists argue that the federal government should run a permanent deficit, and that federal surpluses must be accompanied by private-sector deficits (e.g., lower profits for corporations). Neither Simpson nor Reich acknowledged those facts.

Healthcare

Simpson claimed that the absurdity of healthcare is that consumers are insulated from costs. For example, patients are generally unaware of and unconcerned with the costs of procedures that are covered by insurance. He said that Americans are spending more on healthcare than other developed countries, yet our life expectancies are less. He said, “We spend more and get worse results.”

Reich said that the problem with healthcare is that it consumes 18% of federal expenses, and he agreed with Simpson that our life expectancies are lower. The biggest single driver of healthcare costs, he said, is pharmaceuticals, and second is the administrative costs of running hospitals. The growth of those costs could be slowed, he said, but instead the government has made deals to cut back on the use of generic drugs, limit the import of Canadian drugs, and to reduce the government's power to negotiate on drug costs. "This is big pharma working its power," he said.

The question should not be whether the U.S. spends more on healthcare than other nations, but whether we spend more on federal services that impact health. Those other non-healthcare services include so-called safety-net programs, such as subsidized housing, transportation, shelter and food stamps, all of which impact an individual's health. The U.S. spends less on those programs than other nations. But when healthcare and safety-net expenses are considered together, it is not clear that we spend more than other countries. U.S. life expectancies at birth are lower than those of other developed nations; but our life expectancies at age 35 are comparable. The reason is that the U.S. has a higher murder rate and it claims lives of those under 35. There is no factual support for the notion that U.S. health outcomes are inferior to those of other nations. It is also misleading to say that pharmaceutical costs are the biggest driver of healthcare costs. Although drug costs are increasing at a faster rate than other components of healthcare expenses, they represent only about 10% those expenses.

Social Security

Both Reich and Simpson acknowledged that the Social Security program, if unchanged, faces a shortfall.

Reich said that there are three ways to deal with Social Security. The government can raise the age of eligibility (it was 65 when Social Security was created by FDR, at a time when the life expectancy was 61); the government can increase the cap on income subject to Social Security taxes. Or it can adopt means testing. "If you do this in the next four years, Social Security is fine," he said.

Simpson said that the AARP has lobbied against reasonable increases in the eligibility age. He also said that some have made the claim that, if you raise the cap on income, people won't work as hard.

Reich and Simpson are generally correct in their assessment of the Social Security program. The challenge with raising the eligibility age is that it has a greater impact on blue-collar workers, who generally do not have as long a working career as white-collar workers.

Tax code reform

Simpson said that tax-code provisions – like home mortgage interest deduction – are "tearing the country to shreds." Nobody will touch them, he said. "There are buildings in Washington that exist to protect those things."

Reich said those provisions are hugely beneficial to the wealthy and are regressive. In addition to mortgage interest, he included tax-deductible healthcare and tax-deferred retirement saving.

The political climate

Simpson said "there is a lot of hatred," and its targets include Trump, Clinton, Paul Ryan and Harry Ried. "That is the most dangerous thing going on in America today." He said the hatred came from when the Democrats controlled the House for 40 years, starting in 1955, during which time they "treated Republicans like slaves." The Republicans revolted.

Reich said the venom began in 1995 with the "Gingrich crowd." He said that money from outside Washington is "distorting the legislative process, and makes it impossible to deal with debt or tax reform, even if the two parties were working together."

Simpson said he agrees with Clinton that Citizens United should be overturned and called it "the worst decision of any court." He said that first amendment rights were intended to protect individuals, not corporations. Reich said, tongue-in-cheek, he would be okay with Citizens United as soon as the Supreme Court executes a corporation.

An economic tipping point

Simpson said that a tipping point will come when China or another creditor refuses to buy or reduces its commitment to Treasury securities. He said that would lead to a rise in interest rates and inflation and would "suck the guts out of the discretionary budget. The little guy will get hurt."

Reich said there will be no such tipping point. If China were to do this, it would “stick it to us gradually.”

Reich is more correct. If China were to reduce its commitment to buy U.S. securities, it would have to increase its commitment to another currency, say the euro. That would decrease the value of the dollar and increase the value of the euro, which would trigger an offsetting move by European countries. European countries would sell the euro and buy the dollar. The net result of those moves would be no substantial change in the relative value of the currencies.

Why are Americans so angry?

Reich said that Trump and Bernie Sanders represent an anti-establishment surge that hasn't been seen since George Wallace in 1968. He said that he is not equating Trump to Sanders, though. Both parties were surprised about the success of those two candidates. “This is a tipping point politically,” he said.

Simpson said the anger comes from people getting tired of saying we can solve problems without touching Medicare or the military or healthcare budgets. “That is a lie,” he said, and Americans realize this. “When you've got things that are untouchable, and everyone knows they must be touched, it is frustrating.”

Reich said that something else irks people. Both Sanders and Trump would increase the deficit. Instead, it has a lot to do with the fact that so many people in the country are going nowhere. The median wage has not increased in 25 years, he said.

It is true that the median real wage has not increased appreciably in the last 25 years, based on the way the government measures the data. But Reich is wrong when he says that so many people are “going nowhere.” The standard of living for the median American (or for the lower 10th decile American) has increased dramatically over the last 25 years. Think about the improvements we have in technology, healthcare, the Internet, vehicular safety and food quality. None of those increases in our standard of living are accurately reflected in the government-reported data.'

Governance

Simpson said that whomever governs will do so in an “ungovernable country.” If Trump doesn't accept the results there will be chaos, he said. Simpson said that Gary Johnson, a third-party, lost his credibility when he thought “Aleppo was dog food.” But he said his running mate, William Weld, would have been an effective candidate. Johnson, he said, “has been wrapping his ideas in paper.”

Reich said that, with winner-take-all at the state level in the Electoral College, you can never get a successful third-party candidate. Ross Perot never got an Electoral vote, he said, despite getting approximately 20% of the popular vote. The same happened with Teddy Roosevelt and the Bull Moose Party in 1912.

Reich said the reason for political divide is because of gerrymandering. All the “action” is in the primaries, where candidates tend to be very extreme. General elections are safe, he said. Gerrymandering could be ended by putting the design under an independent citizen's commission, which he claimed has been done successfully in California.

Simpson agreed that gerrymandering is “killing the system.” Americans believe the system is corrupt, but very few politicians really are, he said.

Immigration

Reich said that about 11 million of our population is here illegally. “It's bad for them,” he said, “because they have become second-class citizens and get abused by employers and have no recourse.”

Simpson said he introduced bill to provide a path to a green card and called it “legalization” instead of “amnesty.” He wanted to increase the workforce and protect employers. But he said flash words like “amnesty” and “ID cards” prevented this from happening. Republicans will “wise up,” he said, after they see what happens with the Hispanic vote in the current election

Reich said that If Democrats and Republicans can enjoy each other as much as he and Simpson did during their debate, we can have a better country. Simpson concurred.

This article is part of our Schwab IMPACT 2016 Special Coverage this week. Check out our other articles:

[Liz Ann Sonders: Don't Fear a Recession or Market Overvaluation](#) Oct 25, 2016 9:16a

[Greg Valliere - Two Possible Election Outcomes](#) Oct 25, 2016 12:02p

[Rick Rieder - The Fixed Income Outlook for 2017](#) Oct 26, 2016 10:22a

Ian Bremmer – We Face a Profound Geopolitical Recession Oct 26, 2016 10:28a