

BY ROBERT J. BARRO

THE STATE OF THE UNION: BUSH MOSTLY GOT IT RIGHT



VISION:
On the "axis of evil," the return to budget deficits, and accounting reform, the President has good ideas. But about those volunteers....

President Bush's State of the Union address touched on several important issues. Of course, nothing was more memorable than the characterization of Iraq, Iran, and North Korea as an "axis of evil." According to one Internet joke, other countries, such as Libya, China, and Syria, were upset at being snubbed. "They told us it was full," complained Syrian President Bashar al-Assad in the joke.

Humor aside, one way in which Bush's evil trio clearly stands out is in its dismal economic performance. Since Saddam Hussein took power in Iraq in 1979, the per capita gross domestic product has declined by 6% per year, the worst performance over that period for all countries for which data are available. In contrast, from 1955-79, the growth rate was 4% per year. Therefore, Saddam's military adventures have probably cost Iraq's citizens more than anyone else. Somewhat similarly, Iran grew under the Shah, Muhammad Reza Pahlavi (a favorite target of the world's leftists), at 4% per year from 1955 to 1978. Then, the growth rate became negative (minus 1% per year) after the Islamic Revolution. For North Korea, accurate data are unavailable, itself a telling indicator. However, North Korea was about as rich as South Korea after the Korean War, whereas today the South has a per-capita GDP that is more than 10 times as high.

Bush's State of the Union message also focused on the U.S. budget, which has been heavily influenced by the war on terror. The added military and security expenditures are major reasons for the budget deficit, and I agree that this deficit makes sense in an environment of recession and war. This fiscal stimulus also makes it likely that the recession has bottomed out.

Bush's proposed acceleration of tax-rate cuts would raise the odds of resuming economic growth. However, given the small chance of gaining approval for a well-designed tax-cut package, Bush is probably best off settling for no package and then blaming the Democrats. The November campaign slogan is likely to be: "You trust me on the war. Now trust me on the economy by electing Republicans to Congress."

In the State of the Union, Bush referred indirectly to the Enron Corp. scandal by advocating stricter accounting standards and disclosure requirements. Reforms along these lines could be helpful, but proposals from Congress seem to focus instead on limiting the percentage of workers' retirement plans that can be in the employer's stock. Shlomo Benartzi of John E. Anderson School of Management at the University of Cal-

ifornia at Los Angeles notes in the October *Journal of Finance* that many workers hold lots of company stock in their 401(k) plans. Some of these holdings are required by employers, and these constraints may make sense from the standpoint of giving employees incentives to work.

However, workers also place lots of their discretionary funds into company stock. As an extreme example, at Coca-Cola Co., 90% of total pension plan assets and 76% of workers' discretionary contributions are in Coke shares. Economists do not understand this because workers already have a big stake through their jobs in the profitability of their companies. But the ignorance of economists does not mean that workers, such as those at Coca-Cola, would benefit by having Congress restrict the rights to hold pension-fund assets in company stock.

In the Enron case, it is unclear that the workers would have benefited much from the ability to sell company stock. There is no reason to believe that the typical employee would have wanted to sell, given that no one knew that the share price was headed toward zero. Moreover, anyone who had this foresight could have sold the stock short (or purchased puts) even if the direct selling of shares was prohibited.

My main objection to the State of the Union speech involves the part about volunteerism. We live in a country that owes its high standard of living and its thriving social and political institutions to a market economy. Nevertheless, even President Bush apparently subscribes to the romantic notion that volunteering is somehow better for society than working at a market wage. Think, for example, about William H. Gates III. For most of his career, he pursued profits through aggressive production and marketing of computer software. Compare this with Gates's charitable and volunteer activities, which include aid for health care in Africa. Is it conceivable that the average person will benefit more from this volunteerism and charity than from Gates's profit-seeking activities at Microsoft Corp.? Adam Smith answered this question a long time ago—as a general tendency, it is better if people operate from self-interest than from a desire to serve the public good. So volunteer work may be a route to self-fulfillment, but it is not an especially great thing for society.

However, I should not complain too much about the speech. Most of it was good, and Bush never, even once, used the fluffy expression "compassionate conservatism."

Robert J. Barro is a professor of economics at Harvard University and a senior fellow of the Hoover Institution (rjbweek@harvard.edu).