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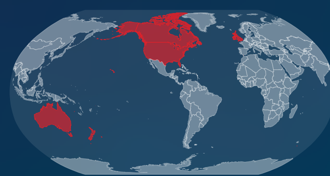
Lessons from the Anglosphere



The Case for Fiscal Reform

Lessons from the Anglosphere

Sean Speer and Alex Brill

November 2017

True North in
Canadian public policy

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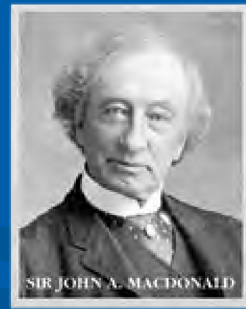
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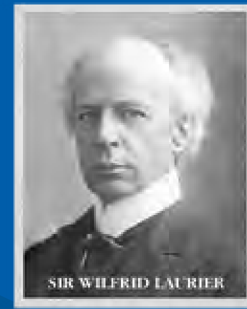
SIR WILFRID LAURIER

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Introduction

Federal fiscal reform in the United States is increasingly necessary but over the last two decades has remained elusive. Another part of the reason for the inaction reflects different political preferences and priorities. Part of it reflects differing views about the possible economic and social effects of controlling public spending and fiscal deficits. The result is that the US federal debt continues to grow unabated.

Resolving disputes about political preferences invariably has its limits. But we can draw on evidence and experiences with fiscal reforms elsewhere to better understand the relationship between particular reform strategies and their economic and social outcomes. The fiscal reform experiences in Australia, Canada, New Zealand, and the United Kingdom – what can be described as the "Anglosphere" – can give some context and background to the US policy debate and ultimately help shape a bipartisan consensus for action.

That is the goal of this essay series published by the Macdonald-Laurier Institute (MLI), a Canadian-based think-tank. We have asked scholars and leading politicians from these Anglosphere countries to describe their respective experiences with fiscal reform, including what factors contributed to the reforms, their composition, and the economic and social outcomes that followed.

> *"US lawmakers should look to the Anglosphere for lessons from their successful fiscal reforms."*

At different times, these Anglosphere countries were each confronted with fiscal crises due to overspending, high debt levels, and the same tendency to "kick the can down the road" that is present in Washington. Eventually, their behaviour caught up to them. It became a matter of "arithmetic," not "ideology," as then Canadian finance minister Paul Martin once said.

Each country subsequently undertook ambitious fiscal reform programs to control spending, cut budgetary deficits, and reduce the size of government. Their actions led to positive economic and social outcomes. Anti-austerity warnings – many of which sound similar to claims heard now in Washington – failed to materialize.

The potential lesson from these real-world experiences is that well-designed fiscal reform can yield economic and social benefits. We hope that US lawmakers from across the political spectrum learn from these experiences and see how fiscal reform can ultimately strengthen the US economy now and in the future.

This introductory essay sets out the reasons that US lawmakers should look to the Anglosphere for lessons from their successful fiscal reforms.

What is the Anglosphere?

The term Anglosphere was first coined, but not explicitly defined, by science fiction writer Neal Stephenson in his 1995 book *The Diamond Age*. British journalist John Lloyd adopted the term in a 2000 essay and defined it as including the United States and the United Kingdom along with the English-speaking Australia, Canada, Ireland, New Zealand, South Africa, and the British West Indies (Lloyd 2000). The *Merriam-Webster* dictionary defines the Anglosphere as "the countries of the world in which the English language and cultural values predominate." American scholar James Kotkin calls it "predominately a union of language, culture and shared values" (Kotkin 2011).

The shared culture and values are unique and strike at the heart of what makes our societies successful. It is no accident that countries in the Anglosphere consistently top the Legatum Institute's Prosperity Index, a result described as the "Commonwealth effect" (Legatum Institute 2016).

What precisely does this mean? It is that our wealth and opportunity are no mere accident but a result of the Anglosphere vision of society – including individual liberty, personal responsibility, merit-based opportunity, free markets, democratic governance, private property, and the rule of law. As a Legatum Institute study explains:

> This "Anglosphere" model of prosperity… has proved the most successful model in delivering prosperity to people. In both the level of prosperity delivered, and the effective conversion of wealth into prosperity, the Anglosphere model outperforms the Nordic model, and the social democracy of Continental Europe. (Maltby 2016)

> *"Our wealth and opportunity are no mere accident but a result of the Anglosphere vision of society"*

Kotkin has argued that the Anglosphere model will continue to be dominant. His 2010 book, *The Next Hundred Million,* anticipated that the US and its Anglosphere allies – Australia, Britain, Canada, and New Zealand – will continue to be the primary economic, scientific, and cultural force in global commerce well into the 21st century. The reason for his prediction is straightforward: the Anglosphere's underlying ideas, institutions, and traditions have given it a linguistic, cultural, and technological advantage.

What Connects Us

There are deep linkages that connect countries in the Anglosphere in various ways, from culture to language to ideas to politics and seemingly everything in between. Political and policy ideas are regularly diffused across the Anglosphere, which is not surprising. Our political cultures are similar, and thus the ideas that animate our politics are generally common. It is interesting, for instance, that Thatcherism predated Reaganism by about 18 months. This historic process of crosspollination is inevitable and is a key source of strength and renewal for the Anglosphere.

The connection is not just a political abstraction or cultural identification. Countries in the Anglosphere have various economic, governmental, and security links. One example is that Australia, Canada, New Zealand, the United Kingdom, and the United States cooperate as what is known as "the Five Eyes" on intelligence gathering.

Yet, notwithstanding our interconnectedness, there have been only limited efforts to understand how we can learn from one another on public policy in general and fiscal policy in particular. It is a curious omission given the similarities of our political cultures and institutions.

Australia, Canada, New Zealand, and the United Kingdom have previously gone through precisely the same debates on government spending, deficits, and debt that we have seen in the United States over the past decade or so. Each country can learn lessons from these experiences by understanding how these debates played out.

> *"Plenty of things bind us together. Sound public policy ought to be among them."*

This essay compilation, including forewords written by leading politicians in each of the four countries, seeks to help US lawmakers derive some lessons from the Anglosphere experiences and put them into action to address Washington's long-term fiscal challenges.

We hope that these essays will not only help to shape a consensus in favor of fiscal reform in Washington, but also serve as a model for similar comparative policy studies across the Anglosphere. Plenty of things bind us together. Sound public policy ought to be among them.

Lessons from the Anglosphere

This compilation comprises essays by policy scholars and experts from Australia, Canada, New Zealand, and the United Kingdom, as well as one from the United States to put the series in context and highlight the need for reform.

The fiscal reform experiences in the four countries were, of course, different. They occurred in different time periods and under different types of governments, were composed of different mixes of tax changes and spending reductions, and ultimately were accompanied by different sets of broader policy changes.

But there are still common lessons that US lawmakers can derive. The overarching message of these essays is that well-designed fiscal reform can produce positive economic and social outcomes – a real-life rebuttal to the Keynesian presumption that greater spending control and deficit reduction will necessarily harm the economy.

In particular, there are five crucial lessons to be drawn from the experience with fiscal reform in the four Anglosphere countries.

Pursue public transparency and coalition building

The political forces in favor of more and higher spending are well-organized and vocal. It is a classic case of "concentrated benefits and dispersed costs" and one of the principal reasons that fiscal reform has failed to gain traction in Washington.

It is essential, therefore, that reform-oriented politicians speak directly to the public about the need for reform, the opportunity it entails, and their plans to achieve it. Voters must understand the magnitude of the problem before they are prepared to accept the remedy. Transparency is thus key to obtaining a mandate and sustaining the political battle in the face of the inevitable hue and cry of special interests. Robert Carling's description in this compilation of the Australian government's fiscal transparency reforms provides a good example.

It also helps to build a common understanding of the problem across political parties. There will no doubt be political disagreements about how to solve a problem, but the first order of business is to build a broad coalition in favour of reform.

Canada succeeded in its fiscal reforms partly because the government was clear about the problem and partly because the prime minister had support from opposition parties who shared the government's diagnosis of the problem. The post-2010 experience in the United Kingdom is similar in this regard. The political marriage between Conservative David Cameron and Liberal Democrat Nick Clegg may have been odd, but they did agree on the need to address the country's deteriorating public finances.

In the United States, pro-reform members of Congress from both sides of the aisle must work with each other to address the federal government's short-term budgetary deficit and long-term debt challenges. This cannot be a party-line issue.

Get the institutional and fiscal governance arrangements right

Establishing clear fiscal rules, targets, and criteria is essential for maintaining political will and demonstrating progress to the public. There are plenty of threats to fiscal reform including the electoral cycle, special-interest pleading, and spending pressure from government departments and agencies. Rooting reform in clear, achievable rules, targets, and criteria can mitigate this risk, and doing so must be an initial priority.

Complex targets like budgetary balance over the business cycle may be conceptually appealing to economists or technocrats, but they risk losing public understanding and hence credibility and support. Politicized arithmetic or bogus spending cuts can have similar effects. It is important that fiscal targets are clear and understandable and that nonpartisan organizations such as the Congressional Budget Office are responsible for reporting to the public on progress.

> *"The Canadian government used a publicly available six-point test that enabled the public to understand how decisions were reached."*

Clear public criteria can also help to justify different fiscal choices and address false claims about politicization. The Canadian government used a publicly available 6-point test that enabled the public to understand how decisions were reached.

Similarly, spending reductions should be embedded in legislation, giving the government or Congress minimal ability to unwind the cutbacks. Firm, legislated rules can minimize (though not eliminate) the risk of budget backsliding.

Focus on government spending – not higher taxes

In the United States, it is increases in federal outlays now and in the future that are driving projected fiscal instability, not any forecast of declining tax receipts. Deficit reduction should therefore focus on addressing this root problem directly.

Moreover, the experiences in the Anglosphere certainly accord with Alberto Alesina's research, which shows that spending reductions are less economically damaging than tax increases. As an example, Bryn Wilkinson addresses this question directly in his analysis of the New Zealand experience when he shows that fiscal reforms – focused primarily on spending – ultimately contributed to the country's pro-growth environment.

The Canadian experience is also relevant here for US lawmakers. Then finance minister Paul Martin understood that Canada's poor tax competitiveness was already an economic drag when he enacted fiscal reforms (World Economic Affairs 1997). Raising taxes would have dampened economic growth and exacerbated the government's fiscal challenges at the precise moment that dynamism and growth were required.

The US tax system is already uncompetitive, particularly with regards to corporate income taxes. Raising tax rates to address the deficit would exacerbate this uncompetitiveness and hurt the economy.

Incidentally, eliminating Canada's budgetary deficit produced a "fiscal dividend" that the government then used to lower taxes across the board, including the corporate tax rate, which was eventually dropped to 15 percent. Fiscal reform could provide the US government with a similar fiscal dividend to address its own tax competitiveness challenges.

Put everything on the table

Fiscal reform must involve a clear-eyed review of *all* federal government spending to understand what should be eliminated, reformed, or maintained. Everything must be up for discussion. For instance, business subsidies and corporate welfare should be a big part of any fiscal reforms, as was the case in Canada.

> *"It is important that any fiscal reform exercise in Washington involve all areas of government spending."*

Excluding certain areas of spending from the exercise precludes the opportunity for administrative efficiencies, consolidation, or other improvements. It also risks undermining public support if people do not believe that the process is fair and that certain groups are being protected.

Daniel Mahoney's essay on the experience in the UK is critical for understanding the risks inherent in protecting various sectors or departments. The government's decision to exclude certain types of spending (such as pension benefits and foreign aid) from its fiscal reform has placed undue burden on other areas of government spending. Mahoney estimates, for instance, that by last year, changes to indexation for pension benefits would have saved £7.4 billion annually.

It is important, therefore, that any fiscal reform exercise in Washington involve all areas of government spending. It is key to making the government more affordable, efficient, and ultimately smaller.

Make fiscal reform part of a broader agenda

Fiscal reform should not just focus on easy or popular cuts. Defunding the Corporation for Public Broadcasting, for instance, may be a good idea, but it is not going to fix Washington's fiscal challenges or markedly improve the country's economic competitiveness. There must be a higher level of ambition.

Here is where Australia and New Zealand really provide models for US lawmakers to emulate. Their fiscal reforms focused more on reforming and modernizing what government does and how it does it than on eliminating the deficit or meeting an arbitrary debt target. The emphasis in such exercises ought to be on right-sizing social welfare programs and altering their structures so they are compliments to instead of substitutes for work, skill training, healthy behaviour, and retirement savings. This is the best way to reduce the size and scope of government in the long-term.

> *"Defunding the Corporation for Public Broadcasting may be a good idea, but it is not going to fix Washington's fiscal challenges."*

The US Congress should see fiscal reform as part of a broader agenda to revive US dynamism and opportunity. Eliminating the deficit and putting public debt on a sustainable path is the first step. Addressing distortionary policies such as agricultural subsidies or federal mandates in education and other state-level responsibilities should be concurrent. The outcome will be not only an improved fiscal position, but a more dynamic and competitive economy.

About the Authors

Sean Speer is a Munk Senior Fellow at the Macdonald-Laurier Institute. He previously served in different roles for the federal government including as senior economic advisor to the Prime Minister and director of policy to the Minister of Finance. He has been cited by The Hill Times as one of the most influential people in government and by Embassy Magazine as one of the top 80 people influencing Canadian foreign policy. He has written extensively about federal policy issues, including personal income taxes, government spending, social mobility, and economic competitiveness. His articles have appeared in every major national and regional newspaper in Canada (including the Globe and Mail and National Post) as well as prominent US-based publications (including Forbes and The American). Sean holds an M.A. in History from Carleton University and has studied economic history as a PhD candidate at Queen's University.

Alex Brill is a resident fellow at the American Enterprise Institute (AEI), where he studies the impact of tax policy on the US economy as well as the fiscal, economic, and political consequences of tax, budget, health care, retirement security, and trade policies. Brill is the author of a pro-growth proposal to reduce the corporate tax rate to 25 percent, and *The Real Tax Burden: More Than Dollars and Cents* (2011), coauthored with Alan D. Viard. He has testified numerous times before Congress on issues including tax policy, labor markets and unemployment insurance, Social Security reform, and fiscal stimulus.

Before joining AEI, Brill served as the policy director and chief economist of the House Ways and Means Committee. Previously, he served on the staff of the White House Council of Economic Advisers. He has also served on the staff of the President's Fiscal Commission (Simpson-Bowles) and the Republican Platform Committee (2008).

Brill has an M.A. in mathematical finance from Boston University and a B.A. in economics from Tufts University.

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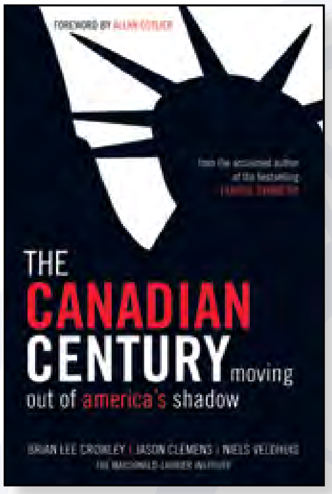

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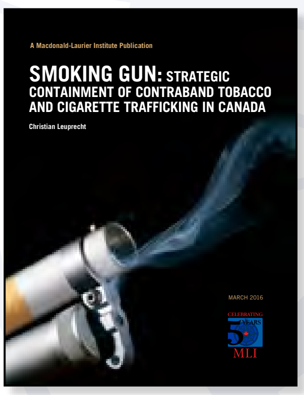

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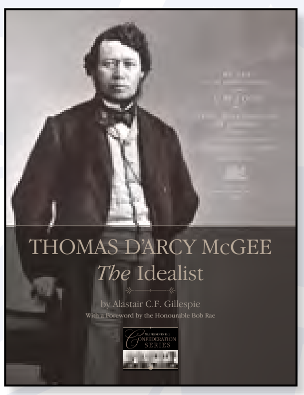

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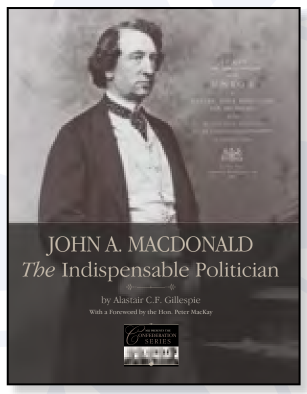

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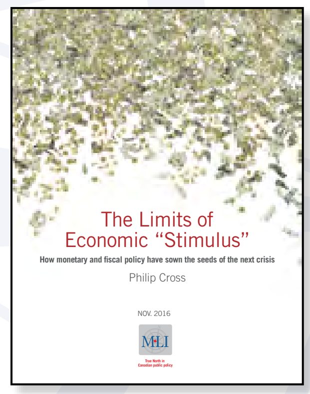

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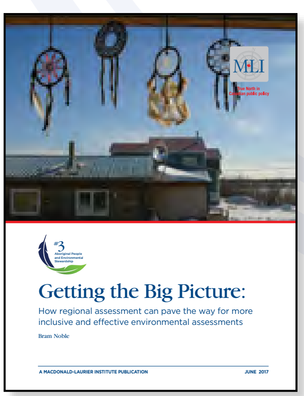

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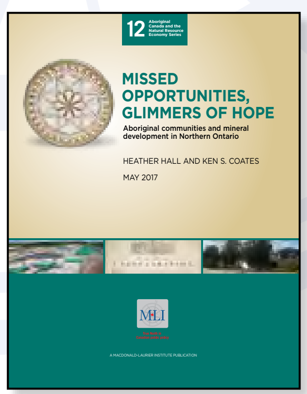

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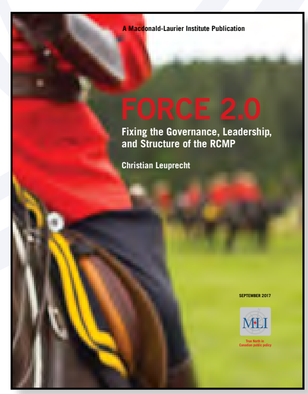

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