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USA

A Trump boom?

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The US stock market continues to jump and has now reached a record high.

[<https://www.internationalviewpoint.org/IMG/png/stock-boom.png>]

Finance capital is getting very positive about Trumponomics with its plans for cutting taxes (both corporate and personal), reducing the regulation of the banks and implementing range of infrastructure projects to create jobs and boost investment. But even assuming all this would happen under a Trump presidency, will it really get the US economy out of its depressingly slow crawl? In my last post, I doubted it. Now JP Morgan economists have taken a similar sceptical line.

They reckon Trump's agenda will likely yield little impact on US employment and inflation in the next two years, while tax cuts will boost growth by only a modest 0.4 percentage points by the end of 2018 (i.e. over two years) at most.

JP Morgan thinks that Trump will introduce tax cuts worth around \$200 billion per year, evenly split between personal and corporate taxes. Interestingly, they agree with me that the so-called Keynesian 'multiplier' (how much rise in real GDP growth from tax cuts) is low: just 0.6 for personal taxes and 0.4 for corporate taxes – meaning for every \$1 in tax breaks received by individuals and by businesses, that will likely boost aggregate demand to the tune of 60 cents and 40 cents in a given fiscal year, respectively.

[<https://www.internationalviewpoint.org/IMG/png/trump-plan.png>]

As a result, JPMorgan reckons US economic growth will hardly pick up at all from its current 2% a year average and will be nowhere near the 4% annual that Trump claims he can get. I would argue that faster growth would depend not on more spending in the shops or more house purchases but on higher business investment and that is what is missing from the equation.

Part of the Trump plan (again I hasten to add if it happens) is to cut the tax rate for companies that hold huge cash reserves overseas if they return these funds to invest at home. Unlike other developed nations, the US taxes corporate income globally, but it allows companies to defer paying tax on offshore earnings until they decide to repatriate that income. As a result, US companies have avoided U.S. taxes by stashing roughly \$2.6trn offshore, a figure cited by Congress's Joint Committee on Taxation. The top five in order of overseas cash holdings as of Sept. 30, are Apple (\$216 billion), Microsoft (\$111 Billion), Cisco (\$60 billion), Oracle Corp. (\$51 billion) and Alphabet Inc. (\$48 billion).

[<https://www.internationalviewpoint.org/IMG/png/shareholder-payouts.png>]

Such an idea was tried back in 2004 under George Bush. But the result was not a rise in productive investment but a new bout of financial speculation. Companies got a tax 'amnesty' but used the cash they brought home on buying back their own shares or pay out dividends to shareholders, driving up the stock price and then borrowing on the enhanced 'market value' of the company at very low rates. In 2004, when US firms brought back \$300bn in cash, S&P 500 buybacks rose by 84%.

Goldman Sachs economists reckon that this will happen again with the Trump plan. Indeed GS reckon that next year could see buybacks take the largest share of company profits for 20 years. They estimate that \$150bn (or 20 percent of total buybacks) will be driven by repatriated overseas cash. They predict buybacks 30 percent higher than last year, compared to just 5 percent higher without the repatriation impact, while productive investment's share will be little changed.

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Asked what he would do with repatriated cash should the Trump administration slash taxes on foreign profits, Cisco Systems Inc. Chief Executive Officer Chuck Robbins said "We do have various scenarios in terms of what we'd do but you can assume we'll focus on the obvious ones â€" buy-backs, dividends and M&A activities."

[<https://www.internationalviewpoint.org/IMG/png/use-of-cash.png>]

Now it is argued by some that the hoard of overseas cash shows that the problem American capital has is not that its profitability is too low. On the contrary, it is awash with profits (and profits not counted in the official stats). But here is an interesting observation by Morgan Stanley economists. Of the \$2.6trn cash held abroad by American companies, only 40%, or roughly \$1 trillion, is available in the form of cash and marketable securities. The other \$1.5 trillion has been reinvested to support foreign operations and exists in the form of other operating assets, such as inventory, property, equipment, intangibles and goodwill. So it has been invested not held in cash after all. And the cash is not so awash.

It's also highly unlikely that companies with factories overseas will shift meaningful production to the US. After all, labour remains significantly cheaper in nations like China. Hourly compensation costs were \$36.49 per employee in the US in 2013, according to The Conference Board. The comparable cost in China was just \$4.12 that year (the most recent figure), even after having increased more than six-fold over the preceding ten years.

Besides, many companies that do still make products in the US are automating production. Consider Intel Corp. The chipmaker has giant fabrication plants in Oregon, Arizona and New Mexico that employ just a handful of people to keep the machines running. Nothing the Trump administration does will stop robots from taking over large swathes of manufacturing in the long run.

Another part of Trumponomics is to implement an infrastructure program of building roads and communications. His plan to fund this from private money in return for ownership and revenues from the projects. This has made Keynesian economic guru, Paul Krugman apoplectic, and rightly so.

As Krugman explains "imagine a private consortium building a toll road for \$1 billion. Under the Trump plan, the consortium might borrow \$800 billion while putting up \$200 million in equity â€" but it would get a tax credit of 82 percent of that sum, so that its actual outlays would only be \$36 million. And any future revenue from tolls would go to the people who put up that \$36 million. Crucially, it's not a plan to borrow \$1 trillion and spend it on much-needed projects â€" which would be the straightforward, obvious thing to do. Instead "If the government builds it, it ends up paying interest but gets the future revenue from the tolls. But if it turns the project over to private investors, it avoids the interest cost â€" but also loses the future toll revenue. The government's future cash flow is no better than it would have been if it borrowed directly, and worse if it strikes a bad deal, say because the investors have political connections."

Second, Krugman goes on, "how is this kind of scheme supposed to finance investment that doesn't produce a revenue stream? Toll roads are not the main thing we need right now; what about sewage systems, making up for deferred maintenance, and so on? Third, how much of the investment thus financed would actually be investment that wouldn't have taken place anyway? That is, how much "additionality" is there?"

Suppose that there's a planned tunnel, which is clearly going to be built; but now it's renamed the Trump Tunnel, the building and financing are carried out by private firms, and the future tolls and/or rent paid by the government go to those private interests. In that case we haven't promoted investment at all, we've just in effect privatized a public asset â€" and given the buyers 82 percent of the purchase price in the form of a tax credit."

So the Trump plans will be ineffective in getting US economic growth rates up, in delivering more jobs, real incomes

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and better transport; but it will boost financial markets and a speculative boom.

[The next recession](#)