Policy Context for CDAs over the Next 20 Years

Introduction
A discussion of Child Development Accounts (CDAs) would be incomplete without considering the implications of a federal government on the brink of dramatic paradigmatic change. The nation is fast reaching the point where the old ways of doing things obstruct vital government reforms, and new ways—a new paradigm—must be found. This “third fiscal turning,” I believe, is inevitable, as today essentially all future revenues (and then some) are already committed to permanent (sometimes labeled “mandatory”) programs adopted by past and sometimes dead legislators. This largely deters investment in new and innovative approaches to social welfare policy. A critical aspect of the current paradigm, and one arguably responsible for this precommitment of resources, is an underlying political agenda that values (and reinforces) adequacy rather than opportunity.

The third turning
The first fiscal turning occurred after the Revolutionary War, when the fledging nation’s reliance on foreign support left it in considerable debt and without adequate resources to support the requirements of a government for a rapidly growing nation. A new fiscal paradigm for government was forged through the adoption of the Constitution, the enhancement of the powers of the Treasury Department, the federal takeover of state debts from the Revolution, and the enactment of a national tariff. It wasn’t easy: think of the enormity of having to move the nation’s capital to Washington, D.C., to forge compromise. The second fiscal turning happened as the industrial era got into full swing:
the growth of great powers domestically and abroad pushed the government itself to become a counterweight to these powers. Once again, a new fiscal paradigm involved enormous changes in institutions and regulations: the adoption of the income tax, antitrust regulation, and the institution of the modern Federal Reserve. And, again, it wasn’t easy. Think of the split-up of the Republican Party between the Roosevelt progressives and conservatives and the enactment of a constitutional amendment for the income tax. Our nation now faces a third fiscal turning; like the previous turnings at the end of the 18th and 19th centuries, the nation is once again extraordinarily constrained in meeting the new needs and requirements of an ever evolving society.

It would be a mistake to think, as policymakers so often do, that today’s constraints are simply repeats of yesterday’s constraints. The constraints of the industrial era did not replicate those of the Revolutionary era. In contrast to the first and second turnings, the primary source of the nation’s current dilemma is not a lack of institutions, regulations, or resources; instead, it is a problem of how resources are effectively already spoken for in advance. Influenced by broad political pressures, policymakers now spend the future before that future has arrived—and before their opponents can do so. Precommitment of resources to programs like retirement and health, for example, is done in a way that ensures that these programs will grow faster than the economy. As these programs continually expand, becoming a larger and larger percentage of gross domestic product (GDP) regardless of other wants and needs, resources for new programs shrink. Meanwhile, on the other side of the political ledger, tax cuts have eaten into remaining resources.

On our current path, all revenues are precommitted to programs adopted by past and sometimes dead legislators. Mandatory spending (including interest on the debt) soon absorbs more than 100 percent of all revenues, which means that discretionary spending
of any type has to be paid for out of deficits. Our current challenge is that such a budget provides little give or flexibility. As it turns out, this lack of flexibility also results in declining shares of the budget for investments, including investments in human capital and saving, and for an agenda focused more on opportunity.

Now consider how this precommitment of resources is bound up with how we think about social welfare. Our current social welfare system largely pursues an adequacy agenda—that is, essentially, it tries to reduce or eliminate poverty, to provide an adequate amount of food, shelter, and health care. The largest items on the adequacy agenda relate to retirement and health (Social Security, Medicare, Medicaid, and health subsidies), which do not require annual appropriations and, moreover, grow automatically along with the growth in new health goods and services, wage growth (Social Security is indexed to grow with wages), and longer lives (more years of benefits).

An adequacy agenda is a perfectly good agenda—but it is not a growth agenda. An adequacy agenda that continues to absorb ever larger portions of revenues, moreover, seems never to be adequate: it tends to squeeze future spending on other new and sometimes more effective programs. Social Security, Medicare, and Medicaid alone are projected to eat up most of the domestic budget if they continue to grow at their scheduled rate, and they already consume most of the additional revenues devoted to domestic spending. Meanwhile, other programs for working families and children are discretionary and too often treated as a leftover in the annual appropriations process.

In sum, an automatically growing adequacy agenda by its very nature anticipates rather than responds to an unknown future and, at its current level and growth rate, tends to limit spending for other social endeavors. I am not seeking here to overturn the valuable gains of the adequacy agenda, but I am asking how we can respond to new and old problems with new solutions. In this context, the key question for the asset-building
field as we muddle through this third turning is this: How can we sustain worthy gains from the adequacy agenda while shifting new resources more toward an agenda of opportunity?

The social welfare budget

We might look briefly and in more detail at where social welfare resources are going now. For the purposes of this analysis, it may be useful to consider the federal budget through the lenses of what we might call the children’s budget, the investment budget, and the mobility budget. To be sure, these categories of spending are imperfect and overlap to some degree, but they allow us sort out social investment spending and examine its relationship to the larger budget. Each category is closely related to an agenda focused on opportunity.

Children’s budget

We define the children’s budget as the amount families with children receive less the amount, if any, they would receive if they did not have children. A recent report (Carasso, Steuerle, et al. 2008) tracks trends in the children’s budget from 1960 to 2007 and projects future investment in the children’s budget to 2018.

Various measures suggest that the children’s budget has increased between 1960 and 2007, but not at nearly the pace of the rest of the federal budget, especially the three major entitlement programs. In terms of real dollars, for example, total spending on children increased from $55 billion to $354 billion, while total federal spending increased from $525 billion to $2,730 billion, and the nonchild portions of Social Security, Medicare, and Medicaid increased from $60 billion to $1,076 billion, or nearly three times as much as federal spending on children. In terms of share of GDP, the children’s
budget grew by 39 percent, from 1.86 to 2.59 percent of GDP, while domestic spending grew from 7.9 to 15.5 percent, and nonchild portions of Social Security, Medicare, and Medicaid increased from 2.0 to 7.9 percent. The story of the children’s budget as a share of domestic spending is a bit more complicated. Between 1960 and 1985, children’s spending as a percentage of all domestic spending decreased from 20.2 to 10.1 percent, but between 1986 and 2007, it increased to 16.2 percent. In total, children’s spending has decreased as a percentage of domestic spending by a fifth since 1960. During the same period, in contrast, the nonchild portions of Social Security, Medicare, and Medicaid as a percentage of domestic spending doubled from 21.9 to 41.9 percent.

Projections of future spending suggest that the children’s budget will not keep pace with spending on entitlement and other federal spending. Between 2007 and 2018, the children’s budget is projected to increase 15.5 percent from $354 billion to $409 billion, while federal spending is projected to increase 29.9 percent and domestic spending 36.4 percent (most of it in increases in entitlement programs). When measured as a share of GDP, the children’s budget is actually projected to decline by 13.4 percent, from 2.59 to 2.24 percent of GDP, while the nonchild portions of Social Security, Medicare, and Medicaid would increase from 7.87 to 9.62 percent of GDP. Similarly, when measured as a percentage of domestic spending, only 13.8 percent of GDP is projected to be spent on children’s programs in 2018, in contrast to 59.2 percent for nonchild entitlement programs.

A long-range view of children’s spending between 1960 and 2018 suggests that the children’s budget will continue to decline. While 20 percent of domestic spending went to children’s programs in 1960, only 16.2 percent supported these programs in 2007, and the share is expected to fall even further, to 13.8 percent in 2018. Even more
disturbing, as spending on the major entitlement programs continues to increase, the children’s budget may be squeezed out of the federal budget altogether.

**Investment budget**

The investment budget measures the use of resources to increase future production output or income rather than to finance current consumption. A recent report (Steuerle, Reynolds, and Carasso 2007) tracks federal investment from 1965 to present and projects future investment to 2017. The report measures five categories of investment, and estimates the proportion of each of these categories that is allocated toward children.

The proportion of the federal budget for investment is small, at just 5 percent of GDP ($646.1 billion) or 22.6 percent of total domestic investment spending (excluding defense spending) in 2006. Federal investment in children was smaller still, at 1.6 percent of GDP or 9.8 percent of total domestic investment spending. Breaking this down into categories as a percentage of GDP, education and research received 1.3 percent, physical capital received 0.7 percent, defense investment 1.3 percent, work supports 0.3 percent, and social supports 1.3 percent. The percentage of GDP that went only to children was 0.4 percent for education and research, 0.3 percent for work supports, and 0.9 percent for social supports, for a total investment in children of 0.4 to 1.6 percent.

Reviewing the trends in federal spending over time suggests that the investment budget is generally becoming less significant. Between 1965 and 2000, although total domestic federal spending increased from 9.0 to 15.2 percent of GDP, the investment budget generally suffered a steep decline followed by only a modest increase. Investment in education, for example, dropped from 14.1 to 5.7 percent of GDP between 1965 and 2000, and then rose only slightly to 7.9 percent in 2006. The proportion of the investment budget allocated to children followed a similar trend, declining from 3.4 percent of
domestic spending in 1970 to 1.4 percent in 1990, only to increase somewhat to 2.3 percent in 2006.

Future projections that measure education and research, work supports, and social supports are even more sobering. By any definition, total and children’s investments are scheduled to decline from 2006 to 2017 as a share of GDP. Despite a projected increase in domestic spending of $647 billion by 2017, the investment budget will experience little growth overall. Investment in education and research will total only $3 billion (less than one half of 1 percent), and investment in work supports amounts to disinvestment because these will decline in total value. Adding social supports increases the total investment budget to $46 billion, but most of this amount reflects higher health care costs rather than greater investment.

Future projections of investment in children follow a similar pattern. Almost none of the projected $647 billion increase in domestic spending, for example, will go to education and research. Adding in work supports actually decreases the future investment to less than zero, while adding in social supports results in an increase in children’s investments to 4.1 percent of the total increase in domestic spending. Even this increase, however, is somewhat misleading, as almost all of it is due to increases in health benefits, which largely reflect rising health care costs. In effect, the domestic spending pie is getting larger, thanks mainly to economic growth, but children are scheduled not only to get smaller shares, but almost none of the additional filling.

**Mobility budget**

The mobility budget measures spending that tries to enhance people’s earning capability, savings and asset accumulation, or intergenerational welfare. A recent report (Carasso, Reynolds, and Steuerle 2008) tracks the mobility budget from 1980 to 2006, and projects
future investment to 2012. The report divides total domestic spending into the mobility budget, the income maintenance budget, and the public goods budget.

Federal expenditures on mobility totaled $746 billion in 2006, with nearly 80 percent of this funding used to support programs in four categories: employer-related work subsidies, homeownership, savings and investment incentives, and education and training categories. However, most of this money does not benefit low- or moderate-income households because it is delivered in the form of tax exclusions. Of the $746 billion mobility budget, more than $500 billion benefit people in the top two quintiles of income, and only approximately $205 billion (28 percent) go to programs that provide significant benefits to low-income individuals. This is significant, because other federal spending that benefits low-income individuals is unlikely to enhance mobility.

In general, programs that address an adequacy agenda, those “aimed at achieving minimum consumption levels,” received a larger chunk of the domestic pie in 2006. The mobility budget in 2006, for example, was 5.7 percent of GDP, while the income maintenance and public goods budgets accounted for approximately 10 and 11 percent of GDP, respectively. Entitlement programs play a significant role in the size of the income maintenance budget, with spending on the retirement and pension category and on the retiree health category accounting for 83 percent of total spending. Entitlement programs also played a large role in increasing the income maintenance budget from 9.3 percent of GDP in 1980 to 9.9 percent of GDP in 2006. Between 1980 and 2006, the nonchild portions of Social Security, Medicare, and Medicaid increased from 5.6 to 7.6 percent of GDP, while the rest of the income maintenance budget actually decreased from 3.7 to 2.3 percent of GDP. Over this same time, the mobility budget increased only slightly, from 5.2 to 5.7 percent of GDP.
Future projections suggest that the gap between the income maintenance budget and the mobility budget will only widen with time. The mobility budget is projected to grow to 5.9 percent of GDP in 2012. In contrast, the income maintenance budget is projected to grow to 10.3 percent of GDP, with most of this growth accounted for by increases in Social Security, Medicare, and Medicaid spending.

Implications for asset-building field and CDAs

Our analysis of social investment spending uses three lenses—spending on children, spending on investment, and spending on mobility—but, for the most part, the view through each lens is the same. No matter how we break it down, entitlement programs are steadily increasing as a share of the federal budget, while programs that focus on children, investment, and mobility are either shrinking or growing at a snail-like pace. This is clearly not a sustainable paradigm, with especially unfortunate implications for the future of social investment. In this climate, the outlook for the asset-building field in general, and CDAs in particular, appears sober. A closer look at how this federal paradigm could shift during this third turning, however, might offer a more hopeful perspective.

Although this paper’s analysis to this point has been primarily economic—demonstrating how resources are overcommitted in some areas and undercommitted in others—the root cause of this imbalanced use of resources is political and historical. There is, first of all, strong political support for the adequacy agenda without much attention, I think, to whether it needs to remain path-dependent upon growth rates that it had in the past. A second and more complicated cause is political support for what we might call a “comfort agenda” throughout the income scale that includes such items as retirement at middle rather than old age and elimination of the estate tax even though
much of that wealth has been in the form of accrued gains never subjected to income tax. From any realistic cost–benefit calculus, the comfort agenda could certainly be pared and some parts could be abandoned. No natural law requires us to retire for nearly a third of our adult lives or to receive close to $1 million in aging benefits per couple, or to maintain federal tax receipts at 17 percent of GDP. Natural law or not, however, it may be politically difficult simply to leave the comfort agenda behind.

Assuming that political support for the adequacy and comfort agendas must be addressed, we might consider more innovative ways of fulfilling—or at least, partially fulfilling—these agendas while integrating them with an opportunity agenda. One way made clear in the study on mobility would be to expand subsidies, such as those for retirement saving, to be more inclusive of all income levels. Another would be to make clearer how an opportunity agenda at the end of the day does promote adequacy—the main difference being that it requires some sacrifice, such as deferred consumption, hard work, or educational effort, along the way. In that context, CDAs and other asset-building policies serve as opportunity-based and inclusive pathways not only to increased aspirations, achievement, and financial security, but to adequacy and comfort.

But we must be honest. One thing that the opportunity agenda—as opposed to the adequacy agenda—cannot do is to guarantee levels of adequacy and consumption. The simplest way to see this is to compare education with retirement income. The latter gives everyone money with which to consume; the former may be offered to everyone, but it will be successful only for those participants who actively take advantage of it. Thus, while the opportunity agenda helps address the highest aspirations of society, at least in theory, it sometimes meets the opposition of some liberals who want to maximize consumption of the poor, conservatives who want to limit the expense of programs that extend to the middle classes, and people of every persuasion who are uncomfortable with
the simple fact that some failures will accompany the risk that accompanies pursuing opportunity.

In developing CDAs, the key challenge for the asset-building field will be designing a policy that buys the most opportunities for the future. In budget language, I am referring to maximizing benefits relative to costs.

What CDAs clearly have to their advantage, in my view, is the opportunity they provide for financial education. Children with CDAs get early hands-on experience interacting with the banking system and making financial decisions. For many, the process of saving and watching savings grow teaches about the power of compound interest, an important concept that can inform a life-long savings habit. Along the way, what I have also discovered from the experience in Great Britain on setting up universal child accounts is that a more universal program of CDAs helps co-opt banks, essentially, into helping get everyone “banked.”

Postscript
Since this speech, the nation has gone through dramatic transformations due to a large recession, large temporary programs created in response to that recession, and the passage of a health reform bill. Some of those programs did increase spending on children and investment, and health reform attempted to expand benefits to an excluded class of non-poor and nonelderly households. Still, huge deficits now put even more pressure on the opportunity agenda, which, outside of large tax subsidies for housing and retirement to the middle- and upper-classes, still falls into the residual or leftover part of the budget. My own view is that recent events have only accelerated the requirements on the nation to address what it means to live in the midst of this third fiscal turning.
References


Notes

1. This section draws on Carasso, Reynolds, and Steuerle (2008); Carasso, Steuerle, et al. (2008); Steuerle, Reynolds, and Carasso (2007).
2. See Steuerle et al. (2007) for definitions of these categories.