How’s that tax cut working out?

By Paul Krugman
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So far, Donald Trump and his allies in Congress have achieved one and only one major legislative victory: passing a large tax cut, mainly aimed at corporations and business owners. The tax cut’s proponents promised that it would lead to a dramatic acceleration of economic growth and produce big gains in wages; they hoped that it would also yield big political dividends for the midterm elections.

So how’s it going? Politically, the tax cut is a damp squib: Most voters say they haven’t seen any boost to their paychecks, and Republicans are barely talking about the law in their political campaigns. But what about the economics?

You might be tempted to say that it’s too early to tell. After all, the law has been in effect for only a few months, and we got our first look at post-tax-cut economic growth only last week. But here’s the thing: To deliver on its backers’ promises, the tax cut would have to produce a huge surge in business investment — not in the long run, not five or 10 years from now, but more or less right away. And there’s no sign that anything like that is happening.

Let’s talk about the economics here.

Anything that increases the budget deficit should, other things being the same, lead to higher overall spending and a short-run bump in the economy (although there’s no indication of such a bump in the first-quarter numbers, which were underwhelming). But if you want to boost overall spending, you don’t have to give huge tax breaks to corporations. You could do lots of other things instead — say, spend money on fixing America’s crumbling infrastructure, an issue on which Trump keeps promising a plan but never delivers.

Furthermore, any short-term boost will probably be quickly squelched by the Federal Reserve, which believes that we’re at full employment and which is gradually raising interest rates to keep the economy from overheating. You can argue that the Fed is wrong, but the case for easier monetary policy has nothing to do with the Trump tax cut.

No, the case for a corporate tax cut is the claim that in the long run it will raise wages. How is that supposed to work?

It never made sense to believe that corporations would immediately share their tax-cut bounty with workers, and they haven’t. Any news organizations that let themselves be bamboozled by cherry-picked stories of firms announcing worker bonuses after the tax bill passed should be ashamed of their credulity.

The real logic behind corporate tax cuts is that they’re supposed to lead to higher investment. This investment, in turn, would gradually increase the stock of capital, simultaneously driving down the pretax rate of return on investment and pushing up wages.

There are two questions about this supposed process. One is how much wages will rise in the long run. Most independent estimates predict only modest gains; the Trump administration’s wildly optimistic predictions aren’t just out of the ballpark, they’re in another universe. Still, to be fair, that’s not a question on which the data have had time to speak.

But the other, equally important question is, how long is the long run? As Greg Leiserson of the Washington Center for Equitable Growth points out, “every month in which wage rates are not sharply higher than they would have been absent the legislation, and investment returns are not sharply lower, is a month in which the benefits of those corporate tax cuts accrue primarily to shareholders.” A tax cut that might significantly raise wages during, say, Cynthia Nixon’s second term in the White

House, but yields big windfalls for stock owners with only trivial wage gains for the next five or 10 years, is not what we were promised.

To get major wage gains before, for example, the 2024 election — never mind 2020 — we'd need to have a huge near-term boom in business investment, mainly financed by inflows of capital from overseas. I mean really, really huge. And there's no sign that this is happening.

True, business investment as a share of G.D.P. is up slightly over the past year, but it's still well below its level before the financial crisis — let alone the heights it reached in the 1990s.

Is it just too soon to expect results? Are businesses getting ready to ramp up investment, so that we'll see them laying out the big bucks in the near future? Not according to a survey by the Federal Reserve Bank of Atlanta. A vast majority of businesses say either that the tax law has had no effect on their investment plans, or that they are planning only a modest increase.

In short, the effects of the Trump tax cut are already looking like the effects of the Brownback tax cut in Kansas, the Bush tax cut and every other much-hyped tax cut of the past three decades: big talk, big promises, but no results aside from a swollen budget deficit.

You might think that the G.O.P. would eventually learn something from this experience, realize that tax cuts aren't magical, and come up with some different ideas. But I guess it's difficult for a man to understand something when his campaign contributions depend on his not understanding it.