

3 Questions: Michael Greenstone on deficit spending

November 2 2010, By Peter Dizikes

Government deficit spending has been a contentious issue during this year's U.S. mid-term election campaigns. Yet some economists believe that additional government spending in certain areas is needed to help spur growth. MIT News asked Michael Greenstone, MIT's 3M Professor of Environmental Economics, and director of The Hamilton Group, a Washington-based public-policy organization, about America's spending priorities.

Q. Due to low borrowing costs, you've likened infrastructure or research investments to finding "a 20-dollar bill laying on the ground," yet the political tide has turned against such spending. Addressing the current opponents of deficit spending, what would you say is the best case for these kinds of investments?

A. The concern about the long-run fiscal situation is encouraging, especially because the political system has seemed unconcerned about this issue for most of the last decade. However, we need to make sure that we don't get so drunk on fiscal rectitude that we imperil our future by failing to make investments in our future. Infrastructure and federal support for basic research are two key areas where [government](#) spending can lay the foundation for a more prosperous future. For example, infrastructure can reduce the costs of moving goods and ideas and basic research can lead to innovations that become the basis for new industries.

However, government support for infrastructure and basic research share

a common Achilles' heel. If the spending decisions are done to serve political goals, rather than economic ones, they will not fulfill their potential and could even be bad investments.

Q. To what extent should the United States' R&D funding in energy be concentrated on the search for breakthrough technologies that could be used globally, versus, say, nearer-term projects making the United States more energy efficient?

A. The proper role for the federal government is to fund research that the private sector would not undertake on its own, yet is key to long-run prosperity. This research seeks wide-ranging scientific understanding that can affect entire industries but does not yet have a clear commercial application. A lot of the research that is done at MIT fits into this category.

In the case of energy, there is currently a stronger case for increased R&D funding than usual one for basic research due to the absence of a global price for carbon or greenhouse-gas emissions. The underpricing of carbon will slow the innovation necessary to reduce the costs of low-carbon energy sources and provides a justification for substantially greater levels of research funding that is aimed at reducing the costs of low-carbon energy sources, demonstrating the feasibility of new technologies at scale, and developing safe and inexpensive methods to capture carbon emissions. Ultimately, a reduction in the costs of low-carbon energy sources would make it easier to reduce carbon emissions.

Q. Broadening from strictly energy R&D to infrastructure, education and other areas, if you could control government appropriations right now, what would your spending priorities be, and why?

A. The last several decades have seen little income growth for many Americans and even income declines for some categories of workers.

My overall theme would be that government needs to focus spending on in areas that are genuinely investments that can increase the long-run prosperity of the entire nation. A challenge is that our budget deficit will need to be reined in and thus even more than usual it is vital to concentrate spending in areas where there is strong evidence of effectiveness. Three areas where increased spending seems justified are:

1. R&D: The exact level of basic R&D funding is a political judgment that must account for other budget priorities, but it seems clear that the current level is inadequate (especially in the energy sector).
2. Education: Back in the 1970s and 1980s, the United States had a large lead over other countries in what share of the population completed a college degree. However at the same time that the global economy has become better integrated, this lead has essentially vanished. France, Sweden and Australia lagged well behind U.S. college graduation rates as recently as 1990, but now clearly exceed the U.S. level. The declining number of well-prepared high school graduates helps to explain these trends. In the last several years, there has been some exciting research on ways to improve the K-12 system of education. This research must continue and then the successful models should be scaled up and funded generously. Successful educational systems are key to advancing living standards.
3. Infrastructure: Several observers report that the nation's infrastructure system is falling apart. There are opportunities to increase infrastructure spending and to redeploy current spending to areas where the returns are greatest.

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