

# **The Outlook for the U.S. Economy and the Policies of the New President**

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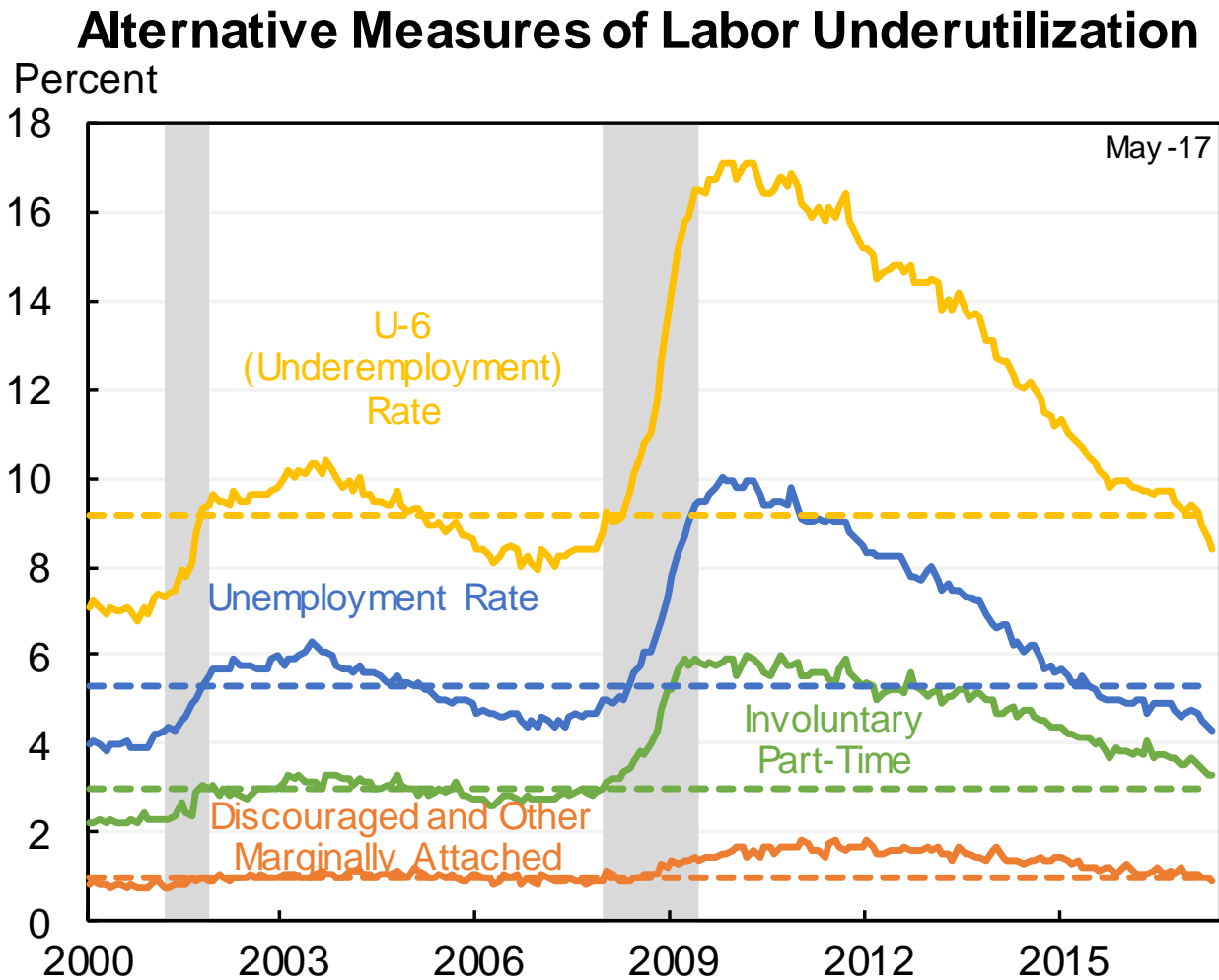
**June 12, 2017**



## Outline

- 1. The short-run outlook**
- 2. The prospects for long-run growth**
- 3. The challenges of inequality and labor force participation**
- 4. President Trump's policy agenda**

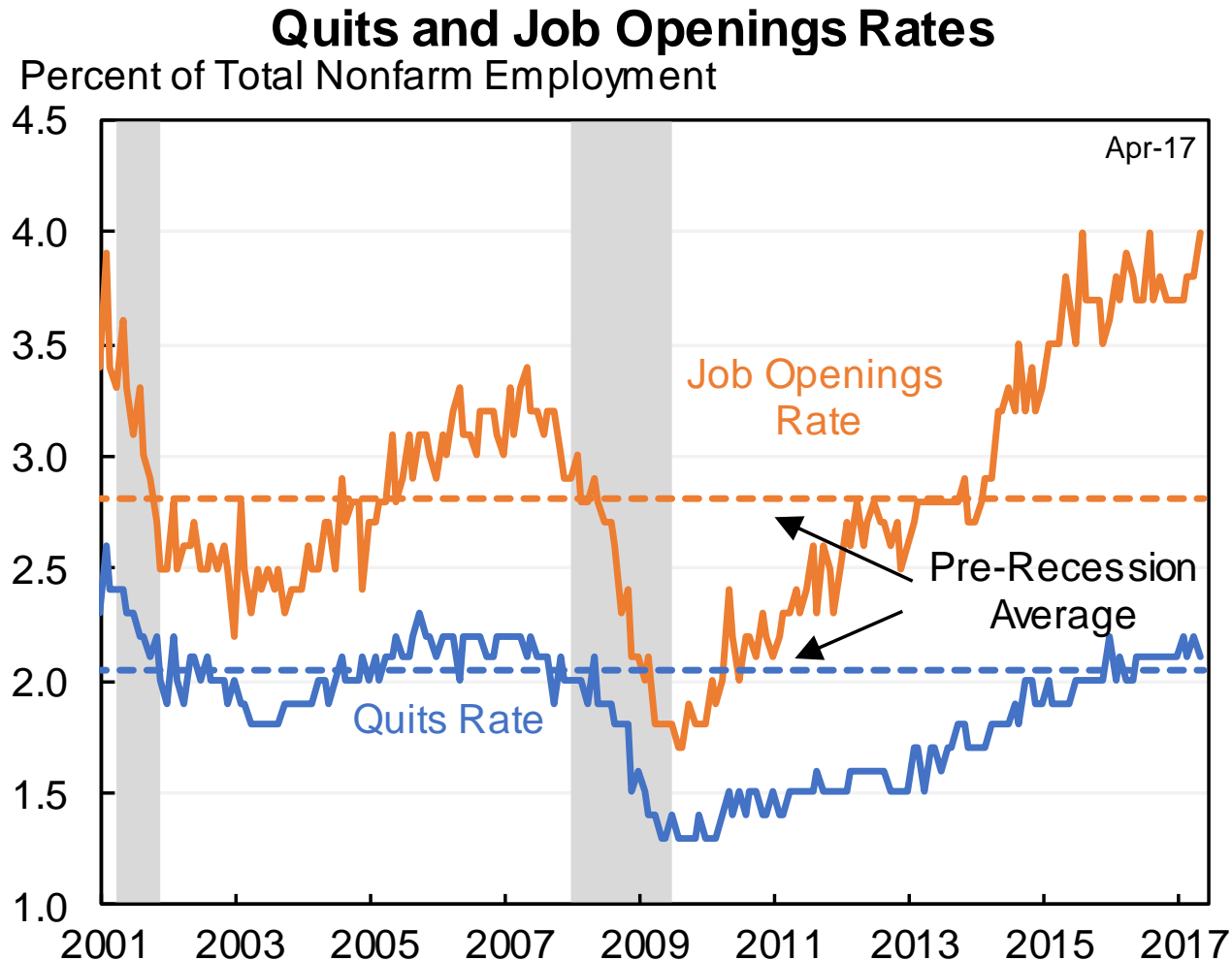
# Measures of Labor Underutilization Have Recovered



Note: Dashed lines indicate averages from December 2001 to December 2007. Shading denotes recession.

Source: Bureau of Labor Statistics, Current Population Survey; author's calculations.

# The Quits Rate is Above Its Pre-Recession Average, While Openings Are Tied for A Record High



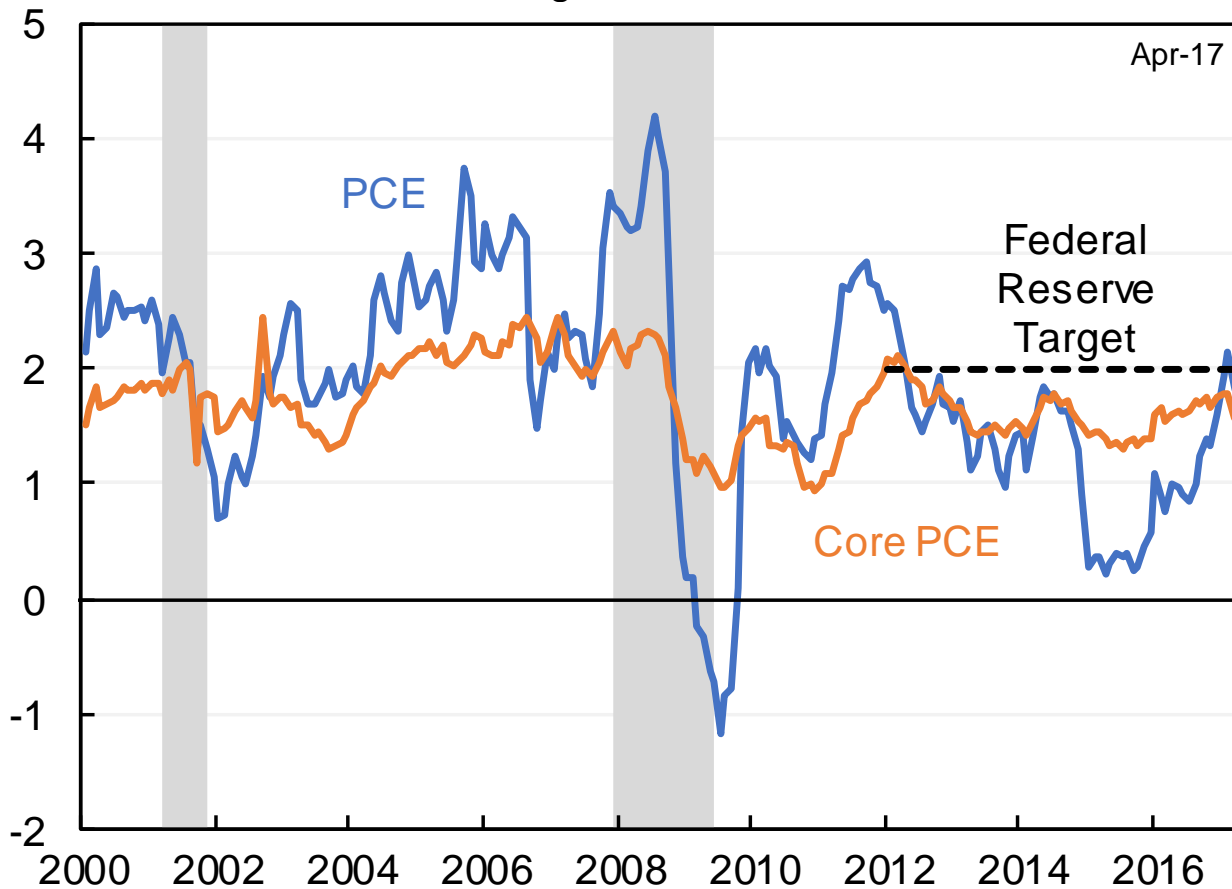
Note: Dashed lines indicate averages from December 2001 to December 2007. Shading denotes recession.  
Source: Bureau of Labor Statistics, Job Openings and Labor Turnover Survey; author's calculations.

# Inflation Has Generally Been Below the Federal Reserve's 2-Percent Target



## Personal Consumption Expenditures Price Inflation

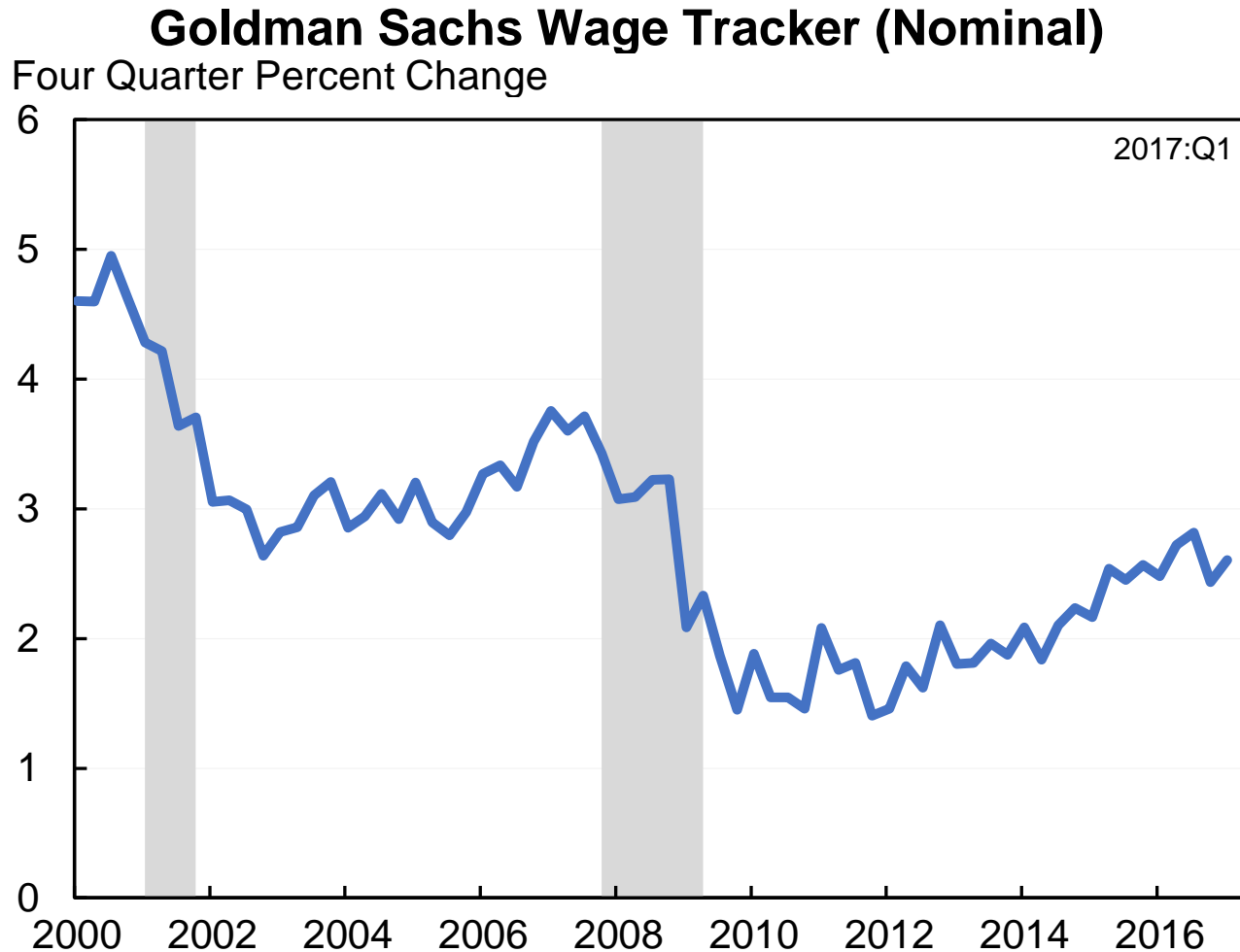
Twelve-Month Percent Change



Note: Shading denotes recession.

Source: Bureau of Economic Analysis, National Income and Product Accounts; Federal Reserve; author's calculations.

# Compensation Growth Has Been More Mixed...

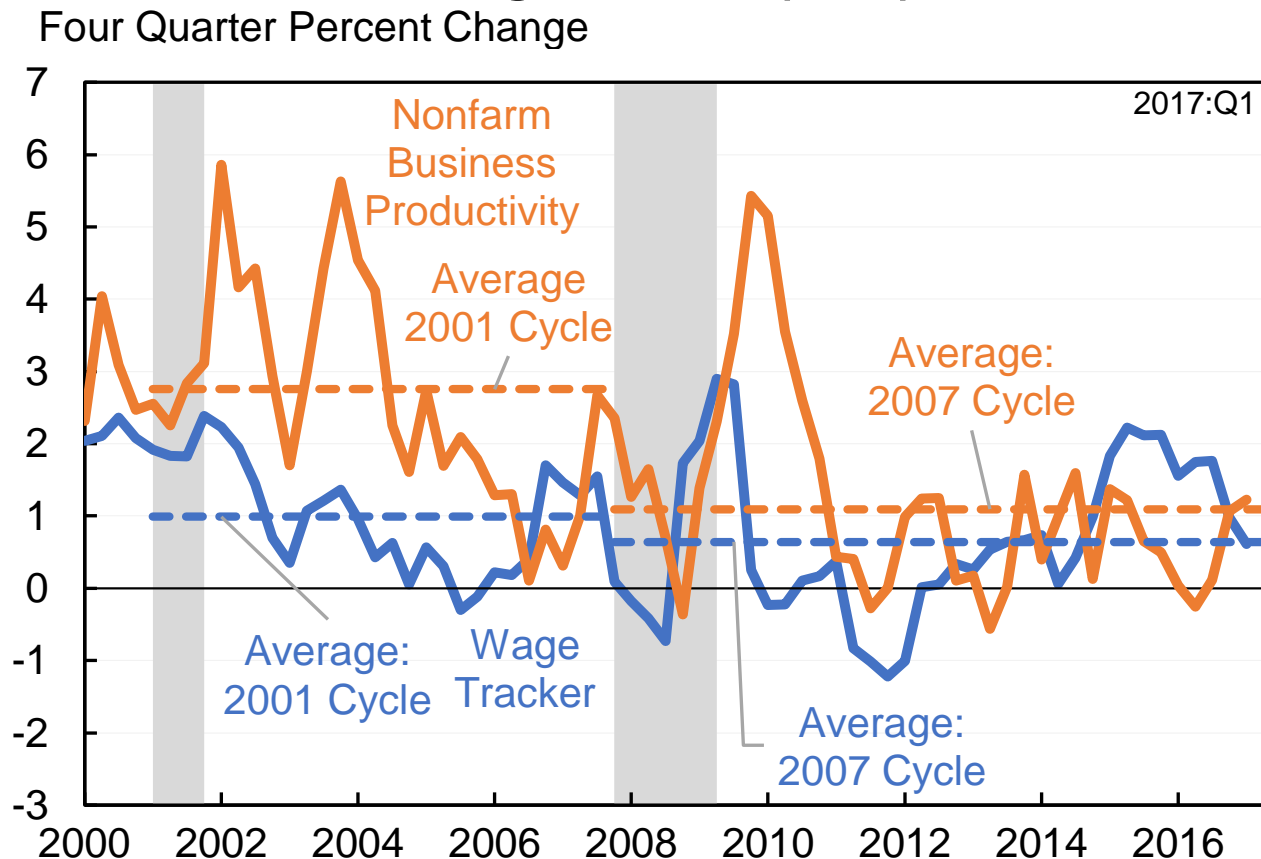


Note: Shading denotes recession.  
Source: Goldman Sachs; author's calculations.

# ...But Real Compensation About What Would Be Expected in a Low Productivity World



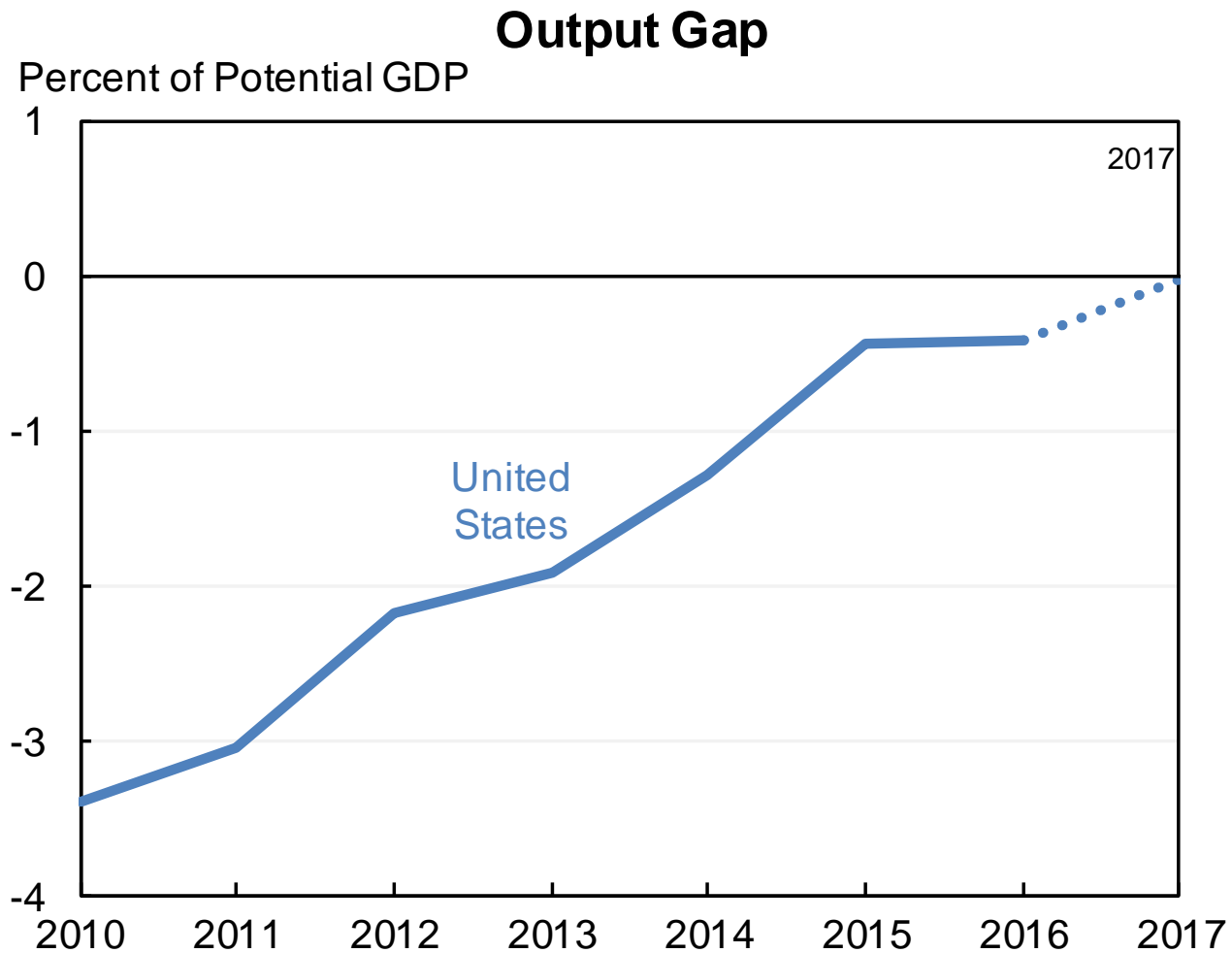
## Productivity Growth and Goldman Sachs Wage Tracker (Real)



Note: Shading denotes recession. Compensation adjusted for inflation using the CPI-U price index.  
Source: Goldman Sachs; Bureau of Labor Statistics; author's calculations.



# Gaps Have Closed In the United States

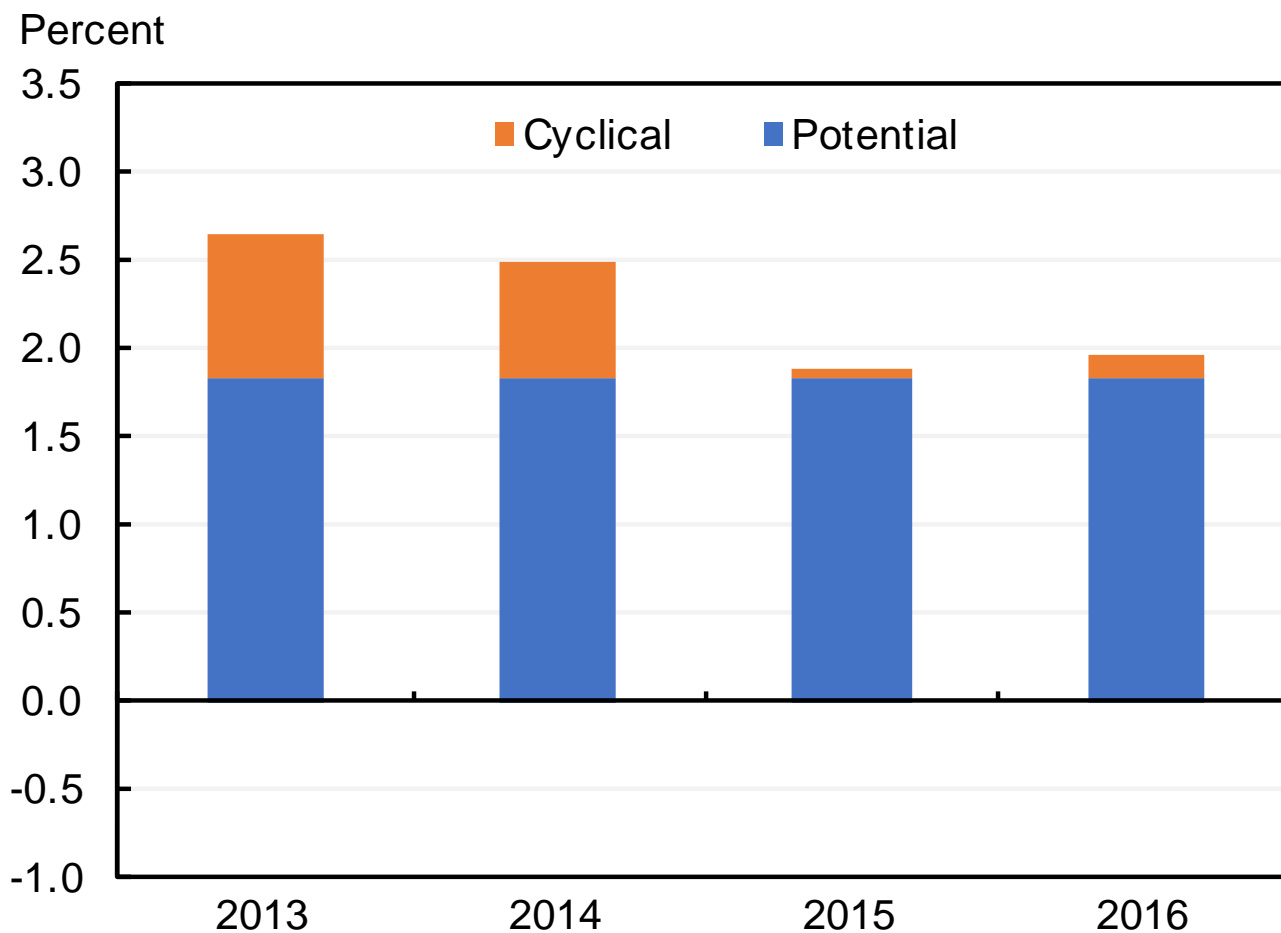




# Going Forward Growth Will Primarily Come from Potential



## Real GDP Growth: Actual vs. Potential



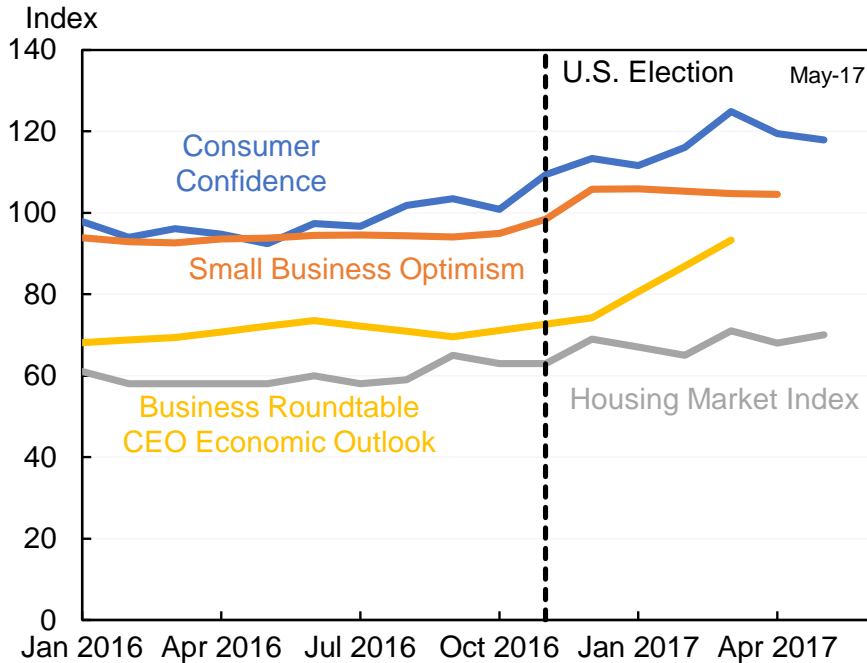
Note: Potential GDP growth is the intercept of an Okun's law regression using four-quarter changes in real GDP and the employment-population ratio from 2007:Q1 to 2016:Q4. All growth rates are Q4/Q4 for the year shown.

Source: Bureau of Economic Analysis, National Income and Product Accounts; Bureau of Labor Statistics, Current Population Survey; author's calculations.

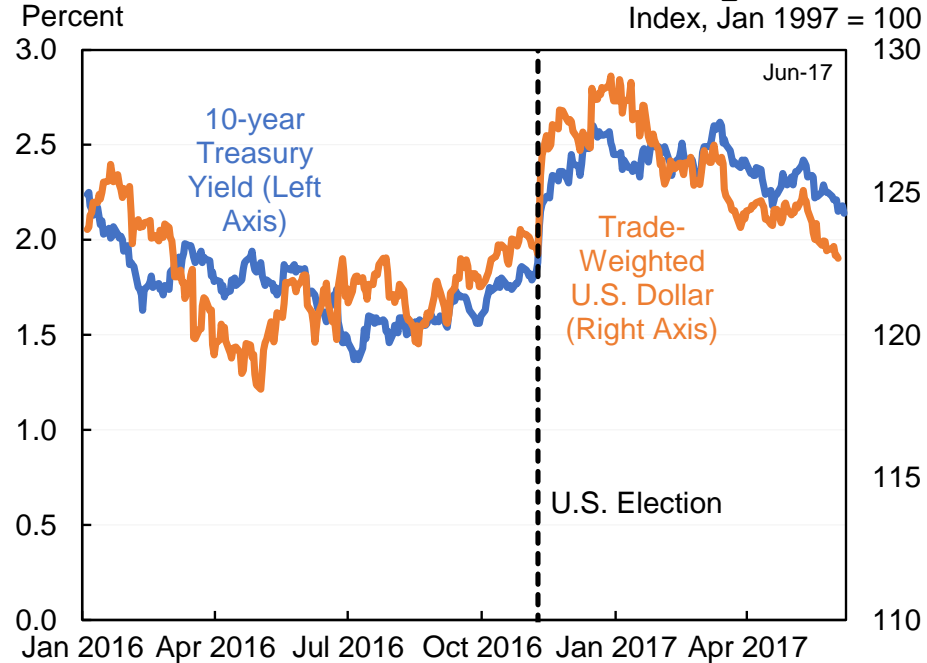
# Measures of Optimism Have Remained Strong Even While Financial Markets Appear to No Longer Be Expecting Stimulus



### Consumer and Business Confidence

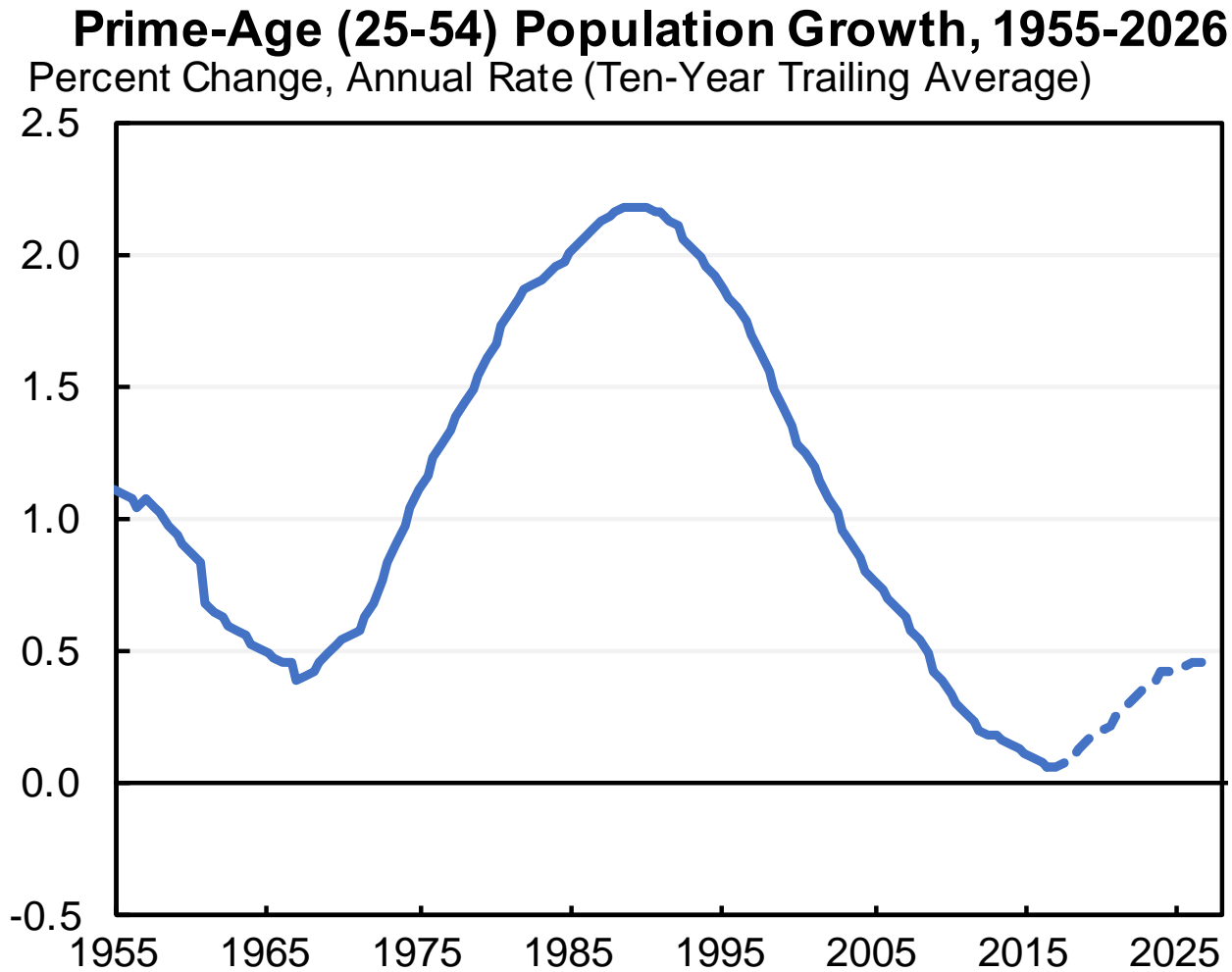


### Government Bond Yields and Exchange Rates





# The Demographic Headwind to Future Growth

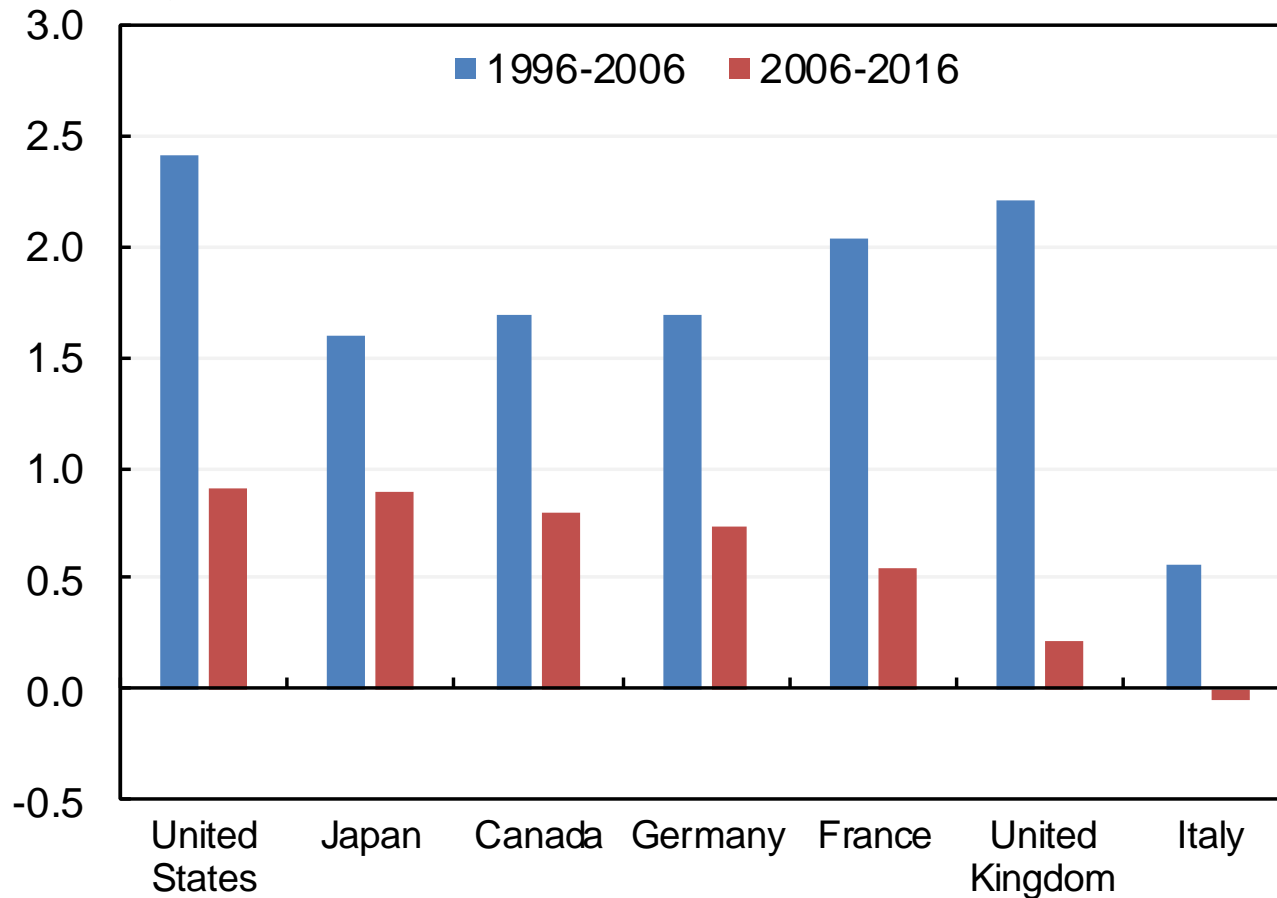


# The Worldwide Productivity Slowdown is Not Helping, Either



## Labor Productivity Growth, G-7 Countries

Percent, Annual Rate



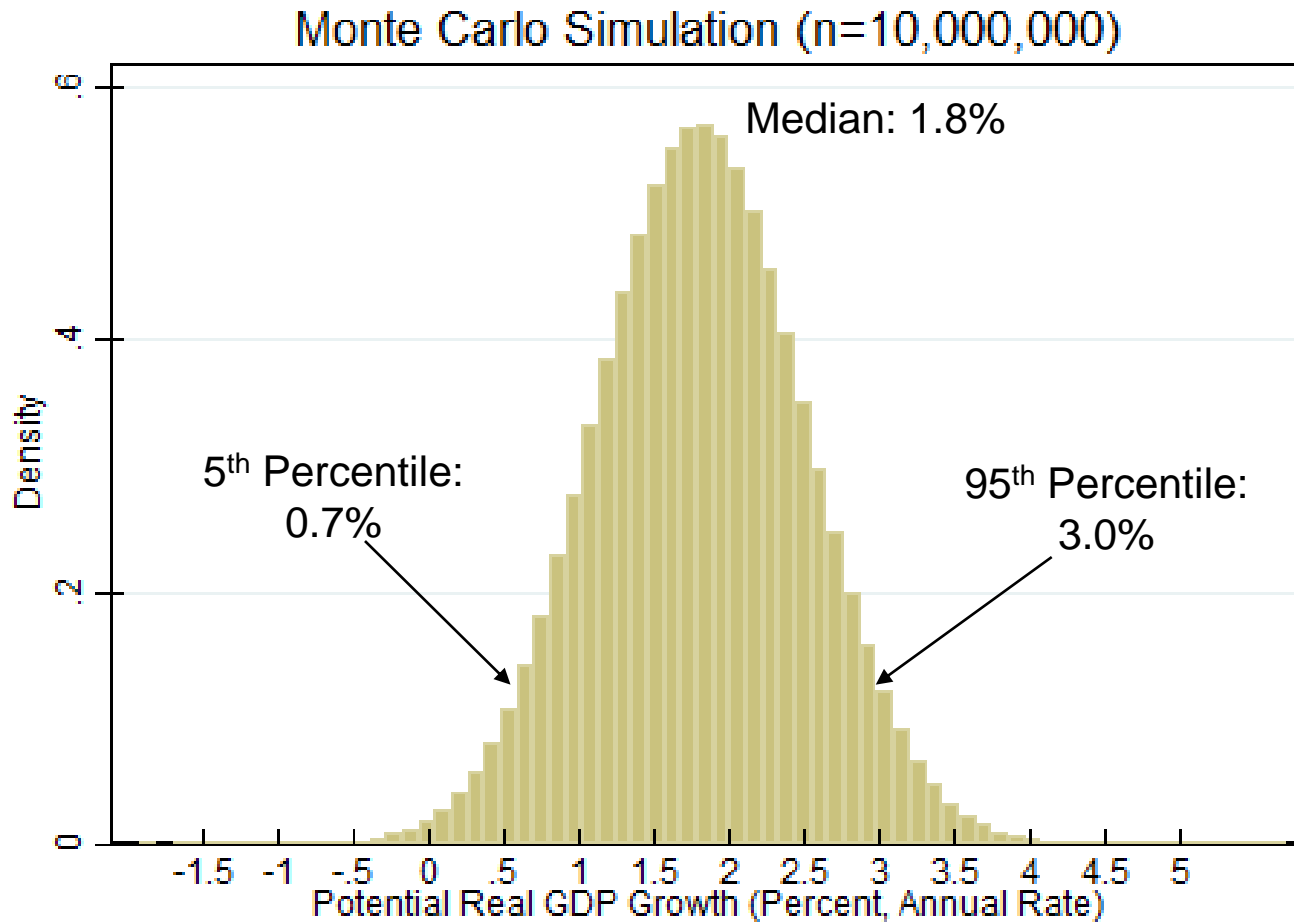


# The Base Case for Potential Growth

## CBO: Selected Components of Potential Real GDP Growth, 1953-2026

Component	Growth Rate, Percentage Points at Annual Rate	
	History	Forecast
	1953 to 2007	2016 to 2026
Population	1.4	0.8
Potential labor force participation rate	0.2	-0.4
Potential real output per hour (productivity)	2.1	1.7
Other	-0.5	-0.3
<b>Potential real GDP</b>	<b>3.3</b>	<b>1.8</b>

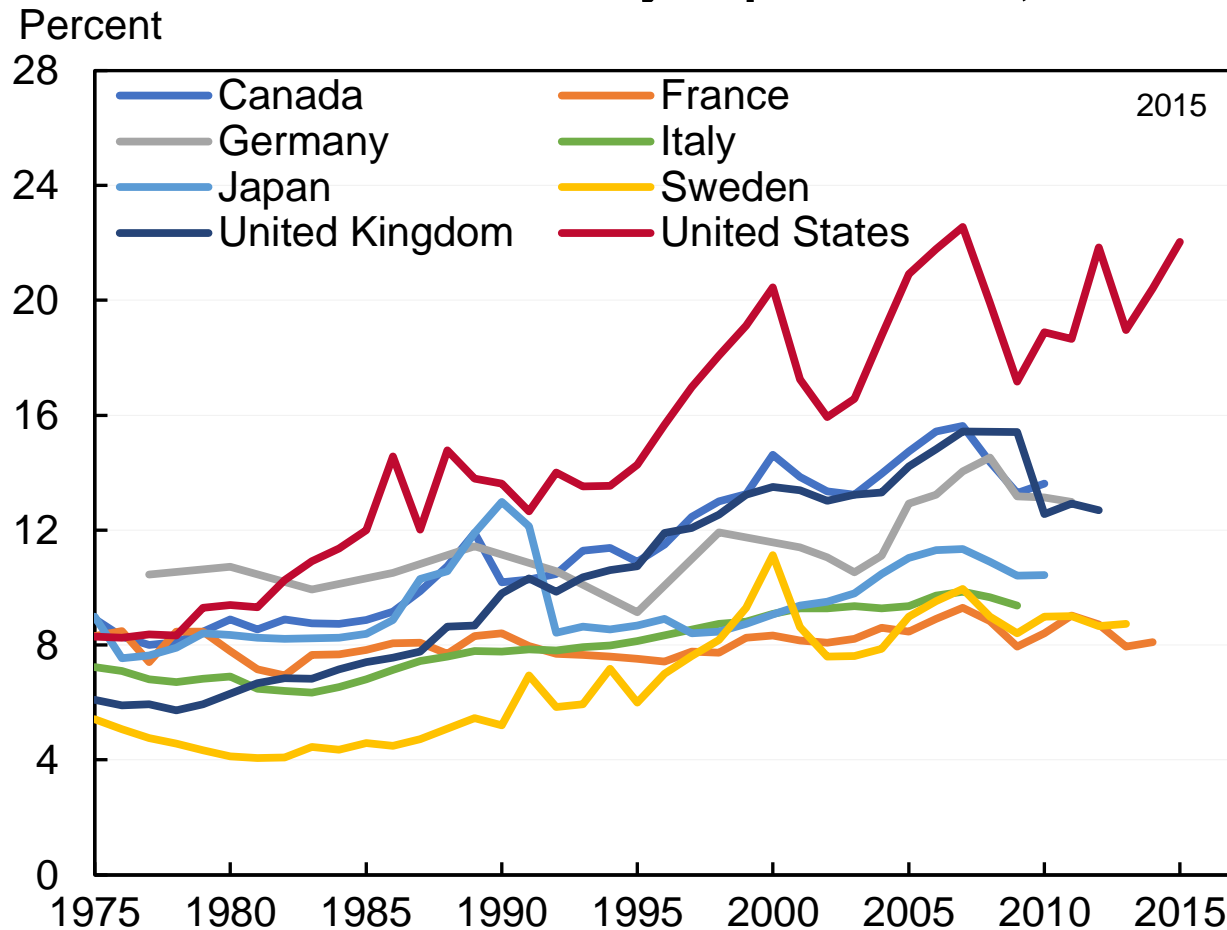
# Alternative Scenarios For U.S. Potential Growth



# Top 1% Share Has Risen Further and Faster in the United States



## Share of Income Earned by Top 1 Percent, 1975-2015

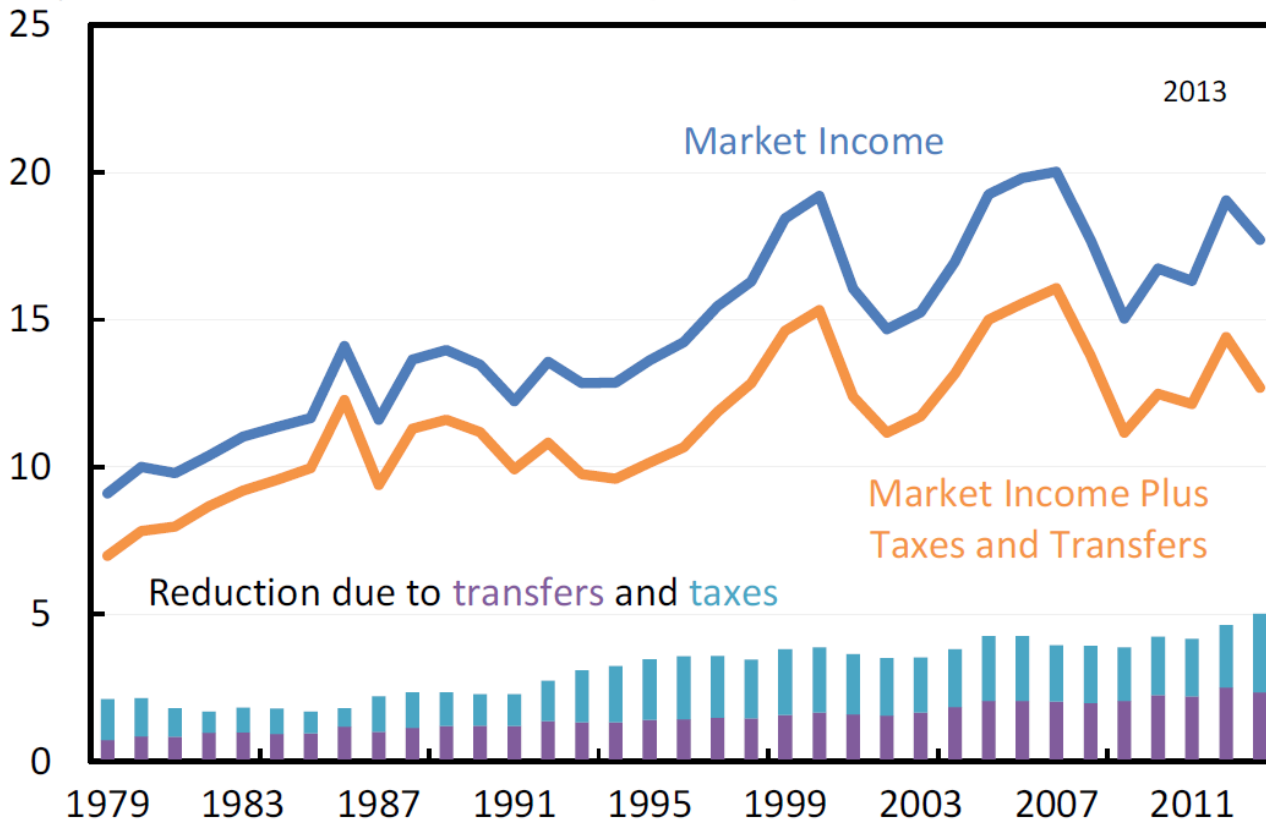


# Taxes and Transfers Have Played a Bigger Role In Reducing Top 1% Inequality in the United States...



## Top 1 Percent Share of Income and the Effects of Taxes and Transfers, 1979-2013

Top 1 Percent Share of Total Income (Percent)

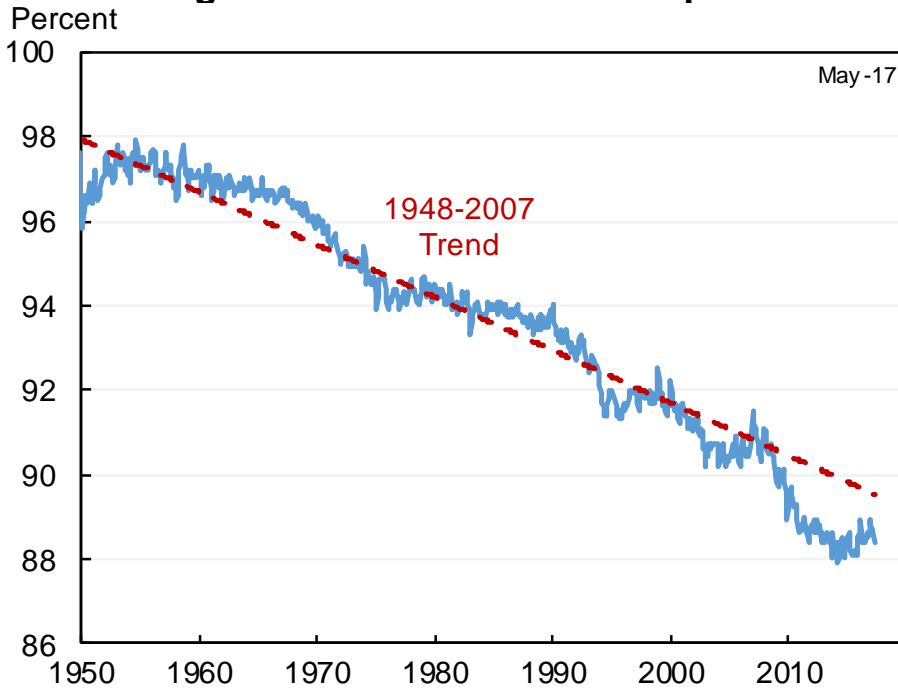




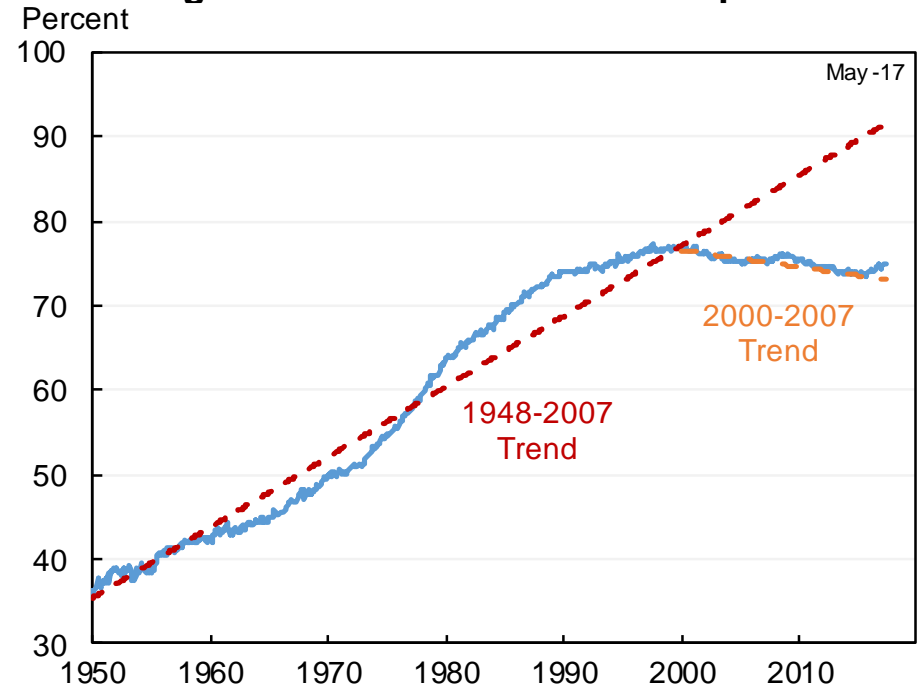
# Inequality Compounded by Continued Decline in Labor Force Participation for Prime Age Workers



## Prime-Age Male Labor Force Participation Rate



## Prime-Age Female Labor Force Participation Rate

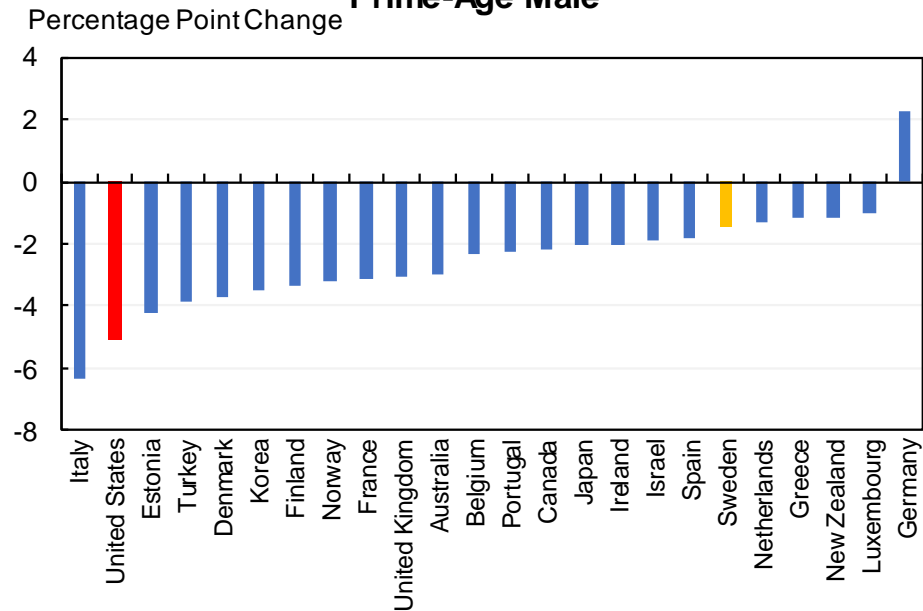


# The Decline Has Been Larger than Almost Any Other OECD Country

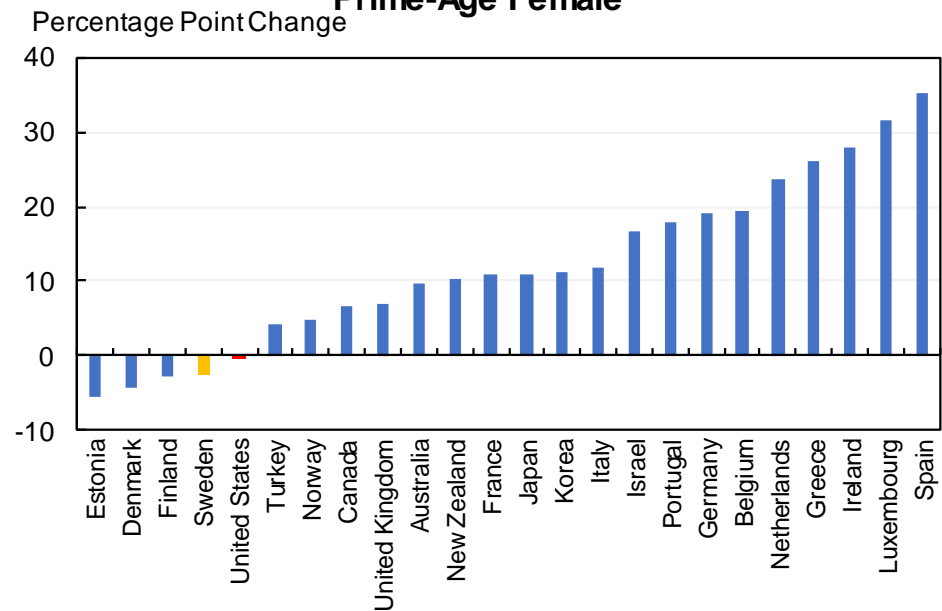


## Change in Labor Force Participation Rates Across the OECD, 1990-2015

**Prime-Age Male**



**Prime-Age Female**



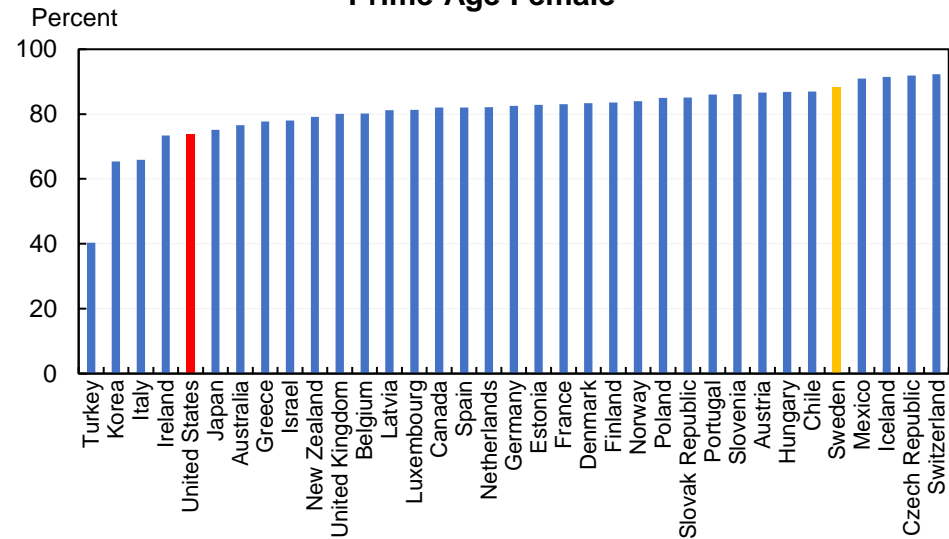
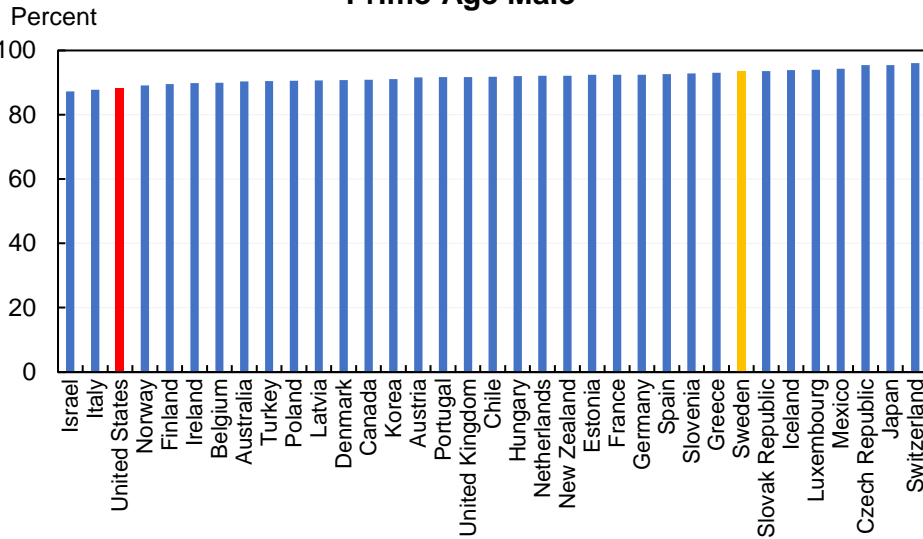
# Putting the United States Toward the Bottom of the OECD in Prime Age Labor Force Participation



## Labor Force Participation Rates Across the OECD, 2015

Prime-Age Male

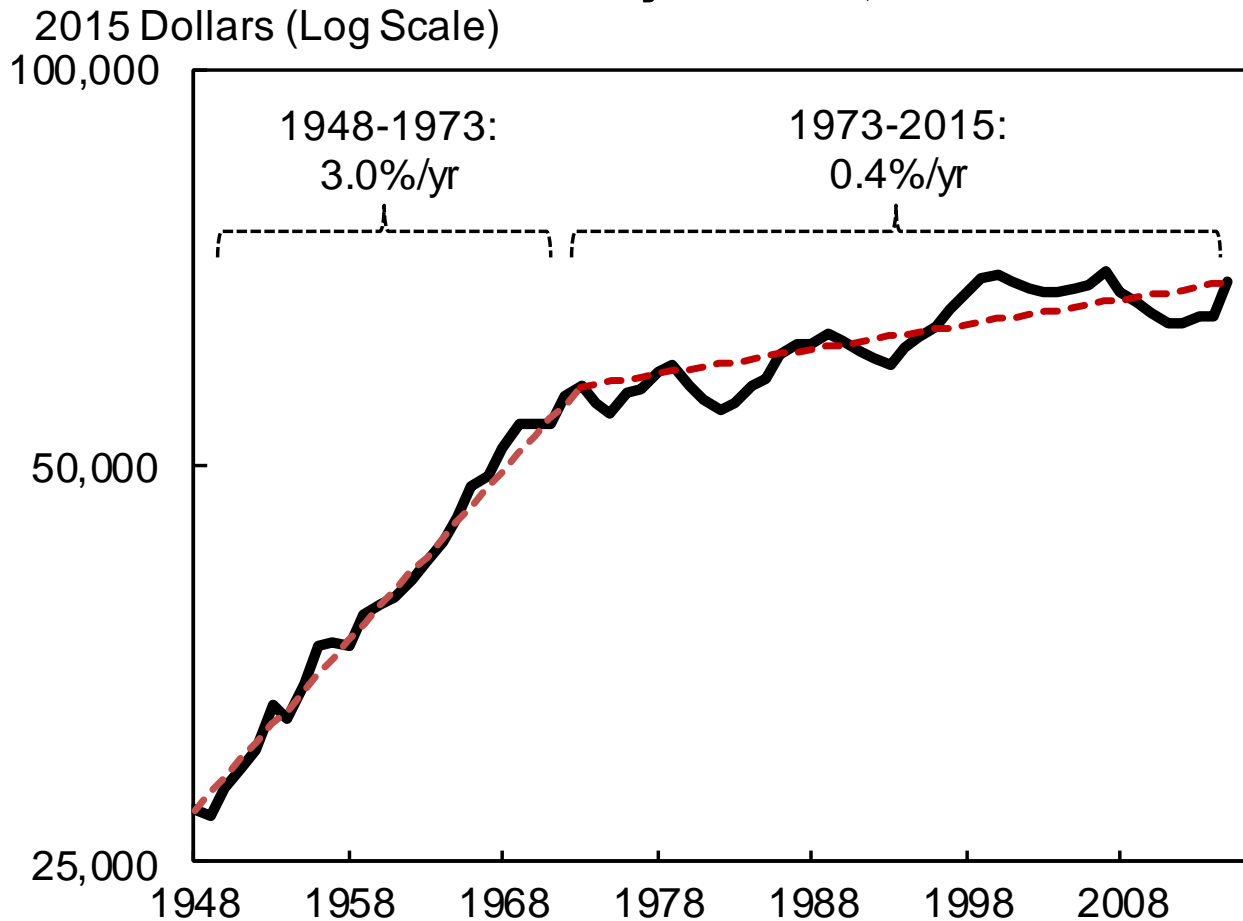
Prime-Age Female



# Slower Productivity, Rising Inequality, and Declining Participation Have Combined to Slow Median Income Growth



## Real Median Family Income, 1948-2015





# The Policy Agenda

## 1. Fiscal Policy

- a) Tax Policy
- b) Infrastructure
- c) Other fiscal changes
- d) Fiscal trajectory

## 2. Regulation

## 3. Immigration

## 4. Trade

## 5. International Cooperation

# Tax Policy



**Tax cuts or tax reform?**



# Tax Policy

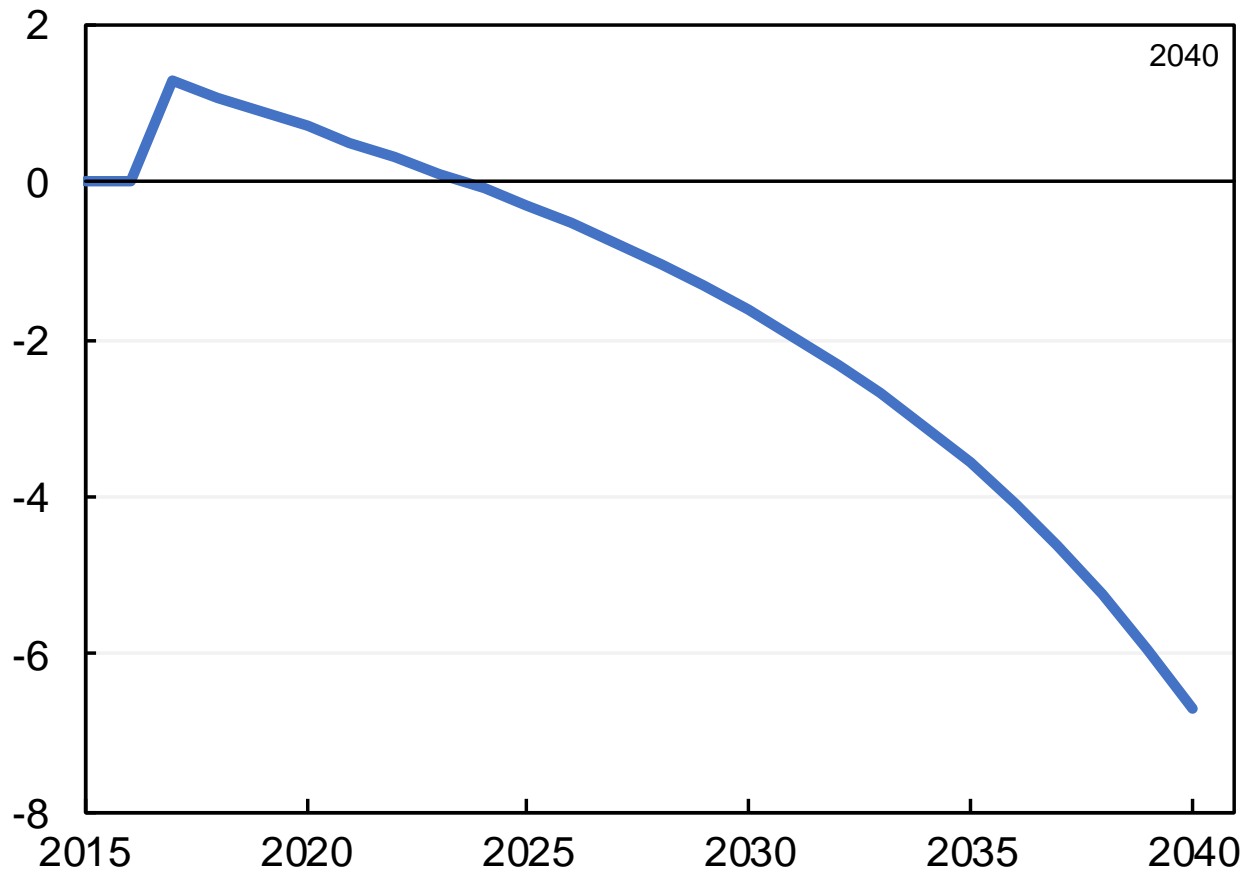
	Current Law	President's Principles	House Republicans
Corporate Rate	35%	15%	20%
Expensing / No interest Deduction	x	x	✓
Border Adjustment	x	x	✓
Top Individual Rate	39.6%	35%	33%
Broader Base		Some	More
Cost		~\$5.5 trillion	Goal is \$0
Share Top 1%		~33%+	99%

# Deficit-Increasing Tax Cuts Could Hurt Long-Run Growth



## Change in Real GDP Under Trump Campaign Tax Plan

Percent Change from Baseline



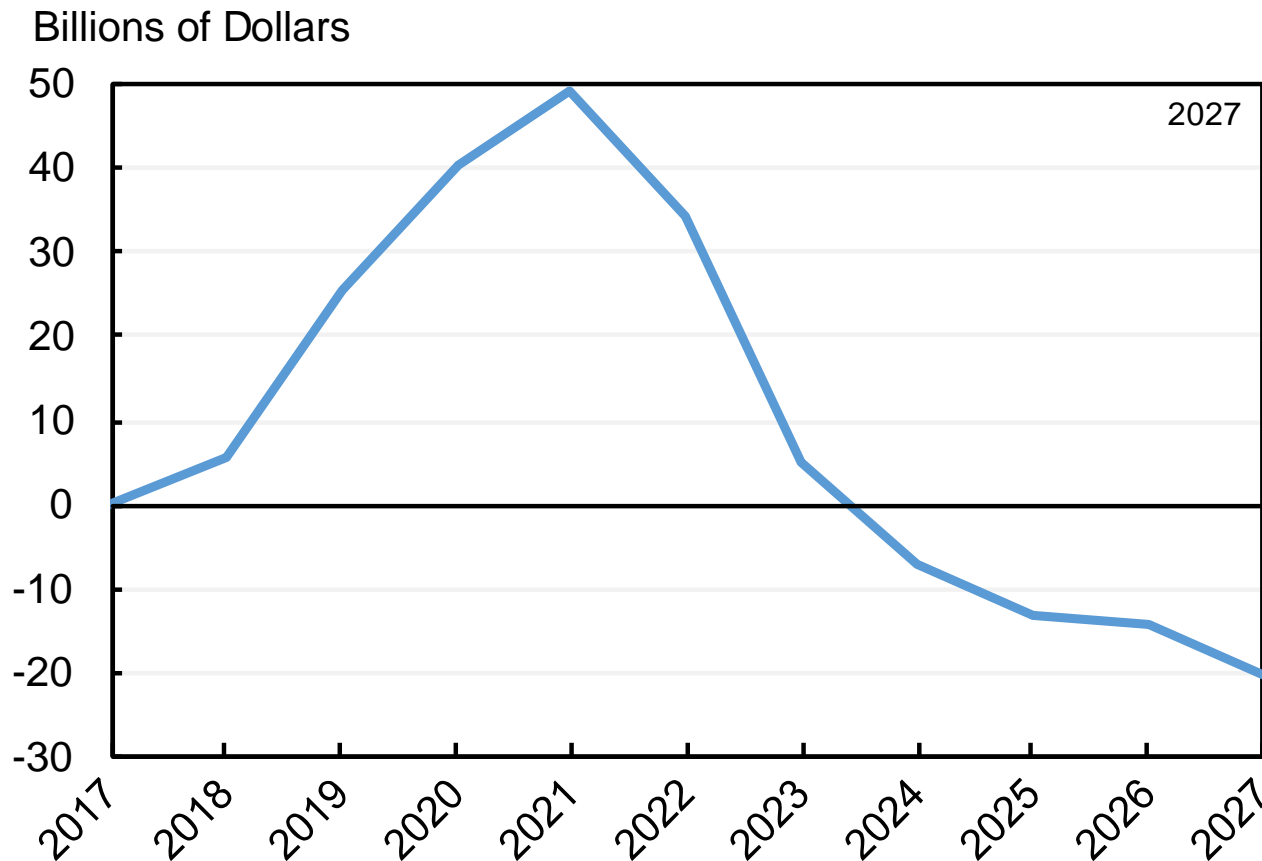
Note: Based on medium elasticities scenario.  
Source: Nunns et al. (2016); author's calculations.





# Infrastructure Proposal: Short-run Increases Followed By Long-term Reductions

## President's FY 2018 Budget: Change in Infrastructure Spending Relative to Baseline by Fiscal Year





## Other Budget Policies

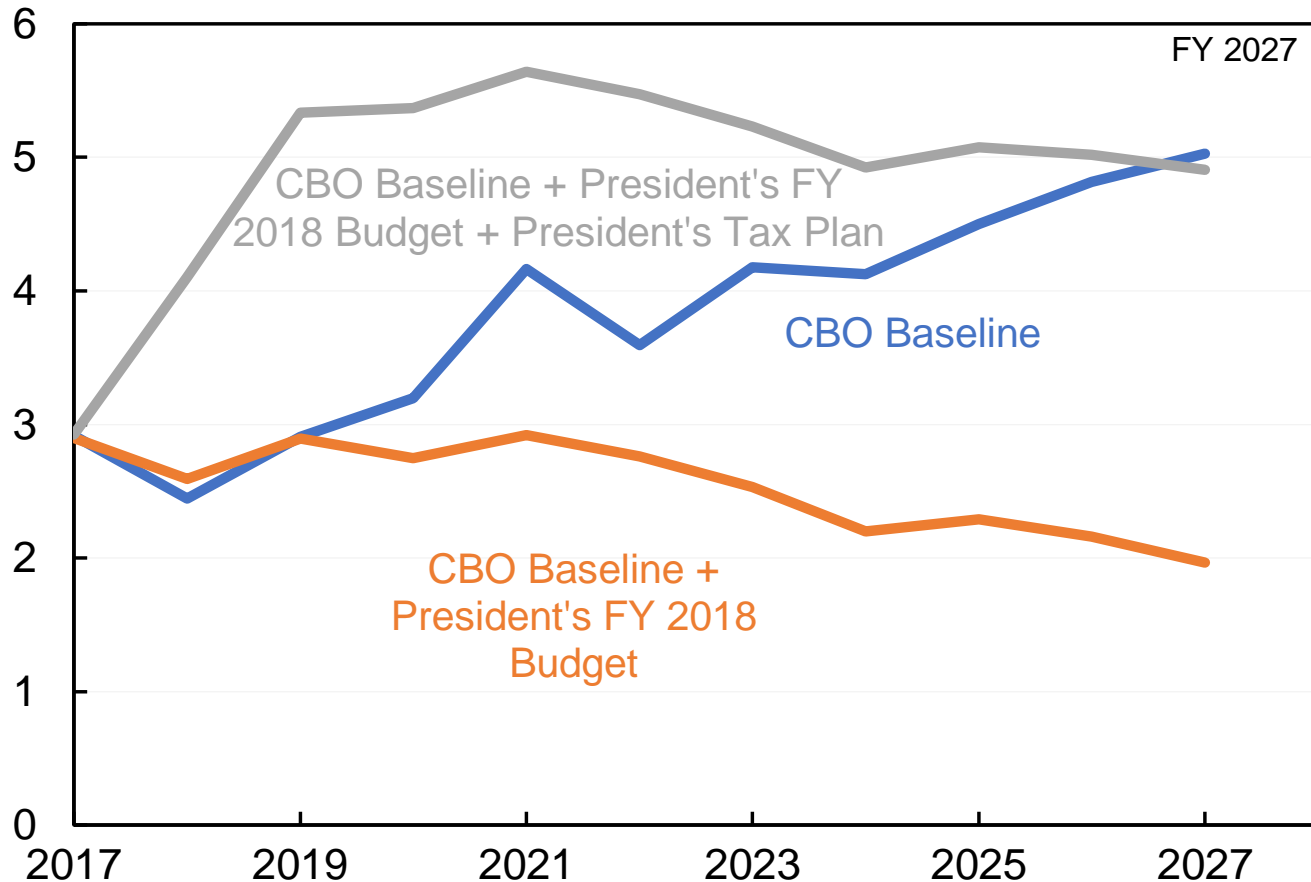
- **8 percent increase in defense spending in FY 2018**
- **13 percent decrease in non-defense spending in FY 2018**
  - 11 percent cut in National Science Foundation
  - 22 percent cut to the National Institutes of Health, including 19 percent cut for cancer research
  - 23 percent cut in financial aid for college
  - 34 percent cut to training and employment programs
- **\$2.5 trillion decrease to low- and moderate-income programs over ten years, 15 percent reduction**
- **Repeal/replace of the Affordable Care Act—including health reductions to pay for high-income tax cuts**

# Overall Fiscal Outlook Under Current Law and the President's Policies



## Federal Deficit as a Percent of GDP, FY 2017 - FY 2027

Percent of GDP





# Regulation

- The Trump Administration has expressed interest in reducing regulation across a number of sectors: e.g. banking, health care, energy markets, labor markets
- Effects of deregulation on growth are likely to be small
  - One estimate is that full repeal of Dodd-Frank would add 0.06 p.p. to annual growth rate (Holtz-Eakin 2015)—effects of partial repeal are smaller
- Growth effects of deregulation also limited because of less control over State and local regulation
- In most likely case, deregulation could add at most 0.1 p.p. to growth rate



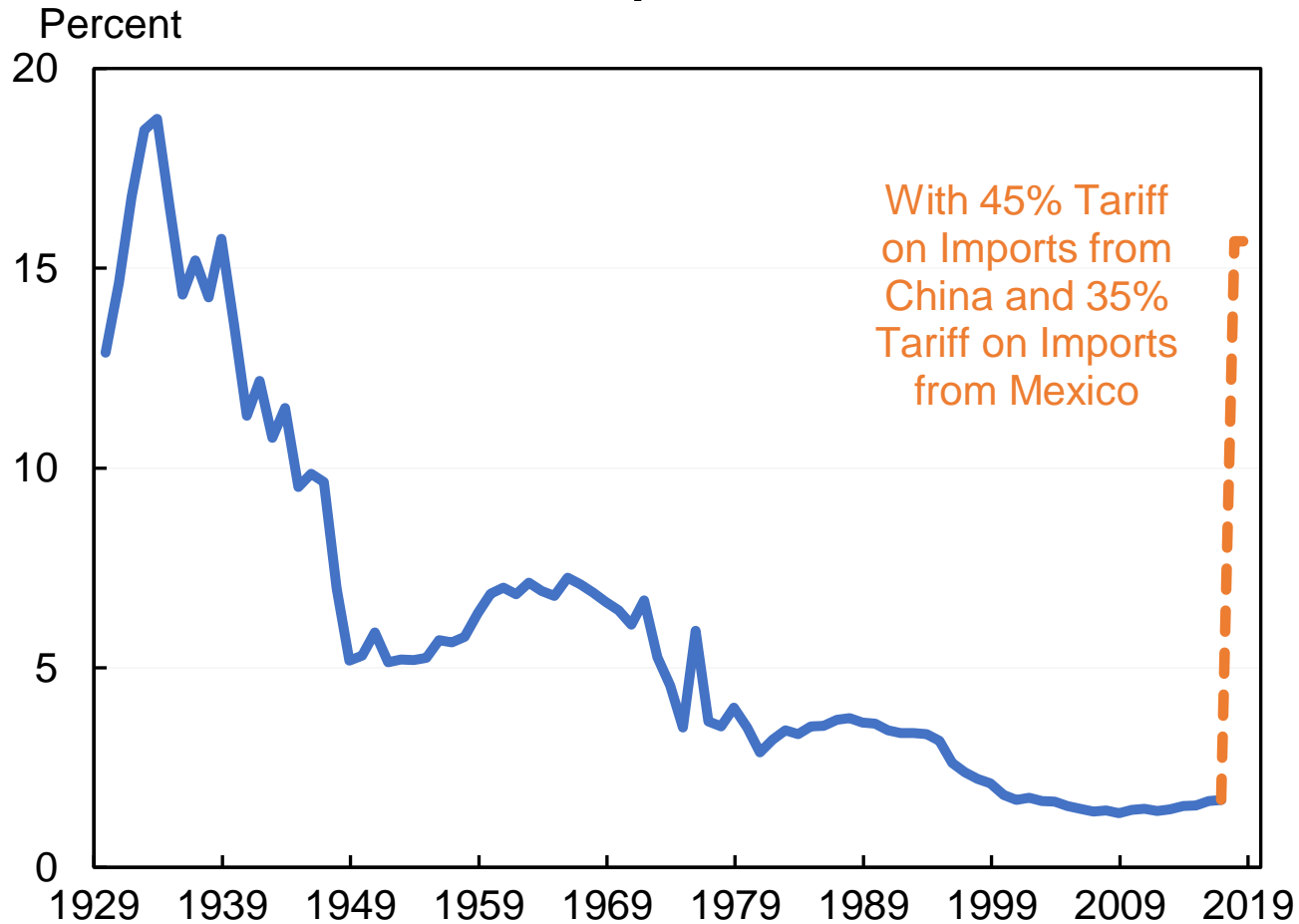
# Immigration

- Restrictions on legal immigration and increased uncertainty for unauthorized immigrants would harm growth:
  - RAISE Act (Sens. Cotton and Purdue) would cut legal immigration in half after a decade
  - Implies reduction in annual growth rate of 0.2 p.p. over next decade

# President Trump Has Not Followed Through on Campaign Promises for a 45% Tariff on China and a 35% Tariff on Mexico...



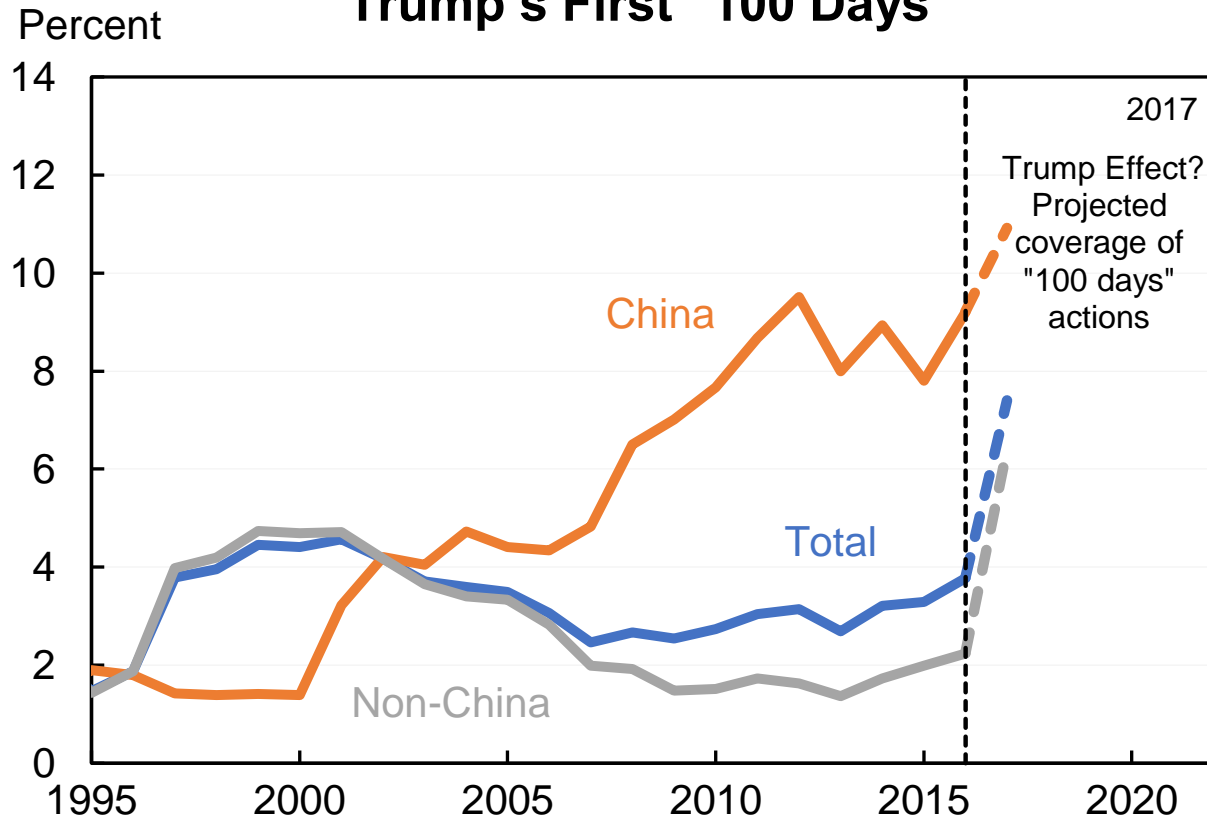
## Effective Import Tariff Rate



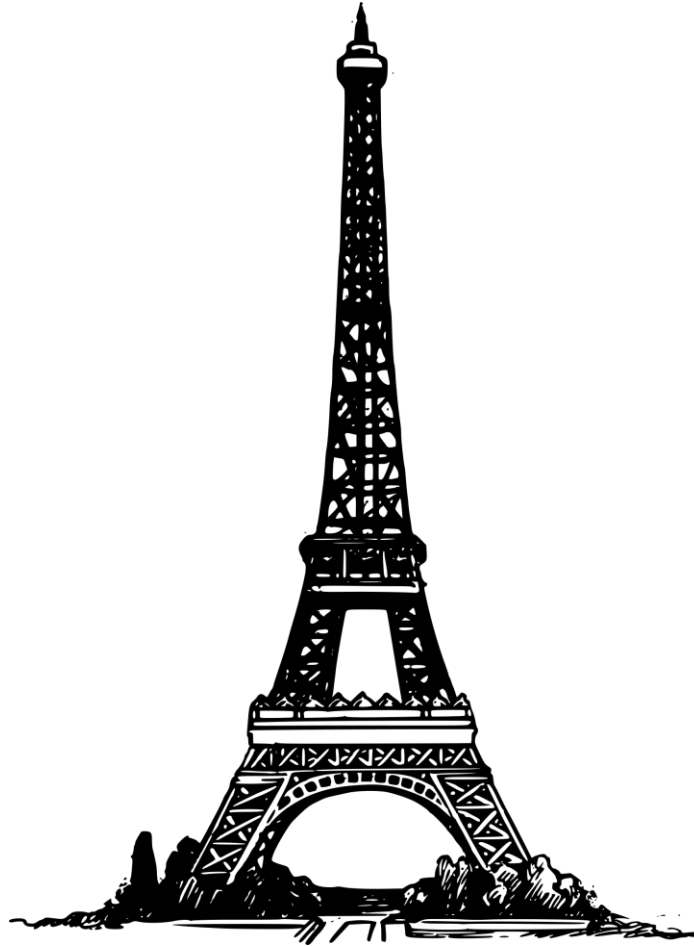
# ...But There Has Been a Significant Increase in Import Restrictions in the First 100 Days



## Share of U.S. Imports Covered by Barriers Imposed under Trade Laws, Including Projection for Trump's First "100 Days"



# Change in U.S. Multilateral Role







## In Conclusion

- U.S. economy at/near full employment. Wage growth is lower than desired largely because of slow productivity growth.
- The outlook is for growth ~2%. This assumes unfavorable demography continues and productivity bounces back somewhat.
- Inequality and labor force participation compound low productivity growth, leading to slow income growth.
- President Trump's policy agenda could hurt growth further—and promote greater inequality of incomes.

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