Project Syndicate

Will Americans Become Poorer?
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CAMBRIDGE – Robert Gordon of Northwestern University has launched a lively and important debate about the future rate of economic growth in the United States. Although his book The Rise and Fall of American Growth will not be published until January 2016, his thesis has already garnered coverage in the Economist and Foreign Affairs. Clearly, Gordon's gloomy assessment of America's growth prospects deserves to be taken seriously. But is it right?

Gordon argues that the major technological changes that raised the standard of living in the past are much more important than anything that can happen in the future. He points to examples such as indoor plumbing, automobiles, electricity, telephones, and central heating, and argues that all of them were much more important for living standards than recent innovations like the internet and mobile phones.

I agree with Gordon that I would rather give up my mobile phone and even the Internet than go without indoor plumbing and electricity. But that just means that we are lucky to be living now rather than a century ago (and even luckier to be living now than two centuries ago or in the middle ages). The fact that these major innovations happened in the past is not a reason to be pessimistic about the future.

Gordon also points to the recent slowdown in real (inflation-adjusted) GDP growth. According to official US statistics, real GDP per worker grew at an average annual rate of 2.3% from 1891 to 1972, but by only 1.5% since then.

But the official statistics on GDP growth fail to capture most of the gains in our standard of living that come from new and improved goods and services. That means that the official growth rate does not reflect the rise in real incomes that came with air conditioning, anti-cancer drugs, new surgical procedures, and the many more mundane innovations. Moreover, because the US government does not count anything in GDP unless it is sold in the market, the vast expansion of television entertainment and the introduction of services like Google and Facebook have been completely excluded from the national account.

This means that the true rise in real incomes was actually faster than the official statistics imply – possibly much faster. That is true of the data for the first half of the twentieth century, and it continues to be true today. It is not clear whether the measurement problem was bigger in the more distant past than it has been recently; but it is irrelevant when we think about the future. Whether growth in per capita income that is officially estimated at 1.5% is in reality more like 3%, we are enjoying the higher level of real incomes inherited from the past. So will future generations.

Indeed, there is simply no reason for the view, often expressed in surveys and appearing in Gordon's book, that the children of today's generation will not enjoy a standard of living as high as their parents'. That may be true for some people, especially those with relatively high incomes, but it is definitely not true for most people.

Think about a 30-year-old new parent at the middle of the income distribution. Thirty years from now, the child will be as old as her median-income parent is now. If real incomes grow at just 1.5% a year, the median income 30 years from now will be nearly 60% higher than the income of today's median-income individual.

Even if the child earns 30% less than the median at that time, her income would still be higher than today's median income. And if product innovations and improvements imply that per capita real incomes grow at 3% a year, the median income of someone 30 years from now would be more than twice today's median income.

So Americans are lucky that they have inherited the innovations of the past, and that real incomes will continue to grow in the future.

But that is not a reason for complacency. The US can increase its future growth rate by improving its education system, raising its rates of saving and investment to where they were in the past, and fixing the features of its tax and transfer systems that reduce employment and earnings.

Gordon focuses on the effect of technological innovation on Americans' real incomes. But an important limitation of his

argument is that it gives short shrift to policy innovation. America's economy – and those of many other countries – could grow faster in the future if policymakers adopt the appropriate reforms.

Read more at http://www.project-syndicate.org/commentary/robert-gordon-future-us-economic-growth-rate-by-martin-feldstein-2015-08#VCB865iQYZ6m3DsO.99

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