Reaganomics: What Worked? What Didn't?

Lawrence Kudlow

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In terms of defending President Ronald Reagan and the economic policies he started fifteen years ago, and to which I contributed, I knew I was onto something during the presidential campaign of 1996. A lot of people felt that it was a fairly lackluster campaign, and I suspect from the Republican perspective it was. For me, probably the most interesting aspect of it was that candidate Bill Clinton essentially ran on a platform that emphasized smaller government, lower taxes, and traditional family values. And just like the politician who made these winning issues—namely, Ronald Reagan—Clinton won easily.

A lot of conservatives in Washington and other places are resentful and angry and cranky and even pessimistic over the current state of affairs. I am not, and I am glad that Mr. Clinton continues to run and govern on what are essentially Reagan principles—admittedly Clinton's own interpretation of those principles, but imitation is the sincerest form of flattery. It shows the power and force of Reagan's ideas and vision.

Furthermore, the fact that Reagan's ideas, and the U.S. economy, can survive the Clinton presidency is one hell of an achievement. In fact, it may be spawning new Clintons. There's one in Great Britain today, Prime Minister Tony Blair, who sounds a lot like Margaret Thatcher. In some ways he sounds more like Thatcher than John Major did, which reminds me of the fact that Bill Clinton often sounds more like Reagan than George Bush did. Regrettable, but true. A week or two after Blair was elected, he gave a speech to a socialist enclave in Northern Europe. At the conclusion of the speech he was roundly booed, which I regard as tremendous progress. If I gave a speech before a bunch of socialists and was booed it would be one thing, but for that to happen to Tony Blair, the Labour Party prime minister, is quite a different matter. In that respect, we have come a long way, and it makes it all the easier to defend the Reagan legacy because it is a living legacy. Its spirit, principles, and ideas are the dominant influence on both political parties today.

We've come a long way in economic terms since the late 1970s and early 1980s. When I went to Washington to work on the Reagan transition—the Office of Management and Budget and Treasury transition, to be precise—in late November 1980, I was a young man in my early thirties. The economy and the world situation then were a lot different from what they are today. It is almost hard to imagine what it was like. I say this not for any dramatic effect; it is just a matter of fact. The United States had lost its place in the world. The Soviet Union was gaining not only in the territorial battleground, but also in the ideological battleground and certainly in the media battleground. We were in a very precarious international place. In economic terms, we had just weathered our second oil shock and our inflation was running upwards of 12 to 15 percent. Distinguished Wall Street economists like Henry Kaufman were talking about the end of our financial markets as we knew them, with long-term federal bonds at double-digit yield levels. The economy basically stopped growing in 1978 and didn't begin to grow again until 1983. It was one of the longest business downturns in history.

Today it is a different ball game. The cold war is over; the United States is supreme. American ideas, values, and economics dominate the world scene. I believe firmly, with respect to the great success President Clinton has had in this economy, that it was President Reagan who gave him the ground he is standing on.

From Stagnation to Innovation

First and foremost, I credit Reagan's policies with vanquishing inflation, which is the most pervasive influence, good or bad, on any economy. Reagan reappointed Paul Volcker chairman of the Federal Reserve Board. Reagan appointed Alan Greenspan. He gave both of them the authority to do what it took and, of course, aided them with his own efforts to deregulate the economy. We forget that it was Reagan who turned around the labor situation by standing up to the air traffic controllers in the PATCO dispute, settling it firmly in favor of the American people and against a materialistic union movement, which, to the detriment of the economy, had gotten far too big for its britches.

It was Reagan who gave the primary thrust to deregulating energy. He argued with Department of Energy economists in 1981 that the price of oil would not go to $80 or $100 a barrel, and that if our policies of disinflation and currency stability, along with the tax and deregulatory efforts, were successful, oil would go to $20 or $25 a barrel. I remember betting Jim Schlesinger, our distinguished energy secretary, a fancy French meal on this subject. Jim lost.

The president was instrumental in deregulating the transportation industry and the banking and financial services industry. He was instrumental in setting loose the forces that led to the deregulation of telecommunications and, more recently, utilities. All of these policies are still playing out, even through one or two generations of policy people in the federal departments and agencies.

It was Reagan who was foursquare behind the notion of free trade. We had a hell of a time getting Canadian free trade, but we did. Reagan really did that with the force of his personality. That was expanded later to Mexican free trade and what we now call NAFTA. It was Reagan who floated the notion of hemispheric free trade, the notion that at some point in the future, Canada, the United States, Mexico, and all of Latin America would be linked into a free trading zone.

Of course, in an area that goes beyond my expertise, it was Reagan who stood up to the Soviet Union time and time again. But it wasn't possible to just stand up to them. We had to have behind our moral force and our military and diplomatic initiatives an economy that would show the Soviet Union we meant business when we said we would outspend and outarm them if we had to.

This is where the controversial supply-side tax cuts came into play, along with the other economic innovations I referred to. Income tax rates were up 70 percent. They had been raised by Republicans and Democrats from the late 1960s through the late 1970s, and the combination of double-digit inflation and unindexed, highly progressive marginal income tax rates created what we used to call tax bracket creep. That is to say, as you earned more, if you were able to, you were pushed into the higher tax brackets, and inflation pushed you into still higher tax brackets. Families earning real incomes of $30,000 to $35,000 a year were paying at the top end of the tax rate system, and that was one of the reasons the economy had stagnated. We had the worst of all worlds. We had high inflation and high unemployment at the same time.

So a band of supply-siders, of which I was a part, helped President Reagan enact the Kemp-Roth tax cut bill in 1981, which later evolved down to the flat-tax reform of 1986. The top rate was reduced, in steps, from 70 percent to 28 percent, which spurred economic growth. There was a lot of doom and gloom in the 1980s while economic growth was recovering. This is a part of the story that interested me a lot. People focused on budget deficits and trade deficits and the early stages of transforming our industrial economy into an information-age economy. They said the dollar was too high, or the dollar was too low. Hardly anybody in those days (hardly anybody, that is to say, in certain media circles and some left-of-center intellectual circles) would focus on the main change—that the economy was recovering and jobs were growing. The expansion of the 1980s lasted over seven years and created roughly 20 million new jobs. The economy grew at a 4 percent annual rate and the inflation rate was just over 3 percent. The unemployment rate was taken down from a peak of 11 percent to about 5 1/2 or 5 1/4 percent at its lowest point. Pretty impressive. It was the longest peacetime expansion in history. My friend Robert Bartley, editor of the Wall Street Journal, referred to it in his book The Seven Fat Years—a biblical reference, and a very appropriate one.

Strategic Use of Debt

People will continue to criticize President Reagan and the rest of us for the deficit problem, so I want to comment on it briefly before moving on to more interesting topics. Deficits are a fiscal policy tool. By themselves, they have no moral content. Nations that run recurring deficits over decades and decades are probably going to have trouble. But as historian John Steele Gordon has written in his recent book Hamilton's Blessing, there are times throughout American history when deficit finance and the accumulation of debt have served important national purposes. Certainly Alexander Hamilton's consolidation and selling of debt was one of the cornerstones to setting our fragile new republic on solid ground in the 1790s, and it led to forty years of prosperity. Certainly debt was floated in the Civil War and in World War I and World War II. Indeed, the highest debt to gross domestic product ratio occurred during and after World War II, when debt ran upwards of 115 or 120 percent of our gross domestic product. We needed that to win the war and maintain our freedom. Likewise, I believe we needed to employ deficit financing in the 1980s to win the cold war and bolster our economic freedom.

Moreover, I believe the single largest cause of the deficit was the sharp reduction of inflation, from a zone of 12 to 15 percent in 1980 and 1981 to a zone of 2 to 3 percent in 1986. The government had been living on inflated revenues and inflated personal income revenues for over a decade, from LBJ through Nixon and Ford to Jimmy Carter. The government's appetite for inflated revenues was virtually insatiable, and it supported, nourished, and ultimately overfed the rise of the entitlement state. Reagan inherited that.

Rising inflation was a huge effective tax increase on the economy on top of the already high actual tax rates. So getting inflation down was a huge tax cut, though it probably resulted in a loss of nominal GDP income of, I would say, by 1986 close to a trillion dollars from what might have been the case if inflation had continued at a 10 to 12 percent annual rate. If the choice is to finance a deficit in order to lower inflation and improve the economy or to oppose a deficit and maintain the inflation that was destroying our economy, I would take the former anytime. I believe Reagan made a brilliant economic and political decision to give Paul Volcker the green light to do what he had to do.

The supply-side tax cuts are usually blamed for the deficit, but the facts really don't support that position. That's the interesting part. We've learned now that even in the first couple of years of the tax rate cuts, we only lost about $30 billion or $40 billion in personal income taxes. A lot of studies have been done on this, and over the course of the expansion from 1982 to 1989, it turns out that revenues nearly doubled in nominal terms, and in real terms went up by 35 percent! If it were true that tax cuts caused lost revenues and deficits, then why did the level of revenues go up so much during that period?

My answer is that the Laffer curve worked. Economist Arthur Laffer argued that reducing tax rates from a punitively high range will not only encourage more entrepreneurship, more work effort, more risk taking, and more capital formation, but will also pay off in a relatively short period of time with better economic growth and a higher revenue volume. That is exactly what happened in the 1980s, so I really don't accept the criticism that the tax cuts caused the deficit expansion—although I recognize that mine is a controversial view. I believe it was the sharp inflation drop that was truly responsible. However, both were necessary for our economic security, and the reinvigoration of our economic security was a crucial tactic in the effort to reclaim our national and international physical security. When President Reagan went to Reykjavik in 1986, he was able to stand tall with an economy that was in its third solid year of growth at a time when Europe, for example, was still in a recession. Mikhail Gorbachev knew, in that negotiation and subsequent ones, that Reagan had his economy behind him. It was clear we could afford to do and spend whatever it took if that's the game the Soviets wanted to play. They folded their hand, and part of the reason was the recovery of our domestic economy.

The last issue on the deficit, of course, is the buildup of military spending. The Defense Department under Caspar Weinberger spent about 1.6 trillion real dollars. This was part of the game plan actually begun under President Carter, who in the last year of his administration finally understood that the Soviets were not our friends. Better late than never. But it was left to President Reagan to really boost defense spending, and that boost was not only a crucial factor in the end of the cold war, but also the fundamental reason why we never had a hot war. Instead, we got just a glimpse—a snapshot—of the awesome military power we had created in the 1980s when we triumphed so quickly and decisively in the Persian Gulf War in early 1991.

People say this is the inheritance we're handing to our children and our grandchildren—this debt that is really about 50 percent of our gross domestic product, very much at the low end of our historical range. I say that what we are really leaving to the next generation is a strong economy with maximum opportunity: we're the leaders of the global, information-age, high-technology transformation that will be the economic story of the twenty-first century. We have bequeathed to future generations a world that is not only prosperous, but also peaceful. And I wouldn't underestimate the peaceful part as something that will contribute in a feedback, flow-back effect to the prosperous part.

These are Reagan's legacies.

We will pay the debt down in the next twenty or thirty years. Slowly but surely, any clever Treasury secretary with good debt management policy advisers can begin to redeem the debt by slowing down its issuance, as Robert Rubin has been doing. He's paid down about $65 billion worth of debt so far in fiscal year 1997 by simply not reopening a number of Treasury note and bond issues. This is the right way to do it. There is no obsession here. It doesn't interfere with any market forces. It's just done as a matter of course.

An Unprecedented Boom

What interests me most is the long-continuum, big-picture story. Except for about eight months (late 1990 and early 1991) during a Bush administration that neglected Reagan's economic principles, the U.S. economy has been in continuous growth and prosperity for nearly fifteen years. That is an awesome achievement. We have created more than 36 million new jobs. As I said earlier, 20 million came in the 1980s alone. We are experiencing the greatest bull market in stocks in our nation's history. It shows no signs of fatigue or end and it has, so far, according to Federal Reserve statistics, created $17 trillion—about two and a half times the entire European gross domestic product—in new household worth, and we did that in just the past fifteen years! According to the published data, real gross domestic product since 1982 has grown at a 3 percent annual rate, and the annual inflation rate has been slightly above 3 percent, but I believe all of these will be remeasured to better encapsulate the high-technology investment, production, services, and spillovers of the information age.

Some economists like Leonard Nakamura of the Philadelphia Federal Reserve and Michael Cox of the Dallas Federal Reserve argue that over this period we have underestimated productivity by at least 1 percent and maybe 2 percent. Therefore, we have underestimated real GDP by at least one percentage point, maybe two, and we have overestimated the inflation rate by at least one percentage point and maybe two. When historians, let's say in the year 2050, look back on this period using a refined measurement process that captures all the contributions to the economy of high-technology advances, it may turn out that the 1980s and 1990s were a period when the American economy grew at close to 5 percent a year with about 1 percent inflation and 3 percent productivity growth. For years I resisted this, but I have now come to believe that Jack Kemp was right. We can grow at 5 percent per year, and it is just a matter of time before some national politician runs for high office on that very plank.

Along the way, we have so democratized and deregulated financial markets, as well as other sectors, that today, according to surveys, there are roughly 125 million people invested in the stock market! That number is almost identical to the entire workforce of this country. Virtually all working Americans—and, by implication, their children—are invested in the stock market. They've got a piece of the rock. This is the greatest advance of democratic capitalism in world history. This is not a market of rich people. This is not a market of elites. This is a market of ordinary people saving through stockbrokers and mutual funds and IRAs and 401(k)s and you name it. That $17 trillion increase in net worth, a function of the stock market's wealth-creating processes, is real money.

This is one reason why Americans are at their highest level of confidence in years. Roughly speaking, we are as confident today as we were about ten years ago, at the height of the Reagan boom, and as we were in the early and mid-1960s at the height of the Kennedy/Johnson era.

Let me make a couple of forecasts. By the end of President Clinton's term of office in January 2001, I believe we will have had three more years of uninterrupted economic growth. There will have been no recession. This will have given us roughly eighteen years of prosperity. I believe at the end of his term we will have a zero inflation rate. I believe at the end of his term we will have a 4 percent unemployment rate, and if I'm wrong it will be because it's lower than that. I believe at the end of his term we will have a 5 percent Treasury bond rate, a 4 percent mortgage rate, and a Dow Jones average somewhere near 12,000. That will merely be a step on the way to the 40,000 Dow I think likely by the year 2020 when I retire at age seventy-three, God willing.

What's more, in furtherance of Reagan's spirit and legacy, I believe we will be running budget surpluses of $100 to $150 billion a year, the first of which will appear in fiscal year 1998. I'm not even convinced that fiscal year 1997 won't be a balanced-budget year. The economy is really throwing off revenues. We have solved the problem. Supply-siders argued that by some manner of flexibly freezing federal spending and by maintaining incentives to grow the economy, we would solve the problem. We are solving the problem. We have the lowest deficit in the industrial world. In fact, only the United States meets the G7 Eurodollar deficit requirements.

There is a fad in Washington right now that says if there are surpluses we must spend them immediately. Others think we should use the surpluses to retire the debt. I don't agree with either position. I think we should turn the money back to the taxpayers. I think we have a lot of unfinished business to take care of in that respect.

I am reminded of two of my favorite heads of state who inherited large deficits and debt and were able to retire them through supply-side means. One was the famous Victorian British prime minister William Ewart Gladstone. Gladstone was chancellor of the exchequer when Sir Robert Peel repealed the Corn Laws. Those were steep tariffs, as were the tax rates of the day. Gladstone also eliminated most taxes throughout the United

Kingdom when he was prime minister, and in so doing grew the British economy to a point that virtually all of England's Napoleonic War–related debt could be retired.

In this country in the 1920s, Calvin Coolidge lowered the Coolidge-Mellon income tax rates and, at the same time, extinguished post–World War I debt and put the budget in a surplus. First he cut taxes, then he waited for economic growth, then he retired the debt. First Gladstone cut tariffs, then he waited for economic growth, then he paid down the debt.

The Unfinished Reagan Agenda

The Reagan agenda has a number of unfinished aspects. I regard myself as a conservative, free-market reformer, and I think there is no better time to reform than during periods of prosperity. It is very difficult to make large-scale reforms when economies are turning down and people are unhappy and social conditions are contentious. But when people have more confidence, when jobs are plentiful, when prosperity exists, it's a great time to make the reforms that need to be made.

My laundry list of reforms, which I believe follows directly from Reagan's agenda (and which, incidentally, I think Clinton may have some sympathy with), includes, first and foremost, tax streamlining. The Reagan 1986 Tax Reform Bill was a great step in this direction. A lot of loopholes were closed. A multitude of tax brackets were collapsed into two—the good old 28 and 15 percent brackets—and the spirit of tax reform was sufficiently and surprisingly bipartisan. I don't remember the final votes on the bill, but people like Senator Bill Bradley and Congressman Richard Gephardt were tax reform Democrats in those days, and it isn't at all clear to me that President Clinton couldn't become one now. Jack Kemp is actually meeting with Clinton to discuss tax reform; that is an interesting odd couple meeting, and some good might conceivably come out of it.

I will say editorially that the biggest impediment to an administration plan to streamline the tax code and lower tax rates is Clinton's own Treasury Department. It is an odd story. As much as I admire Clinton and Robert Rubin—who has done a wonderful job of working with Clinton and with Alan Greenspan to keep the inflation rate down—for their spectacular free trade policies (they have done a terrific job of following in Reagan's footsteps), Rubin is a class warrior and a revenue redistributor when it comes to tax policy. He is not a capital formation, progrowth reformer. It's very odd, and I don't know why this is.

I think we should create a tax system—and I believe Reagan strongly advocated this—in which entrepreneurs and ordinary men and women will be permitted to spend their own money. They will spend it more wisely than the government will. The root of this is not only an economic vision of incentives, but also a vision of personal responsibility and accountability—a spiritual vision in addition to an economic incentive vision.

What is more, I heard President Reagan say repeatedly that the ideal tax code is one in which all income is taxed only once. Such a system would stop taxing saving and investment three and four times as wages, as salaries, as dividends, as interest, as capital gains, as inheritance taxes. These are reforms that are currently out there, and all fall very much under the Reagan rubric.

President Reagan's Achilles' heel was Social Security. I believe the biggest mistake he made was signing the 1983 Social Security Reform Bill, and I believe that because, number one, it triggered a series of payroll tax increases, thereby burdening even more the already burdened middle class. Number two, it offset and diluted his own income tax reform plan. And number three, it didn't take any small steps in the direction of a privatized Social Security system that would link our contributions to the investment markets. The rate of return offered by these markets, of course, is superior to that of the Treasury bill market (which has itself diminished). One of the great tragedies of the past fifteen years is that we have been denied by the federal Social Security system the opportunity to invest our Social Security contributions in this phenomenal bull market. States and localities have for years invested retirement money in the stock market and have seen terrific performance as a result. It is a pity that the general citizenry is not allowed to do the same. I wish Reagan had moved toward privatization. I and others recommended it at the time, but it remains an unfinished agenda item along with tax streamlining.

Additionally, I think we can still make quite a few reductions in the level of federal spending. A lot of unnecessary departments and agencies could be cut out entirely. Regrettably, not much of this is in the current budget bill. Reagan would have preferred a significantly smaller government, meaning not only fewer dollars spent every year, but also fewer federal departments and agencies. Unfortunately, there were only two terms, and only so much time in the day, within which to achieve these goals.

Finally, I think an unintended aspect of Reagan's policies was the extraordinary explosion of this information-age high technology that has become the backbone of the economy in the 1990s. It started really in the mid- to late 1970s, but so many of the new computing devices, both hardware and software, that were developed in the 1970s were not sufficiently commercialized, brought to market, and distributed until the 1980s. I have to believe it was no coincidence that lower inflation, lower taxation, less onerous interest rates, and so forth combined to bring these things to commercial success. It's as if Joseph Schumpeter became an adviser to Reagan, though he never had a formal place at the table.

Schumpeter is my favorite dead economist. He was the foremost proponent of the entrepreneurial theory of growth and, particularly, of the technological innovation theory of growth that plays such a huge role in our present economy. At hand is the greatest burst of high-tech innovation and risk taking and commercialization in our nation's history, certainly in the past hundred years. A lot of experts who know more about this than I do have argued that the information-age technological innovations are more powerful than the steam engines, railroads, automobiles, and other industrial breakthroughs of the nineteenth century because the information-age breakthroughs have more spillovers and more applications for more people and more businesses. I think that's true. We know they have raised productivity and our economy's potential to grow. So, in a sense, I believe Schumpeter met with Reagan.

Schumpeter recently had lunch with Alan Greenspan, too, which is a very important point. We are headed toward literally zero inflation. Price indexes are now registering zero inflation. The producer price index has not grown in twelve months. That is a phenomenal achievement. Schumpeter always believed that an entrepreneurial economy would create innovations. Those innovations, put into business, would do two things: they would raise output and lower prices. So another spillover from the Reagan revolution may be the end of the Phillips curve. Unlike many Wall Street bond traders and many economists at the Federal Reserve, Reagan believed you could have good economic growth, low unemployment, and price stability all at the same time. He believed that, and he encouraged Volcker and Greenspan to keep their eye on gold as a reference point for the value of money. We are as close to a Bretton Woods gold system as we've ever been, and it has helped entrepreneurs. Schumpeter, in at least some imaginary sense, is telling Greenspan, "Don't worry about economic growth. It's all coming from the investment side, from the technological side, from the innovation side. It won't cause inflation, it will actually lower it." Compaq just announced strong earnings, a tougher marketing process, and lower prices. It is just what Intel said two or three months ago. That is Schumpeter's influence. And with Greenspan having gone back to the hard-money philosophy of Reagan, I think short-term interest rates are likely to go down, not up. This is another spillover from the Reagan years.

Prosperity: A Breeding Ground for Principles

Finally, we have the notion that prosperity and price stability improve the national soul—one of my favorite topics. The data actually show that malignant social trends have reversed of late, at least a bit. Crime rates are down. Property crime rates are way down, but violent crime rates are down as well. Teenage pregnancy is starting to turn down. Family breakup is starting to turn down, as is divorce. Much drug use is also waning.

I am indebted on this point to historian David Hackett Fischer's new book, The Great Wave, in which he talks about how rising inflation causes social deterioration and how falling inflation or stable inflation (what he calls price equilibrium) causes an improvement in the moral fiber and the moral character of nations. In particular, Fischer discusses the Victorian age. For seventy-six years, from 1820 to 1896, prices were stable and inflation was nonexistent. I mentioned Mr. Gladstone, my favorite prime minister from that period, who contributed to that situation in England. In the United States, except during the Civil War, the case was the same. Our inflation rate was zero during that period. Fischer points out that during the Victorian equilibrium we saw a decline of crime, a decline of murders, alcohol consumption, and illegitimacy. We also, during that period, had an increase in real wages. We also had a decline of income inequality, and Fischer concludes—and I wish to agree strongly—that we had a decline of social despair and a rise of moral value during the Victorian equilibrium.

I believe, along with Nobel Prize–winning Chicago historian Robert Fogel, that we are in the midst of another such great awakening, a great spiritual awakening, in this country. Much of this has nothing to do with economics, but much of it does, because it sure is easier to attend to our spiritual flaws and defects if we have a job and a more secure financial future and some money in the bank and some retirement investments that are rising in a bull market.

What I wish to do here is connect some dots from Reagan to Clinton. These are really primarily the American people's dots. We are in a period of great change and transformation. Our evaporating inflation rate and our rising economic growth rate are mirrored in the phenomenal increase in the stock market, which is a metaphor for our times. We can look forward to improving social, family, and spiritual conditions. We have a marvelous confluence of events: stable prices and free trade, information-age entrepreneurship, the promise of new tax reform and Social Security privatization, and the end of the false paradigm of the trade-off between growth and inflation. We now know we can have low unemployment and zero inflation at the same time. An era of renewed moral and spiritual values, an era of global peace and prosperity, is upon us. I think we are about a third of the way into this long cycle, and I believe strongly that it was Ronald Reagan who began it.

We are changing. We are reforming. We are transforming. It is all of a piece. This is a story about the economy, but it is a story that is much bigger than the economy. This is a story, really, about our unlimited potential to use our God-given talent and creativity. I can't predict how long this will go on. There is no end in sight in terms of the stock market and the economy. But I will argue that, with the help of millions of people around this country and billions of people around the world, it was Ronald Reagan who led this revolution, who established this new higher ground, who provided us with the spirit, the vision, and the road map that the most successful politicians on the world scene are still following today. So keep the faith. And in the words of my favorite president from California, the best is yet to come.

Following his talk, Lawrence Kudlow took questions from members of the American Experiment audience.

Dan Holy: That was a very bullish and very positive forecast to the year 2000. What do you think are the biggest threats to its coming true?

Lawrence Kudlow: The biggest single threat I can think of just off the top of my head is the physical condition of Alan Greenspan. He is a very healthy seventy-one-year-old, recently remarried, and he is active on the tennis court. He is, in my opinion, the best Fed chairman of my professional lifetime, and probably in the whole history of the institution. We want to keep him healthy. President Clinton just indicated in a Business Week article that he would reappoint Greenspan in June of 2000, and that is very reassuring. We always look at various indicators of the economy's health and the money supply and gold and commodities, but somewhat glibly, yet somewhat seriously, I would suggest watching Alan Greenspan's EKG. It's a very important factor in the outlook.

Clarkson Lindley: You threw out a lot of statistics, but the one I was stunned by—I wondered why lightning didn't come down and strike—was your assertion that Secretary of the Treasury Robert Rubin has paid off $65 billion of debt this year. Why wasn't there one of those ceremonies with Clinton walking across the White House lawn in front of the troops, or a mortgage-burning ceremony on the steps of the White House?

Lawrence Kudlow: I think the reason is that Clinton is a very successful politician. It is not that big a deal, and the president knows full well that his political bread is buttered by prosperity. I think Clinton, more than most Republican politicians, understands the force of Reagan's growth message and his politics of optimism. I neglected to focus on that. It was Reagan who taught us about the politics of optimism as well as the politics of growth. Regrettably, neither George Bush nor Robert Dole was able to digest the politics of optimism. Mr. Clinton was. Regrettably, many of my conservative intellectual friends today have themselves forgotten. Fortunately, there are still a few of us left to spread that word.

I wrote a couple of long editorial columns on the politics of optimism this year, and I'll probably revisit it again. I believe that in free democracies, optimists win and pessimists lose. I learned that from Reagan, but I have seen enough of it in my own political meanderings to be convinced. Democracies are about optimism and progress. Second, I believe that optimists are profoundly democratic with a small d, profoundly populist. They believe in ordinary people. Pessimists are people who believe in elites and governments. They believe that famous Ivy League college professors are smarter than ordinary men and women. A pessimist believes the government has to tell you how much money you get and where to spend it. An optimist believes that you should keep more of what you earn and that it is totally up to you how you use it.

To understand the deep-rooted optimism of Ronald Reagan is to understand that he really was the first populist Republican politician of stature in this century, or at least since Coolidge. Populists who believe in people are optimists, and I think American politics during this long wave of prosperity (to which I see no end in sight) will revolve around those leaders who take an optimistic view and who are, therefore, populist believers in markets and ordinary people.

What is interesting to me about this debate between optimism and pessimism and between populism and elitism is that it's difficult to tell which politicians in which parties are going to buy into which view. In that important sense, I believe Reagan was a true bipartisan president, and the older I get, it seems, the more I tend to look at these issues in a bipartisan, almost nonpolitical sense. I think this era of prosperity and optimism opens up tremendous opportunities for either political party or, for that matter, new political parties. It was Reagan who taught me about optimism and populism and freedom. That is a lesson successful politicians must learn. n