Can ‘Modern Supply-Side Economics’ Build Back Better?

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Traditional supply-side policies stimulated U.S. growth to such an extent that by 1906 U.S. workers became the richest workers in the world, a trend that continues to this day.

Last week, Treasury Secretary Janet Yellen proposed relabeling President Biden’s *Build Back Better* policies as “modern supply-side economics.” Yellen says, “Modern supply side economics seeks to spur economic growth by both boosting labor supply and raising productivity, while reducing inequality and environmental damage.”
Yellen wrongly claims Biden’s modern supply-side strategy is superior to traditional supply-side economics, which stresses limited government spending, cuts in regulatory burdens, and lower tax rates. According to Yellen, traditional supply-side policies have failed to produce their promised benefits.

Let’s examine the history of traditional supply-side economics and consider the extent to which it “failed to produce its promised benefits.” Then, let’s look at the history of the Biden administration’s “progressive” policies, which Yellen has relabeled “modern supply-side policies.”

The Real History

America was founded on traditional supply-side policies designed to provide individuals with maximum freedom over their economic lives. These were the policies promoted by Adam Smith, the 18th-century classical economist and author of “The Wealth of Nations.” Smith said countries would enjoy the greatest prosperity when they adopt low tax rates; when they limit government spending and regulations; allow markets to respond freely to supply and demand; provide a stable monetary policy; and follow the rule of law to protect people and their property from others, including government.

It was these policies that led to U.S. workers surpassing those in the UK in 1906 to become the richest in the world. In the 115 years from 1900 to 2015, average worker real take-home pay increased 211 percent. Today, U.S. workers remain the most prosperous workers of any major country in the world. Countries with less economic freedom than the United States, such as Japan, China, and most of Europe all have living standards well below those of the United States.

Countries with the least economic freedom produce abject poverty. Individuals will risk their lives in an effort to escape to America's freedom and prosperity.

Although the United States has a relatively high level of economic freedom, we have moved far from Adam Smith's ideal of low tax rates and minimum government interference. The move away from free-market classical economic principles was not steady.

My book, "Rich Nation, Poor Nation," presents the history of U.S. economic policies from 1900 to 2015. Since 1900, there were only 50 years when economic policies clearly moved in the direction of traditional supply-side economics. In contrast, there were 52 years when policies were moving away from these free-market classical principles. The remaining years, 1940 to 1953, involve policy moves back and forth in response to wartime conditions. As a result, policies during this time were not consistent with a clear policy alternative.

Yellen claims traditional supply-side policies failed to produce promised benefits. However, during the 50 years when U.S. policies clearly followed free market classical principles, our country enjoyed its greatest progress. Almost all of the 211 percent increase in average worker real take-home pay, 87 percent, occurred during these 50 years. The remainder occurred from 1940 to 1953, when there was no clear move in one policy direction or the other.

I chose to label moves away from traditional supply-side policies “progressive” economic policies. During these “progressive” policy years there were rapid increases in federal spending and regulations, controls over markets, and increases in tax rates.

The first such period came from 1913 to 1920. President Woodrow Wilson, the father of progressive policies, promised to replace free markets with active government action. His intent was to make the economy more productive and prosperous and reduce inequality. Wilson’s policies involved sharp increases in the money supply, rapid increases in government spending and burdensome regulations, wage and price controls, and tax increases intended for businesses and the rich.

Instead of real take-home pay rising at its prior rate of close to 2 percent a year, Wilson’s “progressive” experiment ended with gains of a mere 0.07 percent a year, ½ percent over the seven years. The policies created such havoc, the public responded in 1920 by throwing those responsible out of office.

Newly elected leaders reinstated classical economic principles. From 1920–1929 there were major reductions in tax rates, federal spending, and regulations. Average real take-home pay increased by 1.7 percent a year. The period became known as the “*Roaring Twenties*.”
In what has been a pattern, the next shift to progressive policies began in 1929 under Republican President Herbert Hoover. Hoover was enamored with such “progressive” ideas as increasing government spending and using government intervention to control the economy. His moves to place high tariffs on international trade and increase federal spending and taxes created economic carnage. In 1932, voters responded by putting the original “progressives” back in power. Their policies extended the depression through to the end of the decade. Although real after-tax wages rose by 1.4 percent a year from 1929–1940 there

was a major increase in poverty due to high unemployment during the period now known as the Great Depression.

Remaining periods of "progressive" policies were also very disappointing. These moves in 1965–1981, 1988–1995, and 2004–2015 all failed. The annual change in average workers' real take-home pay was -0.7 percent, -0.5 percent, and 0.06 percent, respectively.

Average yearly change per Period:	Worker Real Wages after Federal Taxes				
Supply-Side years	1900-1913	1920-1929	1953-1965	1981-1988	1995-2004
Changes	1.8%	1.7%	2.4%	1.5%	1.9%
Progressive years	1913-1920	1929-1940	1965-1981	1988-1995	2004-2015
Changes	0.07%	1.4%%	-0.7%	-0.5%	0.06%
Source: ClassicalPrinciples.com					

The first line in the chart shows years when U.S. policies moved clearly in the direction of traditional supply-side policies. The third line shows years when U.S. policies moved clearly in the direction of "progressive" policies. The percentage changes below each period show the change in average take-home pay per year during those periods. (ClassicalPrinciples.com)

'Progressive' Policy Legacy

During the entire 52 years when "progressive" policies were clearly in effect, average worker take-home pay failed to increase. It was the only extended period in U.S. history when the greatest country in the world failed to provide its workers with any increase in living standards. As great as America's economy is, when we adopted policies similar to those found in underdeveloped nations, America's economy behaved as an underdeveloped nation.

Changing the label on failed policies doesn't change those policies any more than putting lipstick on a pig makes it pretty. The historical record is clear. Whatever we choose to call them, whenever America has followed policies to increase federal spending, regulations, and tax rates, the result has been economic failure. So long as U.S. policies move in the direction of those favored by the Biden administration, the recent decline in real wages will continue, followed by economic stagnation and a recession.

In order to reignite America's potential, it will be necessary to return to free-market classical policies. Specifically, we must reduce the growth in government spending and regulatory burdens; eliminate government controls over energy, labor, and health markets; adopt a more stable monetary policy; and lower taxes to prevent built-in automatic increases.

The history of the past hundred years provides encouraging news. Today's destructive economic policies are nothing new. We have endured their ill effects before. Each time we recovered. We can do it again. *Traditional* supply-side policies have stood the test of time. Their proven effectiveness will end the current economic turmoil, raise living standards, and allow America to resume its unprecedented history of prosperity.