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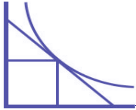

"THE OPTIMAL BUNDLE"

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How to Stop Worrying and Love the National Debt

While politicians denounce high government debt on the campaign trail, economist Brad DeLong offers a surprising hypothesis: the U.S. national debt is too low. DeLong argues the low interest rates on government bonds — lower than the nominal GDP growth rate — means the U.S. government is borrowing too little. His prescription to reverse slow growth is to borrow until the interest rate on government bonds equals the growth rate. The increasing growth rate would ensure the government can repay the debt. *Wall Street Journal* chief economics commentator Greg Ip contends the societal return on investment from infrastructure projects like highways, airports, water treatment plants, and schools must be higher than low government bond yields. However, DeLong's proposal has significant risk. Former IMF economist Paulo Mauro suggests deficit spending might fail to accelerate slow growth if inadequate supply — not demand — persists. Moreover, the government's ability to borrow in a financial crisis could be weakened if it has already accumulated high debt. DeLong's solution has its merits, but it necessitates treading carefully. —JK

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Brad DeLong is a Professor of Economics at the University of California, Berkeley. He formerly served as Deputy Assistant Secretary of the U.S. Department of the Treasury in the Clinton Administration.

The Magical African Economy

African economic growth has been surging in recent years. Is it the next boon for emerging market investors?

The consistent growth of the African economy is coming as a surprise to many economists. The African economy, which is heavily commodity-based, has managed to pull off a magic trick by growing as commodity prices fall. Nigeria, where 90% of total export revenues are comprised of petroleum exports, has been growing more than 5% annually for the past three years. Angola, another oil dependent country, grew at 5.1% in 2013. The growth observed in both cases is not a result of oil exports because oil revenues have remained stagnant in recent years. Rather, growth has come from activities like construction, manufacturing and services. This economic change referred to as diversification has levitated the economy. This has raised expectations of growth to 5% for 2016, according to the African Economic Outlook. The goal seems easy to achieve, as even Ebola couldn't infect African economic growth. —WI

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Do Not Pass Go; Do Not Collect $200 Million Revenue

A recent veto by Pennsylvania's Governor, Tom Wolf, allowed the Pennsylvania Liquor Control Board to maintain control of its monopoly on wine and liquor sales. According to *The Pittsburgh Post-Gazette,* the changes to Pennsylvania's liquor system would have increased revenue for the state by $200 million next year. Why was this change not allowed when it would have increased state revenue while simultaneously lowering prices for consumers? There are a few reasons, according to Jonathan Adler, a law professor at Case Western University. First, jobs would be lost to the private sector. Second, constituencies such as beer wholesalers may become upset at the increase in competition. Lastly, opponents of demolishing the monopoly argue that liquor will become more widely abused. In other words, they fear that privatization will lead to cheaper, more accessible alcohol. But aren't cheaper goods what consumers want? With this in mind, it's confusing to see why such a change to the system did not come to fruition. But, hey, at least Wolf froze in-state tuition. —SL

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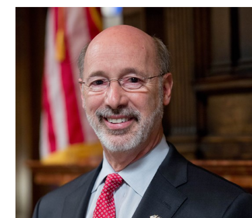

Pennsylvania Governor Tom Wolf vetoed a bill which would have privatized the state liquor system. Pennsylvania and Utah are the only two states which have complete control over wholesale and retail operations.

Op-Ed

Are Cigarette Taxes Addictive?

The question of whether cigarettes are harmful to their consumers is well-researched, and the answer is agreed upon by doctors and other medical experts. However, their benefit to government budgets is a different story, and so is the idea that the revenues which cigarette taxes generate discourage consumption.

Cigarettes benefit government tax revenues in a tremendous way. According to Reuters, “even adding a $1 per pack tax to cigarettes could raise more than $9 billion a year for (U.S.) states.” As reported by USA Today, the U.S. government collected up to $25 billion in 2010 from taxes on cigarette sales and on American cigarette companies, making it a favorable source of income. Cigarette taxes are a stable source of tax revenue for the U.S. government because they increase nearly every year, according to the National Institutes of Health.

While Americans are statistically smoking less in recent years, Indonesian smoking rates are high, causing cigarette tax revenues to explode. As a result, huge American cigarette companies such as Phillip Morris (known for Marlboro) and R.J. Reynolds (known for Camel) are targeting Indonesia as one of their main markets. The fact that Indonesian smoking trends are extraordinary — 67% of Indonesian adult males are smokers — shows there is a lucrative opportunity for big companies. The market shift to Indonesia generates 10% of Indonesian tax revenue from cigarette sales and provides 10 million jobs related to the cigarette industry and businesses. In comparison, the U.S. generates less than 1% of its tax revenue from cigarettes.

Tax revenues from cigarette sales are favorable for governments to collect whether they’re small or large. Because cigarettes are an inelastic good due to their addictive properties, increasing cigarette taxes does not necessarily reduce cigarette consumption. Ergo, it does not substantially decrease cigarette tax revenue. Thus, the laws of economics cannot suit the demand for cigarettes because the price inelasticity of cigarettes is high. The danger governments now face is allowing the effectiveness of generating tax revenue to undermine the very reason the tax was implemented. —RA

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