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# Social Democratic America

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# Toward the Good Society: An American Path

*AMERICA IS* A very rich nation. And in coming decades we will become richer still. Despite our affluence, however, too few ordinary Americans have adequate economic security, too few who grow up in disadvantaged circumstances are able to reach the middle class, and too few have seen their boat lifted when the economic tide rises.

This book is about how we can do better. The problems we confront are big ones, but they are not intractable. The key to a solution? Government social programs. Social programs function as a safety net, a springboard, and an escalator: they provide economic security, enhance opportunity, and ensure rising living standards. Over the past century, we have gradually expanded the size and scope of such programs. Given recent economic and social shifts, we need to do more. Our history and the experiences of some other affluent nations point us in useful directions, and they suggest we can expand government without destroying liberty, breaking the bank, or wrecking the economy.

Can it happen? The notion that we are likely to further increase the size and scope of our social policy may seem blind to the reality of contemporary American politics. After all, some on the left of the political spectrum feel America's safety net is complete,<sup>1</sup>

many in the center favor cutting public spending to reduce our government debt, and many on the right demand lower spending and taxes full stop. But step back and consider the long run. The lesson of the past 100 years is that as the country gets richer, we are willing to spend more in order to safeguard against risk and enhance fairness. Advances in social policy come only intermittently, but they do come. And when they come, they usually last.

### Three Failings

From the 1940s to the 1970s, Americans up and down the income ladder enjoyed improved economic security, expanding opportunity, and steadily rising incomes. But since the 1970s, the story has been quite different. Progress has stalled, or even reversed.

Too many Americans have incomes so low that making ends meet is a struggle. Too many experience a sizable income drop at some point during their working career. And too many have no health insurance or inadequate health insurance. This isn't just a function of the 2008–9 economic crisis and its aftermath. It was true before the economy fell apart, and it will still be true once we return to our long-run growth path (and after the 2010 healthcare reform is fully implemented).

In the past half century the United States has made considerable progress in boosting opportunity: most women and many African Americans now have a much better chance to obtain an advanced education and to thrive in the labor market than did their counterparts a generation ago. Yet the story for Americans who grow up poor is much less encouraging. Their odds of climbing into the middle class, already low, have been shrinking.

Since the 1970s, the incomes of households in the middle and below have risen slowly, despite sustained growth in the economy. Income growth has been decoupled from economic growth.

## Our Hypercompetitive, Risk-Filled Economy

For society as a whole, competition is a force for immense good, stimulating economic progress and improving living standards. But competition can wreak havoc on the lives of particular individuals. Since the 1970s, competition has become a much more pervasive feature of America's economy. Firms selling goods or services in international markets confront intense foreign rivals. Domestic industries, such as restaurants and hotels, face more competitors too, as technological advances, falling construction and transportation costs, and deregulation have reduced barriers to entry. In addition, shareholders now want rapid appreciation in stock values. Whereas a generation ago they were happy with a consistent dividend payment and some long-term increase in the stock price, they now demand buoyant quarterly profits and constant growth. Robert Reich has an apt label for this new economy: "supercapitalism." American firms, he notes, "now have little choice but to relentlessly pursue profits."<sup>2</sup>

This shift benefits investors, consumers, and some employees. But it encourages companies to resist pay increases, drop health-insurance plans, cut contributions to employee pensions, move abroad, downsize, replace regular employees with temporary ones, and pursue a variety of other cost-cutting strategies that weaken economic security, limit opportunity for the less skilled, and reduce income growth for many ordinary Americans.<sup>3</sup>

For better or worse, the new hypercompetitive, risk-filled economy is here to stay. In coming decades more of us will lose a job or work part-time or irregular hours, fewer of us will get a good healthcare or pension plan from our employer, and more of us will go long stretches without getting a pay increase.

## Our Faltering Social Institutions

Families, civic organizations, and labor unions play important roles in a capitalist society. They help give us a good start in

life, provide job security and a bigger paycheck, and ensure that if we fall through the cracks, there is someone to help us get back on our feet. But over the past half century, these institutions have been unraveling. Americans marry later and divorce more frequently. Fewer children grow up in a home with both biological parents. Participation in local civic associations has declined. And barely one in ten employed Americans is a union member. Even more problematic, these changes have a class tilt: families, community organizations, and unions have weakened most among those with less education and income.<sup>4</sup>

Some believe the best way to address the stresses and strains of the new economy is to strengthen these institutions. It's a laudable aim. It would be good if more American children grew up in intact families, if unions ensured stable jobs and rising wages for a significant share of workers, and if community organizations provided guidance and support to more people in difficult circumstances. But that's not likely to happen.<sup>5</sup> Advocates of revitalizing these institutions tend to offer lots of hope but little evidence that it can be done. Nor do we find cause for optimism abroad; similar trends are evident in most rich nations.

Even if we could make progress in reversing the decline of families, unions, and community organizations, it wouldn't be good enough. At their best, these institutions leave a significant portion of the population uncovered. There has never been a society in which all children grow up in stable two-parent families, all workers enjoy union-negotiated wages and benefits, and civic associations serve the needs of all the disadvantaged. Only government has the capacity to help all Americans.

## Affluence, Insurance, and Government

Most of us try to steer clear of risk events, and we attempt to insure ourselves against potential harm or loss in case we do get hit by one. We save money in case we lose our job or outlive

our working years. We bind ourselves in long-term partnerships (marriage) in order to spread childcare duties and safeguard against financial difficulty. We purchase health insurance in case we need expensive medical care. We buy auto insurance in case we get in an accident. We purchase home insurance in case our house is damaged or destroyed.

When our income is low, we can't afford to spend much on insurance, so we often go without. The more income or assets we have, the more insurance we buy. This is true of individuals and of nations. As a person's income or assets increase, she will tend to spend more on insurance. Similarly, as a nation gets richer, it will tend to allocate a larger portion of its income—its gross domestic product (GDP)—to insurance.

For some types of insurance, private markets do an effective job. Auto insurance is a good example; the incidence of accidents and the repair or replacement sums are sufficiently low that private companies can offer insurance at prices most drivers can afford. In other areas, government is a better provider, because it can spread the cost across a larger pool (all citizens), having a single payer reduces administrative costs, and government can insist on cost reductions and safety measures by private actors.<sup>6</sup>

Most of what we call social policy is actually public insurance.<sup>7</sup> Social Security and Medicare insure against the risk of having little or no money in your retirement years. Unemployment compensation insures against the risk of losing your job. Disability payment programs insure against the risk of suffering a physical, mental, or psychological condition that renders you unable to earn a living.

Other public services and benefits also are insurance programs, even if we don't usually think of them as such. Public schools insure against the risk that private schools are unavailable, too expensive, or poor in quality. Special education services insure against the risk of having a disability that inhibits participation in school. Retraining and job-placement programs insure against the risk that market conditions make it difficult to find employment. The

Earned Income Tax Credit (EITC) insures against the risk that your job pays less than what's needed for a minimally decent standard of living. Social assistance programs such as the Supplemental Nutrition Assistance Program (SNAP, or "food stamps") and Temporary Assistance for Needy Families (TANF) insure against the risk that you will find yourself unable to get a job but ineligible for unemployment or disability compensation. Even affirmative action programs are a form of insurance; they insure against the risk of being in a group that is, or formerly was, discriminated against.

Over the past century, the United States, like other rich nations, has created a number of public insurance programs. But we haven't done enough. From our own experience and that of other affluent countries, we know there are significant risks we could insure against but currently don't, and others for which the protection we now provide is inadequate.<sup>8</sup> We need the following:

- Universal health insurance
- One-year paid parental leave
- Universal early education
- Increase in the Child Tax Credit
- Sickness insurance
- Eased eligibility criteria for unemployment insurance
- Wage insurance
- Supplemental defined-contribution pension plans with automatic enrollment
- Extensive, personalized job-search and (re)training support
- Government as employer of last resort
- Minimum wage increased modestly and indexed to prices
- EITC extended farther up the income ladder and indexed to average compensation or GDP per capita
- Social assistance with a higher benefit level and more support for employment
- Reduced incarceration of low-level drug offenders
- Affirmative action shifted to focus on family background rather than race

- Expanded government investment in infrastructure and public spaces
- Increase in paid holidays and vacation time

Now, to some, this will look like a predictable laundry list of left goals. Yet I've arrived at this list not by consulting the latest edition of the "Progressives' Handbook,"<sup>9</sup> but by examining the problems we face and the experiences of the world's rich nations in addressing them. As I explain in chapters 2, 3, and 4, the evidence suggests that we can do better at enhancing economic security, expanding opportunity, and ensuring shared prosperity, and that these policies are the best way to do so. Moreover, you will see, if you read on, that I believe the prevailing wisdom among the American left on some key issues—taxes, regulation, competition in services, wage levels in low-end service jobs, and others—is mistaken.

## Government Social Programs Have Economic Costs, but Also Benefits

Of course, spending on insurance has an economic cost. When we allocate funds to insurance, we forgo other uses of the money that might have contributed to economic advance, such as investment in research or new companies or in expansion of existing businesses. Moreover, the existence of insurance increases the incentive for people to engage in risky behavior or to avoid employment. Given these costs, it isn't surprising that some object to the expansion of public insurance.

At the same time, insurance has economic benefits. Schooling and medical insurance improve productivity via better knowledge, creativity, and health. Bankruptcy protection encourages entrepreneurship. Unemployment compensation reduces efforts to restrict employers' flexibility in hiring and firing, and it facilitates employees' skill upgrading and geographic mobility.<sup>10</sup> Programs that

boost the income of poor households, such as the Child Tax Credit and the EITC, increase the future employment and earnings of children in those households.<sup>11</sup> Many insurance programs reduce stress and anxiety, enhancing productivity. Insurance also lessens conflict within firms and within society as a whole, contributing to economic stability.<sup>12</sup> Finally, the de facto choice often isn't insurance or no insurance. It's insurance or regulation, and the former interferes with markets and competition less than the latter.<sup>13</sup>

The experience of the world's rich countries over the past century suggests no reason to fear that a rise in the size and scope of public social programs would weaken the economy. In the United States, social policy expenditure has steadily increased, yet the country's rate of economic growth has not slowed.<sup>14</sup> Affluent nations that spend more on public social programs have tended to grow just as rapidly as those that spend less.<sup>15</sup> There surely is a level beyond which public social spending hurts the economy. But the evidence says America hasn't yet reached that level. In fact, we're probably well below it.

## Social Democracy

Social democracy originated in the early twentieth century as a strategy to improve rather than replace capitalism. Today, we associate it with European social democratic political parties and the policies they have put in place, particularly in the Nordic nations.<sup>16</sup> I believe our array of social programs will increasingly come to resemble those of the Nordic countries. It is in this sense that I say America's future is a social democratic one.

Let me be clear about what that means. A generation ago, the label "social democratic" referred to policies that make it easier for people to survive with little or no reliance on earnings from employment.<sup>17</sup> Social democracy meant, in effect, a large public safety net. Today that's too narrow a conception. In recent

decades the Nordic countries have supplemented generous social insurance programs with services aimed at boosting employment and enhancing productivity, from early education and active labor market programs to public infrastructure and support for research and development.<sup>18</sup> And for the most part, these countries believe in a market-friendly regulatory approach.<sup>19</sup> There are regulations to protect workers, consumers, and the environment, to be sure. But these exist within an institutional context that aims to encourage entrepreneurship and flexibility by making it easy to start or close a business, to hire or fire employees, and to adjust work hours.

In other words, modern social democracy means a commitment to extensive use of government policy to promote economic security, expand opportunity, and ensure rising living standards for all. But it aims to do so while facilitating freedom, flexibility, and market dynamism.

Freedom, flexibility, and market dynamism have long been hallmarks of America's economy. These are qualities worth preserving. The Nordic countries' experience shows us that a nation can successfully embrace both flexibility and security, both competition and social justice. Modern social democracy can give us the best of both worlds.

There are understandable worries about the transportability of Danish or Swedish policies to a large, diverse nation such as the United States. But as I explain in later chapters, the grounds for concern dissolve once we consider specific policies. Indeed, if you look carefully at the policy suggestions listed earlier, you'll notice that many of them are already in place in this country. Getting closer to the good society entails doing more of what we already do, not shifting to something qualitatively different.<sup>20</sup>

Moreover, I'm not suggesting that we copy the Nordic countries' playbook in full. Our future array of public social services and benefits will be broader and more generous than it is now, but it will retain a distinctively American flavor. Indeed, in a few respects,

the Nordic and other European nations may come to look more like us.<sup>21</sup>

Expansions in the size and scope of our social programs won't always constitute progress. Policy makers will make some poor choices, and the structure of the US policy-making process ensures that we seldom get optimal policy. But that has always been true, and yet American policy makers have managed to craft a host of programs that work quite well, from Social Security to Medicare to the EITC. As our evidence base grows, and particularly as we learn more about best practice in other nations, there is reason for optimism about the quality of future social policy.

## Can We Afford It?

For the past half century, our government has taxed and spent a smaller portion of the country's economic output than have most other affluent nations. In 2007, the peak year of the pre-crash business cycle, government expenditures totaled 37 percent of GDP in the United States. As figure 1.1 shows, in most other rich nations the share was well above 40 percent, and in some it was above 50 percent.

The added cost of the new programs and expansions I recommend plus our existing commitments to Social Security and Medicare is likely to be in the neighborhood of 10 percent of GDP.<sup>22</sup> If that sounds massive, keep in mind two things. First, if our government expenditures rise from around 37 percent of GDP to around 47 percent, we will be only a little above the current norm among the world's rich nations. Second, an increase of 10 percent of GDP would be much smaller than the increase that occurred between 1920 and today.

How can we pay for it? As a technical matter, revising our tax system to raise an additional 10 percent of GDP in government revenue is simple. Adding a national consumption tax could get

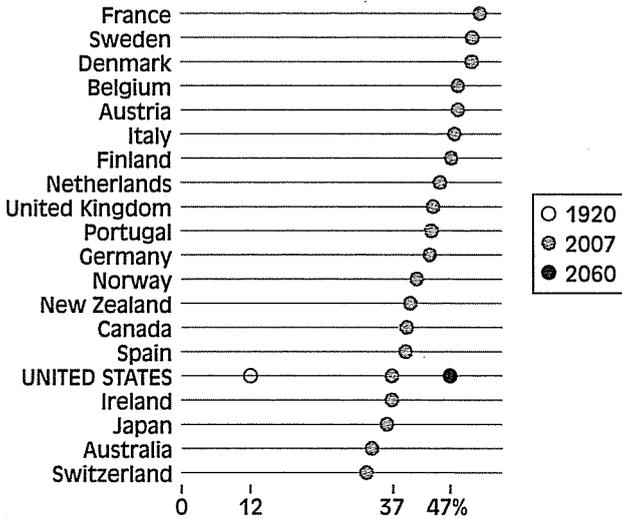


FIGURE 1.1 Government expenditures as a share of GDP

Includes government at all levels: national, regional, local. 2007 is the most recent business cycle peak year. *Data sources:* OECD, stats.oecd.org; Vito Tanzi, *Governments versus Markets*, Cambridge University Press, 2011, table 1. US 47 percent in 2060 is my projection.

us halfway there, and an assortment of relatively minor additions and adjustments would take us the rest of the way.<sup>23</sup>

Since 1980, much of America's left has thought about taxation in terms of its impact on the distribution of income, putting tax progressivity front and center. But we can't get an additional 10 percent of GDP solely from those at the top, even though they are getting a steadily larger share of the pretax income. We would have to increase the effective tax rate paid by the top 1 percent or 5 percent to a level far exceeding what it has been at any point in the past half century.<sup>24</sup> This news may disappoint some. But all rich nations have tax systems that are roughly proportional: households up and down the income ladder pay approximately the same share of their pretax income in taxes. Income redistribution occurs largely via government transfers rather than taxes. The key difference between America's tax system and those of highly redistributive countries such as Denmark and Sweden isn't that ours is less progressive; it's that it raises less revenue.<sup>25</sup>

## Are There Better Alternatives?

Some will sympathize with the ends I propose but favor different means. Suggestions include shifting to a smaller and more targeted public safety net, expanding our existing private safety net, privatizing service provision, revitalizing families and communities, putting the brakes on globalization, promoting manufacturing, strengthening unions, expanding profit sharing, mandating a high wage floor, instituting a basic income grant, and facilitating asset building. I consider each of these in chapter 4. Some of them might help. But none, I conclude, would be as effective in addressing economic insecurity, inadequate opportunity, and slow income growth as the public programs I listed earlier.

## The Progressive Trajectory of American Social Policy

What about the politics? America has more public insurance than we did a century ago, but given the structure of our political system and the divisiveness of our contemporary politics, is it reasonable to expect that we'll go farther? I believe it is.

Policy makers, drawing on reason and evidence, and perhaps with a push from organized interest groups or the populace, will recognize the benefits of a larger government role in pursuing economic security, opportunity, and rising living standards and will attempt to move the country in that direction. Often they will fail. But sometimes they'll succeed. Progress will be incremental, coming in fits and starts. But it will have staying power. New programs and expansions of existing ones will tend to persist, because programs that work well become popular and because our policy-making process makes it difficult for opponents of social programs to remove them. Small steps and the occasional big leap, coupled with limited backsliding, will have the cumulative effect

of significantly increasing the breadth and generosity of government social programs.

This is not a prediction about the timing or conditions under which specific policy advances will occur. It's a hypothesis about a probabilistic process. Over the long run, new programs occasionally will be created and existing ones occasionally will be expanded, and these additions and expansions are unlikely to be reversed.<sup>26</sup>

This is, in fact, an apt description of the history of American social policy over the past century. Many advances occurred when Democrats held the presidency and both houses of Congress, but not all.<sup>27</sup> Some came during bad economic times, others in healthier conditions. In some instances labor unions were strong proponents, in others not. Sometimes support from key sectors of business was critical, but not always. Some changes hinged on interparty compromise, while others didn't.

Two features have been common to all expansions of US social policy. One is problem solving: policy makers attempt to figure out a useful course of action given needs, aims, resources, and available knowledge.<sup>28</sup> The other is policy persistence: policy advances tend to stick, partly because they become popular and partly because the American policy-making process is laden with "veto points" that make it easy for a minority to block proposed policy changes. Problem solving and policy persistence are likely to continue. Over time, they will produce a rise in the size and scope of government social programs in the United States.

There are potential obstacles: Americans don't like big government, the rhetoric used by modern opponents of big government can be persuasive, the left may increasingly struggle to get elected, the balance of organizational power in politics has swung to the right, and the structure of our political system hinders progressive policy change. Given these obstacles, is a social democratic future for the United States just an ivory tower fantasy? I don't think so.

The typical American is ideologically conservative but programmatically progressive. It's true that we aren't fond of the idea of

big government. But when it comes to specific programs, we tend to be strongly supportive.

Opponents of big government contend that it frequently fails to achieve its objective, makes things worse, or jeopardizes other desirable aims. A generous public safety net, they say, makes the poor worse off in the long run by discouraging employment. High taxes weaken the economy. These arguments, termed the “rhetoric of reaction” by Albert Hirschman, can seem persuasive. But they are subject to empirical scrutiny, and their sway is likely to diminish as scientists expose their flaws with more and better data.

A significant expansion of public social programs in coming decades hinges on electoral success by Democrats, but some think their fortunes are dimming. They have lost support among working-class whites, a key element of the New Deal coalition that dominated American government from the 1930s through the 1970s. Yet Democratic presidential and congressional candidates have fared well with a new electoral base of urban professionals, women, African Americans, and Latinos. Will a flood of private money into election campaigns, encouraged by the Supreme Court’s 2010 *Citizens United v. Federal Election Commission* ruling, doom the Democrats? Maybe, but private campaign contributions have been growing in importance for several decades, and so far the Democrats have managed to keep up. And while demographics, electoral coalitions, and campaign funding certainly matter, the state of the economy tends to be the chief determinant of the outcome of national elections. If Democrats manage the economy reasonably well when they are in charge, they are likely to remain electorally competitive.

Some contend that the key determinant of American policy is the strength of organized interests outside the electoral arena, where the balance of power has shifted to the right. Businesses and affluent individuals have mobilized, while the labor movement, the key organized interest group on the left, has steadily declined in membership and, arguably, in political influence. Yet this has slowed, not stopped, the advance of social policy. Unless

the balance of power shifts farther to the right, the advance is likely to continue.

Finally, as I noted earlier, the veto-point-heavy structure of America's political system makes it relatively easy for opponents to block policy change. Given this structure, the recent disciplined obstructionist approach by the Republicans is a threat to the forward march of social policy. But only if it continues, and history suggests it won't.

If we extrapolate from the past century, the most likely course for American social policy is continued advance. Political obstacles old and new may slow progress, but they won't halt it.

## Will Outcomes Improve?

Economic and social shifts that threaten economic security, opportunity, and shared prosperity are likely to continue. In fact, they may worsen. If that happens, an expansion of social policy won't guarantee improved outcomes. Aggressive government action might not be sufficient to offset these trends. But it will help. Outcomes will be better than if public programs remain in their current state.

## The Book

In chapter 2, I examine our failure to ensure economic security, opportunity, and shared prosperity. In chapter 3, I propose a set of policies to address these maladies. In chapter 4, I consider potential objections and alternatives. In chapter 5, I explore the politics.

The book offers an evidence-based case for the desirability and feasibility of an expanded government role in providing economic security, enhancing opportunity, and ensuring rising living standards in the United States. There are grounds for concern but also for optimism. The bad news is that economic and social shifts

have made life more difficult than it should be for many ordinary Americans. We aren't doing well enough in protecting against risk, providing everyone with the opportunity to thrive, and ensuring that economic growth benefits us all. The good news is that we can and likely will do better. We know what policies can help, and history suggests we will, in time, make more and better use of them.