



Washington View

November 23, 2006

Globalization and the new majority

- Putting the war in Iraq and corruption scandals aside, the most important factor cited in different polls is the uncertainty about the benefits of current growth for middle class Americans
- There is disagreement amongst Democrats regarding policy solutions. While economists involved in the "Hamilton Project" favor policy that may better distribute the benefits of globalization, an important fraction of Democrats dismisses globalization altogether
- Democrats advocate the introduction of budget rules and pledge to cut pork barrel spending; however, there's no clarity if any reform will actually pass given how important discretionary spending has traditionally been for incumbents of both political parties

The outcomes from the 7 November elections for Congress were the consequence of a growing dissatisfaction of voters towards current management in Washington DC. Although everyone in the Capitol agrees with this assessment, analysts disagree on the exact causes of voters' discontent. The diagnosis to be reached, especially by Democrats who obtained the mandate, will affect the course of the legislative branch for the next two years.

Putting the war in Iraq and corruption scandals aside, the most important factor cited in different polls is the uncertainty about the benefits of current growth for middle class Americans. In particular, there is a growing skepticism about the benefits that globalization has brought to this sector of society. Disappointment in this area is shared by all, even by the most vocal proponents of globalization within Democratic ranks, such as Robert Rubin, Lawrence Summers and other economists at the Hamilton Project (a think-tank created by Rubin). However there is disagreement amongst Democrats regarding policy solutions. While economists involved in the

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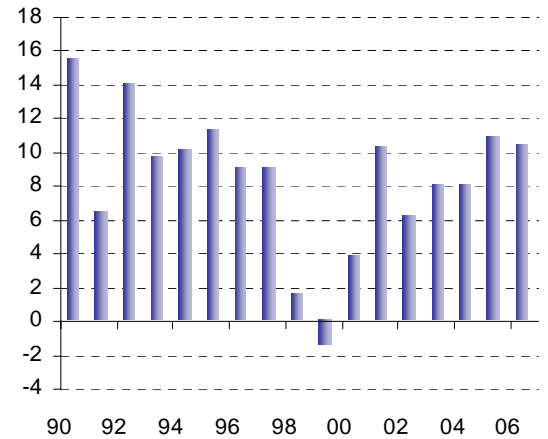
"Hamilton Project" favor policy that may better distribute the benefits of globalization, an important fraction of Democrats dismisses globalization altogether. Since June of 2006, critics of globalization have been crafting an alternative policy and are expected to present it in January 2007. The battle of ideas has already started. While the Hamilton Project has already drafted several proposals, around such issues as revamping unemployment insurance, the second group is coordinating a more aggressive move towards blocking new trade agreements. This is one of the most important debates taking place in Washington today, and its resolution will have and immediate effect on current trade negotiations with Peru, Colombia, South Korea, Malaysia and Thailand, but at the same time it may have a long lasting effect on the process of globalization.

October's Budget Statement

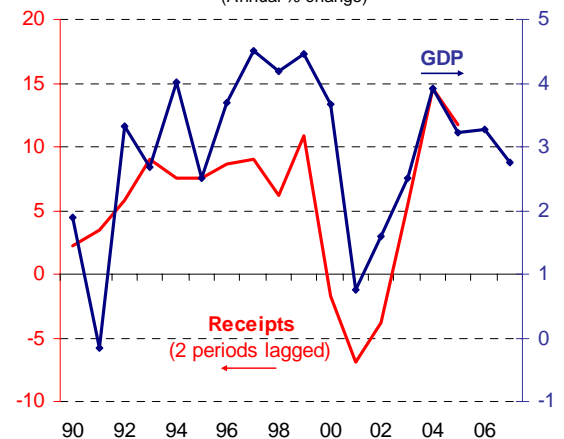
In October 2006, the budget deficit widened to \$49.3 billion, from \$47.3 billion a year before. Both revenue and outlays reached record levels for October. Net outlays rose by 10.3% to \$216.9 billion, the biggest increase in three months. Spending on Medicare surged 70% to \$33.97 billion as a result of prescription-drug benefits. In addition, spending on national defense rose 10.3% to \$51.2 billion. Revenues continued expanding at a solid pace of 12.2% to \$167.7 billion. Individual income taxes rose 15.2% to \$86.22 billion and corporate income taxes edged up 53% to \$9.35 billion. October's budget showed that revenues expanded strongly during the first month of the fiscal year. Although this is positive, it could prove to be short lived as the economy slows through 2007. This could worsen the fiscal outlook for the short term, especially if the current pace of government spending continues.

The future of spending, especially for defense and entitlements, relies more than ever on the interaction between Congress and the White House. During the campaign, Democrats appeared to be more concerned about deficits than Republicans. Most of the newly elected Democrats advocate the introduction of budget rules and have pledged to cut pork barrel spending. But there is no clarity if any reform will actually pass given how important discretionary spending has traditionally been for incumbents in both political parties. The issues that stir higher consensus among Democrats are in the revenue side of the equation, and that's why they will surely try to stop President Bush's intentions to extend tax cuts before they expire in 2010.

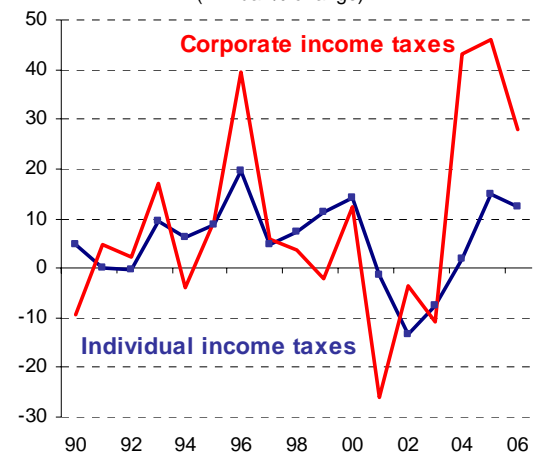
Spending on Medicare
(Annual % change)



Real GDP and fiscal receipts
(Annual % change)



Individual & Corporate Income Taxes
(Annual % change)



Opinion Pulse

The new Democrat Congress surge with a strong support from the public, which will give them more bargaining power to pass its core propositions into law

"Do you have more confidence in President Bush or in the Democrats in Congress to deal with the major issues facing the country today?" (11/17-19/06)

	%
President Bush	33
Democrats in Congress	54
Both	2
Neither	8
Unsure	3

Source: CNN Poll conducted by Opinion Research Corporation. Nov. 17-19, 2006. N=1,025 adults nationwide.

"As best you can tell, do you approve or disapprove of Democratic congressional leaders policies and plans for the future?" (11/9-12/06)

	%
Approve	50
Disapprove	21
Unsure	29

Source: Pew Research Center for the People & the Press survey conducted by Princeton Survey Research Associates International. Nov. 9-12, 2006. N=1,479 adults nationwide. MoE ± 3 (for all adults).

However, not all of these proposals appear to be the most important for voters; in fact, the public seems to prefer the minimum wage and accountability issues rather than other important Democratic proposals like rolling back tax cuts or encourage stem cell research

"As I read you some things the new Democratic Congress might do over the next two years, please tell me if you think each should be one of their top priorities, a lower priority, or should not be done at all. What about [see below]? Should this be one of their top priorities, a lower priority, or should this not be done?"

	One of top priorities	A lower priority %	Not done at all	Unsure		One of top priorities	A lower priority %	Not done at all	Unsure
Increasing the minimum wage					Broadening the kinds of stem cell research that can receive federal funding				
11/9-10/06	68	21	10	1	11/9-10/06	48	31	17	4
10/19-20/06	68	21	9	2	10/19-20/06	44	31	19	6
Investigating government contracts in Iraq					Rolling back some of the Bush tax cuts				
11/9-10/06	60	29	10	1	11/9-10/06	40	32	24	4
10/19-20/06	58	29	8	5	10/19-20/06	38	28	28	6

Source: Newsweek Poll conducted by Princeton Survey Research Associates International. Nov. 9-10, 2006. N=1,006 adults nationwide. MoE ± 3.