



Politically or Economic Correctness: where is my Grant?

In an age when being “pc” doesn’t mean you are computer literate, isn’t it about time to speak the obvious? We have a major economic mess on our hands but the focus in Washington D.C. is on political correctness. No one can applaud the fact that our newly designated Treasury Secretary had problems observing our tax laws. Nor does one have to repeat Caesar’s admonition to his wife (“be above suspicion”) to remind the President that a vetting process is for his protection as well as ours. The President has already given us a *mea culpa*, but he now must be reflecting on that other President from Illinois who searched for some three years to find a General who would carry out his military-political plan. One can imagine President Obama as he tries to find a way through the economic wilderness, muttering to himself, “Where is my Grant?” Our civil war is not secession. It is a recession threatening to run into economic disintegration. Leadership, as it always is in Washington, is at a premium.

Financial markets have been left hung out to dry because the TARP was Plan A, and there is no Plan B—at least so far. Without a clear plan to (1) get the banks functioning again, (2) create a viable exit for our mortgage crisis; and (3) prioritizing the stimulus plan, economic policy is at a standstill. The White House has not gotten its priorities clear as between righting the wrongs against the middle class, cleaning up the environment and actually stimulating the economy, but the recent Op Ed by Professor Alan Blinder in today’s WSJ suggests that even “liberal” economists are moving to a centrist position. Blinder correctly identifies the “time is of the essence” aspect of the current proposals. Much of the meat comes too late for the dinner. What is critical is raising personal disposable income and that means focusing on tax reductions and transfers with some serious thoughts as to mitigating the mortgage crisis. Blinder has suggested that we chop the payroll tax severely (although for some reason, he doesn’t seem to advocate chopping it on the employer side?). He is even willing to see the Federal Government induce States to create a sales tax holiday and the revenue loss be made up by Washington. If we can move from there to a proposal that embodies cutting personal income tax rates; corporate tax rates and other taxes on the returns to capital, we are well on the way to creating a stimulus plan that has a chance to increase real disposable income now, not in 2010 when the problem will be even larger, but starting right now!

Moving on the tax and transfer front rather than getting bogged down in determining whose pork gets served to which region, the President could show real leadership where it is badly needed. Sorting out the methodology of addressing inadequate bank capital and who should administer Bad Bank or Bad Banks or whatever the formulation is for toxic asset holding, is a pressing need. What counts is getting the economics right, not the politics of capping executive compensation.

Mr. President: It is time to focus your thoughts. Bank executives may well have been paid too much and maybe some heads should roll. In the totality of what it will take to “bail out the economy,” the excess of 20 billion dollars of executive compensation is “chump change.” Whatever the morality, what counts is getting our financial system functional without emasculating the Fed through an ever increased balance sheet tied to Treasury policy. The Bond Vigilantes are already on the prowl. Witness the sudden and unwelcome lift at the long end of the curve. Mortgage re-fi costs have risen some 50-100 basis points since your inauguration. If you and your economics advisors think cheaper mortgage finance is part of the rescue plan, then you had better worry about encumbering the Fed with an endless amount of mortgage cum Treasury paper. TIPS are getting more attractive because markets see inflation in our future—maybe stagflation? The Vigilantes are asking how the Fed is going to take back all that liquidity if our economy continues moribund. Whatever the merits of an improved highway system, extending broadband and promoting carbonless energy, don’t forget your Democratic predecessor’s epic lines: “It’s the economy, stupid.” Let’s get on with economics and forget about political correctness, at least for now! Where is your Grant?