

A Kennedy/Reagan-style stimulus package

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Earlier this year the Obama administration pushed through Congress its \$787 billion stimulus package amid dire predictions for the U.S. economy. The package was designed to get America working and keep unemployment below 8.5 percent. Now, with unemployment at 9.5 percent and predicted to go higher, Vice President Joe Biden has seemingly opened the door for another round of government spending, stating he believed the White House underestimated the severity of "the worst economy since the Great Depression."

Yet, President Obama's own Labor Secretary, Hilda Solis, said recently that much of the stimulus money was moving slowly, especially construction projects. The glacial pace of approval has led to only 10 percent of the stimulus package being spent to date. At this rate, it will be three years before the entire package makes its way into the economy. Meanwhile more than 3.4 million jobs were lost to the U.S. economy so far this year. U.S. Congressman Eric Cantor (R-Va.), stated that the purpose of the Obama administration stimulus package was to preserve, protect and create jobs and "it has failed miserably." Considering the above, why has the president's stimulus package had less than intended results?

The Problem

The problem is not, as Mr. Biden would have us believe, that the government didn't spend enough, or that government bureaucracy is slowing the pace of stimulus spending, which it is. The problem is with a package that didn't cut taxes enough or in all the right places. People have little confidence in government spending as a catalyst for economic growth and long term prosperity. They know that business creates jobs; government largely creates taxes, regulations and spends. The U.S. economy is burdened by: onerous regulations, the third highest corporate income tax rate (39.27 percent) in the world, and a combined state and federal personal income tax rate that can exceed 46 percent in certain states.

Despite all the money coming in, the U.S. national debt is now \$11.2 trillion dollars, or 78 percent of U.S. GDP, and will likely be above 100 percent of GDP by the end of next fiscal year, surpassing the 1949 level of 97.5 percent which included costs associated with World War II and post war reconstruction.

Many key U.S. competitors have much lower national debt to GDP ratios with China at 21 percent and Russia at 10 percent. By comparison, the next stimulus package this economy needs is not more of the same but a massive incentive-based tax cut to allow the U.S. to be competitive globally... currently we are not! Consider that while dealing with the moral, political and economic challenges of transitioning from communism to capitalism Russia has out-performed the U.S. over the last 5 years with a smaller national debt to GDP ratio, often friendlier regulations, a corporate income tax rate of 24 percent and an average personal income tax rate of 13 percent. The U.S. has higher corporate and personal income tax rates than Canada and Mexico, as well as much of the industrialized world. The accounting firm, KPMG reported that the global average corporate income tax rate for all countries in 2008 was 25.9 percent with the EU average at 23.2 percent, the Latin American average at 26.6 percent, the Asia-Pacific average at 28.4 percent and the OECD average at 26.7 percent.

The Solution

It seems that the presidencies of John F. Kennedy and Ronald W. Reagan serve as strong cases for the effectiveness of tax cuts in stimulating economic growth during difficult times. Recall what President Kennedy said about his own tax-cut based stimulus package in 1962: "In short, to increase demand and lift the economy, the federal government's most useful role is not to rush into a program of excessive increases in public expenditures, but to expand the incentives and opportunities for private expenditures." President Kennedy's tax cut was implemented after his death by President Johnson in 1964, with personal income tax rates declining 23.1 percent for the top income earners and 30 percent for the lowest. Corporate income tax rates were reduced by 9.6 percent the same year. The economy responded with an average annual real growth rate of 4.65 percent in U.S. GDP from 1963 to 1968, and unemployment dropped from 6.6 percent in 1961 to 3.7 percent in 1968. President Reagan's across the board tax cut of 25 percent was phased in from 1981-1983 and helped bring the U.S. economy out of the severe economic recession of 1981-82 which saw the prime interest rate peak at 21.5 percent in 1981 (the highest since the Civil War), real GDP declined by 2.2 percent in 1982, and unemployment reach 10.8 percent also in 1982. The economy responded with an average annual real GDP growth rate of 3.87 percent from 1982-88, unemployment declined to 5.4 percent by 1988, and real tax revenue grew by 25.5 percent from 1983 to 1988. Finally, it should be recalled that average government spending exceeded average tax revenue growth by 4.22 percent for most of the 1980s, thus creating the budget deficits of the Reagan years and hopefully providing a lesson for today's policymakers?

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