

A Year of Trump: The Politics and Realities of President Trump's Economic Policies

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ABSTRACT

The election of Donald Trump came as a surprise to the vast majority of political scientists, election forecasters, and senior political office holders, of both political parties. On top of that, then candidate Trump ran a decidedly unconventional political campaign. He spoke in broad outlines about what he was for, but gave very few specifics about what he would actually do. Few republicans sought to emulate Trump, and thus almost all other Republicans running for office ran on more traditional republican themes. President Trump thus has become the face of the Republican party, but he is only one man in the U.S. Governmental system. The most important one, yes, but one who still has limited powers to achieve any policy goals without working in concert with republican congressional majorities, or through the vast federal bureaucracy he now at least nominally heads. This paper seeks to detail out the relationships and constraints that are at play in the Donald Trump Presidency, to attempt to see what impact on economic policy, and through that policy what impact on the real economy, has occurred, and will continue as President Trump's enters his second year in office.

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JEL Classification: H1, H11, H50

1. Introduction

While it still seems premature to try to exactly define what President Trump’s final economic policies and priorities will be, a year after his election it seems safe to point out some trends that seem to be emerging. Some of them confirm things he said on the campaign trail, and some contradict them, and all of it is complicated by his relationship with the Republican party.

In analyzing the Trump Presidency, it is important to remember that Donald Trump likes to talk. What he doesn’t like to do is read the briefing reports, focus group the issues, test the waters, or many of the other things that a normal politician will do. President Trump wings it, and thus often it seems like he is thinking out loud. Anything that one tries to say about his policy preferences or beliefs can be refuted by something else he said. He often contradicts himself, sometimes in the same paragraph.

This does not mean that he has no beliefs, or policy preferences, or tendencies, only that in analyzing him, it is important to understand that he says a lot that is contradictory, ill-informed, or flat out untrue. Paraphrasing Jack Welch, one should take Donald Trump seriously, but not literally. In the case of any politician, but especially Donald Trump, the old adage about “judge a man by what he does, not by what he says”, seems to apply. Given some of the things candidate and President Trump has said, and still says, let us hope so. It is also important to note that President Trump is not only ideologically inconsistent (or incoherent), but he is also blissfully unashamed and unaware of that. Like most voters, he just wants to do whatever works, without having a firm idea of what that actually is, or having a well developed ideological framework to use in judging things.

Furthermore, while Donald Trump may know in broad strokes what he wants, he came into office with a particularly small set of actual policy plans. Candidate Clinton's campaign website had a 25-page policy brief on health care, that included 57 bullet points and links to many other pages expanding on its ideas. Candidate Trump's was two pages long, and he contradicted it in a speech days after it came out.¹ One can see the unpreparedness of the Trump team in the rollout of his executive order that imposed a temporary ban on immigrants from seven countries. It was produced internally in the White House, it was not vetted by the bureaucracy and caused immediate confusion in its implementation², and was quickly struck down in court, before he withdrew it for a rewrite. The rewrite was also almost immediately struck down, though it was eventually reviewed by the supreme court, which lifted most of the various injunctions on it and allowed it stand with only minor changes, pending a full review in the fall³. President Trump appears likely to prevail on it in the end, but the process of getting to a victory was internally chaotic, and politically embarrassing.

The above was just an executive action, an area where Trump can largely act alone. Serious changes or impacts to

¹ "Trump's healthcare plans trouble GOP" The Hill, Aug 6, 2016
<http://thehill.com/policy/healthcare/282587-trumps-healthcare-plans-trouble-gop>

² "How Trump's abrupt Immigration ban sowed confusion at airports, agencies", Reuters, 28 January 2017 <http://www.reuters.com/article/us-usa-trump-immigration-confusion-idUSKBN15D07S>

³ "Why Trump's Immigration Order is Legal and Constitutional", National Review 20 March 2017
<http://www.nationalreview.com/article/445905/trump-immigration-order-legal-constitutional-five-federal-judges-explain-why> Since the second travel ban has now expired, the third one (also struck down by lower courts) will probably be the one that the supreme court actually reviews.

the economy, outside of trade and certain regulatory matters, will require some degree of congressional support. While a vocal minority, perhaps even a plurality, of Republicans support Trump whole-heartedly, many others support him to the extent that he is a winner. But that does not mean that his policy is their policy.

Republicans have held the House of Representatives since 2010, and in House Speaker Paul Ryan they have a political leader whom they see as more policy oriented than most politicians. Since become speaker of the House in 2015, the Republican controlled House has been busy generating plans, and passing bills that he knew President Obama would veto or that Democrats in the Senate would kill, in preparation for the day when Republicans would again be in power. Republicans took the Senate in 2014, and held it in 2016, an event as unexpected as President Trump's election.⁴ Senate Leader Mitch McConnell is not as policy oriented as Speaker Ryan, and has spent the last several years in tactical combat with now retired minority leader Senator Harry Reid. While McConnell is a very skilled and experienced congressional tactician⁵, most of the intellectual ideas, and economic policy plans, have originated in the House of Representatives.

Neither Senator McConnell nor Speaker Ryan can be described as being from the Trump wing of the party. Both long predate President Trump, and both acted during the

⁴ "Republicans hold the Senate in stunner" Politico, November 9, 2016
<http://www.politico.com/story/2016/11/senate-2016-election-results-control-230926>

⁵ Donald Trump's one clear victory since the elections has been the appointment of Judge Neil Gorsuch to the Supreme Court – an event that was made possible solely by Senate Leader Mitch McConnell's willingness and ability to block President Obama's nomination of Judge Garland before the election.

presidential campaign as if they expected to be around long after “Trump-fever” had passed. Their primary concern during the election seemed to be how to contain the damage of a Trump loss, not with what to do after Trump won. Since the election, President Trump has gone out of his way to court them, except when he doesn’t, and both seem to have adjusted to him, without in any way becoming unquestioned allies. They are both their own actors, and both are keenly aware of two realities that President Trump seems to ignore or deny. Donald Trump won the electoral college, but he didn’t win the popular vote. And in most down ballot races, Republicans not named Trump did better than Donald Trump did himself.⁶

Furthermore, any changes Trump plans to make will depend on the many personnel decisions he and his cabinet are making, a process that has been particularly slow in part because of Democratic obstruction, but also because then nominee Trump’s campaign came into office unprepared for it. While the American press has made much of the ideological diversity of Trump’s emerging cabinet, pointing out how it doesn’t add up into anything coherent, in point of fact there does seem to be one thing that unifies most of his cabinet picks. Most of them are primarily defined by the fights they have had with the very departments they are now tasked with running. To give a few examples: Betsy DeVos at the Department of Education is a prominent supporter of school vouchers, Tom Price (since resigned in a scandal) at

⁶ President Trump lost the popular vote by almost 3 million votes. The total number of votes for house members, the best proxy we have for a generic republican or democrat vote, was won by republicans by almost 3 million votes. President Trump’s current (late October 2017) popularity is about where it was when he won the presidency, up from its low point this past summer. Congressional Republican’s popularity has fallen considerably.

Health and Human Services is a medical doctor who has been a vociferous critic of Obamacare, Scott Pruitt at the Environmental Protection Agency is a climate change skeptic who has been involved in several lawsuits with the EPA, Jeff Sessions as Attorney General is notably hostile to many of the Justice Department's recent positions on civil rights cases. Trump's most embarrassing cabinet pick so far was General Flynn at the National Security Agency, who was asked to resign after only three weeks on the job. The ethical transgressions that he committed are not (as of this writing) still fully clear, but the process that led to his resignation is clear – the agency he was tasked to lead secretly recorded him and selectively leaked details of it to the press⁷.

President Trump's White House staffing decisions have been even more chaotic. Normally, a new president is surrounded by trusted aids, campaign consultants, and political allies that he has built up over years of climbing the ranks in elected politics. These people have had years to gain the trust of the new president, and have an understanding of the new president's tendencies, habits, and ideology. Donald Trump came to the White House with almost none of this. The presidency was the first elected office he ever ran for, and he went through three campaign managers, and multiple pollsters, communications directors, advisors, etc. All this with a campaign staff of less than 100 – Hillary's campaign staff was close to 700⁸. This small organization, combined with the President's mercurial temperament, meant his

⁷ "Former Obama Officials, Loyalists Waged Secret Campaign to Oust Flynn", Washington Free Beacon, 14 February 2017
<http://freebeacon.com/national-security/former-obama-officials-loyalists-waged-campaign-oust-flynn/>

⁸ "Trump Lags Behind Clinton in Campaign Staff, Pollsters", The Hill, 22 July 2016 <http://thehill.com/blogs/ballot-box/presidential-races/288867-trump-lags-behind-clinton-in-campaign-staff-pollsters>

campaign could rapidly respond to events, though not always constructively. It also meant that he was rarely directing events.

Since becoming president, the trend has continued. He has replaced his National Security Adviser, Deputy Chief of Staff, Communications Director, Press Secretary, Chief of Staff, Deputy Communications Director, and Communications Director (again), and several cabinet members as well.⁹ While staff turnover in the early days of a new White House is not unusual, the turnover under President Trump has been somewhat higher than normal. It has also been very, very public, as President Trump seems unconcerned about publicly undermining or belittling his own staff. A president who wants to fundamentally transform Washington can not do so without an organization around him that can prioritize needs and set an agenda, especially if the people in it don't feel secure in their jobs.

This is especially important for President Trump, since for reasons that will be detailed in a later paper, the permanent Washington bureaucracy (sometimes referred to as the “deep state” by partisan Republicans, or the “administrative state” in academic literature) has gone into passive, and in some cases active, resistance to a Trump Presidency. And President Trump in turn, is at least rhetorically prioritizing bringing them into line. To do so, he will need to staff all the political positions in these bureaucracies, and he will need to do so much more quickly

⁹ “All the firings, resignations, departures, and job changes from the chaotic first 8 months of the Trump administration”, Business Insider, Smith Allan and Skye Gould 30 September 2017
<http://www.businessinsider.com/trump-fires-resigns-leaves-administration-2017-7>

than has been happening¹⁰. Rural and non-college educated whites may have been the base of his electoral support, but they are not going to be his allies inside the bureaucracies. To put a check on the perceived excess of the Justice Department's Civil Rights Enforcement Division, President Trump will need to draw on the institutional power of the Republican party to find Republican/conservative lawyers skilled in the management of large, public bureaucracies that are often hostile to what Republicans, or President Trump, want to achieve. That this discussion is still happening close to a year after Trump's election, speaks volumes about the difficulties the administration is having.

Any attempt to address the economic impacts of a Trump presidency must of necessity make some judgments about politics. Addressing what one can expect of an incoming administration tends more towards opinion than facts at the best of times, this is particularly true this time, because of the nature of President Donald Trump. That said, there are institutional constraints and political realities that have, and that will continue to, constrain any economic policies that a President Trump proposes, which allows for at least some predictive rigor.

The remainder of this paper will be devoted to explaining a few important political facts or perceptions within the U.S. that I have noticed are very difficult for non U.S. economists, even ones trained in the U.S., to understand. I also attempt to give the views on things as Republicans or Trump supporters (not always the same thing) view them. Though I am at times sympathetic to some of those views, I am not seeking to endorse or refute them in this paper, I am

¹⁰ "Donald Trump's Long March Problem", Washington Examiner, 12 April 2017 <http://www.washingtonexaminer.com/donald-trumps-long-march-problem/article/2620147>

merely attempting to inform readers of what they are. Almost half of all voters in the last election voted for President Trump, and more than half of them voted for Republican House members – and very, very few of them think they did so because they believe themselves to be racists or bigots.

All that said, there are three important things about America that need to be addressed before moving on to specific economic issues. These are issues that will come up again and again, and they are issues that are not well understood outside the U.S.

2. The filibuster and the Senate

The filibuster in the senate is an old institution, and though not originally in the constitution it has been part of the senate's rules for almost 200 years. It is a tool used by the minority party to slow down the legislative process by engaging in an endless debate about whatever is being opposed. Originally, it was a means extending the debate about an issue, a debate that could only be ended if a supermajority of either 2/3 or 3/5, (the exact number has varied over the years) of the senate voted for cloture – where cloture ended the debate and then one went on to actually vote. It effectively meant that for very important, far reaching changes, the senate required a supermajority to achieve anything. This led to compromise or inaction – something the original framers of the constitution did not envision but almost certainly would have approved of.

In the last 30 or so years, the nature of the filibuster has changed. It used to be, that in order to filibuster, one had to actually do it. Now, one just needs to get enough senators to agree that they will, in which case there is no point in the majority going on. The filibuster is no longer a means of extending debate, it is a means of ensuring that there never is

one. Both parties have used it with increasing regularity, and have extended it to areas that it was not at first ever used for, such as the senate's role in approving judges or executive branch appointees.

The senate long ago carved out an exception to the filibuster – budgetary matters. This was done (both parties supported it) because the actual running of the government required a budget, and nobody thought it a good idea that a minority party could hold the whole government hostage. This change to senate rules came about because a supermajority of senators supported it. In 2013, Senate democrats changed the filibuster as it pertained to non-supreme court judicial and executive branch nominations. To do this, they had to use a majority vote (52 to 48) to change the senate rules. In essence they set a new precedent – on issues where one needed a supermajority, a majority could vote to change the rule to majority rule, and then he does not need a supermajority any more. Republicans in turn recently ended the filibuster on supreme court nominations to approve Judge Gorsuch.

The above is important, because Republicans only have a 52 to 48 vote majority in the senate. Senate Democrats have a great deal of power to block Republican legislation, as long as the filibuster survives. There is no evidence at all that Donald Trump supports it. There is a very real possibility that it will not survive the Trump Presidency, though Republicans seem less inclined to end it then earlier in the year. And though Senate Majority leader McConnell ended it for Supreme Court nominations, he is a strong supporter of the filibuster.¹¹

¹¹ GOP Senators dismiss Trump filibuster change” The Hill, 2 May, 2017
<http://thehill.com/homenews/senate/331668-gop-senators-dismiss-trump-filibuster-change>

Regardless of the above, the filibuster does not apply to budget issues. The problem becomes defining what is a budget issue, and what isn't. To give just one example, Obamacare regulations constrain insurers to only offer plans that include all kinds of benefits that make the plans more expensive. Because those plans are purchased on a private market, they have a huge impact on the budget of individual Americans, but not on the government – so changing the regulations is subject to a filibuster. Obamacare also subsidizes the costs of the plan to some Americans, so that they can pay for the plans. There is a general agreement that subsidies are a budget item, and thus not subject to the filibuster. But if the subsidy is for an expensive plan, and the plan is expensive because of the regulation, is the regulation that makes the subsidy expensive subject to a filibuster or not? If this paragraph has caused confusion, do not worry, Senate Republicans can't figure it out either.

3. The 2018 Electoral Map

The 2016 senate map was brutal to Republicans, but they came through only losing two seats on net, the 2018 map looks much better for them, though reaching a 60 seat filibuster-proof majority would still be highly improbable. Of the 33 senate seats up for election in 2018, 25 are held by Democrats or Independents who caucus with them, 8 by Republicans. 10 Democrats are up for re-election in states Trump won, only one Republican will be running in a state that Clinton won. Senator McConnell has plenty of opportunity to apply pressure to his vulnerable senate colleagues.

More generally, it appears at the moment that Republicans have a small structural advantage in both the

Senate and the House¹². Less populous states get the same Senate representation as populous ones, and given the correlation between rural voters (overwhelmingly Trump) and low population states, Republicans are somewhat over-represented in the Senate. A similar dynamic exists in the House, though for different reasons. A combination of civil rights era laws, and Republican gerrymandering (drawing congressional district lines in such a way as to concentrate or spread out votes for political advantage) has left Democratic House votes more heavily concentrated, resulting in Democrats winning by larger margins, but in fewer districts.¹³ Since most Democrats are in safe seats – seats that Democrats normally win with a large margin, the Democrats have also trended leftward over the last few election cycles.

The above concentration on the federal government often masks another important change. Republicans held the House and Senate, and won the presidency when few thought they would, but they also increased their already substantial majorities at the state level. This is important because the state parties are where rising talent comes from in American politics¹⁴.

¹² “The GOP’s Long-Term Structural Senate Advantage”, Roll Call, 20 February 2017

<https://www.insideelections.com/news/article/the-gops-long-term-structural-senate-advantage>

¹³ To give an intuitive example more familiar to readers - Donald Trump won the electoral college, but lost the popular vote by close to 3 million votes. Of that 3 million votes, 4 million of them were in California alone. Had the extra 4 million votes Hillary won in California been spread proportionately over the rest of the country, Hillary would have won an electoral college landslide. Instead, she won a landslide in California, and lost the presidency.

¹⁴ “The Decimation of the Democratic Party, visualized” Washington Post, 10 November 2017

The great question in 2018 will be can Democrats motivate their voters to go to the polls. Under normal conditions, non-presidential election cycles favor Republicans, a larger share of Democrat voters skip non-presidential year elections than Republicans.¹⁵ Conversely, an argument can be made that Democrats are so angry with the Trump presidency, that they will be more motivated to vote, especially when President Trump continues to (in their view) screw everything up, as Democrats assume he will. This is an especially important question this cycle, given that for many Republicans the strongest argument for voting for Donald Trump was that his name was not Hillary Clinton – a person who will not be on the ballot in 2018. Of course, the second biggest reason for voting for Trump for many Republicans was that they didn't want any Democrat appointing judges to the Supreme Court – and given the age of the current supreme court, there is good chance that another vacancy will occur before the 2018 election. Current polling favors the Democrats, but it is the same polling that told them they would win the presidency in 2016. Only time will answer these questions, but everyone in Washington is already looking ahead to it.

4. The Congressional Budget Office (CBO)

Everyone who follows U.S. politics and economics vaguely knows what the CBO is, but few people know what it actually is, and what it can, and can't, do well. The CBO is

https://www.washingtonpost.com/news/the-fix/wp/2016/11/10/the-decimation-of-the-democratic-party-visualized/?utm_term=.f3083f92ce6e

¹⁵ “Trump Will Help Democrats Solve Their “midterm Falloff” Problem”, New York Magazine, 5 April 2017
<http://nymag.com/daily/intelligencer/2017/04/trump-will-help-dems-solve-their-midterm-falloff-problem.html>

not part of the executive branch, it rather is set up by, funded by, and supervised by, congress itself. It was set up that way, in 1974, so that congress would have its own research arm, separate from the Office of Management Budget (OMB), which as part of the executive branch reports to the president. Because the CBO is supervised by congress, the minority party always has a role in monitoring it, and in ensuring that it remains objective. And since the CBO is not charged with running anything, as the OMB is, they (theoretically at least) don't have any temptation to fudge numbers to show that the policy they are implementing is working, or in ways to better sell what the executive branch wants to do.

Because of these traits, the CBO has largely supplanted the OMB in the minds of congress, the public and the press, as the best source of data about budgetary and economic policy. It is seen as being non-partisan, and as a source of good data and economic forecasts about the economy as a whole, and about the potential impacts of legislation. The CBO does not engage in a lot of retrospective research of the sort that is the norm for most research economists, though it does often use that research as the basis for its own forecasts. The CBO forecasts the future, to give congress assistance in choosing among competing policies. The CBO has a deserved reputation for doing a good job of it, but there are two important constraints on the CBO that should be kept in mind.

The first is that when the CBO “scores”, i.e. estimates the budgetary effects of proposed legislation, it does so for only ten years into the future, and it does so based on the text of the legislation. Both of these rules are designed to constrain the CBO into doing straight research on what has been presented to it, and to do so in way where different legislative proposals can be directly compared, since they are

being measured the same way. Both goals are laudable, and for a long time worked.

Politics being what it is, congress has learned ways to game the system. To use two recent examples, consider Obamacare. Politically, it was very important to Democrats in 2009 that the CBO score Obamacare as costing less than 1 trillion dollars over its first 10 years. So the first thing they did was they delayed the implementation of the exchanges and the Medicaid expansion until after 2013. But many of the special taxes associated with the law, especially ones on medical device makers, pharmaceutical companies, and the supplemental capital gains tax, were immediately implemented. In effect, the legislation was written with ten years of tax revenue, but only 6 years of program outlay. The CBO was perfectly aware of this, but by law could not account for it at the time. Four years later, when the CBO again scored the cost of Obamacare, it had doubled¹⁶.

That said, the above was not enough to get the ten year cost down below a trillion dollars (about double Thailand's annual GDP), so Obamacare also eliminated the "Doc Fix". In 1997, the Medicare Sustainable Growth Rate (SGR) rule was enacted, which was intended to prevent Medicare spending on doctors from increasing faster than GDP. Since health care spending as a percent of the economy was rising, this meant that physician fees had to be reduced. So in 2003 congress passed a supplemental budget, - the doc fix - to raise fees for one year. When that money was gone, they did it again, a total of 17 times between 2003 and 2014.¹⁷ By

¹⁶ "CBO: Obamacare costs double to 1.8 Trillion in first decade"

Washington Examiner, May 14 2013

<http://www.washingtonexaminer.com/cbo-obamacare-costs-double-to-1.8-trillion-in-first-decade/article/2529655>

¹⁷ In 2015 Congress abolished the practice of periodically voting on a doc fix, and instead created a formula to define future payment increases.

doing it this way, all incumbent members of congress got to claim they had increased spending on the poor AND on had increased spending on Doctors (who are not, in fact, poor). Politicians of both parties loved doing this, Washington can be very bi-partisan when doing so helps incumbents of both parties in elections.

Obamacare assumed no future doc fix, which would have resulted in a 20-25% reduction in Medicare reimbursement rates. This saved money both by paying less for services delivered, and also through all the services that the CBO estimated would no longer be delivered, when doctors dropped out of the program. These savings were enough to bring the estimated cost of Obamacare below a trillion. The problem is, nobody – including the CBO - actually believed that congress would have allowed this to happen. The CBO was none-the-less constrained to produce budgetary estimates as if it would, even as the two parties were negotiating a separate deal to again pass a doc fix.¹⁸

The above sorts of gamesmanship, and the fear of it, is what leads to the final CBO constraint – by law it was prohibited from engaging in dynamic scoring. When the CBO scores a bill, it is allowed to estimate the direct effect of changes in behavior from the bill. So in the above example of the doc fix, the CBO estimated that some doctors would stop seeing Medicare or Medicaid patients, which would increase wait times and reduce medical care. Budgetarily, this meant

¹⁸ “The Doc Fix is Small Change Compared to what will be needed to Fix Obamacare”, Forbes, 7 April 2015
<https://www.forbes.com/sites/johngoodman/2015/04/07/the-doc-fix-is-small-change-compared-to-what-will-be-needed-to-fix-obamacare-2/#6af7791b7eee> While I gave two particularly egregious examples of gamesmanship related to Obamacare, I don’t want to imply that all this gamesmanship comes from that particular program, or that only Democrats do it. Republicans are certainly not immune to this temptation.

that Obamacare again now appeared to be less expensive than it would actually be, and eventually was – since government outlays were being converted into other, off the book costs. However, the CBO did not, because it was not allowed to, estimate what effects those changes might have on the broader economy as a whole, GDP, unemployment, etc.¹⁹

There are both methodological and political reasons for this. The methodological one is that it is very, very hard to do. All kinds of assumptions about consumer behavior, elasticities, future shocks, etc. need to be made. So better to leave the federal reserve system to do that sort of forecasting, and to just compare bills on a clean, consistent standard. And for most smaller bills, that have a limited macroeconomic effect, the difference between a dynamically scored and a statically scored budget projection is fairly small. The trade-off between accuracy and consistency weighs heavily towards consistency. When considering something as all-encompassing as Obamacare, the Republican replacement plan for it, or President Trumps proposed tax reforms, they will all almost certainly change behavior in broad ways.

As an example, consider the CBO's projections about total enrolment in the Obamacare exchanges. Given below (Figure 1) are the CBO's estimates made in 2010, 2012, 2014 and 2016, as well as the actual data from 2014-2017. The CBO has consistently overestimated the Obamacare exchanges²⁰, and continues to do so. It should be noted that

¹⁹ In essence, the CBO models of the economy can use well established “parameters” for calculating effects, i.e. income or price elasticities, Okun's coefficient, the Philips curve, etc. The CBO is prohibited from assuming that legislation can change those parameters.

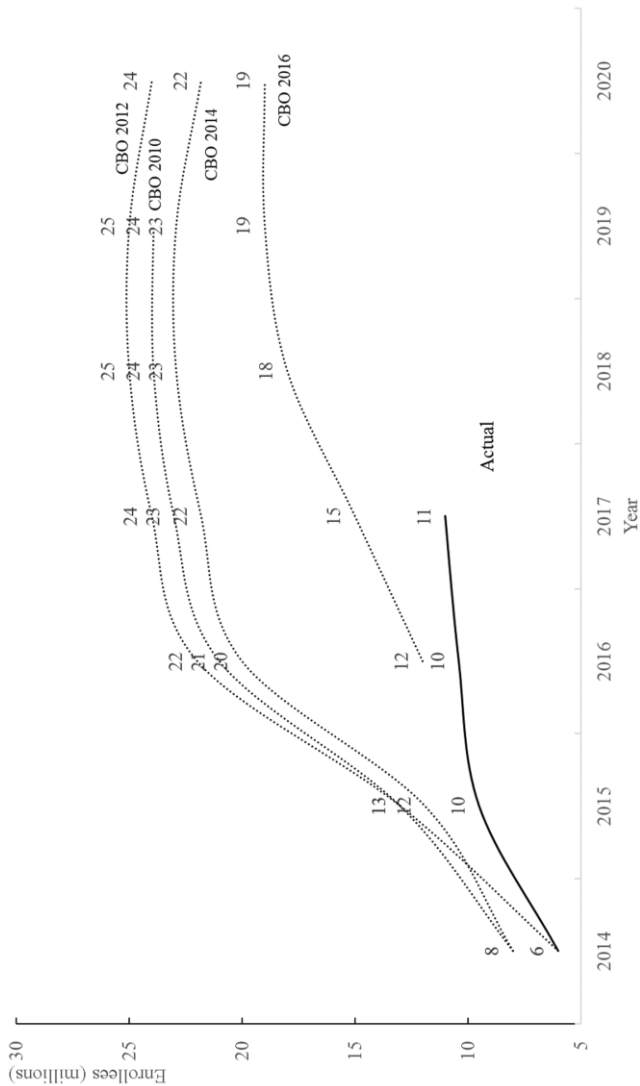
²⁰ “Learning From CBO's History of Incorrect ObamaCare Projections”, Forbes, 2 January 2017
<https://www.forbes.com/sites/theapothecary/2017/01/02/learning-from-cbos-history-of-incorrect-obamacare-projections/#7816ccbb46a7>. In the

the CBO's estimates of how many people would have lost insurance under the House's AHCA (fully explained later) was based on their 2016 projections of enrolment in Obamacare, which is to say they assume that if the ACA continues as is, enrollment in the exchanges will increase to 19 million in the next two years.

There is also a strong political calculus for not using dynamic scoring, though the two parties arrived at that conclusion for different reasons. Democrats were opposed to dynamic scoring because it would tend to make tax cuts look less damaging to the government's ability to raise revenue, as taxes go down, some of the lost revenue is recouped through greater economic activity. Likewise it would make many large government policies appear more damaging to the economy, if we included the estimated deadweight losses and altered behavior that inevitable come about with government programs. Republicans were against dynamic scoring because they wanted to keep things simple, the moment dynamic scoring began, the fear was, one was allowing technocrats to start making value judgements about things. Republicans assume all technocrats are Democrats at heart, at least until proven otherwise. It should be noted that the rules have recently been changed, and the CBO is now beginning to do some dynamic scoring in addition to its older static scoring methodology.

CBO's defense, their estimates were better than most, but that everybody was so far off in the same direction, implies a systematic problem with this sort of modelling, or a serious bias in the data everyone is using.

Figure 1. CBO ACA Projected Enrolment Over Time, and Actual Enrolment (millions of Enrollees)



Source: CBO Reports, 2010-2016

The CBO still has a fairly good reputation, and to the extent that it has been damaged recently it is at least in part because of the games its political masters have been playing. The CBO also has a very tough job, especially when huge programmatic changes, or tax cuts or increases, etc. are proposed, especially given the political uncertainty of what will actually happen. The CBO is aware of its own limitations, and tries to remind everybody that its calculations are actually just estimates. It is still the best game in town, but its estimates were never as accurate as others claimed, and they have become less accurate recently as they have been fed more bad data and misleading legislative proposals to estimate.

5. The Affordable Care Act (Obamacare) and the Future of American Healthcare

There is almost no evidence that Donald Trump has ever seriously engaged in the issue of Healthcare. Conversely, no other government program has generated more controversy, political battles, electoral swings, or heated Supreme Court battles than this since 2008. At this point, Obamacare²¹ is President Obama's one great political triumph, and the program is his legacy. It is not particularly popular, and it has faced intense opposition throughout its existence. Though it gained popularity when Republicans were trying to repeal it, now that that effort has, for now at least, failed, it is again losing popularity. At its most popular point, it still barely

²¹ The formal way to refer to the Affordable Care Act would be the ACA, but I chose to refer to it by the more colloquial term Obamacare to clearly distinguish it from the Republican alternative, the American Health Care Act (AHCA). This should hopefully make it easier for the reader to distinguish between the two programs in the analysis to follow.

topped 50%, and only 26% want to keep the law as it is, while 30% still want outright repeal.²² Strong opponents still outnumber strong supporters. Furthermore, the Obamacare exchanges are in trouble, and absent government intervention to save them, it is not at all certain that they will not simply collapse if insurers withdraw from them.²³

According to the Kaiser Family Foundation (KFF), Obamacare has reduced the number of uninsured, from about 17% of the population to 10%²⁴, but how it did so is complex. Between 2013 and 2015 The KFF calculates the number of people insured by Obamacare on the exchanges reached 11 million, with another 15 million enrolling in the expanded Medicaid program²⁵. The total number of uninsured dropped from 41 million to 28 million, so the total number of uninsured dropped about 13 million – which means the exchanges and Medicaid combined are now insuring about 13 million who already had insurance. Most healthcare economists believe that most of the newly insured are on Medicaid, but nobody is really sure.

²² “Affordable care act Gains Majority Approval for First Time” Gallup 4 April 2017 <http://www.gallup.com/poll/207671/affordable-care-act-gains-majority-approval-first-time.aspx>

²³ Rough day for Obamacare as another insurer quits in Virginia” Washington Examiner 3 May 2017 <http://www.washingtonexaminer.com/rough-day-for-obamacare-as-another-insurer-quits-in-virginia/article/2622050>

“Aetna CEO: Obamacare Will Continue to Deteriorate If Nothing Happens” Washington Free Beacon 8 May 2017 <http://freebeacon.com/issues/aetna-ceo-obamacare-will-continue-deteriorate-nothing-happens/>

²⁴ “Key Facts about the Uninsured Population” Kaiser Family Foundation, 19 Sept 2017 <https://www.kff.org/uninsured/fact-sheet/key-facts-about-the-uninsured-population/>

²⁵ *ibid*

Republicans have been running against Obamacare since the day it passed, and once they gained unified control of the federal government in the 2016 election, they appeared to believe themselves to be politically compelled to address it. Under Speaker of the House Paul Ryan, they first passed the American Health Care Act (AHCA)²⁶, which had to be pulled from the House floor before a vote, since it could not pass. He revised it, and on May 4th, the House passed the revised version of it. At that point, it went to the Senate, which began revising the proposed legislation in all sorts of ways. Competing plans were put forth, but ultimately in late September Republicans abandoned the effort for this legislative year.

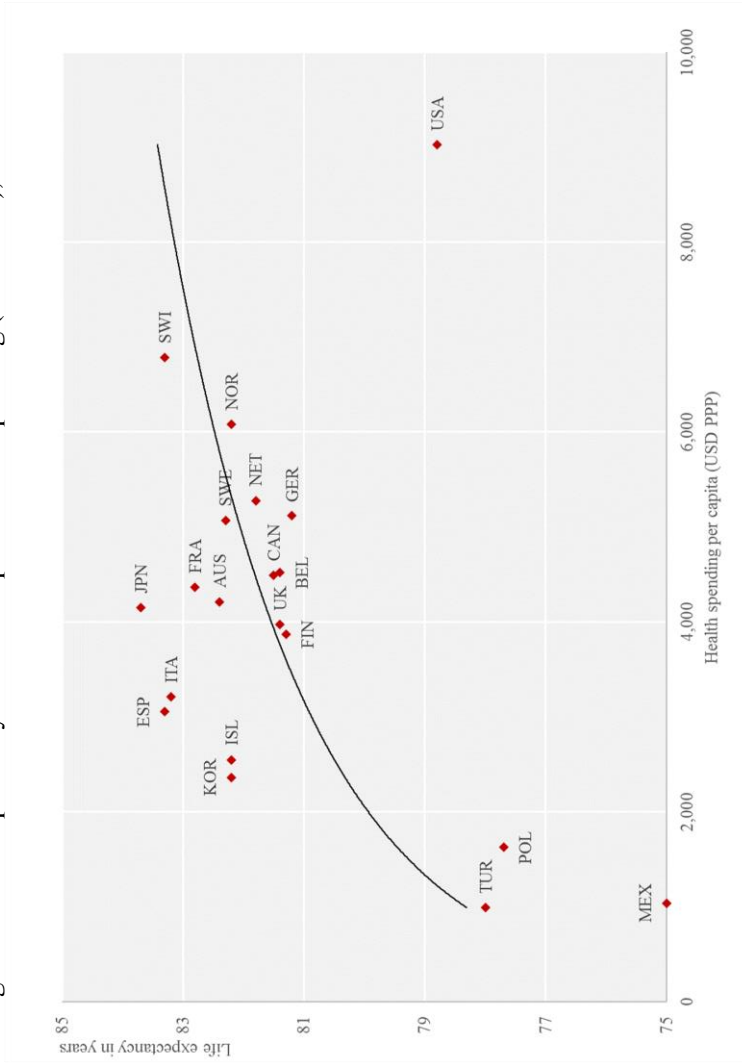
The impetuosity for passing it, aside from the current problems with Obamacare, go to the heart of the real problem of U.S. healthcare, as Republicans see it. As one can see from the chart below (Figure 2), life expectancy in the U.S. is lower than the OECD average (78.6 years vs. an OECD average of 81.2), but that difference is small, and largely (in the Republican view) explained by differing lifestyle and behavioral choices²⁷. But the amount Americans pay for health care is about double the OECD average, and that is the great problem of U.S. healthcare.

²⁶ H.R. 1628 – American Health Care Act of 2017

<https://www.congress.gov/bill/115th-congress/house-bill/1628>

²⁷ “Why do Americans have shorter life expectancy and worse health than people in other high-income countries?” Avendano, Mauricio and Ichiro Kawachi, US National Library of Medicine, National Institutes of Health, 9 January 2014 <https://www.ncbi.nlm.nih.gov/pmc/articles/PMC4112220/>

Figure 2. Life Expectancy and Per Capita Health Spending (USD PPP), Selected Countries



Source: OECD Health Statistics (2015)

The heart of the Republican critique of Obamacare was that it was addressing the wrong problem, it was trying to get more people enrolled in insurance, and it was trying to force them to purchase more generous insurance, when the real problem with American health care is cost. Forcing more people to purchase a more generous version of an already overpriced product would only worsen the fundamental problem of U.S. healthcare. While a detailed explanation of all the reasons for health insurance in the U.S. to be so costly is beyond the scope of this article, the Republican explanation can be summed of quite briefly.

Everything in the U.S. healthcare system is paid for by a third party, and thus one has a massive system of people paying for the care of other people, using a third person's money. The revised AHCA, and its various later iterations, were the Republicans first attempt to change the healthcare system while actually having the potential votes to do so. It²⁸ would do so through two primary mechanisms, both intended to lead to a more market-based approach than Obamacare.

In the Obamacare exchanges, Ryan's plan significantly restructures the way those exchanges work, currently they use strict and restrictive community ratings and the mandate to force the young to purchase expensive and actuarially overpriced plans, which then subsidize the insurance of older Americans. The AHCA reduces or eliminates the scope of regulators to enforce community ratings on the prices insurers are allowed to charge for insurance policies, which limits the cross-subsidies that are the heart of the exchanges. It also gives insurance companies far more scope to use actuarial values in pricing insurance, and allows states to opt-

²⁸ I will refer the AHCA and its subsequent plans as "it", though in reality there were several plans – but to go through all the differences in each would be extremely tedious

out of the generous “essential health benefits” that drive up the costs of plans.

The intent of this is to allow insurance plans to correspond to the actual costs of issuing them, instead of trying to force some people to subsidize others. By allowing states to opt out of essential benefits, the older low cost catastrophic insurance plans can be brought back. The mandate would be eliminated, replaced with a surcharge for those who buy insurance after getting sick. Other elements of the law encourage states to create high risk pools, which the federal government would help fund, to deal with pre-existing conditions. The intent of this is to make sure that the truly sick still get treated, but also to remove them from the normal insurance market, so that it can function as it used to, which would reduce premiums (Republicans believe) dramatically.²⁹

This last point is an attempt to address the changing nature of health care and health insurance since the early 1980s. World War II price controls were the initial incentive for providing health care through insurers – since it was an untaxed benefit and not subject the very low wage ceiling put into place during the war, it offered employers a way to pay workers more in a very tight labor market. Since firms didn’t actually know how to provide healthcare, they offered it as insurance, and once this system was in place it proved popular, and gradually came to dominate how Americans consume healthcare.

Until the 1980s, most routine healthcare was still paid out of pocket, insurance was for “catastrophic events”, as is

²⁹ A good introduction to the underlying logic of the plan would be Roy, Avik S. A. *Transcending Obamacare: A Patient-Centered Plan for Near-Universal Coverage and Permanent Fiscal Solvency – Second Edition*, The Foundation for Research on Equal Opportunity, 2016, Austin, Texas

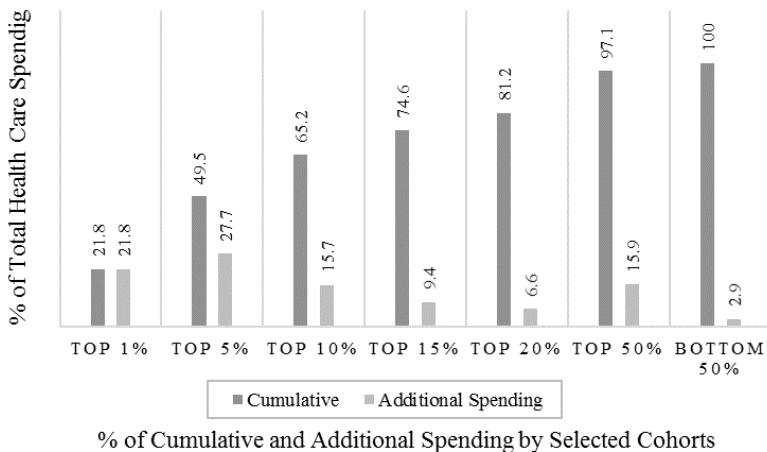
standard in other insurance markets. Normal day to day doctor visits, minor surgeries, dental work, etc. was paid by consumers. Catastrophic events were paid for by insurance, but those costs were generally capped as a practical matter. If one were in a car accident and broke his leg, insurance would kick in. But after a year, his leg was better, and the catastrophe was over. Conversely, if he got lung cancer, he was going to die, the medical issue now was pain management – which was not particularly expensive for the insurance company, and again of limited duration. What has changed since then is that technology now allows us to deal with chronic conditions that in the past were untreatable, they killed a person or he endured them. A person with crohns disease, for example, can live a much healthier, and longer life today than 30 years ago, but it will require large expenditures on healthcare every year of that person's life.

As part of the AHCA reforms to the individual market and Medicaid, the states were given incentives to create programs to move the chronically ill out of standard insurance policies or Medicaid, and into high risk pools. These high risk pools – basically a health care insurance program specifically designed to deal with the chronically ill - would be a separate program, where states would be given considerable freedom in how managed them. Possibly states would directly pay doctors, or they would subsidize policies for those in the pools, or pay insurers a lump sum to handle the cases for them, or any number of other ways of dealing with this population. The point is, separate the chronically ill from everybody else, and then tackle that problem directly. States would also have been allowed to enroll anybody whose healthcare expenditures was expected to exceed a certain amount, into the high-risk program.

The attraction of the high risk pools and the changes to Medicaid goes to the way costs actually occur in a market. In

a normal market, people do not pay averages, they pay by the case. As stated earlier, on average it costs about six times as much to insure a 64 year old as a 25 year old, but what we are really saying is that for any group of 64 year olds, many will cost 3-4 times as much to insure as a 25 year old, and a few will cost over 50 times as much.

Figure 3. Concentration of U.S. Health Care Spending (2009)



Source: Kaiser Family Foundation and U.S. Department of Health and Human Services

As the above chart (figure 3) shows, the distribution of health care spending is highly concentrated in a few people. The bottom half of the population costs 3% of total health care expenditures, and 49.5% of health care expenditures are on just 5% of the population (and almost half of those expenditures are on just 1% of the population. Of the 5% who are spending half the healthcare costs – most of them will be just as expensive the next year. Health care expenditures are highly correlated across time.

Once the chronically ill (of any age or income level) are separated out, insurance premiums would immediately fall. They would fall because now the primary consumers of health care are in a different market, which would effectively mean that there were far fewer high-expenditure cases in the rest of the market, and those cases would be of people without pre-existing conditions, i.e. healthy people who needed protection from an unforeseen catastrophe – exactly the sort of thing insurance is good at dealing with. There would also now be an upper cap on what an insurer had to pay out for any medical event, because if a health care issue became chronic, that person would eventually transition into the high risk pool. To use the example of an accidental fall on the ice, somebody who broke their leg would be covered by the insurer, and once they were healed life would go back to normal. Somebody who was permanently paralyzed in the same fall, requiring lifetime coverage and healthcare, would also be covered initially, but at a certain point they would be transitioned off the insurance books and into the high risk pools³⁰.

Overall, the Ryan plan would have reduced taxes associated with healthcare in many ways. Some of these reductions come from reducing many special excise taxes or surcharges that Obamacare placed on employer provided plans, medical device manufactures, and other parts of the healthcare system, or capital gains. But it also eliminates the direct subsidies in the exchanges for poor and middle class

³⁰ Exactly how the high risk pools would reduce costs was not made clear in the Republican plan, partly because they were leaving it up to the states, and partly because Republicans are unsure exactly what mix of policy options would be optimal or feasible or (critics would add, justifiably) would work. Their point was to get them out of the insurance market, so that that market could go back to working, and to attack the problem of chronic care directly.

purchasers, instead converting them into a non-means tested tax credit. This would most likely have priced many of the near-poor and the middle class, and people in their 50s and 60s who are not yet eligible for Medicare, out of the market. The tax credit is also regressive, it benefits the wealthy more (since they pay higher marginal taxes), and it especially helps them if they are the only ones able to afford healthcare, and thus the only ones to get the credit.

By far, most of the criticism of the new plan among Republicans was of these tax cuts. It seems clear that Speaker Ryan was trying to not just replace the implicit taxes³¹ built into the Obamacare subsidies, but to also not raise marginal rates. As it is, the tax rebates combined with the Medicaid cutoff point at the poverty line would in turn create a Medicaid cliff – where if one exceeded a certain income level, he would lose Medicaid and suddenly have to pay thousands of dollars for private health coverage. More than any other part of the bill, this is the part that the various senate plans all sought to change.³²

The other big changes in the AHCA act were in Medicaid, which at 72 million currently enrollees has 4 times as many recipients as there are in the individual market, and 7

³¹ An implicit tax is a reduction of a government benefit as income goes up. So for example, if my income goes up \$100, but that reduces the government subsidy I receive to purchase health insurance by \$50, I paid an implicit tax rate of 50%. Obamacare, especially when it was first rolled out, had very high implicit taxes built into it.

³² Most of this summary of the impact of the AHCA on the exchanges is explained at greater length at “If the senate doesn’t Fix the Houses’s Obamacare Replacement, the GOP Will Pay a Steep Price” Forbes, 4 May 2017 <https://www.forbes.com/sites/theapothecary/2017/05/04/if-the-senate-doesnt-fix-the-houses-obamacare-replacement-the-gop-will-pay-a-steep-price/#721898d04a58> , though my analysis differs in some details.

times the enrollment in the exchanges.³³ The AHCA reforms it in two important ways, first it again limits Medicaid to those at or below the poverty level. Secondly, it grants states the ability to take Medicaid money as a block grant rather than as a matching grant for every state dollar spent. This would allow states much more freedom in how they administer and the run the program, and would eliminate at least some of the incentives for fraud³⁴, estimated at close to \$100 billion a year, that have long bedeviled Medicaid. Medicare has been largely ignored throughout this process, unlike Medicaid it can't be reformed without a filibuster proof majority.

Once the bill made its way out of the House, the Senate took it up. It quickly became apparent that while Republicans were unified on wanting to repeal Obamacare, they were not all onboard with the House's AHCA. The Senate quickly concluded that it would not accept the House version as written³⁵, and instead produced its own version. Senate Majority Leader McConnell brought the bill to the floor, withdrew it, revised it, and brought it to a vote only to see it lose. Other senators then began creating their own versions and revisions, but all the new bills suffered from serious defects due to the speed at which they were being drafted. The process, and the CBO's scoring of it, combined to make the Republican proposals extremely unpopular, and

³³ *ibid*

³⁴ For an excellent short description of how that fraud is committed, and some historic examples, see "The \$272 billion swindle" Economist 31 May 2014 <http://www.economist.com/news/united-states/21603078-why-thieves-love-americas-health-care-system-272-billion-swindle>

³⁵ "Senate GOP to Snub House Obamacare Repeal Bill and Write Its Own" Bloomberg , 5 May 2017 <https://www.bloomberg.com/politics/articles/2017-05-04/senate-gop-plans-own-obamacare-repeal-bill-after-house-action>

Obamacare became more popular. Under normal circumstances, one would have an engaged President helping the process along, but throughout this whole process, one of the least important people in Washington was President Trump. His first attempt to help the process along, by trying to convince House Republicans to vote for it the first time it came up, was an embarrassing failure.³⁶ After that, he confined himself to tweets about it, with no discernable positive impact.

In late September, Republicans made a last ditch attempt to produce something, but could still not quite get to the 50 votes they needed. At that point, they abandoned the effort, and instead moved on to tax reform and judicial issues. But that does not mean the issue is over.

Throughout the summer, as this whole drama was playing out, other things were happening in the healthcare market. Insurers began dropping out of markets, indeed Aetna eventually dropped out of all the markets³⁷. By the end of the summer, about 25% of U.S. counties only had one health insurer in the individual markets. At the same time, in preparation for the November 1 – December 15th open enrollment period, insurers began to apply for their rate increases from the various state insurance regulators. At the time of this writing, the exchanges have only been open 2

³⁶ “Reports: Trump’s “Art” Didn’t Work on Failed AHCA Deal” New York Magazine, 25 March 2017
<http://nymag.com/daily/intelligencer/2017/03/reports-trumps-art-didnt-work-on-failed-ahca-deal.html>

³⁷ “Aetna completely exits Obamacare exchanges, cites massive losses” Kimberly Leonard, Washington Examiner, 10 May 2017
<http://www.washingtonexaminer.com/aetna-completely-exits-obamacare-exchanges-cites-massive-losses/article/2622734>

days, it appears that the standard premium for a silver plan has on average increased over 35% above 2017 prices.³⁸

At the same time, the Trump Administration has begun issuing executive orders on health care that will have serious effects on the exchanges. They are ending the cost-sharing insurance subsidies³⁹, a program that reimburses insurers for higher out of pocket expenses (required by law) when they issue insurance policies to the poor. While allowed in Obamacare, the law provided no mechanism to fund the subsidies, the Obama administration took the money from other accounts. A court challenge to prevent the Obama administration from paying the subsidies has been working its way through the courts, but a new challenge that would force President Trump to continue paying for them has already lost its first court challenge⁴⁰. At this point, it looks like the payments will indeed end, further roiling the exchanges.

Additionally, the Trump administration has begun the process of changing regulations on short-term insurance⁴¹.

³⁸ “Premiums for the benchmark silver Obamacare plan will soar 37%, on average, for 2018” CNN Money 30 October 2017
<http://money.cnn.com/2017/10/30/news/economy/obamacare-premiums/index.html>

³⁹ Trump Axes ACA cost-Sharing Subsidy Payments to Insurers” Robert Lowes, Medscape, 13 October 2017
<https://www.medscape.com/viewarticle/887004>

⁴⁰ “Judge rejects request to force Obamacare subsidy payments” Ariane de Vogue, CNN Politics, 25 October 2017
<http://edition.cnn.com/2017/10/25/politics/obamacare-subsidy-restraining-order-lawsuit/index.html>

⁴¹ “In Start to Unwinding the Health Law, Trump to Ease Insurance Rules” Louise Radnofsky, Stephanie Armour and Anna Wilde Mathews, Wall Street Journal, 11 October 2017 <https://www.wsj.com/articles/in-start-to-unwinding-the-health-law-trump-to-ease-insurance-rules-1507771015>

One of the important goals of the ACA was to eliminate “catastrophic” insurance plans, to force people to purchase comprehensive plans. When the exchanges were first implemented, people discovered that short term insurance, the sort purchases by travelers to the U.S., exchange students, or people between insurance plans, were exempt from many of the ACA regulations. In response people began purchasing these plans to escape Obamacare, the Obama administration created regulations to limit those plans to 3 months, and to make them non-renewable, to force people back onto the exchanges. President Trump has begun the process of changing those rules, which will potentially make a form of catastrophic insurance again viable, though it will further destabilize the exchanges.

Finally, the administration has also begun to take the first steps towards loosening, or simply not enforcing, the individual mandate. At the time of this writing, it is not clear by how much, or if it part of a negotiating ploy to try and force Democrats to negotiate about other parts of the Obamacare, but as with other recent administrative moves, changing it will bring further instability to the Obamacare exchanges.

It seems clear at this point that Republicans want to move on to Tax reform, and to shelve healthcare reform for another year. But given the real problems that existed in Obamacare before they tried to reform it, and given the recent administrative changes that the Trump administration has begun, it is quite possible that health care will force its way back into the news much sooner than most people expect.

6. Tax Reform and Entitlement Reform

Nowhere is the overlap between President Trump and the Republican party greater than on the issue of tax reform, and nowhere is the gap larger than on entitlement reform. Both are for tax reform, and while they differ on some details (most notably a border adjustment tax), most of those differences are about rates, not principles, so there is plenty of room for compromise. And politically, tax reform has the advantage of being, at least potentially, popular.

Conversely, Paul Ryan made his name within the Republican party as the person who knew, could explain, and had the courage to confront, entitlement reform⁴². Most Republicans, at least in the abstract (where “the abstract” refers to a place that doesn’t impact their chances of re-election next cycle) support entitlement reform, because it is clear that someday the U.S. government will no longer be able to pay for all the things it has promised to pay.⁴³ Since coming to prominence, first as the chairman of the House Ways and Means committee, then as the Republican Vice presidential nominee in 2012, then as the Republican House Leader, and then Speaker of the House in 2015 – Paul Ryan has been associated with entitlement reform.

⁴² Democrats have a very different, and substantially more negative, view of Ryan as a serious thinker about public policy issues.

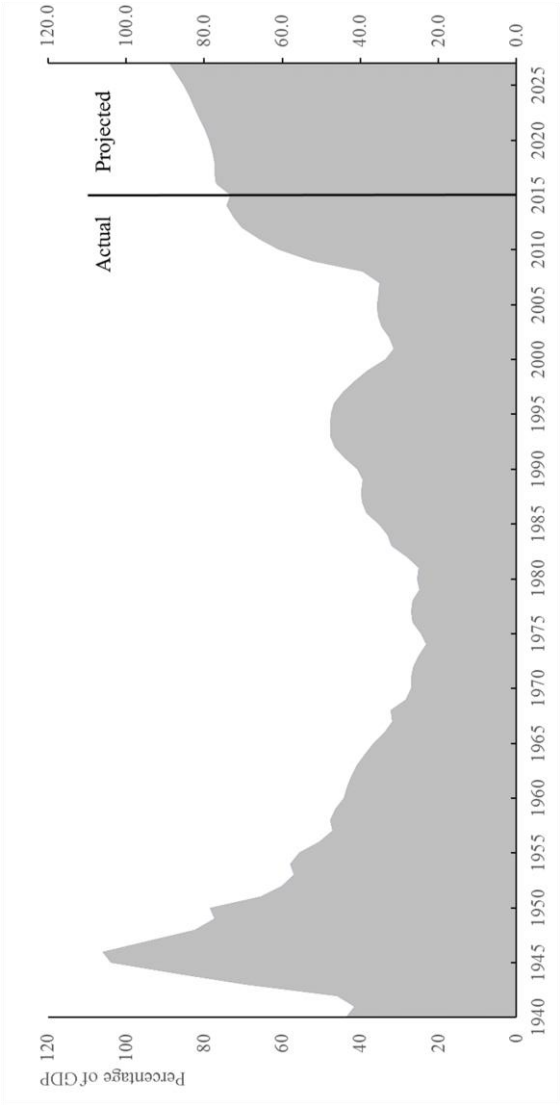
⁴³ The official National Debt in 2015, according to the CBO, was 13.1 Trillion dollars, about 75% of GDP, but that only counted publicly held (non-U.S. government held) debt. If one adds intergovernmental debt such as the social security trust fund, the number rises to 18.2 trillion, a bit over 100% of GDP. Beyond that, there are all the future entitlement payments the government owes, which brings the figure well above 150 trillion, but most (not all) of that will come out of projected future revenue. There is considerable debate about how bad the future unfunded liabilities are, but they are significant, and sooner or later will need to be dealt with.

Outside of healthcare, where the problems of Obamacare are such that repeal or reform may (in the long term) be unavoidable, and where any changes will certainly benefit at least some people given how the mandate and subsidies work, any significant plan to reform entitlement programs will require real political leadership and courage. The public is in agreement with many Republicans, in that they believe, in the abstract, that some sacrifice is necessary. In the here and now, they punish anybody who asks them to do so. President Trump ran on a platform of not reforming entitlements, and his first budget proposal reflected that⁴⁴, indeed he made vague statements at times about expanding them. It is very hard to see a politician who cares so much about being liked, and who has no mandate to reform entitlements, who may or may not really understand the issue anyway, being willing to do the heavy lifting necessary to reform them. Without significant presidential leadership, it is hard to see Congressional Republicans doing it themselves, unless of course they are forced to by events.

This basically means that U.S. fiscal policy will run about the same as it has, assuming no significant tax reductions. The U.S. will continue to run budget deficits, the size of the debt will grow, and the U.S. fiscal situation will deteriorate. The two major entitlement programs, Social Security and Medicare, will continue to grow as the baby boom generation retires, squeezing other parts of the budget. In the Republican view, this is not sustainable in the long run. But it is sustainable in the short run, just nobody knows at what point it becomes a crisis. As Stanley Fischer so aptly put it, “a financial crisis takes a long time to happen, and a

⁴⁴ “No cuts to U.S. entitlements programs in Trump budget: Mnuchin” Reuters, 26 February 2017 <http://www.reuters.com/article/us-usa-trump-economy-idUSKBN1650LL>

Figure 4. Publicly Held U.S. Federal Debt (% of GDP)



Source: CBO: The Budget and Economic Outlook: 2017 to 2027

financial crisis happens very quickly”. Below is the CBO’s most recent estimate of U.S. deficits (not counting inter-governmental debt), assuming no significant policy changes, and moderate economic growth – which is to say nothing much bad happens.

Total publicly held debt would go up from about 82% of current GDP, to perhaps 95%. To put that number in some perspective, one can compare it to national debt levels for the selected countries in Table 1, below.

Table 1. Public Debt as a % of GDP (% Change from Previous Year)

	USA	Thailand	Greece	Germany	Japan	China
2007	37 (5)	41 (9)	107 (27)	68 (15)	171 (-2)	21 (9)
2011	63 (11)	43 (18)	146 (3)	83 (9)	200 (19)	16 (17)
2015	87 (11)	54 (14)	151 (-17)	85 (0)	248 (-1)	17 (13)

Source: The Economist Intelligence Unit.

The U.S. is not at Greek levels of debt, or Japanese levels. But the U.S. position has deteriorated compared to other countries, and in comparison to where it was before the great recession. This is worrisome, because the only major change to entitlements since 2008 has been Obamacare, a vast expansion of the entitlement state. The U.S. debt levels are now above the European average, though since U.S. growth has exceeded European growth since 2008, the U.S. has more room to grow its way out of the debt. That said, European countries have begun to actually grapple with their debt and demographic futures.⁴⁵ Germany has raised the

⁴⁵ “Entitlement Reforms in Europe: Policy Mixes in the Current Pension Reform Process”, NBER Working Paper No. 18009 April 2012

retirement age from 65 to 67, and since 2015 has run budget surpluses. France has also raised its retirement age, and has begun reining in its public sector pensions. At some point, the U.S. will need to address this problem, there is little reason to think this is that point.

A further complication is the differing ways in which debt is held. Most of the U.S. debt is held domestically, though significant exposure to China and Japan remains. Still, when a public debt is primarily held domestically, there is less chance of a financial meltdown, especially of the sort Greece is going through. This is especially true for the U.S., because the last thing either Japan or China want is for U.S. government securities to lose value. The old adage “loan a man a thousand dollars and you own him, loan him a million dollars and he owns you” could well hold in this case.

Furthermore, because the U.S. has its own currency, monetary policy can in part ease the burden of debt, assuming trade-offs in inflation, exchange rates and/or interest rates are acceptable. And since the dollar is still the world’s reserve currency, the U.S. still gains the advantage of seignorage (taxation through the creation of money) with regard to the rest of the world. While a general consensus exists that domestically held debt is better than foreign held debt for dealing with a financial crisis, there is debate about how much better it is. Still, at this point U.S. finances seem sound for the next few years, and President Trump’s nomination of Jerome Powell to be next Chairman of the Federal Reserve is generally seen as a good, normal choice.

While non-healthcare related entitlement reform seems unlikely, tax reform and/or tax relief is an area of broad agreement between President Trump and republican lawmakers. In early May President Trump released his

proposal for tax reform⁴⁶, one which was very popular with Republicans, and equally unpopular with Democrats. At 2 pages long, it was more of an executive summary than a plan, but it is at least a statement of general principles, and gives Republican lawmakers an idea of President Trump's thinking on the issue.

Taking its effects on income taxes first, it reduces the number of tax brackets from 7 to 3, at 10%, 15% and 35%. The standard deduction is doubled to about 24,000, which would remove large numbers of the poor from the income tax rolls. The alternative minimum tax, the estate tax, and the Obamacare supplemental capital gains tax are all eliminated. The deductions for home mortgage interest and charities are retained, the deduction for state and local taxes is eliminated.

The impact of a tax reform like this will be threefold. First, it would lower taxes overall, in percentage terms probably more for the poor and middle class, but in absolute terms more for the rich.⁴⁷ Secondly, if we ignore the potential economic effect of spending that money on more government where it would be used more efficiently (republicans don't believe that, democrats do), it would serve as a mild fiscal stimulus, and potentially as a boon to the economy as it reduced various deadweight losses. While some elected

⁴⁶ TRUMP: Tax Reform that Will Make America Great Again
<https://assets.donaldjtrump.com/trump-tax-reform.pdf>

⁴⁷ The overall equity benefits and costs depends very much on where the brackets are drawn, and since this isn't in the released details, it is very tough to estimate this. Almost any general income tax reduction is going to have a huge absolute effect on the rich, since the top 3% of taxpayers (\$250,000 and above) pay more than half the income tax. "High-income Americans pay most income taxes, but enough to be "fair"", Pew Research Center 13 April 2016 <http://www.pewresearch.org/fact-tank/2016/04/13/high-income-americans-pay-most-income-taxes-but-enough-to-be-fair/>

Republicans claim the cuts will pay for themselves (the Laffer curve), only a tiny number of economists (including many who work for right leaning think-tanks) believe that would happen⁴⁸. There is going to be a great deal of dispute in the coming months about how much revenue would be lost, since there will be dispute about how much growth the tax plan will generate. What we are really talking about, here, is a dispute between equity and efficiency. Republicans are willing to trade off some equity for more efficiency; by and large Democrats are not.⁴⁹

President Trump is also supporting corporate tax reform. He has proposed reducing the corporate tax rate from 35%⁵⁰ to 15%; the OECD average is about 25% and no OECD country other than the U.S. has a rate above 30%. This would be combined with the elimination of many corporate tax

⁴⁸ I was not able to find any searching at the American Enterprise Institute, the Heritage Foundation, the Cato Institute or the Mercatos Center. I don't want to say there are none, but I can't find them.

⁴⁹ "Trump's Tax Plan" Hoover Institute 1 May 2017
<http://www.hoover.org/research/trumps-tax-plan> Many Republican lawmakers believe the "Reagan boom" of the 1980s was due to the Reagan tax cuts. While there is dispute in the academic literature as to how much of an effect those tax cuts had, there is a general agreement that they had some impact. They did, however, also increase the deficit. And even if one believes that tax cuts are good for the economy, there is a great deal of difference between cutting marginal tax rates from 85% to 30%, and cutting them from 40% to 30%, as would be the overall case today.

⁵⁰ The top corporate tax may be 35%, but many pay less. According to the Institute on Taxation and Economic Policy, the 258 fortune 500 corporations who all made profits each year between 2008 and 2015 paid an average tax rate on their profits of about 21%. General Electric paid none in that period – "GE is a tax avoidance firm that happens to make washing machines", as the joke goes. "The 35 Percent Corporate Tax Myth" The Institute on Taxation and Economic Policy, March 2017
<http://www.itep.org/pdf/35percentfullreport.pdf>

deductions. As with the income tax changes, this would serve to make corporate taxes lower but broader, something most economists support. But again, the basic proposal as Trump has made it would not be revenue neutral, the elimination of deductions would bring in less income than the rate would lose. According to calculations the Economist published, based on OECD and CBO data, the ten year cost of Trump's Corporate Tax plan would be over 2 Trillion in lost revenue, the elimination of deductions would bring in about 1.25 trillion.⁵¹

The corporate tax reforms would also move the U.S. to a territorial tax system. This would end the practice of the U.S. government taxing money earned outside the U.S. that has already been taxed by other governments, when companies bring that money back to the U.S. To give just one notable example, Apple has almost 250 billion in overseas cash and financial assets, that it refuses to repatriate to the U.S. when 40% of it would be taxed away.⁵² A one time tax would be charged on this money, allowing firms to repatriate it to the U.S. tax free afterwards, which would bring new investment money into the U.S. Again, there is widespread agreement among economists that the current U.S. system of trying to tax money earned in other countries (both corporate and personal income) is a bad idea.

One thing that was notably absent from President Trump's tax outline was the border adjustment tax (BAT). The BAT is an *extremely* complicated tax, that would in essence eliminate any tax deductions on imports – which

⁵¹ "Donald Trump's Corporate tax plan doesn't add up The Economist, April 2017
<http://www.economist.com/blogs/graphicdetail/2017/04/taxing-times>

⁵² "Apple isn't really sitting on \$216 billion in cash" MarketWatch, 27 January 2017 <http://www.marketwatch.com/story/apple-isnt-really-sitting-on-216-billion-in-cash-2016-01-26>

would primarily impact intermediate goods in corporate supply chains, essentially taxing them, while also eliminating all taxes on revenue from exports. In theory, this would tax imports and subsidize exports, reducing the U.S. trade deficit, and the taxes are how we get Mexico to pay for the wall.⁵³

House Republicans have been pushing for it, at least in part because they hope it would convince President Trump to not impose punishing tariffs. But the BAT has drawbacks of its own. The first is that in a standard frictionless model of an open economy, the dollar will simply adjust to counteract the higher domestic prices of imports. Most economists doubt that would happen because of all the frictions associated with these sorts of cross border supply chains, but since nothing like this has been tried, nobody is quite sure what the effect would be. Secondly the BAT would almost certainly be challenged by the WTO as an unfairly discriminatory tax. Though much of the summer was spent on the issue, at this point it seems that house Republicans and Speaker Ryan have dropped the idea.

It should be noted that for many Republicans, the objections are political or public choice economics, not the standard economic calculus. The BAT would bring in revenue, revenue that could be used to offset revenue lost from other, more important, parts of the proposed corporate tax reforms. Given the nature of the filibuster, corporate tax reform may well need to be revenue neutral to get through the Senate. But many Republicans are very worried about the long run implications of a BAT. To administer it, the U.S. would have to set up the same sorts of monitoring and administrative systems that exist for running a Value Added

⁵³ “Border Adjustable Tax Another Way to Grow Government” Mercatus Center 17 April 2017 <https://www.mercatus.org/commentary/border-adjustable-tax-another-way-grow-government>

Tax (VAT). The U.S., unlike most other countries, does not have a national VAT. While most economists believe a VAT in the U.S. would be good (it taxes consumption, and does so broadly which minimizes deadweight losses) Republicans are intensely hostile to one. They believe that a VAT of zero is politically sustainable, it is hard to implement a 3% VAT if we do not have one. But once we have a 3% VAT, it (Republicans believe) is easy to raise it bit by bit, until we end up with a European level of taxes, and all the new government that money can fund. In this view, aside from all the other unknowns associated with a BAT, if it opens the door to a VAT it needs to be opposed.⁵⁴

President Trump's tax proposals drew fairly strong support from republican lawmakers, but there was concern about the process. Many republicans asked why it took four months to produce a two page plan. This isn't a case where some of the details still need to be hammered out, this is a case where all of them do. For these proposals to go into effect and have any impact on the 2018 midterm elections, they need to be done soon.

That said, while tax cuts of the sort President Trump has proposed have their difficulties, tax reform is easier. Revenue neutral changes can't be filibustered, and many changes can be made at the margin. If President Trump were to lower the corporate tax rate from 35% to 25%, instead of 15%, and still cut most of the deductions being discussed, the change would be revenue neutral (or at least close to it) and would still be a step towards reforming the tax system in a way President Trump and Republicans would prefer.

On October 19th Republicans in the senate narrowly (51 votes) passed a budget, the house had passed one earlier. The two budgets now are subject to reconciliation, where the

⁵⁴ *ibid*

competing budgets are brought together, until the same budget can be sent to both the house and senate for approval. Crucially, reconciliation is not subject to a filibuster, so Republicans now only need 50 votes (the Vice president breaks ties) to pass a budget, one that includes tax cuts.

- At this point, the Republican plan would⁵⁵
- Reduce the tax brackets from 7 to 3, at 12%, 25% and 35%. It does NOT specify at what brackets those taxes would take effect, except at low the lower end, where the 12% bracket would start at
- \$12,000 for a single person, or \$24,000 for a married couple, would be the new standard deduction, and thus the new zero tax bracket, reducing or eliminating taxes for many of the working poor.
- Create a broader child tax credit, from \$1,000 to an unspecified higher number. Additionally, other dependents (typically, but not exclusively, elderly parents) would now be eligible for a \$500 tax credit.
- New rules for small businesses. In the U.S., most small businesses are Corporations, Partnerships or Sole Proprietorships. They would be taxed at 25%, but new rules would be put into place to ensure that the wealthy could not set up “dummy corporations” to pass their money through them to get a lower tax rate.
- Corporate Expensing changes. Instead of pro-rating the expenses of a purchased unit of capital over multiple years, the full cost of the purchase could be

⁵⁵ “What’s In And What’s Out: The GOP Tax Reform Proposal” Kelly Phillips Erb, Forbes 27 September 2017
<https://www.forbes.com/sites/kellyphillipserb/2017/09/27/whats-in-and-whats-out-the-gop-tax-reform-proposal/#2d6a0cb077c4>

deducted (subject to other tax rules) at the time of purchase.

- Fewer itemized deductions. As currently proposed, most itemized deduction would be eliminated, the only significant deductions that would be remain would be for home mortgage interest and charitable contributions. This would eliminate real estate tax deductions, medical expenses, and the state and local tax deductions.
- Eliminating the AMT. The Alternative Minimum Tax (AMT) is a tax that only applies to those who itemize so many deductions that their taxes fall below a certain threshold. Basically it ensures that no matter how many deductions the wealth can take, they none-the-less pay some taxes.
- Federal Estate Taxes. Currently if someone dies, a “death tax” is imposed on his heirs if he leaves any of them more than 5.49 million dollars (double for a couple). This tax would be fully eliminated
- A reduction in business tax credit deductions. Business’s would be taxed at a lower rate, but could take far fewer deductions in turn.
- Global taxation and a repatriation tax. The U.S. would move to a global tax system, as almost every other country in the world has adopted. The U.S. would stop trying to tax profits earned in, and taxed in other countries, or at least would only tax the difference between their tax rates and the U.S. tax rates if U.S. taxes are higher. Additionally, a one time repatriation tax would be implemented, allowing companies to bring the money they have been stockpiling overseas back into the U.S while paying a one time tax far below the current corporate tax.

While Republicans have a path towards tax reform, what happened to their attempts at reforming or repealing Obamacare could just as well happen to their efforts to change the tax code. In the House, the biggest hurdle will be getting House members from high tax blue states, such as New York, California, New Jersey, or Connecticut, to agree to ending the deduction of state and local taxes from federal taxes. This is a very popular provision in those states, and Republicans already have trouble winning elections in them. The revenue that this change would bring in will be large, which can be used to offset the revenue lost from lower overall rates. But the beneficiaries will primarily be to taxpayers in smaller government red states, who get less or no benefit from the deduction today. If these blue state house Republicans revolt on this provision, it seems likely the whole effort will collapse.

In the Senate, it is easy for Republicans to get to 45 or so votes. But getting the remaining 5 votes will be difficult, as the Senate suffers from a “holdout” problem. The closer it gets to 50 votes, the greater the incentive for an individual Senator to holdout for something more to bring back to his voters, or to move the system in a direction that that Senator deems important for the country. Again, a more normal President could usually be counted on to be able to persuade or cajole a few reluctant Senators into supporting something like this, but it is not clear President Trump can. He has publicly feuded with several Republican Senators, who in turn clearly despise him, and in two cases are not seeking re-election but will be around until 2018.

That said, there is one thing that is working in the Republicans favor – desperation. While President Trump has low approval ratings for a President at this point in his Presidency, he has always had that. Republicans in general did better than President Trump or the Democrats in 2016.

But their inability to repeal Obamacare, or to pass much legislation in general, has made them look weak and ineffectual. The “Trump wing” of the party, those people who love Donald Trump and everything he does, are not blaming Trump for the problems, they are blaming Congress. Congress needs to work President Trump, but the legislative process involves negotiations, creating coalitions, back-room horse trading, and all the other things that are necessary to get things done. It requires work, an attention to detail, and above all order. President Trumps mercurial nature, disengagement from the issues, and management style are the opposite of that. The current perception among Republicans that Tax reform is their last chance to get a legislative win⁵⁶ – and to not suffer greatly in the 2018 midterm elections.

7. The Administrative State and the Judiciary

President Trump has had one notable success to his presidency, new Supreme Court justice Neil Gorsuch, and there could well be one or more additional vacancies soon. Beyond that, there are an unusually large number of judicial vacancies at the federal level⁵⁷, the filibuster for judicial nominations has ended, and even if republicans do poorly in the midterm elections, they will still almost certainly hold the Senate at least until 2020. More so than on any other policy issues, Republicans have the ability to reshape the Judiciary for at least a generation. While many of the contentious issues to be dealt with are about cultural issues, one economic issue has become important.

⁵⁶ Trump is getting more involved on tax reform as the clock ticks for a Republican legislative win in 2017, Joe Perticone, Business Insider, 24 October 2017

⁵⁷ “How Trump can reshape the federal courts”, CNN 2 January 2017
<http://edition.cnn.com/2017/01/02/politics/trump-federal-court-vacancies/>

Since 1984, the Judicial branch of the U.S. government has been guided by the “chevron rule”, a legal test decided in the case of “Chevron vs. Natural Resources Defense Council, inc.”. The chevron rule granted government agencies broad discretionary power in how they interpreted congressional standards, basically taking the position that Judges should defer to an agency interpretation of a congressional statute so long as the interpretation was reasonable. Reasonable in this context did not mean correct, only that it could be correct – even if a judge thought it wasn’t true they should defer since the agency presumably had a better understanding of the technical and on the ground issues associated with those things it was regulating.⁵⁸

Though the original decision was unanimous, in recent years there has been growing criticism of the rule among judges and legal scholars, including Judge Gorsuch.⁵⁹ Critics of the rule argue that it has strengthened the executive branch at the expense of the other two branches of government. The Chevron rule allows agencies to interpret congressional statutes in ways congress did not intend, which allows those agencies to make law without congressional input. And by requiring judges to defer to agency rules that judges think contradict the intent of congress, it undermines the courts in their role as the arbiters of what the law says.

Unlike many other issues, this issue cuts against the grain of many traditional republican/democrat politics. In general, Republicans are against “activist” courts – especially

⁵⁸ “Why the Chevron Deference matters in the Age of Trump” Notre Dame News, 6 February 2017 <http://news.nd.edu/news/why-the-chevron-deference-matters-in-the-age-of-trump/>

⁵⁹ *ibid*

judges who believe in a living constitution⁶⁰, but increasingly view some activism as a necessary counterbalance to expansive, unaccountable, and increasingly unsupervised, federal agencies. Many Democrats also have problems with the chevron defense and the deference it pays to the executive branch – and an executive branch that is headed by President Donald Trump is a very strong motivator toward revisiting this issue.

Politically, this is the one area where President Trump has a great deal of power, it is also the one area where he has unambiguously delegated power in a way that helps him with other Republicans. Law schools in the U.S., like academia in general, lean significantly to the left. Lawyers in general also are more likely to be Democrats than Republicans, though not by nearly as much as law professors.⁶¹ This tends to mirror the overall degree of Democrat dominance of higher academia (where Democrats outnumber Republicans about 12 to 1)⁶², with one very important difference.

In most of the social sciences, the dominance of Democrats in the research communities has led to a corresponding dominance of the professional organizations,

⁶⁰ In the U.S. context, this means a court that re-interprets clearly written or historically settled laws to such an extent that the law now means something new.

⁶¹ “The Political Ideology of American Lawyers” the journal of Legal Analysis, University of Chicago, 26 August 2015 https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2652706 A summary of it can be found at “The (Mostly Liberal) Political Ideologies of American Lawyers, Law Schools, and Firms” Above the Law, 1 September 2015 <http://abovethelaw.com/2015/09/the-mostly-liberal-political-ideologies-of-american-lawyers-law-schools-and-firms/?rf=1>

⁶² “Faculty Voter Registration in Economics, History, Journalism, Law, and Psychology”, Econ Journal Watch, Volume 13, issue 3 September 2016 <https://econjwatch.org/articles/faculty-voter-registration-in-economics-history-journalism-communications-law-and-psychology>

such as the American Association of Economists. This is also true of the American Bar Association (ABA), but the U.S. legal community has since 1983 had a second, competing organization, the Federalist Society, that is avowedly conservative. While it is still significantly smaller than the ABA, the Federalist Society is none-the-less large enough to provide all the same services, its own legal conferences, continuing education programs, research journals, etc. In 2001, newly elected President George W. Bush ended the tradition (since 1948) of the ABA's pre-screening judicial nominations to the federal courts to ensure they were qualified, and began to rely on recommendations from the Federalist Society instead.

During his presidential campaign, candidate Trump committed himself to appointing a supreme court justice from a list of 21 candidates that had been compiled by the Heritage Foundation and the Federalist Society. He honored that promise with the appointment of Neil Gorsuch, and has since nominated additional judges for the appellate courts, and has begun making nominations for the lower courts as well. The candidates are overwhelmingly drawn from the lists and proposals of outside conservative groups or from the office of his Attorney General, Jeff Sessions.

This is important for two reasons. Firstly, it means that President Trump is largely being advised by, and is taking the advice of, traditional Republican conservatives. Fears that he would turn judicial nominations into another White House drama have not come to pass. But secondly, it means that President Trump has also ignored the normal course of judicial appointments in American politics. While all presidents are looking for judges who are both qualified and ideologically congenial, they also use judicial appointments as a means of rewarding allies and getting legislation passed. Thus state governors and U.S. senators often have an input

into the process, suggesting new appointees, asking for favors, etc. A president who needs a senator's vote on a crucial piece of legislation is normally willing to take that senators recommendation of a judicial appointment, as long the new appointee is at least minimally qualified, and would sacrifice ideological purity to do so. Since President Trump has largely absented himself from this process, his judicial nominees have been uniformly excellent – at least from the standpoint of Republicans.

After almost a year, not a single Trump nomination has run into difficulty with Republicans. Because Democrats ended the filibuster for judicial appointments in 2014, the only means they have to stop qualified nominees that they are ideologically opposed to is the “blue slip” tradition. Traditionally, any candidate for a federal judgeship is subject to approval of the two senators from the same state as that candidate. If either or both senators objected, the nomination would not go forward.⁶³ In October of 2017, Senate Majority Leader McConnell indicated he was going to end this tradition, in order to speed up the approval process of President Trump's judicial nominations. At this point in his presidency, President Donald Trump has made more nominations to the Federal Courts than any of the previous five U.S. presidents, and all indications are that the Senate is about to start expediting the process of holding hearings and votes⁶⁴.

⁶³ This tradition was adopted to account for the fact that senators from a state would presumably know the local issues, politics, and scandals of the state better. Thus, if they objected to someone, it was because the presumably knew about, or at least suspected, something about the person that made them unfit for office. Given the distance of most states from Washington, and the time it took information to travel in that period, this was not an unreasonable assumption.

⁶⁴ *ibid*

The legal critique of the chevron rule and administrative law that is currently being made by conservative legal scholars is mirrored by President Trump's unconcealed hostility to many regulatory agencies. Though already famous in New York City, Donald Trump first became a national figure with the Wollman Ice Skating Rink. A part of New York City's Central Park, the ice skating rink was closed for renovation by the city in 1980, at an estimated cost of 9 million dollars, and 2 years of work. Six years and 14 million dollars later, Donald Trump offered to finish the project for the city, in exchange for the concessions and opening a restaurant. The city agreed, and Trump finished the project in 4 months, underbudget.⁶⁵ Donald Trump's first foray into national celebrity painted him as businessman who could get things done, and government as dysfunctional and incompetent.

As is true with most businessmen, Donald Trump was perfectly willing to use the courts and regulations to get his way when he could, but he viewed them as bothersome and wrongheaded otherwise. But in this respect, he seems to mirror the U.S. public as a whole. They like regulations on others, but view regulations on themselves as counterproductive.⁶⁶ Of course, since it can't have escaped the president that many federal workers, and not just Obama administration political appointee holdouts, hold him in open contempt, there is probably a personal element to this as well. And Steve Bannon, President Trump's Chief Strategist until

⁶⁵ "Donald Trump And The Wollman Rinking of American Politics"
Forbes 24 August 2015

<https://www.forbes.com/sites/offwhitepapers/2015/08/24/donald-trump-and-the-wollman-rinking-of-american-politics/#5eb3f2782fc8>

⁶⁶ For Thai academics, simply consider how the government regulation is generally viewed, and compare that to how useful one finds the Department of Education's TQF 3, 5 and 7 exercises.

August, has long been an avowed enemy of the administrative state.⁶⁷

In his first 100 days, President Trump issued 90 executive actions, (orders and proclamations). Many of those orders are either symbolic or of little practical importance, such as his order on 24 March 2017 to declare March 25 Greek Independence Day, or his designation of a “National Poison Protection Week” or a “national Consumer Protection Week”. Many of his other actions were about reordering parts of the White House or cabinet responsibilities, i.e. routine bureaucrat actions. His orders with regards to immigration have sought to get the agency to apply the laws as written, and to force local governments, the so-called “sanctuary cities”, to comply with federal rules, or at least to not resist them. His orders with regards to trade have mostly served to lay the groundwork for further actions, so far the only economically important one was a tariff imposed on Canadian lumber, but in isolation this is not a big issue.⁶⁸

Outside of trade, immigration and law enforcement, most of his economically important executive orders have been aimed at restraining agencies, not empowering them. Actions include reviewing last minute regulations issued by the Obama administration, ordering all agencies to create regulatory budgets, a rule demanding that for every new regulation, two old ones be rescinding, and enhanced scrutiny on the costs of regulations.⁶⁹

⁶⁷ “Trump Wants to Deconstruct the Regulatory State? Good. Here’s How You Start” National Review, 24 February 2017

<http://www.nationalreview.com/article/445226/administrative-state-deconstructing-its-good-goal-trump-heres-how>

⁶⁸ The precedent it sets, however, is worrying.

⁶⁹ For anybody who wants to see them all, in a fairly good format with a balanced assessment of what each order does, see “Trump signed 90 executive actions in his first 100 days – here’s what each one does”

In the public eye, much of this is about regulations that impact the culture wars, things like gay marriage, how universities fund women's sports, can Christian bakers refuse to bake a cake for a gay wedding. While these are important to those engaged in the activity, the economic effects are generally small. Much regulation, however, is not of this sort. Many regulations are imposed on businesses or individuals who are engaged in commerce or production, mandating that they not do some things, and that they either do things they otherwise would not, or that they do things in ways they would not.

These sorts of regulations do impose costs, both in complying with them, and in evading them. To give just one Obamacare example, the employer mandate forces firms with 50 to 199 full time employees to offer health insurance or pay a fine. When HHS discovered that many firms were employing people 39 hours a week, they changed the definition of full time worker to 32 hours a week. Firms in turn cut hours below that level, and now many people in the restaurant industry work jobs at two different restaurants. They work the same overall number of hours, but because they are split between two different businesses, the hassles and difficulties associated with scheduling work shifts is vastly increased.

Since World War II the overall cost of regulations has risen, by some (highly disputed) estimates into the trillions of dollars.⁷⁰ It seems clear the Trump administration wants to

Business Insider 3 May 2017 <http://www.businessinsider.com/trump-executive-orders-memorandum-proclamations-presidential-action-guide-2017-1/#executive-order-april-29-renegotiating-trade-agreements-1>

⁷⁰ "The Cumulative Cost of Regulations", Mercatus Center, George Mason University, 26 April 2016
<https://www.mercatus.org/publication/cumulative-cost-regulations>

pursue regulatory reform, what is less clear is if it can. The permanent bureaucracy endures, because it is permanent⁷¹. Ronald Reagan, and every republican president since, came into office determined to tame the bureaucracy, none really succeeded.

While it is still in its first year, the Trump administration has had success in this area. According to the Competitive Enterprise Institute, a research and advocacy oriented think tank devoted to the issue of deregulation, the Trump Administration has had notable success, to the point where they claim he has deregulated more than President Reagan did during his first year in the White House. President Trump's administration has, for example, reduced the Federal Register, the official journal of the U.S. Federal Government, from 67,900 pages at the end of the Obama presidency, to 45,678 today⁷². Early in his presidency, Trump signed an executive order that two old regulations had to be scrapped for every new regulation imposed, and any new costly regulation had to be matched by eliminating one or more other regulation of equal cost (generally known as the "regulatory budget"). The Trump administration has issued 2,183 rules in its first year, compared to Obama's 2,686, and many of those rules were simply rules repealing previous rules. All of the above methodology has problems – for example replacing

The Cost of Regulation and Intervention: Ten Thousand Commandments 2016", the Competitive Enterprise Institute, 3 May 2016
<https://cei.org/10KC/Chapter-1>

⁷¹ Milton Friedman's famous quote: "Nothing is so permanent as a temporary government program"

⁷² For anybody who wants to see what the actual Federal Register looks like, one can use the link provided. Keep in mind that it 268 pages, and there are 81 other volumes. Federal Register, Vol 82 No. 188 Pages 45421-45678 <https://www.gpo.gov/fdsys/pkg/FR-2017-09-29/pdf/FR-2017-09-29.pdf> Disclaimer: I did not read all of it myself

two long, detailed regulations with one short broad one could well leave an agency with more discretionary power – but the direction seems clear.

In no part of the federal government is this been more clear than at the Environmental Protection Agency (EPA). President Trump’s selection of Scott Pruitt, the former attorney general of Oklahoma who made a national name for himself with his battles against the EPA, was an early indication of what was coming. No agency had been as aggressive in pushing the limits of rule-making to see what they can regulate as the EPA, including greenhouse gases, waterways, coal and energy production, and much else besides. The EPA was an early innovator in the field of “sue and settle” (explained later), it was actually the first Obama agency where Freedom of Information (FOI) requests were routinely evaded by senior management using private, non-public email accounts.

Symbolically, the most important thing was the EPAs involvement in several high profile litigations, where they ordered families or small business’s to comply with EPA rulings about how they could use their land, and imposed ruinous fines for non-compliance, rulings that the EPA also asserted could not be challenged by the parties subject to them. This goes to the heart of the Republican critique of administrative law. It reverses the assumption of innocence – the citizen must prove they did not violate the regulation – and the agency that made the initial ruling is also the entity that decides if it did so correctly. As Judge Alito observed when the case of *Sackett vs. EPA*⁷³ made its way to the Supreme Court in 2012,

⁷³ Alito’s quote is taken from the article “Supreme Court Justices Blast EPA For Thwarting Couple From (sic) Building On Protected Wetlands” Business Insider (and AP), 9 January 2012. The story tells much of the

"You think maybe there is a little drainage problem in part of your lot, so you start to build the house and then you get an order from the EPA which says: 'You have filled in wetlands, so you can't build your house; remove the fill, put in all kinds of plants; and now you have to let us on your premises whenever we want to,'" Alito said. "You have to turn over to us all sorts of documents, and for every day that you don't do all this you are accumulating a potential fine of \$75,000. And by the way, there is no way you can go to court to challenge our determination that this is a wetlands until such time as we choose to sue you." Justice Alito, Supreme court oral arguments

While the above is an isolated incident, it represents a growing sentiment among many Republicans about administrative law and government bureaucracy. It is a sentiment that is far more widespread among Republicans than just the Trump portion of the party.

Scott Pruitt's changes to the EPA administration has put over 800 regulations proposed by President Obama on hold, and has ended the policy of "sue and settle"⁷⁴. In sue and settle, an environmental group would sue the EPA for not enforcing environmental law as the environmental group claimed it was written. The EPA would put up a token defense in court, but then would settle with the environmental group, agreeing to enforce the laws in a stricter way. Once a Judge had signed off on the order, the EPA would now do

background to the case, which the Sacketts won 9-0. 4 years later, they are still in litigation with the EPA, and their house is still unbuilt.

<http://www.businessinsider.com/justices-epa-sackett-wetlands-2012-1>

⁷⁴ "Administrator Pruitt Issues Directive to End EPA "Sue and Settle", EPA Press office, 16 October 2017

what it wanted to do anyway, which was to impose new regulations by enforcing existing regulations much more stringently than congress had ever intended, and then claiming they had to because the courts had ordered them to.

Scott Pruitt has also brought those impacted by the EPA into the process, inviting industries and communities that would bear the costs of regulations to have greater input into the making of decisions. And he has removed many senior advisors on regulatory panels from the panels, citing conflicts of interest since those advisors often were receiving grants from the EPA. He has made the EPA more transparent, public notices about rule making are now being widely disseminated, and not gamed to exclude dissenting voices. And he has severely curtailed the EPA's activities with regard to global warming, claiming his views on the subject are irrelevant because the Congress has never authorized the EPA to act in that area⁷⁵.

Needless to say, Democrats, environmentalists, and many others are furious with these changes. But so far at least the courts have sided with the administration. Republicans have celebrated the changes at the EPA so far, but a large caveat remains. No significant legislation has been passed to make any of these changes in administrative priority permanent, so any gains (as Republicans would measure them) could be transitory, especially given that many of the career bureaucrats at the EPA are hostile to the new

⁷⁵ All of the paragraph above is supported by "Pruitt Corrects Course on Obama-Era Water Regulation" The Editors, National Review Online, 28 June 2017 <http://www.nationalreview.com/article/449059/scott-pruitts-water-regulation-rollback-epa-restoration-rule-law> However readers should be warned that many, many people would argue with the tone, conclusions, or values expressed in the article. I cite it as it representative of how many Republicans view the EPA, not as an endorsement or refutation of the views.

administration. To do that would require that congress tackle the issue of administrative law, and then years of litigation to see how the courts end up enforcing it. So far none of that has happened. Additionally, the vehemence of the fights has almost certainly had a detrimental effect on the science that underlays much of what the EPA does. Both sides accuse the other of scientific malfeasance, and of being beholden to industry or to activists, and of selectively enforcing the laws.

It is very difficult to actually calculate what the costs of regulations are. It is also hard to predict whether the Trump administration can actually implement strong deregulation, the EPA seems to be an outlier, not the norm. Assuming the administration was successful, it would be reasonable to assume an uptick in economic growth rates in the U.S., though by how much depends very much on one's assumptions about how stifling to growth the regulations are. And the costs to the health and safety of Americans would also need to be considered. American industry would become more competitive globally, though how this would affect trade balances and currency changes depends on many, many other factors. At least potentially the unemployment rate would go down as well.

8. Trade and Immigration

Trade and immigration were two of the keystones of the Trump campaign, so one would expect them to be congressional priorities. So far this has not happened. Partially, this is because the Trump administration has executive authority over elements of it, but it is also because of the difficulty these issues pose for congressional republicans, and democrats.

On the subject of immigration, broadly speaking there are two factions in the Republican party. One group, the business wing of the party (big business, the chamber of

commerce) is broadly in favor of immigration, while the cultural wing (much of rural America, the white working class, small business) is broadly against it. Those in favor of it have the money and traditionally much of the institutional power, but those against it have the votes, and much of the passion. Likewise for the Democrats, the money and institutional power of the Democrats, in universities, the media, Hollywood, and other big businesses are all in favor of immigration, but the Unions, the poor and working poor, and many lunchbox voting Democrats by and large see immigrants as either taking jobs or reducing wages, or both. That said, the passion among Democrats seems to be with the cultural wing of the party, not the economic wing.⁷⁶

The effects of immigration on wages and employment are highly contentious issues. Most economic models predict that immigration will bring in people with complementary skills, allowing for a greater division of labor which will lead to rising prosperity for all, and there seems to be a weak consensus that this is the case.⁷⁷ High skilled legal immigrants almost certainly benefit the economy, through increased economic activity and the taxes they pay. Conversely, low skilled illegal immigrants tend to be poorer

⁷⁶ A good primer on this issue, for the technical economist, would be “Who is Against Immigration? A Cross-Country Investigation of Individual Attitudes toward Immigrants” *The Review of Economics and Statistics* Vol. 88 no. 3, pgs 510-530 October 2006 <http://www.mitpressjournals.org/doi/abs/10.1162/rest.88.3.510#.WRaif2iGOUk>

The paper provides both a standard economic model of immigration, and then a cross-country study of the demographic and economic factors that determine attitudes on immigration. This has the advantage of cutting through a great deal of the “noise” associated with partisan politics – a problem with analyzing the situation in both the U.S. and Europe at the present time.

⁷⁷ *ibid*

on average, so they contribute less to the economy, and much less in taxes. This is at least partly offset by the fact that they can't receive some government benefits and support that citizens are eligible for, though there are benefits (especially in the health care sector) that they are eligible for. Everybody agrees that immigrants add to the overall size of the U.S. economy, but most of that addition to total GDP is consumed by the immigrants themselves, whether legal or not, and if they are consuming more than they contribute, that would be a net loss to native born Americans.

Even then, there is a significant difference between net effects, and local or sectoral effects. It is broadly believed that illegal immigration has somewhat reduced the wages of Americans without a high school degree. Beyond this, again there is no strong consensus. Immigration is concentrated in some regions, and in some sectors of the economy. Highly educated immigrants in the tech industry, uneducated illegals in labor intensive agriculture. Some neighborhoods are intensely effected, other states have seen barely any. Like trade, a net positive can still leave many individuals worse off⁷⁸.

President Trump's current position on immigration is somewhat more nuanced than it is often portrayed as. He wants illegal border crossing and entry into the U.S. curtailed, and he wants illegals in the U.S. who commit crimes deported. This seems as much about law and order as it is about economic issues. He has not committed himself to, nor has the Department of Homeland Security (DHS) or the Immigration and Customs Enforcement Agency (ICE) begun

⁷⁸ A good, readable primer on the subject that fairly addresses everything listed above, would be The Costs and Benefits of Immigration, the Brookings Institute, July 2017 https://www.brookings.edu/wp-content/uploads/2016/07/braingain_chapter.pdf

to, deport law-abiding illegal immigrants. President Trump has not come out against legal immigration, rather he wants to change the criteria the U.S. uses for selecting them. Currently, the U.S. system prioritizes family re-unification, President Trump wants to change the system to a merit based or “points” system, similar the ones used by Canada or Australia.⁷⁹ These systems screen potential immigrants for their likelihood for success, admitting the skilled and educated, and rejecting those likely to become a drain on public resources. He has also stated he wants to cut the number of legal immigrants.

President Trump’s most substantive activities on this issue have so far been his three executive orders on illegal immigration, which have called for temporary bans on immigrations from a variety of countries where he deems it impossible to get reliable information about the potential immigrants. To give a concrete example, Syria has been put on all three lists, since it doesn’t have a functioning government that we can contact to find out if the potential immigrants have a criminal record. Iran, North Korea and Venezuela are all on the third order, due to animosity with the U.S. restricting the availability of reliable information. All of these bans have been temporary, while the Department of Homeland Security tries to develop new ways of vetting (investigating) potential immigrants from these countries, though one does have to wonder if any real system could be put into place. While all three bans were (or are) subject to court ordered injunctions staying their enforcement, those adverse legal rulings have been coming mostly from one

⁷⁹ “Trump calls for “merit-based” immigration system in address to Congress” CNBC, 28 February, 2017
<http://www.cnbc.com/2017/02/28/trump-calls-for-merit-based-immigration-system-in-congress-speech.html>

federal judge in Hawaii, and then left in place by the 9th circuit judges, a court dominated by Clinton and Obama appointed judges. The supreme court has only ruled on the second ban, but they largely sided with President Trump in that ruling. Finally, for all the negative media that the orders have gotten, they remain popular with the public.

Additionally, President Trump has formally ended the Deferred Action for Childhood Arrivals (DACA)⁸⁰, an Obama era administration action that basically amounted to the administration no longer enforcing immigration law with regard to illegal immigrants who were brought into the country as children. This effectively granted those children amnesty, but it was done not through an act of congress, but by executive fiat – the Obama administration simply announced they would not enforce the law. As a practical matter, legal authorities always have some discretion in law enforcement, as there are never enough resources to go after every broken law or criminal, but this struck many as a step beyond that. By announcing that he would not, under any circumstances, enforce a law that Congress had passed, President Obama was in effect saying he could veto congressional laws, laws that had been on the books for long periods of time.

President Trump ended that policy in September, subject to a 6 month delay, but to date nobody has been deported under it unless there were other illegal activities as well. President Trump also threatened to issue new orders, if congress does not reform immigration by then. Given all the other things congress is doing, that seems unlikely to happen. The net effect of all this is the beneficiaries (known as the

⁸⁰ “Trump ends DACA but gives Congress window to save it”, Tal Kopan, CNN

DREAMERS) are now back in legal limbo, where they have been for the last two decades or so.

Whatever one thinks of the merits of these changes, they amount to little change of the status quo. President Trump may want to end illegal immigration, he may even want to deport illegals whose only crime was sneaking into the country or overstaying their visa, but certainly seems unwilling at this point to take the actions necessary to implement these policies⁸¹.

Given all the uncertainty above, it seems pointless to attempt in this paper to litigate the issue, especially when the politics of the issue seems as much about culture and values as it is about economics. The broad outlines of an immigration reform bill are the same that they have been for the last decade – Republicans are willing to discuss amnesty for current illegal immigrants, but only after there is effective border control and various changes in the criteria for accepting new immigrants. Democrats want to create a pathway to citizenship for current illegal immigrants in the country, and they are willing to discuss changes to immigration policies and border control after that has happened. On a final note, though President Trump has not yet built a wall, or figured out how to get Mexico to pay for it, or gotten one approved by congress, a combination of stricter border enforcement and tougher rhetoric on the issue appears to have had an effect, illegal border crossings are down over 50% since the election.⁸² And on no other issue

⁸¹ In response to the October 31 terror attack in NYC, President Trump has come out against Diversity Visas, a lottery Visa program to bring people into the U.S. from countries which historically have sent few. While symbolically important, the number of Visas given by the program are very small compared to other Visa programs.

⁸² “Does border drop mean Trump’s tough talk is working? CNN, 9 March 2017

does President Trump appear to be more in tune with the public, or his opponents less so.

President Trump also ran against free trade, which he characterized as harmful to the U.S. To give a flavor of his views, as reported in the *Economist*...

Mr. Trump was carried to victory by telling voters that incompetent and corrupt elites either blundered or conspired to send manufacturing jobs out of America, when they could have stayed. He did not just attack such free-trade deals as the NAFTA pact with Mexico and Canada, or the forthcoming Trans-Pacific Partnership (TPP) between America and 11 other Asia-Pacific countries. He claimed—with no evidence—that America had hired “stupid” negotiators who failed to read what was in trade deals, while devious foreign officials “know where every comma is”. Politicians, he added, had colluded in this betrayal of America because “they get massive campaign contributions from others that want to make deals with China, and want to make deals with Mexico”.

Depending on the week, Mr. Trump’s stated remedies have included a promise to order his Treasury Secretary to declare China a currency manipulator, promises to put TPP talks on hold, and threats to place tariffs of 5%, 10% or even 45% on imported goods. He has pledged to browbeat the bosses of such giant firms as Ford, Apple and Boeing to make more of their products at home, with the help of tweaks to the tax code.

China is “killing us”, Mr. Trump told *The Economist* in August 2015. “The money they took out of the United States is the greatest theft in the history of our country.”

Describing how he would approach Chinese leaders as president, he boasted of hiring smart new negotiators, naming his friend Carl Icahn, a corporate raider, as a prime example. Then, he said, he would tell China that countering its currency devaluation might require a 12% import tax, to level the playing field. “And you know what? They’re going to stop playing games with us. Look, they have taken our jobs, they have taken our money, and on top of that they have loaned the money to us and we actually pay them interest now on money.” - The Economist: 9 November 2016⁸³

Since assuming office, President Trump has issued a series of executive orders reviewing America’s trade agreements with other countries. He has withdrawn the U.S. from the Trans Pacific Partnership. On April 26, President Trump threatened to withdraw from NAFTA. On the 27th, he agreed not to, but demanded renegotiation, which Canada and Mexico agreed to. He threatened to take the U.S. out of the Paris Climate accord, and after some back and forth positioning, did so. He has repeatedly called the Chinese currency manipulators⁸⁴, then stopped doing so after they assisted the U.S. in dealing with North Korea. He has offered Great Britain a preferential trade deal with the U.S., depending on how Brexit goes, though nothing has been

⁸³ “How Donald Trump thinks about trade” The Economist, 9 November 2016 <http://www.economist.com/news/united-states/21709921-americas-next-president-wants-pull-out-existing-trade-deals-and-put-future-ones>

⁸⁴ They probably are, but they appear to be engaged in propping up the Yuan, not in depreciating it, the opposite of what President Trump is accusing them of. “China is spending big to prop up its currency”, CNN, 7 December 2017 <http://money.cnn.com/2016/12/07/investing/china-foreign-exchange-reserves-yuan-trump/>

worked out since Brexit hasn't happened yet. What to make of all this?

There are two broadly sympathetic views of Trump's position on trade. One view is that President Trump is making maximal demands to get people's attention, then he negotiates and pockets the concessions he gets. In this view, he is simply being a cagey businessman who knows how to drive a hard bargain. After President Trump threatened to withdraw from NAFTA, he agreed to reconsider it the next day after being personally called by the leaders of both Canada and Mexico.⁸⁵

A related view is that President Trump is simply recognizing the changes that have happened to free trade over the years. From the same economist article quoted above, we have Donald Trump's then trade advisor saying:

“Free trade is a noble academic approach. The problem is that government-managed trade is what we have, and in our case we have managed it very poorly...We have been involved in a trade war with China for two decades. We have just not shown up to fight.” The Economist, 9 November 2016

In this view, most free trade agreements are not, in fact, about free trade. Rather, they are about government managed trade. Most U.S. tariffs with the rest of the world are now below 5%, down from an average of over 40% immediately after World War II. This helps to explain why the proposed Trans Pacific Partnership agreement needed to be over 5,000 pages long. The primary barrier to free trade at this point is

⁸⁵ “Trump threatens to terminate NAFTA unless U.S. gets a winning deal” Washington Times, 27 April 2017
<http://www.washingtontimes.com/news/2017/apr/27/trump-willing-quit-nafta-would-be-shock-system/>

non-tariff barriers (NTBs), which need to be dealt with in minute detail.⁸⁶ In this view, the U.S. has agreed to accept goods into the U.S., without adequately getting other countries to revise their NTBs in ways that allow U.S. goods in.⁸⁷ Even if one does not subscribe to the view that this happened because U.S. negotiators were stupid or corrupt, a case can be made that in the past the U.S. accepted individually disadvantageous deals, as a means of underwriting the liberal world order.⁸⁸

Of course, an alternate view of President Trump's views on trade is that he believes exactly what he says (even the contradictory parts). Likewise, he intends to do exactly what he has said he would do. If this is the case, what he has so far done in the first year of his presidency is to lay the groundwork for withdrawing the U.S. from various trade agreements. He has via executive orders set in motion numerous reviews of trade deals to see if they really benefit the U.S. Once the reports are in, he has laid the groundwork for an assault on existing trade deals. If that is the case, the

⁸⁶ As an example, Kinder Eggs are illegal in the U.S. – because children might choke on the toy inside. Customs can fine someone \$2,500 for each Kinder egg they find on him when crossing into America (usually they just confiscate them, but still)

⁸⁷ An additional problem is the “latecomer advantage”, where the U.S. and Europe have been trading, and reducing tariffs in the WTO, for decades. Then China enters, gets the same tariffs for its exports as the EU and the U.S. do, but keeps their own tariffs high.

⁸⁸ The heart of this argument is that the U.S. was the primary beneficiary of the post war Bretton Woods system, including free trade, and thus a breakdown of that order would disproportionately hurt the U.S. In this view, free trade is a collective good, subject to a tragedy of the commons problem where U.S. trade partners free-ride on the U.S. It is notably that President Trump doesn't just view trade deals this way, he also views many U.S. alliances, such as NATO, in the same light.

prospects of future free trade agreements are bleak, and the risk of a regional or global trade war are real.

This is especially important to supporters of free trade, because neither the Democrats nor the Republicans, at this point, are particularly pro-trade. Both parties have strong protectionist elements, and these attitudes have been growing.⁸⁹ Any future trade deals a President Trump negotiates or re-negotiates would have to get past a skeptical congress, but he has the unilateral power to do a great deal of damage to existing trade agreements.

There is thus far more reason to fear the potential economic effects of a Trump presidency on international trade than on any other policy. To use the example of NAFTA, a tremendous amount of cross border trade already occurs, and the supply chains of thousands of U.S. firms depends upon imported Mexican and Canadian intermediate inputs. Could some NTBs be improved on to benefit U.S. manufacturers? Probably. But the existence of some gains doesn't mean those benefits are large. There does not seem to be all that much potential economic gains from a successful re-negotiation, one that based on past experience would take years of negotiating to conclude.

Thus, *if* President Trump has adopted a calculated policy of sounding scary on trade to frighten others into renegotiating trade deals, and *if* his presidency is competent enough to successfully do so, and *if* nothing else upsets the system, America stands to gain a bit from better trade deals. But there is certainly a possibility that President Trump really believes everything he says. And there is a possibility that President Trump is not, in fact, the skilled negotiator running

⁸⁹ What Donald Trump means by fair trade” The Economist 13 May 2017
<http://www.economist.com/news/briefing/21721935-idea-reciprocity-animates-white-houses-view-trade-what-donald-trump-means-fair>

an ideologically coherent, competent administration that is capable of actually negotiating better trade deals. And possibly, just possibly, there are other factors in the world, such as a nationalist China deciding for its own domestic reasons that a trade war with the U.S. would be good domestic politics,⁹⁰ which could intervene. Any of those things being true, and the potential downsides are much, much greater than any potential gains.

Of course, so far none of the really bad outcomes from a collapse of the world trade order have come about, and it is certainly possible they never will. The flurry of activity the administration engaged in initially has been replaced with almost nothing. The U.S. is still in NAFTA, and talk of China as a currency manipulator has been shelved. Congress was busy with healthcare, and now the budget and tax reform dominate their actions, and the news. President Trump and his administration have been engaged in all sorts of non-economic issues, including Russians, the FBI, a special prosecutor, the NFL, and the internal drama of the Trump White House. While his actions on free trade have certainly indicated hostility to it, all the easy, costless (in present terms anyway) actions have been done.

9. Donald Trump and Southeast Asia

What will the Trump presidency mean for Southeast Asian (SEA) economies? Assuming no shooting war with North Korea or China, and no serious trade war with China, the primary effects will probably be – not that much. The U.S. is primarily concerned with domestic issues right now, and to the extent that it is concerned with the rest of the

⁹⁰ “Into the Abyss: Is a U.S.-China Trade War Inevitable? Cato Institute, 6 February 2017 <https://www.cato.org/publications/free-trade-bulletin/abyss-us-china-trade-war-inevitable>

world, SEA ranks below such issues as ISIS, the fallout from Brexit, U.S. relations with NATO, the EU, Russia, China, North Korea and Japan/South Korea, NAFTA, the implosion of Venezuela, the ongoing crisis in Syria, Turkey's turn towards Authoritarianism, the U.S./Mexican border, Israel, and many other things beyond that. Absent something really bad happening in Southeast Asia, the U.S. under president Trump will almost certainly continue the same policy that the Obama Administration had, benign neglect.

This is not to say that there will be no effects, of course, only that the U.S. is unlikely to have any policies that significantly target Southeast Asia. Instead, under President Trump and the Republican congress, the U.S. will do what it does, largely for its own reasons. On two specific policy's, however, there will be a fairly significant impact on SEA – Trade and Energy.

One of President Trump's first acts in office was to kill the Trans Pacific Partnership (TPP), but that is far less important than most people think, because it may very well have never become law anyway. A significant number of Democrats were opposed to it, including Hillary Clinton⁹¹, and they needed Republican votes to pass it anyway. Many Republicans also opposed it, and not just because President Obama had negotiated it. They viewed it as an example of managed trade masquerading as free trade. In this view, any agreement that is over 5,000 pages long, which creates all kinds of dispute resolution boards, panels on labor practices, etc., is inevitably going to create a bureaucracy to manage it,

⁹¹ "Obama pushes trade in Asia, but has 2016 killed the TPP?" CNN, 7 September 2016 <http://edition.cnn.com/2016/09/06/politics/obama-tpp-politics-congress/>

one that will dilute U.S. sovereignty.⁹² The only way that TPP was going to happen if Hillary Clinton had been elected president would have been if she was insincere in her opposition to it, and democrats had also won the senate and felt compelled to support her.⁹³

In the trade sector, it is doubtful the U.S. will engage in any significant new multilateral trade negotiations or trade deals. President Trump seems primarily fixated on NAFTA, a trade treaty that dwarfs U.S. exports, imports or direct investment with SEA⁹⁴. It seems likely that this issue, at least for the foreseeable future, will consume all the intellectual energy of President Trump's administration on trade issues, and the rest will run on auto-pilot. This is especially true when the Democrats are mostly anti-trade at this point as well, and Republicans are only barely free-trade, and often anti-free trade agreements.

This last point goes to the nature of most free trade agreements at this point. They are not so much about promoting free trade through lower tariffs, as that has mostly happened. Instead, they are about managing non-tariff barriers. The problem with non-tariff barriers is that they can take a near infinite number of forms, and while many of them are exactly what they look like, in many cases what appears

⁹² Trump on Trade: The Good, The Bad, And The Ugly” Forbes, 3 February 2017

<https://www.forbes.com/sites/markhendrickson/2017/02/03/trump-on-trade-the-good-the-bad-and-the-ugly/#1d7abf3d3a93> Republican hostility to subjecting the U.S. the international administrative law is even greater than their hostility to domestic administrative law.

⁹³ If Hillary Clinton had been sincere in her objections, any renegotiation to satisfy her would have completely alienated republicans. If it was just a pre-election position to abandon later, it is doubtful she could have depended on all democrat senators, much less republican ones.

⁹⁴ Office of the U.S. Trade Representative.

to be a trade barrier is sometimes just some law or regulation that has existed a long time, that a country wants to keep for its own peculiar reasons.

This means that modern trade agreements are incredibly long and detailed. The TPP agreement was well over 5,000 pages long. In an agreement of that length, a lot can be in the agreement that nobody really knows about, especially as these agreements are of necessity negotiated secretly. Most of the initial hostility to the TPP came from the American left, which was concerned that it did not have strong enough rules about environmental protection, fair labor practices, and intellectual property rights. The more the Democrats fears were addressed, the more suspicious republicans became about the law. They saw it as encroaching on U.S. sovereignty, and eventually as a trojan horse for the Obama administration to sign a treaty that they had voted for, which would then require the U.S. to do many things they didn't in fact want to do.

This does not mean that the TPP is dead, many of the countries that have committed themselves to going forward with it, though at the time of writing they don't seem to have any concrete plans on how to.⁹⁵ It is also possible for the U.S., even potentially under a President Trump, ask back in the future, though he would almost certainly want some adjustments and opt-outs. At this point it seems unlikely.

There is one sector of the economy that will almost certainly succeed under President Trump, and that is the energy sector. U.S. energy production plateaued in 2005, since then it has grown, and it has done so despite a hostile regulatory structure. Strongly committed to renewable

⁹⁵ “Can TPP go ahead without America?” The Economist 4 May 2017
<http://www.economist.com/news/asia/21721683-pacific-trade-pact-would-still-benefit-other-11-members-can-tpp-go-ahead-without-america>

energy, the Obama administration spent a considerable amount of effort promoting them in his determination to make the U.S. a “renewable energy superpower”. They prohibited drilling or exploring on public land, or offshore, they refused to renew expired leases, they imposed costly new regulations on the coal industry to drive it out of business. Starting in 2009, they refused to approve or deny the Keystone XL pipeline for 6 years, before finally denying it. Almost all of the above was accomplished not through congress, but through the various executive branch regulatory agencies, especially the EPA.

The Obama administration was successful to an extent in hobbling the coal industry, they did not succeed in replacing it with renewable sources of energy like wind or solar, which remain frustratingly uneconomical without heavy subsidies. Instead, the slack was more than taken up by new oil and natural gas. The reason for this is a revolution in two older technologies, hydraulic fracturing and horizontal drilling (colloquially know as “fracking”), have vastly reduced costs for U.S. energy extraction. A great deal of previously unavailable energy sources are now economically accessible. Net U.S. imports of energy have declined to a third of what they were in 2005, and based on current projects (which will surly change) the U.S. will be a net energy exporter sometime after 2020.

Just in the last three years, the break-even price of oil production in the U.S. has dropped from \$80 a barrel to \$50.⁹⁶ The Trump admin has already given its approval for

⁹⁶ This refers to averages across all wells, and some of the drop has come about as less efficient wells were taken offline as prices dropped. But much of the drop is from technological improvements. “Shale Oil Makes \$70 the New \$100” Bloomberg News, 2 February 2017
<https://www.bloomberg.com/gadfly/articles/2017-02-02/oil-prices-70-s-the-new-100-for-shale-breakevens>

the Keystone XL Pipeline⁹⁷, which would eventually bring additional Canadian oil to the market. While the U.S. still remains the world's largest or second largest consumer of energy, as it nears self-sufficiency it is having a large impact on world prices. If the technology keeps improving, and the Trump administration continues to be friendly to the sector, it will continue to be a real robust source of U.S. economic growth, and to depress oil prices worldwide. As a net importer of most energy products, all of SEA except Indonesia stands to benefit.

While the general effects of the above two issues are fairly easy to predict, some other less likely issues should still be addressed. It is hard to see how either healthcare reform, or the lack of it, will significantly affect SEA. A collapse of Obamacare, or its repeal and replacement by a Republican alternative that didn't work, would both be harmful to the U.S. The primary impact it would have on SEA would simply be more neglect from the U.S., as the nation continued to grapple with its health care problems. Conversely, if the Obamacare exchanges finally settle down, or a Republican replacement plan proves workable, at least some political and intellectual capital will open up, but again it seems most likely that it would turn to other issues of much more pressing concern to the U.S. than SEA.

Regulatory reform in the U.S. would serve to make the U.S. more competitive and dynamic, which would lead to greater productivity growth in the U.S., and thus a growing, expanded market for SEA exports. If this comes about through replacement of judges over the next 4 or 8 years, the effects will be much too far in the future to matter in

⁹⁷ "Trump greenlights Keystone XL pipeline, but obstacles loom"
Reuters, 25 March 2017 <http://www.reuters.com/article/us-usa-pipeline-keystone-transcanada-idUSKBN16V1CN>

comparison to the many other events that can happen before then. If the effects were to come about through the Trump administration seriously pursuing regulatory reform, it would happen much quicker. However, this is one of the most difficult and daunting tasks the administration has set itself, and to do so would require an administrative focus and skill that it has not yet demonstrated.⁹⁸

It has been seven years since the great recession ended, and in that time the U.S. never achieved a GDP growth rate of 3% a year, instead averaging just over 2% a year during that period. So there is one school of thought that the U.S. economy must still have significant slack in it, and the right policies, or even just more confidence, will be enough to restore U.S. growth rates to the 3% or so that have been the historic norm since 1948. If that were to happen, the effects on SEA would be almost all positive; a stronger U.S. economy would pull in SEA products, increasing SEA finances and trade balances, with all the resulting benefits associated with that.

But, it has been seven years since the great recession ended. Another view is that the U.S. is living on borrowed time, and a recession is likely soon. If that were the case, there are two ugly scenarios that bear watching. One is that the Trump administration reacts angrily, and starts a trade war (or a real one) with somebody. It is hard to see somebody with President Trump's temperament not blaming somebody else for a bad economy. Since the TPP is already dead, it seems likely that any trade war would not be with SEA, but it would still disrupt global trading patterns.

⁹⁸ The news of FBI Director Comey's firing is 2 days old as of this writing. (XXX Add notes on Trump administration incompetence or lack thereof after review just before final submission XXX)

That said, if another recession comes, it doesn't have to be a shallow one. If one subscribes to the view that the 2008 recession was about debt, then 2017 has some troubling signs. As already mentioned, the U.S. government's fiscal situation is far more troublesome than it was before 2008. The U.S. has less room to use fiscal policy to combat a recession. And while the U.S. Federal Reserve's policy of quantitative easing has been eased, the Fed still has trillions of dollars of debt on its books. And that isn't the only source of debt.

Consumer debt fell from 2008 through 2013, but has been rising since then.⁹⁹ Student loan debt has doubled to well over a trillion dollars, housing and credit card debt are also up. The total amount of consumer debt in absolute terms is back to 2008 levels.¹⁰⁰ But far and away the most worrisome sector is state and local governments.

During the boom years of the 80s and 90s, local and state government in the U.S. expanded. They took on new tasks, provided new services, etc. They also increased the pay of government sector workers. State government employees were paid more up front, and they received excellent benefit packages, government workers in the U.S. are now paid more than their private sector counterparts.¹⁰¹ Most problematically, state and local government employees also received very generous defined benefit pensions, even as the rest of the U.S. was transitioning to defined contribution

⁹⁹ "Quarterly Report on Household Debt and Credit" Federal Reserve Bank of New York, February 2017

¹⁰⁰ Since GDP has grown since then, as a percentage of the economy it hasn't reached its 2008 peak, but it is close.

¹⁰¹ Why Federal Workers Get Paid More" Bloomberg View, 16 March 2017 <https://www.bloomberg.com/view/articles/2017-03-16/why-federal-workers-get-paid-more>

plans¹⁰². This was a great deal for politicians, they could promise large benefits in the future, and then let future politicians find the money to pay. This looming crisis of unfunded pensions has yet to be resolved. Detroit declared bankruptcy in 2013, with 20 billion in debt, Puerto Rico declared bankruptcy last week, with 136 billion in debt. What happens if Illinois, or California, go bankrupt?¹⁰³

While this sort of a nightmare scenario is possible, it does not seem likely. Much of the debt is internally held, so a Greek style collapse does not seem likely. Far more likely would be a much less severe, gradual erosion of the U.S. fiscal situation as entitlement reforms continue to be put off, and as taxes continue to stay below the level necessary to fully fund the U.S. welfare state. In that case, there will be continued pressure on the dollar compared to other currencies, though it seems unlikely the Fed would allow the dollar to depreciate to far, or for inflation to rise too much. The U.S. current account balance in this scenario would also tend to get worse, as the U.S. continues to bring in more resources as it consumes more than it produces.

Of the two potential recession scenarios, a soft, gradual decline of the U.S. seems the more likely, and of course

¹⁰² Most private sector pensions in the U.S. are now defined contribution plans, where the employee and employer both contribute to a savings plan (typically a 401k plan of some sort), which in turn will fund retirement. How well funded a retirement is depends on how much money was saved in the individual account. Defined benefit plans promise to pay a fixed amount upon retirement, from a general pension fund. The payouts are guaranteed regardless of the value of the held assets or the state of the economy. This created a tremendous time-inconsistency problem as today's politicians promised public sector workers future payments, but didn't use today's tax revenue to pay for those promises. U.S. public pension funds are now chronically underfunded.

¹⁰³ Current federal law prohibits state bankruptcy. It also prohibited Puerto Rico from declaring bankruptcy, until it did.

neither is inevitable. If President Trump were to be successful in reforming healthcare, or in enacting a broad regulatory reform, or significant tax reform, and the policy he enacted did actually serve to increase growth, the U.S. could potentially return to a higher growth rate path of GDP. If President Trump were to do all three, and they all worked, he would go down in history as a great president. At this point though, it is not clear that he can deliver on any of them.

It is much too early to predict what the macro-economy under President Trump will look like. But so far, most of the signs appear to be good. In the three quarters he has been president, GDP grew by 1.2, 3.1% and 3.0%¹⁰⁴. Consumer confidence is at a 17 year high, and the Dow Jones Industrial Average has risen from 18,589 to 23,434 (November 2, 2017). As of this writing, President Trump has selected Jerome Powell, a mainstream, respected member of the Fed, to be the next chair of the Federal Reserve. There is plenty of reason to worry about the short, medium and long term prospects of the U.S. economy, and plenty of different ways to apportion the credit or blame for those trends. But so far, President Trump has presided over (or benefited from) a fairly robust economy by recent standards. A good economy for the U.S. will draw in more SEA imports, and will lower the temperature of U.S. politics, both good things for SEA.

10. Conclusions

Before becoming president, Donald Trump upended a great many norms and assumption about how American politics operates. He constantly did things that would have destroyed any other politician, things that he simply shrugged off as he carried on being his own unique self. His command

¹⁰⁴ Data taken from <https://www.statista.com/statistics/188185/percent-chance-from-preceding-period-in-real-gdp-in-the-us/>

of social media, his personal charisma and flair, and his unorthodox style of management allowed him to win an election that almost everybody, friend or foe, thought he would lose.

Since being elected, the U.S. economy has done fine. Predictions of crashing markets, currency or stock market woes, or an immediate slump were proven wrong, instead consumer confidence went up, the stock market went up, and unemployment went down. One could argue that this is the markets expecting a Trump Presidency to be a success. One could also argue that this is markets expecting a Trump Presidency to be irrelevant, he will accomplish little, and thus will do no harm – or at least less than a Hillary Clinton presidency might have.

There is an assumption in much of the world, that because the U.S. President is the most powerful man in the world, that he is thus the most powerful person in the U.S. While he is, his power is constrained, more so than in most other systems of government. A President's institutional power is limited, by design. A successful U.S. president, at a certain point, has to figure out that their power depends upon their ability to persuade, and that there are multiple different parts of the governments that need to be brought onboard for any significant change to occur.

If President Trump has figured that out, he has hidden it well. His public approval ratings are below average, and he has not managed to come close to staffing the government with his people, whomever they may be. While House Speaker Ryan and Senate Majority Leader McConnell treat him with a minimal amount of respect, neither are warm to him or show him deference, and both pursue their own institutional and political goals. Democrats remain unified in their opposition to him, and everything about him. And while

President Trump has had his successes, outside of judicial appointments he has not yet had a significant success in Congress.

A Trump Presidency that continues on this course does not have to be a failure. Absent a serious foreign policy disaster, partisan gridlock can be a good thing, the country will go about its business secure in the knowledge that Washington is so busy fighting itself that it can't much screw up things elsewhere. Public problems may fester, but most of them (Obamacare being the possible exception) can fester a while longer, life goes on. In other words, the constitutional system will continue to work as designed, and the guardrails of American politics will constrain the President, as intended.

Where the Trump Presidency ultimately ends up is a subject for future historians. This paper does not presume to know, it simply attempts to detail out the broad outlines of what Republicans and President Trump hope to achieve, and attempts to explain why, while noting the many political and economic factors that may frustrate those policies.

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