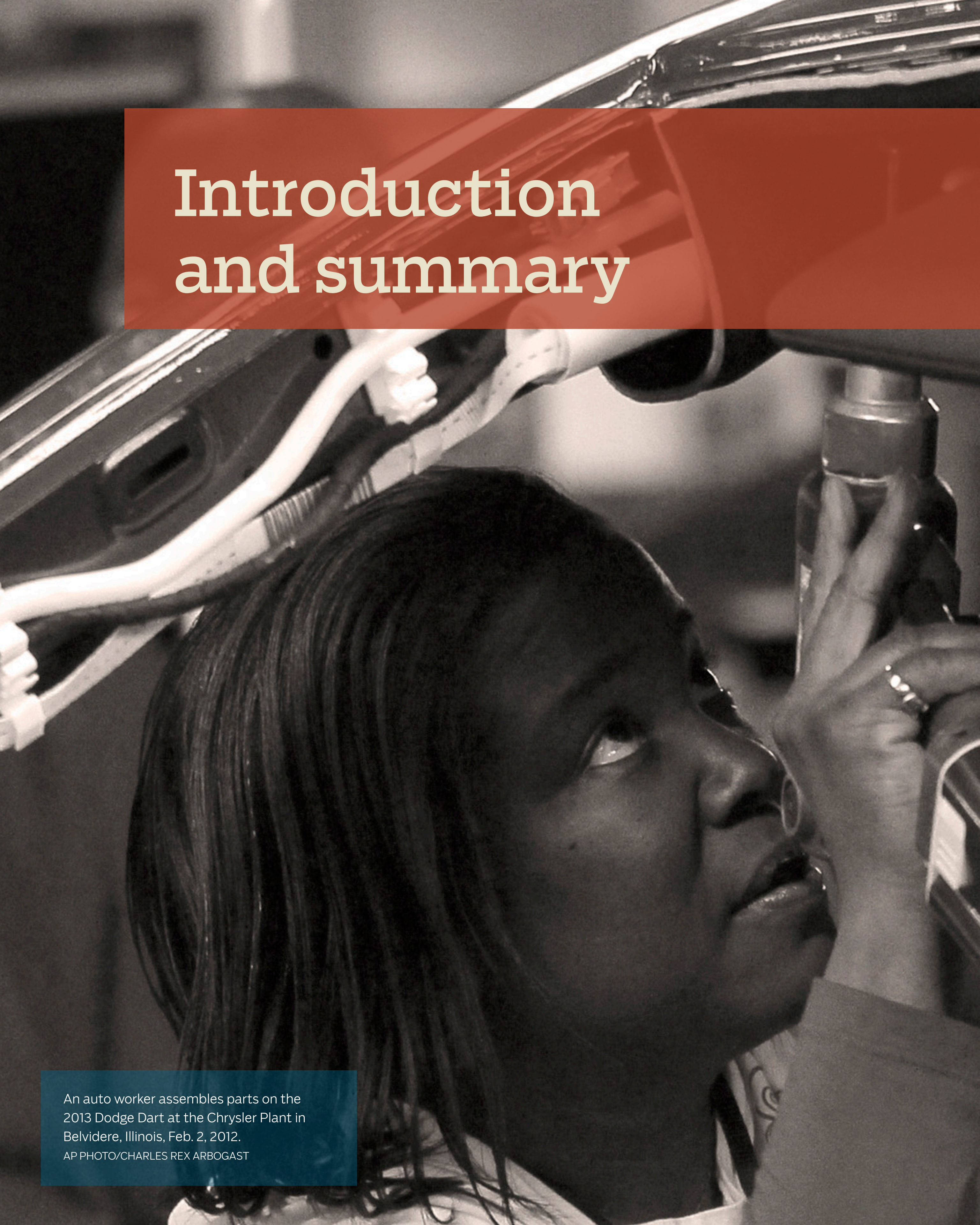
Introduction and summary



An auto worker assembles parts on the 2013 Dodge Dart at the Chrysler Plant in Belvidere, Illinois, Feb. 2, 2012.
AP PHOTO/CHARLES REX ARBOGAST

> It is our generation's task, then, to reignite the true engine of America's economic growth—a rising, thriving middle class.

President Barack Obama, State of the Union address, 2013[1]

If there is one single concern that occupies the thoughts of Americans, regardless of political affiliation, geographic region, job, occupation, or age, it is how to improve our nation's economic prospects.

This report lays out a wide-ranging plan for economic progress. It is a plan that encompasses investment and reform. It is a plan that proposes doing more of some things but, importantly, it is a plan to do more things well.

The agenda presented here is based on what we know makes an economy grow and prosper and what we know are the keys to good jobs and a good quality of life, including:

- A well-educated, secure, and growing middle class that underpins strong demand, entrepreneurialism, innovation, and productivity
- Greater private and public investments deployed more strategically
- A fair playing field for business and workers, both domestically and internationally
- Leadership in science and technology
- Effective institutions and governance

To have a strong and growing economy, we need a strong and growing middle class.

The policies we propose are an important step to redefining our nation's long-term economic prospects and to restoring the American Dream of a better life for each succeeding generation.

Economic growth is a complex process fueled by many factors. When we are setting out to grow the largest, most dynamic economy the world has ever seen, there is no single policy we can rely on to meet our economic challenges. Rather, we need a set of policies that work together to boost our competitiveness and solve our economic challenges. The starting point for our strategy, therefore, is multifaceted and begins with the understanding that people—their work, their ingenuity, their willingness to take risks, and their desire and capacity to build a better life for themselves and their families—are what cause an economy to grow. In the United States, we have 300 million of these engines of growth. To be successful, a country's economic agenda has to strengthen its people. It has to educate them, train them, and reward them with financial security. This is the core of a middle-out plan for economic growth. In other words, as explained in the box on page 6, to have a strong and growing economy, we need a strong and growing middle class.

But while strong, talented people are the most important ingredient in our economic success, they cannot contribute fully if the economic environment in which they perform fails to offer opportunities. For people to build a vibrant economy, they must work in a country committed to technological advancement, readily available capital, quality public infrastructure, a fair playing field for competition, and a strategy for success in the global economy. They must live in a country with thriving businesses, big and small, that are at the vanguard of what's new and are the most efficient in the world.

In short, a robust economy needs strong people working and living in an adaptive economic environment conducive to their success.

Where we are

Our emergence from the Great Recession has been painfully slow. Historically, we have been able to build a bridge out of recessions and find the other side to be as good as or better than where we started. But as we emerge from this recession, we find ourselves in the third in a series of "jobless recoveries" in which unemployment remains elevated well beyond the recovery of growth and profits.

The small stimulus passed under President George W. Bush in 2008 and the larger package passed under President Barack Obama in 2009, plus smaller measures passed since then, restored a level of demand to the economy that created many jobs and prevented others from being lost. Unfortunately, fiscal austerity put in place by the Budget Control Act of 2011 and other tax changes—culminating in 2012 in the so-called fiscal cliff and sequestration-mandated broad, across-the-board spending cuts—are already hurting economic growth in 2013 to the tune of nearly $300 billion.[2]

Given that the U.S. economy expanded at a mere 2.5 percent in the first quarter of 2013,[3] the first brief section of this report, "Creating jobs now," offers policies that we believe would give the economy an immediate boost and that should be implemented as soon as possible. But a lasting economy cannot be built through only short-term measures, which is why we place the focus of this report on longer-term policy suggestions. Adapting to an economic environment that is markedly different from what has come before cannot be accomplished in a year or two or, for that matter, in a single economic plan proposed at a particular point in time.

This raises the question: What has changed that calls us to new policies and approaches? The transformation in the world economy and America's role in it have many faces. Certainly greater global interconnectedness, and particularly greater international trade in goods and services, are important parts of this transformation. The United States now faces more competition from more directions.

To some degree, this was inevitable. Countries poorer than wealthy ones such as the United States can have more potential to grow quickly, and the rest of the world can benefit by learning from innovations originating in the United States. That happened first with Europe and Japan in the decades following World War II, and it's now happening with former communist countries and other nations that have turned the corner on economic development.

The increase in competition isn't a bad thing: A race can bring out the best in us. But we have to up our game if we don't want to be surpassed by others who are better at adapting to the realities of 21st century economic competition.

Meanwhile, there's a new, less inevitable challenge. We are increasingly seeing countries employ aggressive nationalistic economic policies that may work for them in the short run but that undercut the norms of international economic partnership. These practices reduce worldwide economic growth and directly injure those nations that strive to play by the rules.[4]

The economic relationship among nations is, however, but one of the changes affecting the American economy. Another is the development of new technologies and processes that are revolutionizing manufacturing. The shop floors of today's highly innovative high-tech manufacturing companies look nothing like the labor-intensive assembly lines of the past. Technological advances in manufacturing improve productivity and boost growth, but they also demand new strategies to succeed in today's increasingly competitive global marketplace.

Another fundamental change in the economic landscape is climate change. Its costs to businesses, families, and government are often hidden but are becoming less so. And the solutions offer massive new economic opportunities.

Trade, manufacturing, and climate change are not the only areas of the economy to have changed dramatically in the past generation or so. The financial industry has tripled its share of the economy since the 1950s,[5] a trend that carries with it both benefits and risks. Information technology has hugely disrupted industries from publishing to retail, and the result can often mean lower employment. Other countries are also growing their share of the global consumer market and playing an increasing role in setting styles and trends, meaning more competition from around the world for goods and services.

Economic growth faces other headwinds, too, such as the slowing growth of the U.S. labor force and slowing productivity growth. In fact, by 2023 the Congressional Budget Office forecasts U.S. growth will have trended down to just 2.2 percent—far short of U.S. long-term historical growth of 3 percent a year on average.[6]

Where we can go

Properly navigating these changing circumstances can lead to an American and a world economy that has sufficient and good jobs with greater prosperity for all. This is far from the first time we have felt angst over an uncertain economic future even as it has worked out well in the end. During the Great Depression few could have imagined the postwar economic boom brought on by the massive industrialization for World War II and the huge public investments in infrastructure and education that followed. In the 1970s and 1980s, with oil crises, inflation, and Japanese imports seeming to flood the American market, the low inflation and high employment of the 1990s was hard to imagine.

In this photo taken Jun. 3, 2010, Eduardo Mendoza looks over job ads during the ninth annual Skid Row Career Fair at Los Angeles Mission.
AP PHOTO/ADAM LAU

The foundations of the largest economy in the world are still solidly in place, and there is no reason we can't build an economy that capitalizes on our strengths and allows more Americans to participate at the top of their talents. This report describes a set of proposals across a range of areas from education to innovation and infrastructure that are actionable now and would be an important step to putting us on that path.

We divide our policies into two categories: those that strengthen the American people and give them the capability to succeed, and those that build an economic and business environment that puts these talents to use and rewards them. The policies described in this report are numerous and range in scope, interacting and accumulating to form a plan that will boost U.S. economic growth and generate the good jobs that underpin widely shared prosperity.

We summarize below the key problems we are seeking to address, the approach we take to their solution, and examples of the policies that we propose. The rest of this report offers a more detailed analysis of the problems and the full range of recommended policies.

A strong middle class is the key to economic growth

The policies in this report are grounded in an understanding of economics known as middle-out economics. This concept was explained by CAP economists Heather Boushey and Adam Hersh in their paper, "The American Middle Class, Income Inequality, and the Strength of Our Economy." The report shows how an expanded and stronger middle class is a cause and not just a result of a stronger overall economy.[7] It also highlights data showing how an equal-opportunity society—one in which talented individuals can make use of their skills—is not compatible or consistent with a highly unequal society.

For all the disagreements among policymakers, economists generally agree on the ingredients that make an economy grow: human capital, demand, strong institutions and governance, innovation, and financial capital. While all of these are important, since the late 1970s some policymakers have emphasized just one: financial capital. That focus produced supply-side economics and the belief that if government invested its resources in wealthy "job creators," prosperity for all would rain down.

But it didn't because the supply siders had it backwards—a strong middle class is the driver of economic growth, not merely an outcome of it.[8] When one examines the factors that produce a growing economy, the strength of a middle class is critically important to them.

Consider the role of the middle class in these key drivers of growth:

Human capital	A strong middle class better educates itself and demands and gets better education for its children, and this process improves an economy's human capital. For example, U.S. research shows that states where the middle class receives a higher share of overall income also have higher test scores. The same is true in international comparisons.
Demand	A strong middle class creates a stable source of demand for goods and services. This motivates businesses to innovate, invest, and hire. If you want to boost demand, you should focus on boosting the middle class because it is the source of most of the consumption in the economy.
Institutions and governance	A strong middle class demands inclusive and trustworthy institutions, and that governments be more responsive and accountable. This drives governments to invest in the kinds of public goods that make an economy stronger.
Innovation	A strong middle class incubates entrepreneurs and innovators. The majority of our entrepreneurs and inventors come from the middle class. That makes sense: strong middle-class families are the ones that have the skills and financial stability needed for successful risk-taking.

Given that the middle class is key to economic growth and given the mounting stress placed on the middle class over the past 30 years due to stagnant wage growth and rising costs,[9] the question then becomes what policies will grow and strengthen the middle class? Many of the policies in this report are answers to this challenge.

Strengthening the American people

Whatever the future brings, we know that the strength of the American people will be essential to our success. Simply put, in the hyperspeed of today's economy, being able to manage change is a critical skill. We need to empower our people to develop the technologies that will generate wealth and success. Americans must be consumers who inspire innovation and a steady source of demand. They must be entrepreneurs and productive workers in the industries of the present and the future. In short, to reach our potential we need our economy to be fueled by all of America's 300 million engines of growth.

The policies outlined in this section of the report are designed to strengthen individual Americans by building their human capital and making them better equipped to contribute to economic growth.

Make the United States first in education

Americans are falling behind educationally, a trend that impedes our ability to build good lives and a strong economy. While our best schools compete with the best in the world, our average schools do not, and our worst schools have fallen far behind. This situation threatens economic mobility and America's middle class. Only a third of eighth graders perform at or above grade level, and two-fifths of incoming college students are unprepared for college-level coursework. Our students rank 14th in the world in reading, 17th in science, and 25th in math.[10] The United States ranks 16th in the world in the share of the population ages 25 to 34 that has a college degree, down from third in 1997.[11]

> **"To reach our potential we need our economy to be fueled by *all* of America's 300 million engines of growth.**

In the fractured world of American pre-K-12 education governance, the key to change is enhanced and targeted federal funding to leverage greater access to early childhood education, improved classroom teaching, the discovery and adoption of best education practices, and adequate resources for all schools. At the postsecondary level our plan is to harness the consumer power of better-informed students and their families to demand improved, relevant, more affordable postsecondary education; create more flexible and cost-effective paths to a college degree or credential; and ease the financial burden on students and graduates. These policies would help get American K-12 students back on grade level and the United States back up the list in college and other postsecondary training so that we can produce the skilled


In this Apr. 5, 2012, photo, pre-school teacher Sandra Medina, center, is showered with a confetti egg with students Lyvia Pham, left, 4, Howra Aljumaili, 5, right, and Molly Kiniry, 4, rear right, at the Refugee and Immigrant Family Center in Seattle.
AP PHOTO/TED S. WARREN

and productive workers needed to fuel the growth of an ever-changing economy.

Our education proposals include:

- Creating a federal-state program that will substantially increase enrollment of 3- and 4-year-olds in high-quality pre-K
- Reprogramming and boosting federal funding to states to better target funds to where they will make the biggest difference and to promote new best-practice approaches in improving teaching and encouraging science, technology, engineering, and mathematics, or STEM, education
- Requiring colleges to post public disclosures, similar to nutrition labels, that provide clear and accessible information about costs, quality, and earnings potential of graduates
- Making class credits transferable and allowing credit for learning outside the classroom to save costs and ease the path to degree completion
- Training 1 million students through college/industry partnerships, another million through apprenticeships, and an additional million through career-pathway programs

Raise workplace standards

Weak wage and benefit policies and low workplace safeguards threaten the quality of U.S. jobs. Many employers don't provide paid sick days or family and medical leave to their employees. The value of the minimum wage has declined over the past 40 years.[12] Union membership is down to less than 12 percent of the workforce.[13] And about 60 percent of new middle-class retirees are at risk of outliving the savings they accumulated over their working lives.[14]

To make more jobs good jobs and to strengthen and grow the middle class while substantially reducing poverty, we propose guaranteed paid leave and sick days, better protection in the event of layoffs, a higher minimum wage, better forms of retirement savings, and protection of workers' right to join a union. Such policies improve productivity, reduce turnover, and provide the middle class with the stability needed for risk taking and increased growth.

Our policies to boost workplace standards include:

- Creating and giving workers access to SAFE Retirement Plans, a hybrid between a traditional pension and a 401(k) plan that has many of the virtues of both
- Creating a Social Security Cares program to provide up to 12 weeks of partial wage replacement to support workers who need to take time off to care for a new child or seriously ill family member
- Requiring adequate severance packages for all employees of companies that offer "golden parachutes" to their top executives upon termination
- Raising the minimum wage and indexing it to half the average wage
- Enabling workers to join unions by passing the Employee Free Choice Act and by making the right to join a union a civil right

Realize the potential of immigration

The United States has more than 11 million undocumented immigrants who are living in the economic shadows, unable to contribute their full potential. Legalizing these 11 million people would add a cumulative $832 billion to U.S. gross domestic product over 10 years, as immigrants access better jobs, earn higher wages, and spend those higher earnings, generating increased demand for goods and services throughout the economy.[15]

At the same time, our broken immigration system prevents many aspiring Americans who would greatly benefit the economy from coming to the United States. It's time to resolve the status of aspiring Americans already in the United States and to create a rational path to citizenship for new Americans—one that will level the playing field for all workers, raise wages, and grow and strengthen the American middle class.

Our immigration policies include the following:

- Resolving the status of the 11.1 million aspiring Americans currently in the U.S. by providing a pathway to citizenship

- Improving access to permanent visas for foreign graduates of U.S. universities with STEM degrees

- Creating a discretionary pool of visas that can be allocated with flexibility based on determination of broadly defined national interest

Strengthening the economic environment

Even the best-educated and empowered American people will find it difficult to build a new and prosperous American economy if the economic and business environment is not conducive to success. No matter how strong an engine you put into a car, it still needs good roads to run on; in this case, good roads translate to things such as infrastructure and capital. They need institutions and corporations committed to scientific learning and technological breakthroughs. They need a fair playing field so that the United States isn't disadvantaged in global competitiveness and so that the best ideas and the best investments are the ones that win out. They need to live in a country that has a strategy for ensuring that its businesses lead the world and create jobs here at home.

The policies outlined in this section of the report are designed to create a better American economic environment.

Create the mechanisms for an adaptive national economic strategy

The federal government has a variety of agencies, policies, and programs that engage business and industry. But the ad hoc nature of the relationships, the lack of a governing philosophy, the complexity of the system, and the inadequacy of information on the workings of the U.S. economy lead to inefficiency and missed opportunities. Our plan is to restructure the way government effectuates economic policy so that it can more strategically engage with industries to take advantage of opportunities for advancing U.S. competitiveness.

Our policies to better engage businesses in our national economic strategy include the following:

- Reorganizing the federal trade and business agencies into a single department focused on competitiveness

- Creating a common application for the many federal programs aimed at assisting businesses and entrepreneurs and workers seeking to gain new technical skills

- Engaging directly with businesses in building the economy to promote nascent emerging sectors, respond to international competitiveness challenges, and preserve viable industries facing addressable challenges

Lead in clean and efficient energy

The United States is dependent on imported foreign oil, is subject to volatile energy prices, and is starting to face the high costs of climate change. Each of these pressures creates a drag on economic growth. In 2012 roughly 6 percent of our electricity came from renewables, and the United States imported $313 billion in oil.[16] Our country must capture the multitrillion-dollar opportunity of clean energy by stimulating demand, ensuring effective financing, building efficient transmission infrastructure, and prioritizing efficiency. Our goal is for the United States to have clean, sustainable, and economical energy sources—quadrupling renewable use between 2008 and 2020 and slashing oil imports in half—in order to fuel economic growth.

Our energy policies include the following:

- Instituting a $25/ton carbon tax on all large polluters, starting with power plants

- Launching a comprehensive clean energy investment program

- Launching three programs to eliminate waste: Home Star, Building Star, and Rural Star

Promote science and technology research and development

The United States is losing ground in many of the drivers of innovation that will determine technological leadership in the 21st century. It is time to double down on key investments in science and technology and harness the economic potential of top research facilities to spur innovation and economic growth. The goal is to improve public and private investment in research and development and to ensure those dollars are spent effectively, producing the best possible result for the U.S. economy.

Our science and technology policies include the following:

- Increasing government investment in research by doubling budgets for the Department of Energy's Office of Science, the National Institute of Standards and Technology, and the National Science Foundation, and encouraging increased private investment by improving the research tax credit

- Aligning better federal laboratories and research programs with national economic objectives

- Investing in grand challenges with flexible, ambitious, and accessible Frontier Prizes

Balance trade

The United States imported $5.6 trillion more than it exported over the past 10 years.[17] Although supplying an array of lower-cost consumer goods, this mounting trade deficit resulted in lower growth and fewer jobs in the United States. Some of this trade deficit is a result of other countries not playing by agreed-upon rules and norms. To resolve this, we need to more aggressively enforce trade laws and norms to ensure a fair playing field on which American businesses and American workers can compete. We also need to more actively promote exports and foreign direct investment. Our goal is to bring our trade into balance by 2022 by making the country more competitive overall through policies described throughout this report, by reducing oil imports, and by adopting the policies described in the trade section.

Our trade policies include the following:

- Creating a process of automaticity—a clearly prescribed chain of enforcement actions for clear-cut trade violations as tracked by a National Trade Compliance Database
- Adopting a currency misalignment trigger that will flag countries that have currency misalignments with the United States and enforcing a timeline for countervailing tariffs in the event of failure to address the problem
- Strengthening and clarifying international law around state-owned enterprises to ensure fairer competition with government-backed foreign competitors
- Boosting the capacity of trade enforcement agencies

Rebuild our infrastructure

Roads, bridges, public transit, energy transmission, and communications are at the heart of a well-functioning economy, but American infrastructure recently merited a “D+” grade from the American Society of Civil Engineers.[18] The nation needs a coherent infrastructure strategy, a broadening of private financing for public projects, and a boost in public investments.

Our infrastructure policies include the following:

- Launching a National Infrastructure Council to better align scarce infrastructure resources with the country’s most pressing needs
- Creating a National Infrastructure Bank to encourage private financing of public infrastructure projects that generate revenue through tolls and other user fees
- Ensuring that future infrastructure investments account for the impact of extreme weather, sea-level rise, and other climate-change impacts

In this photo taken on Apr. 15, 2010, new home buyers Fred Archambault and his wife Amy, with their dogs Taz and Fletch, enjoy their new kitchen at their home in Santa Clarita, California.
AP PHOTO/DAMIAN DOVARGANES

Restore the housing cornerstone

Housing represents one-fifth of the U.S. economy,[19] and it critically intersects with many other sectors. The financial industry finances home ownership, the construction industry builds housing, U.S. manufacturers produce much of what goes into the construction and furnishing of homes, and home equity provides a source of financing for small-business creation, as well as postsecondary education. Most importantly, stable, safe, and affordable homes and communities are crucial to all Americans and to strengthening and growing our middle class. We offer a set of policies to build a more responsible and sustainable housing-finance system that serves all communities, supports homeownership, and encourages development of affordable rental housing.

Our housing policies include the following:

- Replacing Fannie Mae and Freddie Mac with private companies that purchase home loans, issue securities, and charge a fee that covers the cost of a private guarantee, as well as a government backstop in case of catastrophic loss
- Promoting safe and sustainable lending by preventing predatory practices and aligning incentives among borrowers, mortgage originators, securitizers, and servicers

- Preventing unnecessary foreclosures through effective loss mitigation, refinancing programs, and reform of mortgage servicing practices

- Expanding the availability of affordable rental housing and developing new approaches to rental housing that stabilize communities and help families build savings

Ensure capital is available for growth

Dynamic capital markets, which fuel business investment and expansion, are critical to growth. The recent financial crisis highlighted weaknesses that needed to be addressed in our regulatory system. The Dodd-Frank Act was designed to address these weaknesses, so the appropriate implementation of this law is a top priority for stable economic growth. We propose additional policies to support vibrant capital markets.

Our capital market policies include the following:

- Curbing destabilizing elements of high-frequency trading via a financial transactions tax

- Supporting small-business lending via targeted government programs such as the Community Development Financial Institutions Fund, the State Small Business Credit Initiative, the Small Business Lending Fund, and the New Markets Tax Credit

Construct a responsible, pro-growth tax and budget policy

The federal budget is currently out of balance. We are not raising sufficient revenue to pay the government's bills, let alone to make the investments we need for long-term economic well-being. The tax code has too many tax breaks that have outlived whatever usefulness they once had and has become, in some ways, ill-suited to a 21st century economy. On the spending side there are programs that are not a good use of taxpayer dollars and savings to be had through improved efficiency.

Our budget and tax policies include the following:

- Enacting comprehensive personal income tax reform

- Reducing federal health care costs by introducing reforms that will enhance competition, increase transparency, improve health care delivery, and cut administrative costs

- Devising a framework for the key components of corporate income tax reform

Conclusion

No one has all the answers or can predict with precision what the best economic policies will be in five years or in ten. Economic realities are constantly evolving, and policymaking needs to keep up. But while the future will

The importance of sustainable, broadly shared growth

The objective of many of the policies described in this report is to generate strong economic growth for the United States. Sometimes growth as a policy objective gets a bad name. Environmentalists rightly point out that without growth, the environment would be less polluted and climate change would not be the threat it is. Others observe that growth at the expense of quality of life is a pyrrhic accomplishment. And growth in which the benefits are concentrated among very few people is hardly a goal most of us would care about.

On the other hand, economic growth creates jobs and improves quality of life. The experience of the past four years is a case in point. The labor market has been weak, with millions of Americans unable to find jobs and millions more underemployed. It is not a coincidence that the weak labor-market recovery has been accompanied by inadequate economic growth.

The ostensible conflict between economic growth and other objectives is also not preordained. Our plan, for example, is designed to produce growth that is environmentally sustainable because aside from other considerations, an environmentally degraded world has enormous costs associated with it that are bad for the economy by any measure.

As a preponderance of economic research shows, the goal of sharing the benefits of growth widely is directly aligned with the goal of maximizing the aggregate level of growth. If the benefits of growth all go to the top, growth will stall—we've seen that story unfold. It is an unsustainable model doomed to fail. So, while we might say that we support policies that ensure that the benefits of growth are broadly shared because we care about widespread well-being, we don't even need to get to that. We support the benefits of growth being broadly shared because if they are not, then there won't be any growth to broadly share.

Customers shop at the Grand Central Market in downtown Los Angeles on Dec. 27,2012.
AP PHOTO/NICK UT

always contain unknowns, the policies we propose are grounded in both economic theory and empirical analysis. They would build a stronger economy and provide the means to adapt to changing times.

The United States is at an important juncture. We can proceed as we have in recent years, with income inequality rising, growth stagnating, middle-class incomes falling, crisis compounding on crisis—all circumstances that have coincided with the growth of a philosophical view that is opposed to any public attempts to address shared economic challenges and a fatalism about America's future. Or we can choose to make investments that need to be made and reform the aspects of our economy that are not performing up to 21st century standards. We just have to agree to do so. ■

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