

Economic Effects of Possible Changes in U.S. Fiscal and Regulatory Policy

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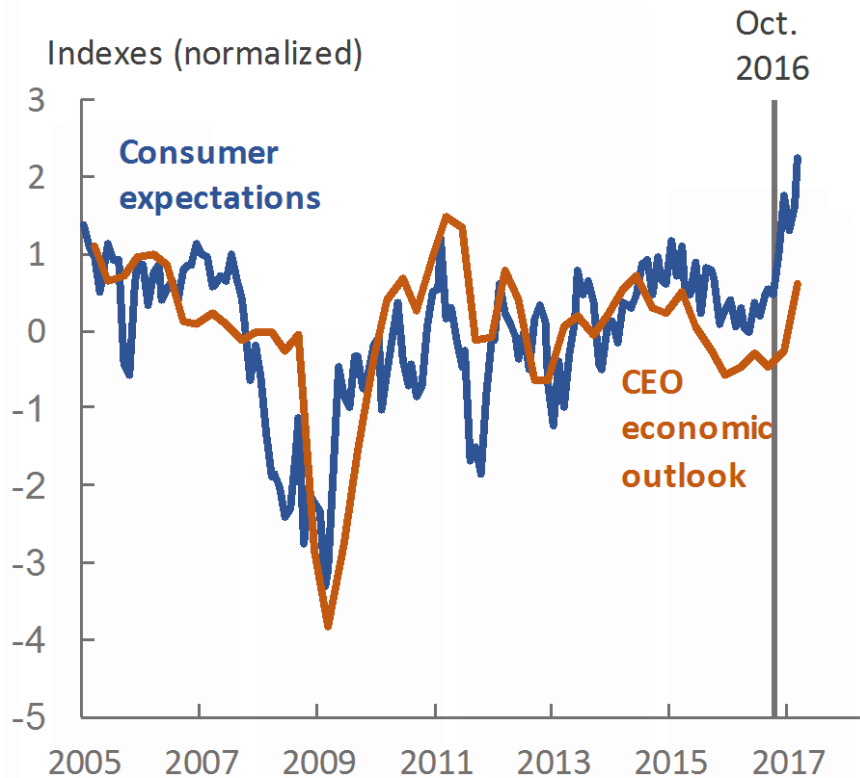
Peterson Institute for International Economics

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Building on Dave's evidence that economic optimism has surged

Consumer and Business Surveys



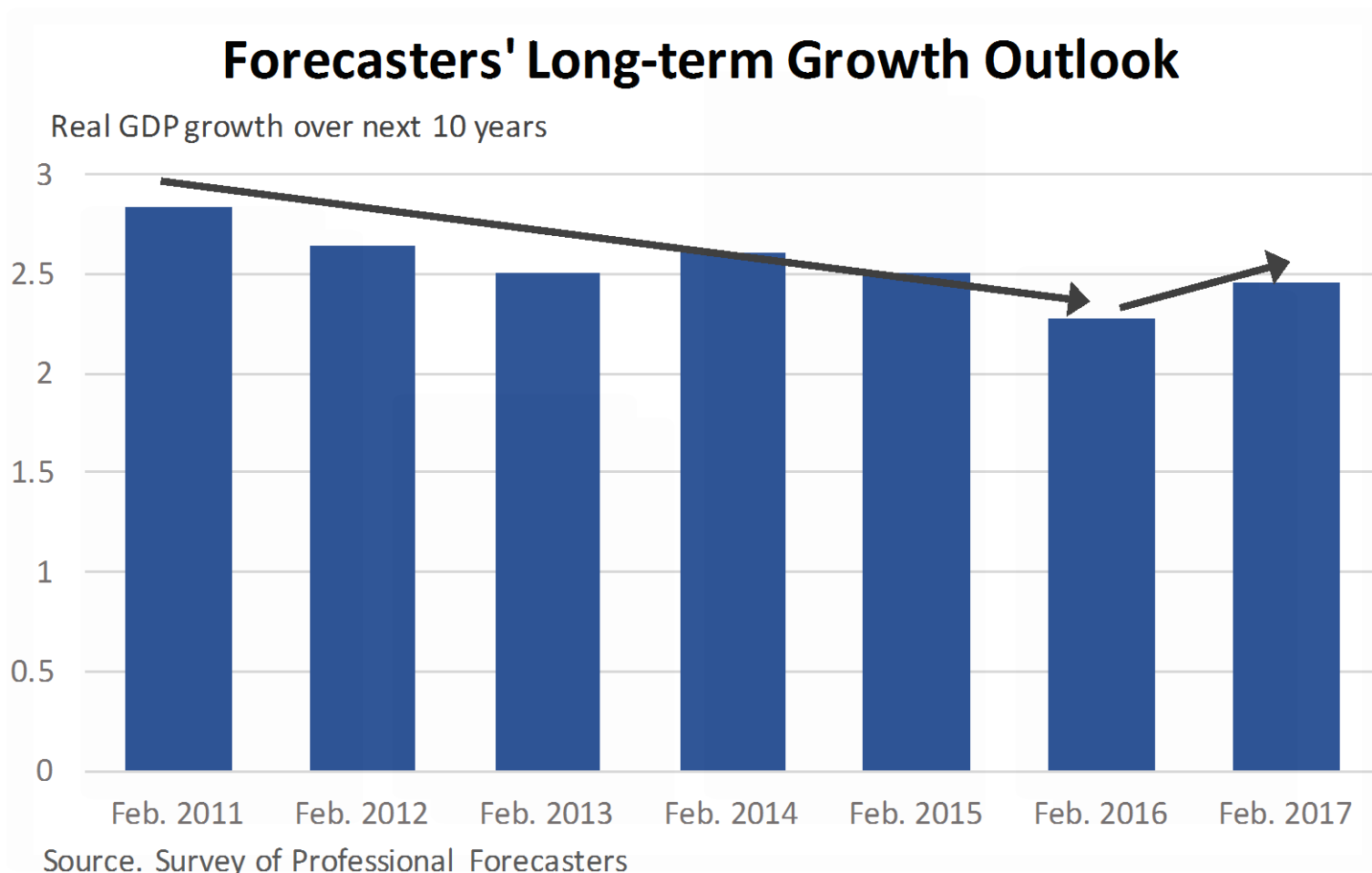
Sources. Conference Board; Business Roundtable

Stock Price Index



Source. S&P Dow Jones Indices LLC

Even forecasters seem cheerier for a change

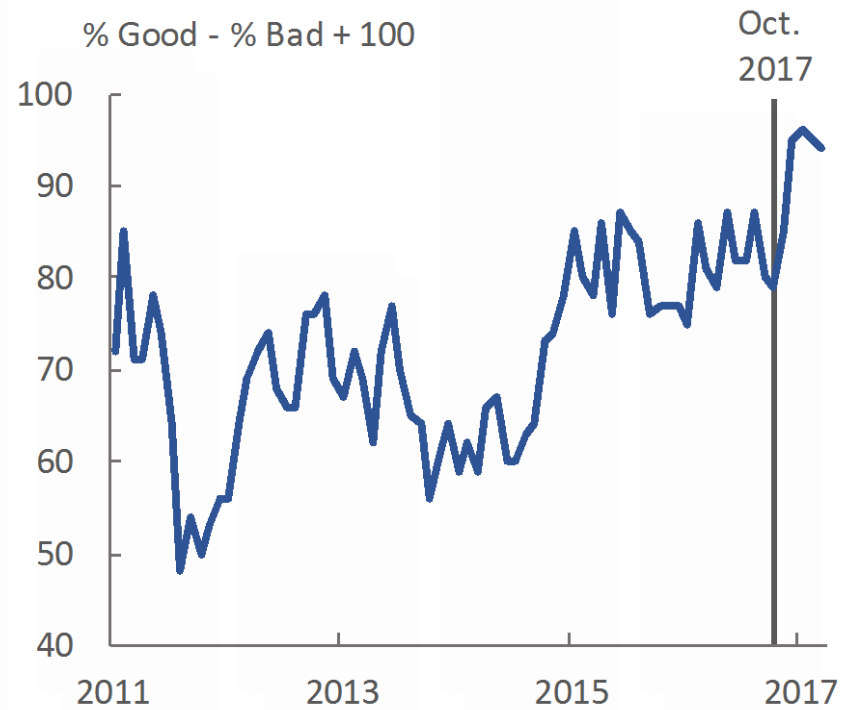




A plausible explanation:

The policies of the new Administration are expected to enhance the performance of the U.S. economy.

Consumer Opinions about Government Economic Policy



Source. University of Michigan Surveys of Consumers.



But the optimism seems overblown: because changes in fiscal and regulatory policy are likely to be more limited and less potent than people imagine.



The “growth challenge”

Powerful supply-side factors explain why growth has been tepid relative to the 70s, 80s, 90s:

- Women no longer surging into the workforce
- Baby boomers starting to retire
- Slow productivity growth

A sustained higher pace of growth requires boosting the supply-side determinants of output.



Tax reform: It's very hard

Widespread support
in principle



Sufficient support
for a specific plan

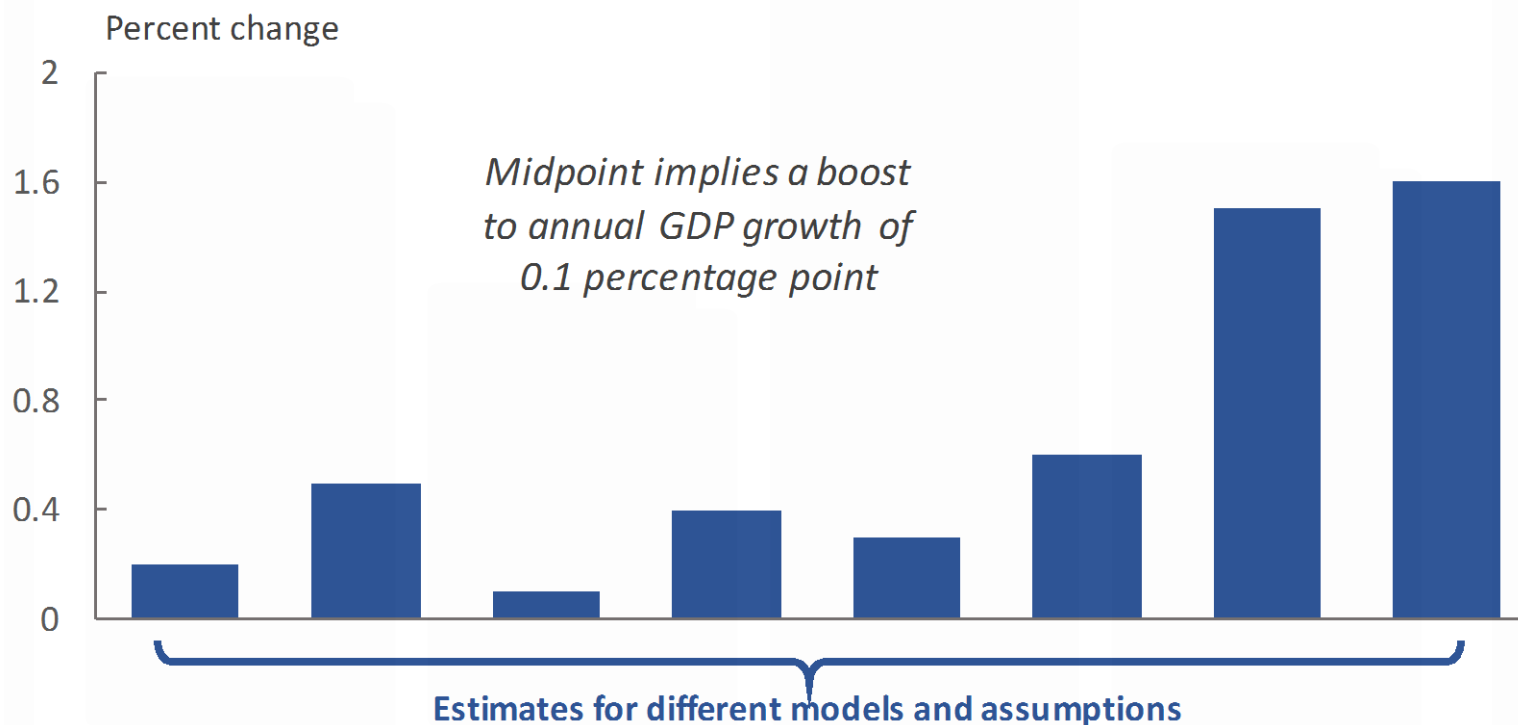
Many **unanswered** questions:

- Revenue-neutral or deficit-increasing?
- Distribution-neutral or favoring high-income taxpayers?
- Shift to consumption tax or stick with the current approach?

Revenue-neutral, distribution-neutral tax reform would have only small effects



JCT Estimates of the Effect of the Camp Plan on Real GDP after 10 Years



Source. Joint Committee on Taxation, U.S. Congress



If broad tax reform fails, some fallback change in the tax code is likely

A tax break for U.S. multinational firms that repatriate funds?

- Perhaps, but would not boost growth significantly.

And/or a plain old tax cut?

- Do-able through reconciliation with just Rs or by structuring plan to win over Ds.
- Limited near-term effects and could be neutral or negative over the longer run.



Appropriations: The first order of business is finishing 2017

Government “shut down” on April 29 if Congress doesn’t act.

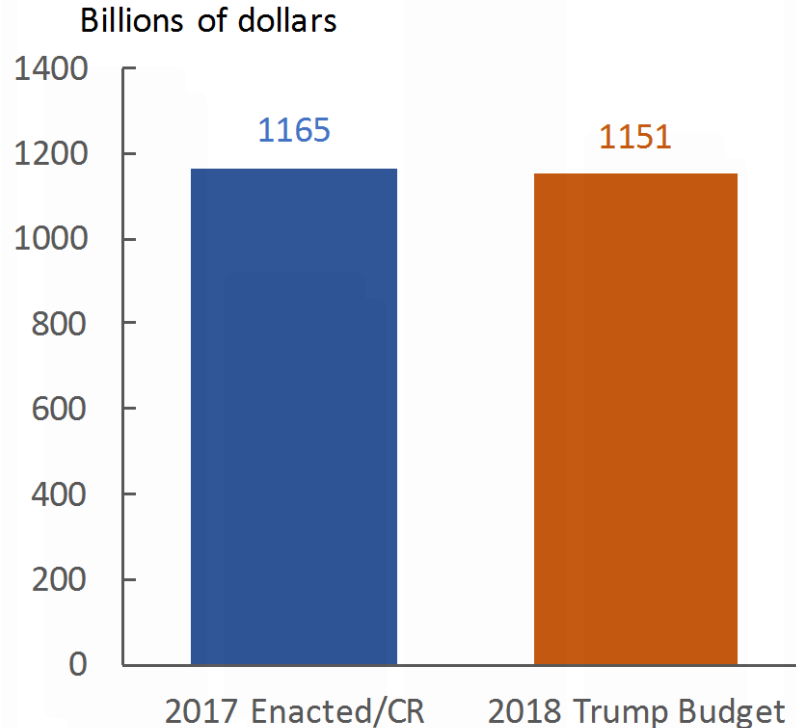
Some support from Democrats required because appropriations bills need 60 Senate votes.

Republican will “own” a shutdown so likely to avoid.



Appropriations for 2018: The Administration's "Skinny Budget"

Federal Total Discretionary Spending



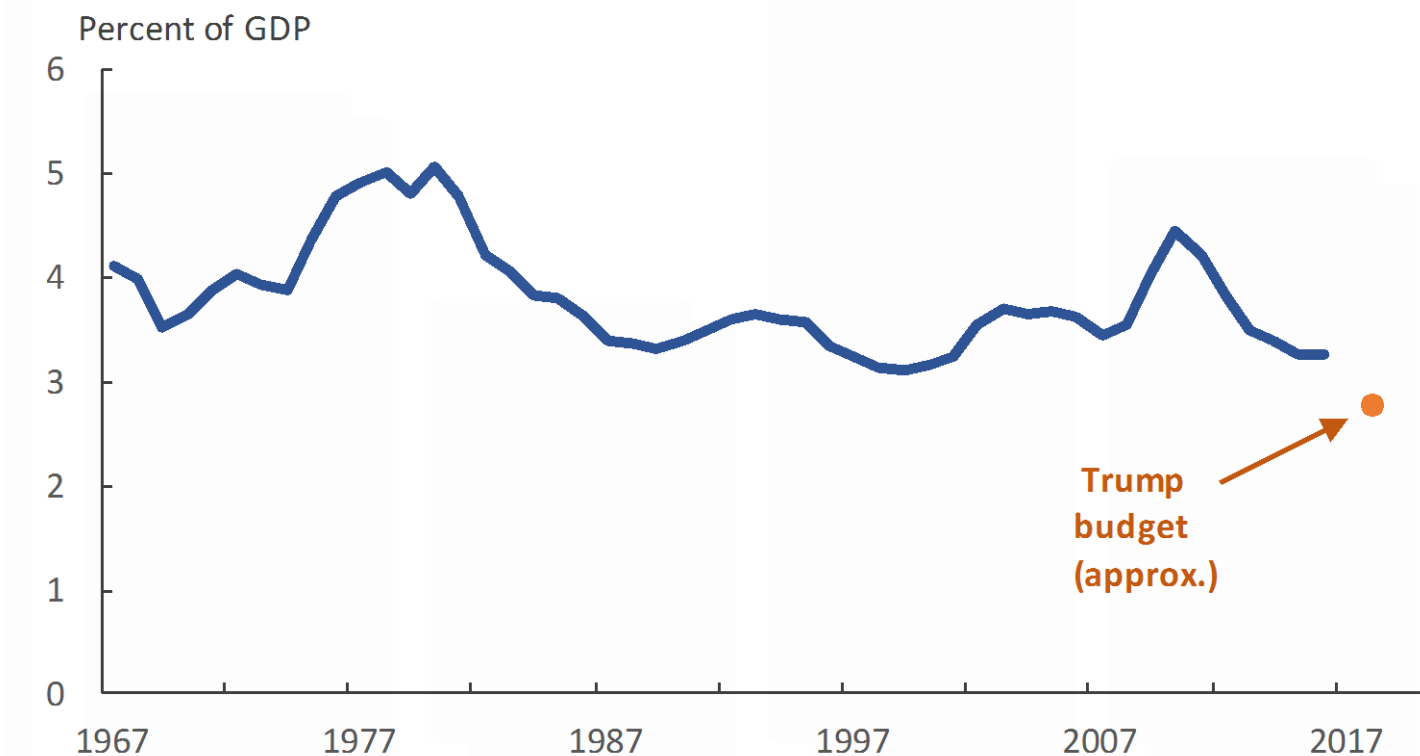
Includes \$54 billion shift from nondefense to defense.

Source. America First Budget Blueprint

Proposed nondefense appropriations at lowest level in decades



Nondefense Discretionary Spending



Sources. Congressional Budget Office; America First Budget Blueprint; author's calculations.



Most likely outcome is some increase in appropriations for 2018

Defense spending is much more likely to rise than nondefense is to fall:

- Many people support increasing defense spending.
- Many people support cutting nondefense spending **in the abstract**—but not cuts for most specific programs.

Appropriations thus likely to rise—but **not enough to avoid a mild contractionary effect.**



Regulatory Relief

Could boost growth—but evidence on the magnitude of effects very mixed.

And some considerable obstacles:

- Changing most regulations involves long and complicated process.
- And need to grapple with trade-offs—worth sacrificing societal objectives?

Other policy changes unlikely to boost growth much either



Infrastructure—totally unclear where we are going.

Health care—changes won't have macro significance.

Immigration—Administration goals would ↓ growth.

Debt ceiling—a lot of noise likely but default unlikely.



Notes on slides

Slide 1: Consumer expectations series is from the Conference Board (last data point = March 2017). CEO economic outlook is from the Business Roundtable (last data point = 2017:Q1). To normalize the series, I subtracted the mean over the period shown and divided by the standard deviation. Shaded regions in this chart and those that follow represent recessions. S&P 500 index from S&P Dow Jones Indices LLC (last data point = April 10, 2017).

Slide 2: Series is the median forecast of real GDP growth over the next ten years from the Survey of Professional Forecasters. This question is asked every February.

Slide 3: Series is from the University of Michigan Surveys of Consumers. The underlying question asks whether the government is doing a good, only fair, or poor job in terms of economic policy.

Slide 7: Estimates come from [MACROECONOMIC ANALYSIS OF THE “TAX REFORM ACT OF 2014.”](#)

Slide 10: Figures come from [America First Budget Blueprint](#), Table 2.

Slide 11: Historical series from the supplementary data provided with the Congressional Budget Office (CBO) report: [The Budget and Economic Outlook: 2017 to 2027](#). The data point representing the Trump budget based on information about proposed nondefense discretionary spending in Tables 2 and 3 of [America First Budget Blueprint](#) and CBO’s forecast for nominal GDP in 2018.