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Gov't Transfer Payments Are Also Behind The Slow Growth

By MIKE COSGROVE

The U.S. achieved strong average annual growth of 3.3%, after inflation, from 1929 to 2012. But from 2002 to 2012 that average growth rate fell to 1.8%. Why the slowdown in growth?

Reasons include the uncertainty dumped on both businesses and individuals by ObamaCare and the unknown costs created by the Fed's unprecedented ultra-easy monetary policy.

The less obvious reason is the rapid growth in the value of transfer payments going to households over the past 30 years.

These payments have clearly altered incentives to work. As recently as 1979, only 20% of U.S. households received more in transfer payments than they paid in total federal taxes.

Total federal taxes include federal income tax, both the employer and employee portion of the payroll tax, excise taxes and the corporate income tax after being allocated to capital and labor.

That means that in 1979, 80% of U.S. households were making a net positive contribution to federal taxes. Individuals had a major incentive to work as transfer payments were a small portion of the economy. Most households were making a net contribution toward federal spending.

Skip ahead to 2009. Sixty percent of U.S. households received more in the value of transfer payments than they paid in total federal taxes, meaning only 40% of U.S. households in 2009 were making a net positive contribution to total federal expenditures, according to the Congressional Budget Office.

This means incentives of 60% of U.S. households may be weighted toward seeking more transfer payments, altering the work ethic, contributing to unemployment.

The proportion of the population 65 and over during this 30-year time period increased approximately 2 percentage points. That 2-percentage-point increase didn't account for the huge increase in transfer-payment households.

The proportion of households making a net positive contribution to federal taxes will decline more in the years ahead for two reasons: (1) the proportion of households that are retired will increase significantly due to demographics, and (2) ObamaCare effects.

ObamaCare subsidies may go to households with income as high as $90,000 or more, making ObamaCare an income-redistribution program that cannot pay for itself despite the current array of ObamaCare taxes.

These two factors combined will create a sizable additional decrease in the number of households making a positive net contribution toward federal expenditures.

The growth in transfer payments has built such a large dependency on federal largess for U.S. households over the past 30 years that the focus of both parties is on tax revenue. They have different ideas about the best way to generate more tax revenue, but both parties are addicted to the idea of more and more federal tax revenue.

Democrats think they can obtain more tax revenue by increasing tax rates on a smaller base, while Republicans expect more tax revenue can be generated by flattening tax rates on a broader base, creating faster growth and more revenue.

The focus on more and more tax revenue is all about re-election. As long as the combination of tax revenue and deficit-financing generates enough revenue for the federal government to fork over transfer payments, the majority of politicians are re-elected.

It is always about re-election. U.S. politicians saw Western European politicians get fired when tax revenues could no longer support those welfare states.

Policies to encourage economic growth in the U.S. take a back seat as revenue for transfer payments becomes the priority for both parties. The result is slower economic growth and fewer households making a net positive contribution to the funding needs of a large central government.

In 20 of those 30 intervening years from 1979 to 2009 there was a Republican president. Republicans have just as much responsibility as the Democrats for turning the U.S. into a large welfare state with high unemployment and major disincentives to work.

Some analysts suggest the effective incremental cost of choosing work versus keeping means-tested transfer payments could be as high as a dollar lost in the value of transfer payments received for each dollar gained by working.

• Cosgrove, principal at Econoclast, a Dallas-based capital markets firm, is a professor at the University of Dallas