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Are Trump’s Policies Hurting Long-Term US Growth?

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CAMBRIDGE – President Donald Trump regularly thumps his chest and claims credit for each new uptick of the fast-growing US economy. But when it comes to economic performance, US presidents have considerably more influence over long-term trends than over short-term fluctuations.
To be sure, Trump’s tax cuts and spending hikes have provided some extra short-term stimulus. So too, apparently, have foreign buyers of US products such as soybeans, who are rushing to stock up before the tariff war fully heats up. Still, it is not easy to speed up a $20 trillion economy, even by running a budget deficit of nearly $1 trillion, as Trump’s administration is doing. In fact, short-term fluctuations in business inventories have arguably held down growth as much as other factors have temporarily propped it up.

In a cantankerous political environment, it is not easy to think about the long term. But, thanks to the magic of compound interest, measures that marginally raise long-term growth matter a lot. For example, the transportation deregulation policies of President Jimmy Carter’s administration in the late 1970s set the stage for the Internet retail revolution. President Ronald Reagan’s massive tax cuts in the 1980s helped restore US growth in the ensuing decades (but also exacerbated inequality trends). And President Barack Obama’s efforts (and before him President George W. Bush’s) to contain the damage from the 2008 financial crisis underpin the strong economy for which Trump wants to take full credit.

What will be the cumulative effect of Trump’s economic policies on the economy ten years from now? Political ruckus aside, the jury remains out.

Let’s start with the likely positive side of the ledger. The end-2017 corporate tax reform was one of those rare instances where the US Congress comprehensively streamlined and improved the US’s Byzantine tax system, though the corporate tax rate should have been set at 25%, not 21%.

Obama would likely have been very happy to pass a similar bill. But, during his presidency, the Republican-controlled Congress insisted that any proposal had to be "revenue neutral" even in the short term, which is a tough political hurdle for any fundamental tax reform. Trump's efforts to scale back regulation, particularly on small and medium-size businesses, are probably also a plus for long-term growth, reversing some excesses that crept in at the end of Obama's term (though Trump is throwing out good regulations with bad ones).

One little-noticed area where the Trump administration seems to be trying out fresh thinking is the retraining of displaced workers and the improvement of vocational training at the high-school level. In principle, technology and big data allow the federal government to help provide better information to parents and workers on what skills are most in demand, and well as the geographic location of jobs.

The president's daughter, Ivanka Trump, is spearheading the effort. While it is easy to be cynical (some say the new program is just an excuse to cut funds from existing retraining programs), the idea that digital platforms can massively improve re-education and training is a good one.

But while the Trump administration has strengthened the US economy's long-term growth potential in some ways, the other side of the ledger is rather grim. For starters, a wide range of studies – from the work of the late economist David Landes to more recent research by MIT's Daron Acemoglu and the University of Chicago's James A. Robinson – find that institutions and political culture are the single most important determinants of long-term growth. Recovery from the damage Trump is inflicting on institutions and political culture in the US may take years; if so, the economic costs could be considerable.

Moreover, in accordance with the administration's disdain for science, the proposed budgets for basic research, including for the National Institutes of Health and the National Science Foundation, were reduced sharply (fortunately, the US Congress rejected the cuts). And anti-trust enforcement, needed to counter excessive monopoly power in many parts of the economy, is essentially dormant. That will exacerbate inequality over the long term; Trump's coal mines and trade tariffs are at best band-aids on a bullet wound.

Last, but not least, many of the regulations that Trump is targeting ought to be strengthened, not eliminated. It is hard to imagine that gutting the Environmental Protection Agency and withdrawing from the Paris climate agreement are helpful for long-run growth, given that the costs of cleaning up pollution later vastly exceed the costs of mitigating it today.

As for financial regulation, the reams of new rules adopted after the 2008 financial crisis have been a dream come true for lawyers. Rather than try to micromanage banking, it would be far better to ensure that shareholders have more "skin in the

game,” so that big banks are more inclined to avoid excessive risk. On the other hand, neutering existing legislation without putting anything adequate in its place sets the stage for another financial crisis.

So, although the US economy is indeed growing rapidly, the full extent of Trump’s economic legacy might not be felt for a decade or more. In the meantime, should a downturn come, it will not be Trump’s fault – at least according to Trump, who is already gearing up to blame the US Federal Reserve for raising interest rates and ruining all his good work.

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