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Sinai's Economic
and
Market Perspectives

One Policy Change
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The following was a response to a Survey question for an article to appear in The International Economy.

Question:

What if you became President of the United States in January 2013 and could accomplish only one realistic policy change to restore economic growth and employment to historic trend levels? What would that policy change be?

Answer:

Within a context of long-run federal deficit and debt reduction, the *single* most important policy change to head the economy and employment toward historic trend performance would be Tax Reform.

By Tax Reform is meant reductions in individual and corporate tax rates, broadening the tax base by eliminating, phasing-out, or capping some itemized tax deductions taken by households, and eliminating corporate tax "loopholes" including untaxed profits held abroad. Capital gains and dividend tax rates should be zero, as capital gains and dividends are already taxed at both the corporate and individual levels. The zero capital gains tax would only be applied to long-run profits and/or income associated with new jobs.

Such a policy could be designed as revenue neutral, ex-ante, and would be pro-growth, generating, ex-post, tax receipts that could partially offset the costs of the rate reductions.

The incentive effects of lower individual and corporate tax rates, elimination of distortions in the tax system, for example, tax subsidies to housing, health care and others, would lead to efficiencies that would help increase economic and jobs growth.

Proper assessment of any policy, especially a revenue-neutral program, needs to be on a dynamic basis, that is taking account of the growth effects, induced tax receipts, and reductions in federal spending that a stronger economy would entail. Even though individual tax rates would be lower, ex-ante, a source of lost tax revenues, any ex-post gains in growth and employment would generate offsetting increases in corporate profits, excise, social security and capital gains tax receipts.

Similarly, on the corporate side, a tax rate competitive with those of other countries would lead to repatriation of profits held abroad, sizeable amounts, that would enhance corporate balance sheets and stimulate business hiring and capital spending.

In a time both of unsustainable deficits and debt and a huge jobs deficit, no other single policy change could achieve so much, especially when account is taken of the macro- and microeconomic effects of such a policy, ex-post.

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