

**Conceptualizing a 21<sup>st</sup> Century New Deal**

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While the parallels between Franklin Roosevelt's inauguration in 1933 and Barack Obama's in 2009 have been the subject of much discussion, data provided by two Berkeley economists point to deeper linkages between the circumstances faced by these two presidents. Emmanuel Saez and Thomas Picketty have been studying long term trends in the U.S. in income inequality using data from the Internal Revenue Service. One of their graphs (Figure 1) shows a remarkable pattern. When income is defined to include realized capital gains, the share of the top 10% of households reached a peak of just under 50% in 1928. After a long period in which the top decile's share stayed around 35%, income inequality began moving upward in the Reagan Administration and after twenty-five years again reached the same peak in 2006.

The symmetry here is startling. In the year after the peaks in 1928 and 2006, there was a market crash followed by a sharp economic downturn. In both eras, the peak maldistribution of income had two dramatic macroeconomic consequences. First, high income households engaged in speculative activity that fueled a spectacular asset bubble. In the 1920's, this activity focused on the stock market; in the current decade, it was evident in the housing market and in the markets for a variety of speculative financial instruments including collateralized mortgage obligations and credit default swaps. Second, the fact that the bottom 90% of households were left with only about a half of all income meant that consumer demand was heavily dependent on increased rates of borrowing. Once the downturn began, consumer credit ceased to be available so that

consumers simply lacked the resources required to revive economic activity.

The parallel suggests the urgency of a 21<sup>st</sup> Century New Deal that would redistribute income to create the foundation for a new period of economic growth comparable to the two decades following World War II. To be sure, Saez and Picketty's data provide a stark reminder that much of the diminished income inequality of the Roosevelt era occurred during the Second World War—a time of shared sacrifice to defeat enemies on two continents. Making similar progress in redistributing income during peacetime would undoubtedly occur more slowly and encounter fiercer resistance. But the effectiveness of New Deal era reforms helps explain why income inequality remained close to World War II levels for another thirty five years.

The big obstacle to conceptualizing a 21<sup>st</sup> Century New Deal is that the structure of the economy has changed radically since Roosevelt's time. Even if one were to use FDR's reform project as a template, it would no longer fit an economy that is significantly different in the structure of the labor force, the technologies of production, and the basic basket of goods and services that make up consumer purchases. The task is to understand how FDR restructured the economy at a higher level of abstraction than specific programs such as Social Security and the Securities and Exchange Commission.

It is also important to recognize that despite the extraordinary nature of FDR's "first 100 days", the direction of New Deal reforms did not become apparent until years later. Roosevelt was a notorious experimenter; some initiatives were simply abandoned, others were thrown out by the Supreme Court, and there were many twists and turns in his policy agenda. The conception of New Deal reforms elaborated here is a retrospective reconstruction that encompasses measures that were adopted between the last year of Hoover's Administration all the

way through to the end of 1948 when Truman served out the remainder of FDR's fourth term.

This caveat is essential to understand what is being argued here. I am not seeking to extrapolate from the policy initiatives of Obama's first one hundred days. On the contrary, I am trying to suggest the magnitude of the reform agenda that needs to be carried out if the Obama Administration were—over the next decade—to launch as significant a restructuring of the U.S. economy as had been accomplished in the 1930's and 1940's.

### **What the New Deal Did**

As we have already seen, the New Deal put in place new rules and new institutions that helped redistribute income downward. The growth of organized labor that followed the passage of the National Labor Relations Act was a major part of this, but so also were New Deal tax reforms and the creation of Social Security and Unemployment Insurance. In the years after the War, the GI Bill played a significant role in equalizing incomes by upgrading the education of an entire cohort of young men.

The New Deal also put in place some of the key institutions required to translate this more equal distribution of income into the consistent demand needed for a period of sustained economic expansion. Specifically, the New Deal helped to establish a mortgage finance system that made possible the significant expansion in home ownership that supported the post-World War II economic expansion. The great suburban building boom of the post-war years was facilitated by these mortgage lending arrangements. While the pattern of development intensified racial exclusion, it facilitated a wave of investment in housing, consumer durables, and suburban infrastructure.

At the same time, New Deal reforms of the financial market worked to discourage some of the more speculative uses of capital that had flourished in the 1920's. The combination of the Securities Exchange Act and Glass-Steagall closed down some of the casino-like practices that had helped to generate the bubble and the crash. Moreover, limited international capital movements during World War II and in the years immediately after the war helped channel available capital to more productive uses. And high marginal taxes on short term capital gains further dampened speculative activity.

But New Deal policies also helped to construct new circuits that directed available capital into productive channels. One was the mortgage credit system that financed suburban housing development.. But the most significant of these mechanisms was the expansion of government itself. In 1929, receipts of Federal, state and local government represented about 10% of GDP but even after the war ended, this had risen to 25% in 1946. Since some of this expanded government was financed by progressive taxation, the consequence was that high income households had less “extra income” that they could risk in speculative investments. Moreover, a substantial share of government spending, particularly in the early post-World War II decades went into education that helped to improve the skills and capacity of the labor force.

The New Deal template, in short, gives us four distinct tasks:

1. Redistribute income away from the top 10% of households.
2. Support new and durable structures of demand.
3. Create regulatory obstacles to the speculative use of capital.
4. Build new circuits that direct capital into the financing of productive activities.

While the ways in which the New Deal accomplished these four tasks can not be replicated,

this inventory provides a useful framework for conceptualizing the reforms that are needed now.

### **Income Redistribution**

It is difficult to exaggerate the importance of a more egalitarian income distribution for the future health of the U.S. economy and society. However, there are distinct dangers—both political and economic—in any effort to achieve this objective through the standard recourse of greater income tax progressivity. “Soaking the rich” is likely to solidify a bloc of high income taxpayers in opposition to the Administration in power, and they will be able to use their formidable financial resources to support candidates who will promise to reverse those tax increases. Since tax cut politics worked to solidify Republican political control for a generation, it would be a mistake to provide another opportunity for conservatives to gain a strategic electoral advantage over the tax issue.

Moreover, there is evidence showing that the most advanced European welfare states constructed their more egalitarian arrangements on the basis of tax systems that were not particularly progressive. Sweden, for example, has funded wide ranging social programs on the basis of a tax system that placed much of the burden on the middle and working classes (Lindert 2004). The political deal was that high income individuals and major corporations did not face major tax increases and they simultaneously benefited as Social Democratic social programs made employees considerably more productive.

The major impact of social programs on income inequality comes by raising the floor for the bottom third of the income distribution. With income maintenance programs, a strong education and training system, and widespread unionization, the people who in the U.S. would be low wage workers are able to achieve a decent standard of living. This is essentially a human

capital strategy in which income inequality is reduced by diminishing the human capital gap between high wage and low wage individuals, and it is supplemented by a regulatory strategy that shuts down the option of creating new pockets of low wage work that could expand over time.

Learning from the Scandinavian experience does not mean abandoning all efforts to improve the fairness of the tax system. There is considerable room to increase revenues by reversing various loopholes, regulatory lapses, and ill-conceived changes that were introduced into the tax system over the last decades. In the list below, action has already begun items 1-3 and needs to be supplemented by progress on 4 and 5.

1. Evasion of income tax through off-shore accounts has become pervasive and requires much tighter regulation of hedge funds and closing down of foreign tax havens that refuse to provide information to the IRS.
2. The corporate income tax needs to be restructured to eliminate incentives for firms to move operations off-shore, force firms to report the same income and profits to the IRS that they report to their shareholders, and eliminate a variety of other abusive loopholes. Redressing these problems could be combined with a lowering of the current marginal rates that are now purely theoretical.
3. Provisions that allow hedge fund and private equity partners to treat their salaries as capital gains need to be changed.
4. Aggressively high marginal tax rates should be imposed on executive compensation and all compensation for financial sector employees in those cases where firms lack mechanisms to align employee behavior with the long term profits of the firm.
5. Marginal tax rates on short term capital gains should be increased substantially since excessive

short term trading in capital markets makes it more likely that traders will collectively overshoot in both up phases and down phases.

But even with these reforms and significant reductions in defense budgets, the corporate and personal income taxes in the U.S. are unlikely to generate revenues needed to make substantial progress towards a human capital upgrading strategy for reducing income inequalities.<sup>1</sup> Moreover, trying to overcome the shortfall by a significant increase in marginal tax rates is likely to fail politically. Since there is also little room and little desirability for expanding payroll taxes, the logical strategy is to emulate the Europeans and introduce a Value Added Tax as an additional revenue stream. As a consumption tax, this would draw support in some conservative quarters and it could be structured in a way to give states strong incentives to repeal state and local sales taxes.

The VAT could initially be set at a rate well below the European levels that are often 20% or higher. Currently, the annual yield from state and local sales taxes is about \$412 billion in 2006.<sup>2</sup> The VAT could be set at a rate to produce \$612 billion in total revenues. This would leave close to \$200 billion per years after funds were rebated to state and local governments to make up for lost sales tax revenues. These resources could be focused on financing programs to

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<sup>1</sup>This is true even if the U.S. were to redefine budget deficits by creating a separate capital budget for the government that could be financed by borrowing. The problem is that spending needs for public sector investment categories such as infrastructure, research and development, and education are already huge.

<sup>2</sup> Since the VAT would cover many service industries that are currently excluded from the sales taxes, it would generate more revenue even at the same rate as current sales taxes.

upgrade the capabilities of employees in the lower third of the wage structure. This could include financing of universal access to health services, subsidies to make quality pre-school available for many more children, a significant improvement in job training and skill development programs as well as strong financial support for adult workers to pursue college and higher level degrees. Ideally, something on the scale of the GI Bill in the 1940's is needed to help a large portion of noncollege educated young people between 18 and 35 to acquire new skills that would allow them to find alternatives to low wage work.

At the same time, significant regulatory measures to improve the bargaining power of low wage workers are needed. This includes passage of the Employee Free Choice Act to increase unionization rates, indexed increases in the minimum wage, actual enforcement of wages and hours rules, as well as immigration reform measures that eliminate the incentives for employers to use undocumented employees to drive down wage levels.

### **New and Durable Structures of Demand**

It should be obvious that the income redistribution strategy is ultimately dependent on strong demand that helps to tighten the labor market. As Figure 1 clearly shows, it was the extraordinarily tight labor markets of WW II that saw the greatest gains in improved income distribution. While it is unrealistic to expect anything comparable during peacetime, something like a decade of unemployment at near the 4% level could produce significant gains. But the growth model on which the U.S. economy has relied since the New Deal has been exhausted. There is no way to return to a pattern of growth based heavily on single family homes, suburbanization, automobiles, and cheap carbon-based energy. But what will people consume

and where will the new job growth occur?

It is here that arguments about postindustrial transition are relevant. Households have already made a shift from goods to services in their consumption patterns. By 2007, services—including housing and transportation other than owner operated vehicles—represented 60% of consumer outlays as compared to only 40% in 1960. This shift is likely to accelerate so that individually-consumer manufactured goods will continue to shrink as a percentage of consumption. Embedded in this shift is the beginning of a transition from quantitative to qualitative growth (Block 1990). This means that some of the fruits of economic growth are now being taken in the form not of commodities but of improved quality of life including improvements in the natural and physical environment. This is already evident in increased health care spending that is intended to extend the life span and improve the quality of life and in increased education outlays that upgrade individual capacities.

For years, critics of the idea of service-led growth have insisted that it makes no sense to construct an economy in which the work that most people do is to take in each other's laundry. But the core of the postindustrial idea is that activities that used to employ a high percentage of the labor force such as farming and working in factories to make durable manufactured goods will inevitably employ only a very small fraction of the population. This means that most of the labor force will be providing services such as health care, education, social services, housing, communication, and entertainment. Moreover, much of this labor is productive in two senses. First, health care workers, for example, are providing a service that consumers very much want and need. Second, quality health care is a critical input into all forms of production because a healthy labor force is more productive.

The real problem is that while consumer demand has been shifting towards these services, the economy's capacity to produce them in greater quantity has not kept up. This is particularly evident with health care, child care, and higher education—sectors that have experienced annual rates of inflation that are two or three times higher than increases in the Consumer Price Index. The continuous bidding up of prices has produced rationing by price that puts these services out of reach for lower income consumers. Moreover, for both the health sector and much of the education sector, there are serious concerns that the average quality of services has not been improving.

This suggests that the first critical element of the demand story is that health care and education need to be reorganized in ways that provide higher quality services for the entire population. One element of this is assuring universal access to health care, availability of quality child care for all 3 and 4 year olds, elimination of the financial barriers that block access to public higher education for many, and increased availability of affordable retraining opportunities for adults. But it is important to recognize that access is only part of the issue; there also have to be institutional reforms that improve the quality of the medical care and educational services that people are consuming.

In the case of health care, this reorganization might not require new job creation, but simply shifting employees from processing paper to participation in direct care. In the case of education, there will be a considerable expansion of employment opportunities as ever greater percentages of the population spend some part of their time in educational institutions. Obviously, the most complicated issue is figuring out the funding formulas of what will be paid for by different levels of government and what will be paid for by individual consumers. But,

however, this is worked out, we can anticipate that demand for education and health services will constitute an ever growing percentage of total demand in the economy.

The second element of the demand story centers on housing, transportation, and energy use. Here it is obvious that the pattern of land use that centers on detached single family homes, long commutes by automobile and cheap energy simply cannot continue. Over the next two decades, the United States needs to invest trillions of dollars in creating greener communities, noncarbon sources of energy, and new forms of transportation. The initial phase of this process will center on large investments in retrofitting the existing housing and building stock to be energy conserving, rapid build out of alternative energy technologies such as solar, wind, and biofuels, and the creation of new rail networks and vehicles powered by electricity or hydrogen. A subsequent phase will continue these initial investments and add two new emphases. The first is a focus on building each year millions of new green, higher density housing units with convenient mass transit access to employment. The second is a redesign of manufacturing and agriculture to reduce energy use and other forms of waste.

Since the U.S. has been spending upwards of \$500 billion per year on imported oil, these huge investments can literally be financed out of future savings on the import bill. Or to put in other terms, currently half a trillion dollars of U.S. demand is diverted overseas. By shifting that demand back into the U.S. domestic economy, the result will be significant job creation and economic dynamism.

The third element of the demand story is a significant strengthening of the U.S. “Innovation economy”—the set of institutions and expenditures designed to transform technological breakthroughs into useful products and services. Continuing and accelerating

innovation is obviously critical for developing efficient new sources of energy and for improving the health care system. But it is also critical for the overall health of the economy; continuous innovation is necessary to reduce the labor required to produce necessary consumer goods. This is the way that the society can afford to shift funds into producing health, education, and other outlays on the quality of life.

While this innovation economy has been growing substantially, it has struggled with insufficient funding. The government's outlays for civilian R&D peaked in 2003 and have been declining ever since. Moreover, the tens of thousands of small, high tech firms that are increasingly responsible for innovations in the economy (Block and Keller 2010) face chronic difficulties in getting the finance that they need. An effort to increase funding to both the public and the private sides of the innovation economy on the order of \$150 billion to \$200 billion per year would go a long way towards accelerating innovation, strengthening demand, and building new jobs and new industries.

### **Regulatory Barriers to Speculative Uses of Capital**

Over the same three decades in which income inequality in the U.S. has worsened, the economy has experienced a long series of financial bubbles in which sudden inflows of new capital have driven asset prices to unsustainable levels. In the 1980's, there was substantial overbuilding of commercial real estate and a frenzy of mergers and acquisitions financed by junk bonds. In the 1990's, there was a huge runup in stock market prices, particularly focusing on internet stocks. When that bubble burst at the beginning of the 200's, the housing bubble immediately began with accelerated increases in prices, the huge expansion of dubious mortgage

lending, and the spectacular growth of collateralized debt obligations and credit default swaps.

These bubbles have been extremely costly for the economy. Their bursting generally produces a period of recession or slow growth, resulting in trillions in lost output. On top of this hundreds of billions are lost through write downs of asset values. Perhaps even more importantly, the diversion of investment flows into these speculative manias deprives the economy of the added output that would have come from more productive investments. Moreover, the bubble economy has been closely linked to the imposition of financial discipline on corporate managers; they face unrelenting pressure to keep stock prices up which often means sacrificing spending that will strengthen firms over the long term (Bogle 2005).

A number of steps are required to reduce the vulnerability of the economy to these bubbles. As described in the next section, new channels must be created to direct capital into more productive domestic uses. The U.S. must also restore its international trade to balance, so that it is no longer necessary to finance the deficit through international borrowing that helps to fuel bubbles. Tax reforms that redistribute income away from the richest households and that increase tax rates on short term capital gains can also dampen speculative activity.

However, regulatory reforms are also a necessary part of the solution. One of the central problems is the erroneous belief that a financial system can consist of one segment of highly regulated banks and insurance companies and another segment of completely unregulated hedge funds and private equity funds. Since unregulated firms have every incentive to gain greater rewards by pursuing more risky investment strategies, this structure is inevitably unstable. On the one side, as long as these risky strategies are paying off, the unregulated firms will grow and prosper and expose the economy to high levels of systemic risk. Moreover, the regulated firms

have no choice but to emulate the strategies of the unregulated or they will lose people, capital, and customers to the unregulated sector. They will use all of their political capital to persuade regulators to allow them to copy the high risk strategies, and that will further increase the system's vulnerability.

In short, there has to be a framework in which all financial actors are subject to regulation. The regulations should be graduated, so that depositary institutions and insurance companies are subject to a stricter set of controls. But large, unregulated financial entities must no longer exist. In fact, the regulations need to be written so that whenever a pool of capital reaches a certain critical size, it will fall under a regulatory umbrella. Without this step, financial entrepreneurs will grow new categories of unregulated entities until they are large enough to jeopardize the entire financial system.

Within this new regulatory framework, four provisions are critical. First, there need to be strict limits on the amount of leverage that hedge funds or other entities can borrow as well as even stricter limits on what banks and other highly regulated institutions can lend to less regulated financial firms. Second, throughout the financial system, compensation mechanisms must be created that block institutions from rewarding their leaders or employees from short term trading strategies that produce longer term liabilities. For example, the bonuses that are given to traders working at commercial or investment banks should take the form of equity in the firm that cannot be sold for a three to five year period. Third, when financial institutions sell loans they originated, they must retain a significant interest in these debts in their own portfolios. This is necessary to prevent the financial system from turning into a game of "pass the trash". Finally, antitrust strategies must be aggressively used to block the creation of "financial supermarkets"

that control a disproportionate share of financial assets and are too big for top managers to provide adequate supervision of the strategies being pursued by traders in diverse markets.

Along with these steps, it would also be highly beneficial to impose a small transaction tax on trades in both domestic and global financial and foreign exchange markets. A major contributor to the bubble dynamic are the financial traders who bet the trend, driving rising markets even higher and falling markets even lower. Transaction taxes—if set at the proper level—would discourage a significant fraction of these entirely speculative trades, decreasing the likelihood that market prices would overshoot both on the upside and the downside.

An additional advantage of the transaction tax is that a share of the revenue could be devoted to the increasing costs of effective global financial regulations. Some of the revenues could be used to assure that investors are no longer able to shop for jurisdictions that are willing to waive international regulatory standards.

### **New Circuits for Capital**

Even with the best regulatory structures, capital will continue to flow towards speculative investments if there are not sufficient channels for its productive use. And in this instance as well, the problem cannot be solved in the United States alone; global solutions are needed to assure that capital is used productively across the global economy.

One of the most important steps is to move U.S. trade back to balance and end the twenty-five year pattern of the U.S. borrowing from abroad to finance its surplus imports. This goal can be accomplished by moving the U.S. towards energy independence, renewed investments in innovation that will translate into stronger exports, and tax reforms that eliminate incentives for

U.S. firms to move production abroad.

While this shift is occurring, there is an urgent need to create new financial instruments that will direct significant capital flows towards the poorest areas in the world. There is a need for tens of billions of dollars per year in investments in poor countries for health, education, and basic infrastructure including clean water and sanitation. Investors in China, Europe, India, and the United States working through regional development banks would be able earn 5% per year returns by purchasing 30 year international development bonds. Governments in the richer countries would subsidize the loans, so that the money could be loaned at 2% or 3% per year to finance projects that directly improve the quality of life or both the urban and the rural poor in the less developed nations. This would be a version of the long discussed “Global Marshall Plan” in which these flows could both accelerate development and create expanded export opportunities for both older and newer industrial powers. Similar investment instruments could be created to accelerate environmental protection and the shift away from fossil fuels in the developing world.

It is also urgently necessary to create new circuits for capital within the United States. According to one source, the U.S. needs more than \$2 trillion of investment to repair the country’s decaying infrastructure. This is well beyond the capacity of the public sector, and there are a variety of ways to allow private capital investment to play a part in this process. One idea is an infrastructure investment bank that would have an initial capitalization by the government of \$60 billion, and would then draw on private funds to finance a much larger portfolio of investment projects. Others have stressed the creation of public-private partnerships to build or repair needed infrastructure.

Similarly, private capital flows are needed to finance the massive investments discussed

earlier to green the economy including retrofitting and ultimately rebuilding much of the residential and commercial building stock and developing alternative fuels and new generations of vehicles. Tax incentives are obviously an important element in persuading both households and businesses to make needed investments in conservation and alternative energy. Along with this, there needs to be the creation of a substantial system of government loan guarantees that provide private investors with some measure of protection as they finance business initiatives in this area. The government has already begun to experiment with the use of loan guarantees as authorized in the 2005 Energy Bill, but expanding these efforts requires considerable care to avoid green bubbles. The case of corn-based ethanol shows that private capital can easily be mobilized for quick fixes that are problematic on both environmental and economic grounds. Ideally, there should be multiple public-private green banks that develop considerable expertise in putting together portfolios of loans with varying degrees of risk to finance \$100 billion a year or more of green investments.

Yet another new channel of capital needs to be created to assure adequate funding for the emergent innovation economy. Part of this involves significant and sustained increases in Federal spending for civilian oriented research and development, including the web of programs designed to accelerate the commercialization of new technologies. In order to keep these critical expenditures from competing with everything else in the Federal Budget, it is possible to create a National Innovation Fund (NIF) that would be financed by a share levy on all new publicly listed firms. Precisely because new businesses are dependent on the huge stock of knowledge created with public funds, firms would be required to give 2% of their shares to the NIF. The Fund would be required to hold shares for ten years, and then it would be permitted to sell shares in an orderly

fashion with the revenues going to support Federal innovation efforts. Had such a program existed, the NIF's holdings of Google stock alone, after ten years, would have been worth \$3 to 4 billion.

But the other critical priority is to find ways to increase private capital's participation in supporting the thousands of tiny high technology firms that employ a growing share of the scientific and technological labor force and that are responsible for many key innovations (Block and Keller 2010). To date, these firms in their early years have been heavily dependent on government money and a relatively small number of "angel investors" who are willing to take on much more risk than venture capitalists who generally wait until firms have completed the process of developing a commercial product. Given these limited sources of support, many of these entrepreneurs are forced to give up or shift into less risky lines of business.

This problem could be solved by creating a highly regulated "dollar" stock market for these budding high technology firms. Once a firm was carefully screened to assess its technology and business model, it could issue up to 10 million shares, at a dollar a piece that would not compromise the founders' control of the enterprise. Newly created venture capital mutual funds would put together portfolios of a few thousand shares from hundreds or thousands of these firms and then be permitted to market their shares to the public and to institutional investors. Even if only one out of twenty of these firms were to prove successful, these portfolios should increase in value as those successful firms graduate to one of the existing stock exchanges. With adequate regulations to avoid fraud and manipulation, this mechanism could ultimately finance tens of thousands of small and medium sized enterprises that could develop innovation goods and services.

A final priority over the longer term is to create mechanisms by which private capital can participate in the gains that come from greater investments in “human capital”—the skills and capacities of the population. Even with the earlier strategy of introducing a Valued Added Tax to finance greater investments in human capital, a shortfall is likely to continue to exist between the needs of individuals for more education and the capacity of government to pay for this. One possible solution could come from a more careful and cautious version of the securitization of debt that played such an important role in the economic meltdown.

Imagine, for example, if the bulk of new loans for students in college, graduate and professional schools were rewritten to be more like a thirty year mortgage with the provision that the amount that students paid in the last ten years of the loan would rise if their annual incomes were above a certain threshold. Colleges and universities would make loans to several cohorts of students and then the loans from a particular geographical area would be bundled into bonds which would predictably return 4 or 5% per year but which might produce higher rates of return in the last ten years depending upon the success rates of a particular cohort. While the idea might sound strange, it is a logical way for investors to participate in the rising incomes that can potentially be created by expanded investments in the skills and capacities of the labor force.

Certainly some of the examples provided here of new institutional mechanisms to redirect capital flows are far too specific. In almost all of these cases, there are multiple institutional innovations that could help generate sustainable flows of private capital to fund important categories of investments that are now currently underfinanced. But some specificity is necessary because we lack recent examples of government redirecting private capital flows. Probably, the creation of new mortgage financing institutions seventy years ago is the most recent

example of a large scale government initiative designed to redirect capital flows.

## **Conclusion**

This paper is not meant to be comprehensive; it is not an attempt to spell out all of the institutional reforms that would be a desirable part of a 21st Century New Deal. Rather, the effort has been to propose the basic skeletal structure of a reform project that would be deep enough to produce a new epoch of sustained and sustainable economic growth. The skeleton would also support a variety of efforts to narrow some of the enduring inequalities in this society of gender, race, immigration status, and geographical regions. It would also be consistent with initiatives to reduce high rates of incarceration, bring corporations under greater social control, and strengthen institutions of democratic governance. But the skeletal structure would permit a range of different possible outcomes on those specific issues.

But what are the probabilities that any significant proportion of the reform agenda outlined here will actually be implemented over the next decade? Given the rarity of reform epochs in U.S. politics, the probabilities are certainly low, perhaps no better than twenty chances out of a hundred. As many analysts have noted, the business community exerts enormous power within U.S. politics and multiple veto points provide entrenched interests with repeated opportunities to block threatening reforms. And even if these obstacles can be overcome, it has often happened in the past that an intensification of international conflicts proves fatal to a domestic reform agenda. This happened most recently when LBJ's Great Society was abandoned in the jungles of Vietnam.

Nevertheless, thirty years of failed market fundamentalism has created the possibility of a swing of the pendulum towards a more progressive political economic agenda. If a skillful and

politically charismatic President can implement significant reforms in his first two years in office, such as a major extension of health care to millions of citizens with insufficient or no coverage, there could be an electoral strengthening of the reform coalition that produces significant momentum for further reforms. As in the 1930's, each successive reform effort could further undermine the previously dominant "free market" ideology, creating additional space for imaginative new policy initiatives.

In short, the possibility is real enough that progressive intellectuals need to be mapping potential reform agendas that could provide guidance to policy makers and politicians. This paper is intended as a contribution to that conversation.

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Figure 1 Data from Saez and Piketty.

