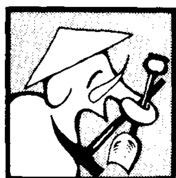
Economic policy

'No conservative will expect what is going to happen'

by David Goldman



Reagan's conservative backers are in for a bigger surprise than the Vice-Presidential selection of George Bush, according to highly-placed sources in the Reagan camp. In a way, the disputes inside Reagan's entourage are not much different than the widely publicized divergence between "old guard" Republican advisers like Milton Friedman and William Simon, and tax-cut proponents like Rep. Jack Kemp, Arthur Laffer and Jude Wanniski. But the "old guard" have not merely won, as was inevitable, but struck an unprecedented sort of economic policy deal with Carter's backers.

"It doesn't matter much at this point who's elected," says an economist at one of the Washington think tanks with close tabs on Reagan policy. "Reagan will do things no conservative would ever expect."

"There is an extremely broad consensus on policy between the administration and the Congress, and it extends into the Reagan camp as well," according to a senior Joint Economic Committee staff member.

The core of the agreement (see Economics) is a Milton Friedman-style austerity program to suppress domestic consumption, through combined monetary and fiscal restriction. Since last October, Federal Reserve chairman Paul Volcker has adopted "worse than Republican" monetary stringency measures, which he told the Senate Banking Committee July 21 would continue for the next years to come.

Contrary to the promised Kemp-Roth 30 percent tax cut, which Reagan embraced earlier in the campaign, some Reagan advisers say, all tax cuts will be linked one-for-one to cuts in spending, along the formula that current Reagan adviser Alan Greenspan devised for President Ford in 1976. That was the demand of the Friedman group—the "old guard" that includes Simon, former Treasury Secretary George Schultze, Greenspan and others, including former Fed chairman Arthur Burns. Their Committee Against Inflation is widely-known in New York financial circles as a factional operation inside the Reagan camp.

Reagan's economic gameplan is no different from the Carter administration's plan to keep the economy under water through 1981. After the weakest sectors are shaken out, Reagan will use the hated methods of dirigist economics to induce an "investment-led recovery."

Among other things, this means that the Reagan tax cut, when it finally comes, will not be oriented toward personal income—along the lines of the Kemp-Laffer-Wanniski proposal—but toward investment breaks, especially in military and export-related sectors. The Reagan group at Georgetown University's Center for Strategic and International Studies, which is the homeground of Henry Kissinger and Richard V. Allen, even expects Reagan to adopt direct credit-insurance tactics to stimulate investment in defense industries, according to a plan surfaced at the beginning of the year by liberal Democrat Henry Reuss.

Kemp adviser Jude Wanniski, the former *Wall Street Journal* editor who popularized Prof. Laffer's belief that a tax cut would pay for itself through economic expansion, disputes all this. Wanniski argues that Reagan is personally enthusiastic about the Laffer approach, fielded strongly by Jack Kemp, and will stick to it. Investment tax credits are "thing-oriented and not people-oriented," Wanniski says. "Accelerated depreciation tax credits emphasize physical capital instead of human capital." According to the Laffer theory, increases in personal after-tax income through reduction of progressive tax schedules will give individuals the incentive to produce more, raising productivity and investment.

"The Kemp-Roth stuff is a bunch of pablum," says another Reagan economist. "There's nothing wrong with using it in the campaign, but it doesn't have anything to do with economic policy."

Rep. Jack Kemp, in fact, negotiated away the Laffer doctrine in an agreement with the "old guard" to link tax cuts to spending cuts in the platform. The hard-core Laffer position, expressed by Kemp in his 1979 book *An American Renaissance*, insists that spending cuts aren't necessary.

From discussions with a large number of individuals

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in the Reagan camp, it appears that the most extremely divergent views have had simultaneous strong reassurances from either Reagan or his campaign manager, William Casey. However, in the case of George Schultze and Bill Simon vs. Jack Kemp, it's like Dracula against the Bobbsey Twins. There's no contest.

The reference point for Casey, Simon, Friedman, and others is the Margaret Thatcher government in Great Britain. Casey's gregarious exterior masks a single-minded, Jesuit-trained political operator. Since he spent most of the Second World War dropping U.S. spies into Nazi Germany, Casey's closest personal identification has been with his old friends from the British Special Operations Executive, most of whom are now behind Thatcher. Casey also has a deeply-entrenched ideological commitment to the economics of Friedrich von Hayek. Although Casey personally hates Henry Kissinger—he identified with former Secretary of State Bill Rogers when Kissinger threw Rogers out of the Nixon administration—he walks in tight enough step to tolerate Georgetown University CSIS chairman Kissinger in the direction of the Reagan campaign.

Unlike Kemp, Laffer, and Wanniski, the Reagan inner circle shares Margaret Thatcher's bitter antagonism to the European Monetary System. They see the EMS, and the efforts of Schmidt and Giscard, as virtually a capitulation to Soviet imperialism. Their predictable response is to use America's best economic resources for trade war against Europe. That is not so say that Reagan will enact major tariff barriers, but that a Reagan administration will follow many of the recommendations of the Georgetown CSIS trade project, funneling capital into electronics, aerospace, and other industries in which the U.S. might maintain export advantages.

'Tax cuts, spending cuts'

The following are excerpts from the economic policy planks of the 1980 GOP platform.

Taxes and Government Spending: Elsewhere in this platform, we have pledged for the sake of individual freedom and economic growth to cut personal income tax rates for all. Republicans believe that these tax rate reductions should be complemented by firm limitations on the growth of federal spending as provided by the Roth-Kemp Bill. The Republican Party therefore, pledges to place limits on federal spending as a percent of the Gross National Product. . . .

By increasing economic growth, tax rate reduction will reduce the need for government spending on unemployment, welfare, and public jobs programs. . . .

We believe that the Congressional budget process has failed to control federal spending. Indeed, because of its big spending bias, the budget process has actually contributed to higher levels of social spending, has prevented necessary growth in defense spending, and has been used to frustrate every Republican attempt to lower tax rates to promote economic growth.

The immediate burden of reducing federal spending rests on the shoulders of the President and the Congress. We believe a Republican President and a Republican Congress can balance the budget and reduce spending through legislative actions, eliminating the necessity for a Constitutional amendment to compel it. However, if necessary the Republican Party will seek to adopt a Constitutional amendment to limit federal spending and balance the budget. . . .

Inflation: We consider inflation and its impact on jobs to be the greatest domestic threat facing our nation today. Mr. Carter must go. . . .

He has fostered a 50 percent increase in federal spending, an increase of more than $200 billion, boosting spending in an era of scarce resources, and driving up prices. . . .

He has permitted continuing federal budget deficits and increased federal borrowing, forcing higher interest rates and inflationary money creation. . . .

Inflation is too much money chasing too few goods. Much can be done to increase the growth of real output. But ultimately price stability requires a noninflationary rate of growth of the money supply in line with the real growth of the economy. . . .

Ultimately, inflation is a decline in the value of the dollar, the monetary standard, in terms of the goods it can buy. Until the decade of the 1970s, monetary policy was automatically linked to the overriding objective of maintaining a stable dollar value. The severing of the dollar's link with real commodities in the 1960s and 1970s, in order to pursue economic goals other than dollar stability, has unleashed hyper-inflationary forces at home and monetary disorder abroad, without bringing any of the desired economic benefits. One of the most urgent tasks in the period ahead will be the restoration of a dependable monetary standard—that is, an end to inflation.

Lower tax rates, less spending, and a balanced budget are the keys to maintaining real growth and full employment as we end inflation by putting our monetary policy back on track. Monetary and fiscal policy must each play its part if we we are to achieve our joint goals of full employment and price stability.

Unfortunately, Mr. Carter and the Democratic Congress seek to derail our nation's money creation policies by taking away the independence of the Federal Reserve Board. . . . The independence of the Federal Reserve System must be preserved.