

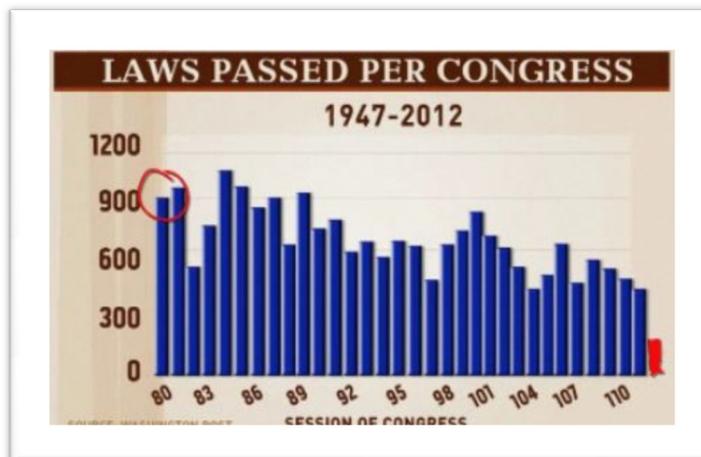
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Politics and Markets

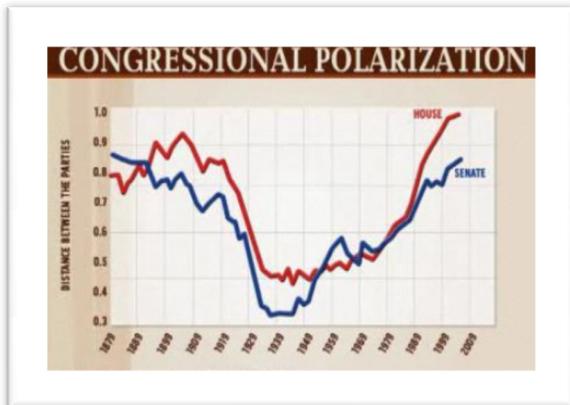
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Capitol Dystopia: Understanding the Polarization

By now we have all heard about the terrible approval rating of Congress. Congress is less popular than porn, although judging from the data about the porn industry's revenues and growth, most things are. But you get the point. Now we have some interesting charts to help us put some more empirical details on the anecdotal bones. These charts were discussed by **Steve Rattner**, on the cable political show, **Morning Joe**, on July 30 (Rattner provides more interesting color on another topic, as we will see shortly).



The little red smudge penciled in by Rattner on the chart (above) represents the laws passed by the current Congress. The data don't lie; the 112th Congress is one of the most "do nothing" Congresses (perhaps *the* most) in the history of the republic. It's true that it is better to pass fewer laws than a lot of bad ones. But Congress's productivity is measure by both the quality and volume of its legislation. That is what legislatures are supposed to do, after all. So on this basic test of productivity, this Congress fails, and fails miserably.

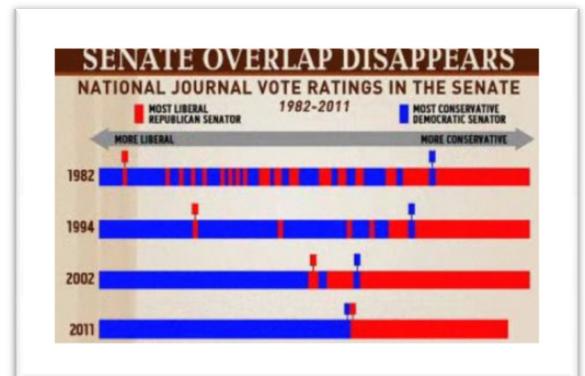


This particular chart (left) tells only part of the story concerning Congressional polarization. But what can be seen here is the widening gap between the House (red line) and the Senate (blue line) when it comes to voting legislation up or down. The gap between the Senate and the House is the widest it has been in decades. What used to be hammered out in Conference Committee, or resolved in the cloak rooms, are now irreconcilable differences that paralyze the legislative

process. The following chart shows the polarization even more starkly. It shows the disappearance of the willingness of members of one party to cross over and vote with the other party in a spirit of compromise. By 2011 it is clear that voting with the other party on legislation is almost nonexistent.

How can we make sense of this? The right wing of the Republican party has decided that several states of affairs are both totally unacceptable and true and, as it sees things, compromise is no longer a virtue but is rather a vice. That is, it has decided that normal politics must be held in abeyance until the remedies to the ailments on this list are properly administered and are taking effect. The right wing thinks that:

- Government is too big, and such is a threat to liberty and personal responsibility
- Government is too intrusive into the private lives of citizens and into the operations of business
- Taxation is out of control



To remedy the problem, it wants to starve government of money, shrink it, and reel in its ability to grow large again, which requires hefty tax cuts and tax reform. And this is precisely what liberals are failing to grasp when they rant and lament that the far right is no longer interested in compromise. They are correct, the far right is in fact no longer interested in compromise, but this is because it believes that compromise is what has led to the “behemoth” federal government (in its view) that exists today. Non-compromise, as the far right sees it, is the only strategy left to bring it under control. Again, they see non-compromise as a virtue, when normally it is a political vice. So appeals to be reasonable or to split the difference on legislation no longer work. **Paul Ryan, Eric Cantor, and Jon Kyl** are on a crusade. Crusaders don’t compromise; they see their mission as holy, morally righteous. The Democrats don’t seem to have gotten the memo about the crusade, and so they think they can reason on such things as Keynesian stimulus efforts and health care reform. But, as far as Ryan, Cantor, Kyl, and their cohorts are concerned, anything that even smells like additional government spending should be shot on sight.



But politics, in fact, never comes to an end, cannot be suspended, and is likely to be the very thing that gets the Tea Party contingent swept out of office. Americans are, for the most part, center-right and pragmatic. They are not about to see the country go over a fiscal cliff, even if the right wing has a grand strategy to bring about such a cataclysm in order to reel in the size and cost of the federal government. **Mitt Romney** is playing a dangerous game by aligning his rhetoric with that of the Tea Party. But, at the moment, it is using him, and he is using it. That moment will soon pass, and if elected, Romney will have to govern, and the true Romney – the pragmatic, results-oriented, moderate, CEO Romney – will soon find himself holding a wolf by the ears.

If elected, Romney will have to govern, and the true Romney – the pragmatic, results-oriented, moderate, CEO Romney – will soon find himself holding a wolf (the Tea Party) by the ears.

The only hope for real compromise will come in one of three ways. One: the Tea Party contingent in Congress will lose their nerve as they see the impending fiscal and economic disaster that will be unleashed on the country if Congressional leaders fail to make concessions on taxes and spending (including stimulus, if more is needed). This could mean that more moderate Republicans will get blamed for going along for the ride, and lose their seats when they are next up for re-election Two: Mitt Romney will win the presidency and the political pressure to allow a new president his honeymoon will not permit the right wing to undermine Romney's first term with demands for measures that are both dangerous and draconian, as the automatic cuts ("sequester") slated for January of 2013 are:

Automatic across-the-board cuts to the budget set for Jan. 2 will cost the United States **1 million jobs**, according to a new study released Thursday by the Bipartisan Policy Center (BPC). The job-loss projection comes from cuts to defense and non-defense spending. The BPC predicts gross domestic product will decline by **0.5 percent** if the full \$109 billion defense and non-defense sequester goes through. (TheHill.com – June 6, 2012)

Three: Obama wins and offers his own and heretofore unannounced proposals to slash federal spending. That is, he will have to lurch to "the right" on fiscal policy, and outflank as many of those in the Tea Party contingent as he can. He will be in a tight spot, however – especially with his base. He cannot be seen as attempting to "reach out" once again to the demands of the far right, as he did in his first year in office when, he too, failed to get the memo about the crusade; but rather he will have to take the lead on budget cuts himself. If he can provide a package of cuts that go deep enough, and



targeted tax increases that seem least intrusive on business and personal pocketbooks, he will be able to elicit the aid of more moderate Republicans to force the Tea Party contingent into a corner – and perhaps, eventually, out of office. Obama is already on the record as saying, categorically, that the extension of the Bush tax cuts for those making over \$250,000 a year is off the table, so he may have to make up their equivalent elsewhere in order to get more moderate Republicans to side with him in order to get a deal done. The voices of such public servants as **David Stockman, Alan Simpson and Jeb Bush** will be needed if we are going to get a long-term recovery plan in place, and avoid another deep recession.

Neither of these scenarios will mean that the Tea Party will have left the game. It just means that the crusade will be on holiday for a while. This may not be a bad thing. On absolute terms, the Tea Party is right about the fiscal mess, and their enthusiasm may be what is needed so that neither Congress nor the President takes their eye off of the ball of long-term deficit and debt reduction.

Sandy Weill's Stumble



In yesterday's *New York Times*, Steve Rattner took **Sandy Weill** (former head of Citigroup) to task for his call to break up the big banks. Weill told the world, on CNBC, that he thinks we should reinstitute Glass-Steagall, which separated commercial banking from investment banking. Rattner was right to point out that the causes of the crisis that hit the financial sector had nothing to do with the role commercial banks played in investment banking, but rather the crisis was caused by the bursting of a large bubble in real estate (and attendant factors) and large bets taken with bank capital.

Weill's remedy sounded more like the sort of comment one might hear from someone whose only knowledge of the banking industry came from the nightly news. Weill's remarks to **Andrew Ross Sorkin** on CNBC started a minor buzz among policymakers and bankers alike. But the effect of that buzz, as Rattner was right to point out, is that attention is being taken off of the more effective reform measures that are now in the pipeline, most notably the Volcker Rule, which does not impose some new version of Glass-Steagall but rather limits the sorts of bets banks can make with their own capital, with taxpayers potentially liable to foot the bill for their blunders.

Bravo to Steve Rattner for setting things straight. It is nice to see that Weill is not a market fundamentalist and can change his perspective regarding the types of banking institution the country now needs, but his voice is late and his suggestions unhelpful and, apparently and amazingly, misinformed.



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