Big Economic Questions of the Day: Trump Tax Cuts, Economic Growth, Inflation. Monetary Policy. Undocumented Immigrants

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Recently I have had several journalists, academics and progressive activists ask me my opinion on some of the key economic questions of the day. Here are some of my replies: on Trump tax cuts and US growth, current immigration debates, wages, expanding income inequality in the US, on what is the real rate of inflation today, and whether proposals for universal guaranteed income, debt jubilee, Modern Money Theory, green new deal are solutions to today's economic problems.

Question 1: Is US economic growth under Trump due to his tax cut policy and what is the future of average or low wage Americans today?

Dr. Rasmus: The nominally higher US GDP growth in 2017-18 has little to do with the Trump tax cuts. The Trump tax cuts passed in early 2018 amounted to more than $4.5 trillion over the decade, targeting to wealthy households, businesses, investors and corporations, which have been 'front-loaded' in 2018. Offsetting this are $1.5 trillion in tax hikes for wage earners, that begins to hit this year and accelerates after 2022. Assumptions about 3% GDP growth for another decade, with no recession, produces a further offsetting of $1.5 trillion. The net result supposedly is the $1.5 trillion reported by the press. But the $4.5 trillion cuts for business and investors have not gone into real investment and generated the Trump 2017-18 GDP growth rates.

Real investment in structures and equipment declined steadily over 2018 as the Trump tax cuts took effect: measured in percent terms compared to the preceding quarter, residential construction was negative every quarter in 2018. Commercial construction, with a lag, turned negative in the second half of 2018. And equipment spending fell from 8.5% in the first quarter to 3.4% by October 2018.

So if the Trump tax cuts did not go into real investment, creating real employment and real GDP where did it go? It went into stock buybacks, dividend payouts, and M&A activity. Several US banks' research departments estimate buybacks plus dividends for just the Fortune 500 largest companies in the US will reach a record $1.3 trillion in 2018. Add the largest 2000 or 5000 companies and its close to $2 trillion. Hundreds of billions more for M&A. This diversion of the Trump tax cuts to financial markets is the main determinant driving stock markets (even after corrections) and other financial asset markets.

The government grossly over-reports wage gains for the average and low paid workers in the US. Independent source reports show that more than half of US workers received no wage gain at all in 2018. The official reported wage gains of 3% are skewed to the top 10% of the labor force, dragging up the 'average' wage. Moreover, the data is for full time employed only, leaving out tens of millions of part time-temp workers' wages. And it doesn't adequately account for local taxes and interest on debt that reduces the take home wage further. Then inflation is under-estimated, making the real wage appear higher. So average workers at best stagnated, with most experiencing a decline in real wages. The rate of inflation in the US is especially under-estimated for median worker family households, while inflation is rising for rents, medical, education, and other major items in household budgets. So the immediate future will mean even less real wage gains for the majority of US workers. If workers were doing so well today, as Trump and the business and mainstream press report, why is it that 7 million of them have defaulted on their auto loans? Probably a like amount for education loans, the defaults of which are grossly under-reported. And why is credit card, auto loans, and education loan debt now all over $1 trillion each? And total household debt load approaching $14 trillion?

Question 2: With undocumented immigrants at 10-12 million, do you believe Trump's claim that immigrants are invading the US economy?

Dr. Rasmus: Immigrants are certainly not invading the US. The 10-12 million number has been stable for several years. And for immigrants for some countries, like Mexico, the numbers are in sharp decline. It is true that more immigrants are coming from central American countries like Honduras, Salvador and Guatemala. But that is due to the economic crises and violent breakdown of the social order in those countries, which is due largely to US support for the corrupt elites of those countries who encourage the gang violence in their countries and do nothing about the economic crises. If there is a problem with immigration in the US, it is a problem of highly educated tech workers being brought in on H1-B and L-1 visas, and rich Asians who can buy themselves a 'green card' residency by promising to spend $50,000 when they come. These groups are taking the best jobs, the high paying tech and other professional jobs, and have been since the 1990s. But Trump is agreeing with the US tech companies to keep bringing them in, taking jobs US workers should and could get. Trump's immigration policy and draconian action against immigrants from Latin America and elsewhere is about his re-election plans in 2020. By creating 'enemies' within and outside the US, he diverts his political base from the real problems of America. Blame the foreigner in our midst has always been a useful fascist argument. And Trump is marching down that road, as witnessed in his latest Constitutional power grab by declaring national emergencies to build his Wall and invoking phony national security to justify his trade wars.

Question 3: Do you believe the widening gap between rich and poor in the era of Trump can boost Americans interest in socialism?

Dr. Rasmus: The income and wealth gaps in the US are not only widening but doing so at an accelerating pace. US neoliberal policy under Obama was to subsidize capital incomes through Federal Reserve cheap money and by extending and expanding his predecessor, George W. Bush, tax cuts for business and investors. He gave more than $5 trillion in tax cuts to business and investors, more than even Bush. Trump policy has accelerated the tax cuts even further and he's now stopped the Fed from raising interest rates. So we have subsidization on steroids now by both fiscal and monetary policy. The direct consequence is booming stock and corporate bond markets, fed by $1 trillion annual stock buybacks and dividend payouts every year since 2011 (now at record $1.3 trillion in 2018). As wage incomes for the 90% of Americans remain stagnant, barely rise, or decline, the direct consequence is accelerating income inequality and wealth gaps. But it's mainly due to the shift toward financial profits by American (and increasingly global) capitalists that's been building since the 1980s.

Will this boost interest in socialism? It already has. A clear majority, well over 60%, of people aged 34 and younger in the work force, have indicated in various recent polls that they prefer socialism over capitalism. It's not by accident, therefore, that Trump and the US business press has been launching an offensive to attack the idea of socialism once again. This shift in public opinion will continue as the Trump policies continue to create a growing gap in income, wealth and opportunity in America.

Question 4: Some critics of US economic statistics on inflation say that inflation may be as high as 9.6% or at least more than 5%. What's your view on this?

Dr. Rasmus: I agree the CPI rate is actually higher. I don't think it's 9.6%, but certainly not 2.1% (core) or 2.4% (headline). The Shadow Stats source has long critiqued US stats, including inflation. Also, employment and wage data, both of which I've been criticizing this past year. The CPI is higher than reported for several reasons. First, as Shadow Stats notes, they make arbitrary assumptions about product quality improvements that lower the actual rate. Second, they use what's called 'chain price indexing' that smooths out, and lowers, the rate over time. Third, the weights for the basket of goods in the CPI is outdated. This is especially true for median income and below families. There should be different weights and definition of the basket for different levels of income, but there isn't. Middle income and below families are experiencing greater inflation due to rising drug and health prices, rising local taxes and utilities, rising interest rates on mortgages, and rising rents. Rent prices are under-reported in particular since they are smoothed out by including what's called 'imputed rents'; that is, assumptions about home owners paying themselves a rent (yes, that's illogical but true in the methodology), which hasn't changed much for years but, when added to direct rents, results in a lower average. There's also issues with how the data is collected on prices.

Of course, we're talking here about prices for goods and services. Not prices for financial assets which have accelerated several fold since 2009, as bubbles have grown. I suspect that real CPI is about 3.5% to 4%, not the 2.1%. That of course means that real US GDP is not 3% in 2018 but actually less than 1% in real terms. (The price index for GDP real adjustment is the GDP deflator index, which is notoriously even lower than the CPI (or the PCE, which the Fed uses).

Watch the first quarter 2019 GDP come in closer to 1% in official reporting later this spring. That means the Trump tax cuts of more than $4 trillion over the coming decade, front loaded in 2018, have had very little effect on real GDP. Most of it has gone to stock buybacks, dividend payouts and M&A financing. Buybacks pus dividends for the just the

Fortune 500 will equal around $1.3 trillion for 2018, a record. Real investment has been sliding throughout 2018, when the tax cuts took effect. Residential construction contracted every quarter. Commercial construction lagged, but turned negative as well in the second half of the year. And equipment investment declined from 8.5% at the beginning of 2018 to 3%-4% by the end. It's a real fiction that Trump tax cuts are responsible for the 3% plus growth in 2018. It's mostly been due to government spending, especially defense, and to consumption driven by household debt for the bottom 80%, although nicely rising compensation for the top 10% has driven consumption as well. Trump cut paycheck withholding in 2018 so that average households would think the tax cut was putting more money in their wallets. But it wasn't. And now, in 2019, most households will start feeling the bite of more taxes. The $4 to $4.5 trillion actual Trump tax cuts are going to the wealthiest individuals, businesses, and corporations, especially the US multinationals. That will be offset by $1.5 trillion in tax hikes for wage earners, which really starts to hit about 2022. Plus phony assumptions about 3% plus GDP growth rates for the next decade, with no recession. That's how Trump gets his $1.5 trillion total deficit from the tax cuts. It's a big fiction that the press also fails to report. Reporters are either stupid or the policy is to report the $1.5 trillion.

In other words, it's not just price stats that are inaccurate, but GDP, wages and jobs data as well. The only thing holding up the house of cards is debt. For households now approaching $14 trillion. For the national government now $22 trillion (and going to $34 trillion by 2028). For state and local governments, trillions more. And for private business well over $20 trillion more. A big problem with leveraged loan debt, junk rate corporate debt, half of investment grade (i.e. BBB) which is also 'junk', and who knows what in derivatives and margin borrowing by investors.

Question 5: Progressive proponents of public banking, and what's called modern monetary theory, both believe that the Federal Reserve could simply create money for all citizens' economic benefit, not just for the banks. What's your view on this? And specifically on the idea of a guaranteed basic income, what's called a debt jubilee of legal forgiveness of debts of households, and a green new deal?

Dr. Rasmus: The Fed isn't feeding the banks to avoid a recession; the Fed is feeding the financial markets to prevent a third major contraction since Feb. 2018 that is coming. Cheap money in excess keeps rates low (or in this case prevents them from rising further). But the money doesn't go into real investment. It goes into asset markets (or flows offshore to emerging markets), or into M&A activity, or into stock buybacks and dividend payouts in the trillions annually (this year $1.3 trillion, after 6 years of an average of a trillion a year).

Yes, the Fed could provide credit to households and non-banks, but that's not why it was created. It was created, like all central banks, to subsidize the banks with cheap credit and to bail them out when they binge too much and create a crisis. In the postscript to my 2017 book, 'Central Bankers at the End of Their Ropes', I provide language for legislation (and a constitutional amendment) that would radically change the mission of the Fed to serve all society not just bankers and investors. But the Fed was set up in 1913 to only lend to the banks, and since 2018 the shadow banks which now control more assets than the commercial banks like Chase, Wells, Citi, etc.

As for proposing a Debt Jubilee that's just nonsense. So long as there's a capitalist system the capitalists will never allow a debt forgiveness on a major scale. You'd have to change the system before to allow it.

What about guaranteed basic income? Something like that is inevitable. McKinsey Consultants recently estimated that Artificial Intelligence technology, or AI, will destroy 30% of all the job occupations in the US by 2030. Already more than 50 million of the US labor force are part time, temp, gig or what's called 'contingent' or precariat labor force. They're working two and three part time jobs to make ends meet and still can't. AI will drive that total to well over half of the labor force. The system just can't manage that many low and underpaid workers. Consumption will collapse, despite providing ever more household debt to fund consumption. However, as most are proposing guaranteed basic income now, it smacks of welfare and that makes it an easy ideological target for capitalists. It's all about raising wages and creating real jobs that families can survive on. We need to be more creative than just UBI. But it does bring attention to the crisis of insufficient wage income for tens of millions of Americans, mostly young workers and the older that are forced to work into their seventies and until they drop.

Funding medicare for all? It's possible to envision how the Fed, as the epicenter of a public banking system (part of my proposal) could provide funding for the infrastructure for medicare for all, in a new layer of clinics and public doctor offices locally. But the real funding for Medicare for all should come from taxing financial markets. That would be more acceptable to voters. Ditto for Green New Deal initiatives.

Progressives enamored with public banking or other monetary solutions (i.e. Modern Monetary Theory advocates) tend to over estimate the potential for monetary solutions to the economic crisis now maturing long run, as real investment continues to slow, productivity falls, prices tend toward stagnation and deflation (wages, interest rates, goods & services), global growth slows, and capitalists turn increasingly to financial asset markets to make their profits instead of past approaches of making things and new services that are useful and provide income for consumption. That is the 'slow grinding crisis' of capitalism today.

I support a public bank, but only as a small part of a larger solution that must include fiscal policy, industrial policy, and external (trade, exchange rate, money flows) policies. Money and banking are only part of the new program needed. But the program means nothing without political organization. The lack of that is the key characteristic of the time we live in. It all comes down to the organization question. Where can people turn to participate in realizing the new ideas? Not the Democratic Party. Certain not the Trumpublicans (there's no Republican Party left, it's now Trump's). And the unions, as they grow weaker, turn to the Dems to save their ass. So forget a labor party based on the unions. That's nostalgia of the 1930s. Won't come again.

MMT theory is just another equilibrium theory that concludes that money can be created without limit, just use it for progressive programs. I don't believe that. The Fed's free money for the bankers and investors since 1980, and especially since 2000, and accelerating after 2009, is leading to unsustainable deficits and debt. The $22 trillion will be $34 trillion in less than ten years. And the interest on it will be $900 billion a year, per the CBO. That means capitalists will either have to give up their tax cuts, reduce their war spending budget, or….massively attack social security, medicare, education, etc. Guess which one is coming? The Trumpublicans make no apologies for it; and the Dems lie about how they won't either.

Meanwhile, Sanders keeps acting the political Don Quixote tilting at the Dem party, trying to reform it, which keeps shitting on him and will do so perpetually. The Warrens, Bookers, and other ersatz progressives will 'talk the talk', the Dem party moneybags and leaders will encourage them to do so in order to outflank and dissipate Sanders' progressive message, but in the end whomever of the progressives gets the next Dem presidential 2020 nomination, the Party leaders will ditch their proposals and programs and bring them in line. Don't forget Obama in 2008, sounding like a progressive, but once in office put the bankers back in charge of his administration. But Biden's the front runner anyway. So it's not likely the party will even choose Warren, Booker, or any of the other ersatz progressive wannabes and Sanders clones.

In short, while I've probably written more about central bankers and financial markets than most 'on the left' (latest book coming in March is 'Alexander Hamilton and the Origins of the Fed'), I'm not a proponent of primary reliance on monetary policy and banking system restructuring as a solution. And nothing matters without having first resolved the 'organization question'.

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This article was originally published on the author's blog site: Jack Rasmus.

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