

The following is the transcript from the AAVC Online Chat on January 29, 2004: "Do tax cuts stimulate job creation?" The text has been edited for flow and typographical errors.

AAVC (Jan 29, 2004 8:32:46 PM)

Welcome, everyone, to AAVC first online chat. Our host tonight is Philip Jefferson '83. The chat will last approximately one hour. I will now turn it over to Philip. Thanks.

Pat Duane Lichtenberg '90 (Jan 29, 2004 8:34:02 PM)

And thanks to Philip for leading this.

Host: Philip Jefferson '83 (Jan 29, 2004 8:34:26 PM)

Hello Everyone. Thanks again for signing up. The economy created 1,000 jobs in December 2003 (a small number.) Does this imply that the tax cuts are not working?

Pat Duane Lichtenberg '90 (Jan 29, 2004 8:34:58 PM)

I am pressed to understand the correlation. 1,000 is a paltry number.

Host: Philip Jefferson '83 (Jan 29, 2004 8:37:11 PM)

Well, each month approximately 150,000 people enter the labor force. They are looking for jobs. Traditionally, tax cuts are thought to stimulate demand for goods and services. This is thought to lead employers to hire more people.

Paul Johnson VCProf (Jan 29, 2004 8:37:05 PM)

I, and many others, didn't expect them to have much if any effect on job creation.

Host: Philip Jefferson '83 (Jan 29, 2004 8:37:58 PM)

To Paul: Why not?

Paul Johnson VCProf (Jan 29, 2004 8:38:16 PM)

The effect on demand requires those receiving the cuts to spend them. Most of the cuts went to folks with low marginal propensities to spend so the effect on demand was small.

Pat Duane Lichtenberg '90 (Jan 29, 2004 8:38:02 PM)

We do not believe that the cuts are working to stimulate job growth for the lowest paid positions.

Ro Mason '67 (Jan 29, 2004 8:38:33 PM)

Where is the tax cut money going?

Paul Johnson VCProf (Jan 29, 2004 8:39:28 PM)

Rather than being spent?

Host: Philip Jefferson '83 (Jan 29, 2004 8:39:39 PM)

Did not everyone receive some form of tax break?

Jane Johnson '64 (Jan 29, 2004 8:39:44 PM)

(This user has entered DigiChat Foyer) (IP = 140.142.184.80)

Paul Johnson VCProf (Jan 29, 2004 8:40:04 PM)

Most received only a few hundred dollars.

Pat Duane Lichtenberg '90 (Jan 29, 2004 8:40:27 PM)

And a few hundred dollars cannot grow much.

Paul Johnson VCProf (Jan 29, 2004 8:41:09 PM)

Most of the money was saved in one way or another.

Pat Duane Lichtenberg '90 (Jan 29, 2004 8:41:29 PM)

How so, Paul?

Paul Johnson VCProf (Jan 29, 2004 8:42:52 PM)

The people who got most of the tax cuts were wealthy, and they have low marginal propensities to spend so not much of the tax cut ended up being spent.

Ro Mason '67 (Jan 29, 2004 8:40:32 PM)

Was that used to lower personal debt?

Host: Philip Jefferson '83 (Jan 29, 2004 8:41:27 PM)

So if people pay down personal debt instead of spending the impact on demand will be small? Is that your hypothesis, Ro?

Ro Mason '67 (Jan 29, 2004 8:42:11 PM)

I think maybe. Debt in a sense is money already spent.

Host: Philip Jefferson '83 (Jan 29, 2004 8:42:45 PM)

All of this saving should lower interest rates. Don't lower interest rates stimulate demand? Think of people buying homes.

Paul Johnson VCProf (Jan 29, 2004 8:43:14 PM)

Rates were low already.

Host: Philip Jefferson '83 (Jan 29, 2004 8:44:19 PM)

Does that mean that more stimuli were not needed?

Paul Johnson VCProf (Jan 29, 2004 8:44:27 PM)

No.

Paul Johnson VCProf (Jan 29, 2004 8:44:43 PM)

It means that monetary policy had done all that it could

Paul Johnson VCProf (Jan 29, 2004 8:44:24 PM)

Low rates only stimulate investment if firms expect to be able to see their out put, and this is not so in a recession.

Host: Philip Jefferson '83 (Jan 29, 2004 8:44:46 PM)

What does Jane think about all of this?

Paul Johnson VCProf (Jan 29, 2004 8:44:54 PM)

Fiscal policy was needed.

Ro Mason '67 (Jan 29, 2004 8:46:10 PM)

Maybe production increased and demand increased but jobs did not because of increased use of machinery and foreign labor.

Host: Philip Jefferson '83 (Jan 29, 2004 8:46:55 PM)

Or could it be that jobs did not respond because workers were more productive?

Ro Mason '67 (Jan 29, 2004 8:47:20 PM)

Seems like a different way to say what I just said.

Host: Philip Jefferson '83 (Jan 29, 2004 8:47:20 PM)

Did the tax cuts raise productivity?

Pat Duane Lichtenberg '90 (Jan 29, 2004 8:47:55 PM)

If anything, job insecurity may have raised insecurity.

Paul Johnson VCProf (Jan 29, 2004 8:48:03 PM)

Probably not. That is a supply side effect and they are relatively slow.

Ro Mason '67 (Jan 29, 2004 8:48:08 PM)

No, but computers took hold. We just would have had more excess capacity without a tax cut.

Jane Johnson '64 (Jan 29, 2004 8:48:56 PM)

By "more productive," do you mean that they worked more overtime? If tax rates are lower than previously, employees get to keep more of what they make, thus possibly encouraging them to want to work more. Also, employers may want more overtime

rather than hiring more new workers, if that costs less in benefits, payroll taxes, etc.

Host: Philip Jefferson '83 (Jan 29, 2004 8:49:11 PM)

Well if I were a supply sider, I might say that the thought of keeping more of my wages induced me to work harder.

Paul Johnson VCProf (Jan 29, 2004 8:49:31 PM)

Don't forget that income effect, Phillip!

Host: Philip Jefferson '83 (Jan 29, 2004 8:50:02 PM)

Now, Paul, you will have to explain that!

Pat Duane Lichtenberg '90 (Jan 29, 2004 8:49:56 PM)

If anything, job insecurity may have raised productivity. Every day we hear of more job cuts. How can that be healthy for the economic psyche? It is not only "job" cuts, but "people" cuts.

Paul Johnson VCProf (Jan 29, 2004 8:50:03 PM)

Besides, the cuts were largely on non-earned forms of income.

Host: Philip Jefferson '83 (Jan 29, 2004 8:51:33 PM)

Pat has an interesting point. Insecure employees do not press for wage increases even when productivity rises. The issue, however, is what does tax cuts have to do with an increase in insecurity?

Paul Johnson VCProf (Jan 29, 2004 8:52:30 PM)

A rise in wages has two effects. The substitution effect is that leisure has become more costly so consume less of that equals work harder. The income effect is that income has risen so consume more of all goods, including leisure, equals work less. The net effect is ambiguous but for permanent tax cuts it is reasonable to expect the income effect to dominate.

Jane Johnson '64 (Jan 29, 2004 8:53:14 PM)

Yes, but these aren't permanent tax cuts!

Pat Duane Lichtenberg '90 (Jan 29, 2004 8:53:54 PM)

I don't believe the two correlate to the "working" man and woman. They are out on the lines making low wages. The few (\$600) might buy a nice Christmas for the kids but it does not stimulate much beyond that.

Paul Johnson VCProf (Jan 29, 2004 8:55:13 PM)

The Administration has begun to push to make them permanent. Their "temporariness" was part of the politicking to get them passed. In any case, if they are temporary the net effect is ambiguous.

Host: Philip Jefferson '83 (Jan 29, 2004 8:55:59 PM)

Now we're talking politics. I don't know if we want to go there.

Jane Johnson '64 (Jan 29, 2004 8:56:57 PM)

I think in a way you almost have to go there, because it's the perception of the effect of these tax cuts that candidates are using right now. Do we want to refute those Democrats' assertions?

Host: Philip Jefferson '83 (Jan 29, 2004 8:57:22 PM)

Whether there will be a dynamic effect of the tax cuts also depends on their impact on the budget.

Pat Duane Lichtenberg '90 (Jan 29, 2004 8:57:44 PM)

Why not (talk politics)? Does not the party in power dictate the economic policies?

Jane Johnson '64 (Jan 29, 2004 8:58:16 PM)

Yes, the budget (deficit) has become a great huge issue in the campaign so far.

Host: Philip Jefferson '83 (Jan 29, 2004 8:58:53 PM)

Sadly, yes! But politics and good economics do not always go together.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:00:01 PM)

Philip, and that's where we are — the friction between politics and "good" economics.

Jane Johnson '64 (Jan 29, 2004 9:00:10 PM)

I agree that politics and economics are not always the best bedfellows. But we use economic analysis to verify or refute the politicians' assertions. There's a lot of mileage right now from doing that, in my estimation!

Paul Johnson VCProf (Jan 29, 2004 9:00:27 PM)

Agreed

Jane Johnson '64 (Jan 29, 2004 9:01:20 PM)

So...what are we trying to do here? Make some sense of some of the rhetoric we're hearing right now?

Host: Philip Jefferson '83 (Jan 29, 2004 9:02:27 PM)

I do not know if it's all rhetoric. I get the sense that some really believe that tax cuts help to get the economy moving again.

Jane Johnson '64 (Jan 29, 2004 9:03:06 PM)

And you don't think that loose fiscal policy had any impact on the last recession?

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:02:03 PM)

I am a lay person (not an economist) — is there any hope of aspiring to a joining of politics and economics?

Ro Mason '67 (Jan 29, 2004 9:03:35 PM)

The economy expanded, but without jobs. I would like to know what you think allowed this to happen.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:04:01 PM)

I have a hard time understanding that — unless the tax cut to the rich was so advantageous as to stimulate the economy. And that is contrary to what Paul has said.

Host: Philip Jefferson '83 (Jan 29, 2004 9:04:06 PM)

I'd be interested in hearing about two issues. Why has the job market not recovered? What's going to happen with the tax cuts given the growing federal budget deficit.

Jane Johnson '64 (Jan 29, 2004 9:05:05 PM)

I think there are a number of other factors at work — both blue- and white-collar jobs going to other countries, more overtime, etc. I'd be interested to know what would happen if, heaven forbid, US workers would actually work for less than their current wage level...

Paul Johnson VCProf (Jan 29, 2004 9:05:40 PM)

Better that we become more productive and increase wages here.

Ro Mason '67 (Jan 29, 2004 9:05:47 PM)

Federal debt should raise interest rates and dampen expansion. In the ultimate, it might cause terrible inflation as the government pays off debt in degraded money.

Host: Philip Jefferson '83 (Jan 29, 2004 9:06:06 PM)

My conjecture for the first question is that employers are hesitant to expand employment because of geopolitical uncertainty and the need of possible retrenchment.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:06:57 PM)

Would there not have to be a (if you'll pardon the expression) trickle-down effect on the cost of all other goods and services. If

US workers took pay cuts it would have to be portioned out equitably.

Paul Johnson VCProf (Jan 29, 2004 9:07:07 PM)

Probably much of the story — less costly to pay overtime than to hire additional workers that you may have to lay off soon.

Host: Philip Jefferson '83 (Jan 29, 2004 9:07:36 PM)

That's part of my point, Paul.

Jane Johnson '64 (Jan 29, 2004 9:07:27 PM)

If so, these are exogenous variables that we don't easily fit into our economic models. Perhaps we really are living in very different times right now.

Paul Johnson VCProf (Jan 29, 2004 9:08:40 PM)

The increase in debt won't have much effect on rates if the tax cuts are saved.

Host: Philip Jefferson '83 (Jan 29, 2004 9:08:43 PM)

An issue is whether there is another type of public policy that could stimulate job creation if tax cuts don't.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:08:49 PM)

And let's not forget the massive "out-sourcing" that is going on in corporate US, thus, side stepping the need for benefits and long-term growth.

Paul Johnson VCProf (Jan 29, 2004 9:10:33 PM)

I hope they don't outsource profs!

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:11:15 PM)

Outsourcing profs? Not very Vassar!

Paul Johnson VCProf (Jan 29, 2004 9:11:35 PM)

Whew!

Host: Philip Jefferson '83 (Jan 29, 2004 9:09:54 PM)

I'm not sure outsourcing is a bad thing. As a consumer, I like lower prices. As a worker, I do not like losing my job.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:10:35 PM)

Well, that sounds like you are talking out of both sides of your economist's mouth!

Host: Philip Jefferson '83 (Jan 29, 2004 9:11:08 PM)

If not tax cuts, how can a policy maker stimulate job creation?

Paul Johnson VCProf (Jan 29, 2004 9:11:13 PM)

That's what makes it difficult — costs to some and benefits to others.

Ro Mason '67 (Jan 29, 2004 9:11:48 PM)

Getting back to the total debt, of which the tax cuts are but a part. It is overwhelming, on the current course and it seems to me big enough to lead to some real problems if not stopped.

Paul Johnson VCProf (Jan 29, 2004 9:12:54 PM)

Granted. Some have suggested that the current federal budget situation is unsustainable in the long run.

Host: Philip Jefferson '83 (Jan 29, 2004 9:13:04 PM)

The debt will not spiral out of control. Why not? The financial market will punish the government so much that it will be forced to get its fiscal house in order.

Jane Johnson '64 (Jan 29, 2004 9:13:18 PM)

Debt in itself isn't all bad. It's bad when you're paying current operating expenses with debt, but not when you're investing in new

capital, for example. Then you spread the investment over future generations of taxpayers. But I realize this is a minority viewpoint.

Host: Philip Jefferson '83 (Jan 29, 2004 9:14:00 PM)

Following Jane: It's what you do with the money.

Jane Johnson '64 (Jan 29, 2004 9:14:16 PM)

Interesting enough, interest rates actually declined during the 1980s when Reagan cut taxes. The conventional wisdom at the time was that those tax cuts would drive rates up, but they didn't.

Paul Johnson VCProf (Jan 29, 2004 9:15:10 PM)

Not true, Jane. The early '80s saw record high real interest rates. Nominal rates fell as inflation fell.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:14:21 PM)

But can we say that the government is doing what Jane hopes?

Ro Mason '67 (Jan 29, 2004 9:14:30 PM)

But money for Iraq comes back only through the servicemen's buying. What goes to Iraq would appear not to come back. That would seem to be useless debt, to us.

Paul Johnson VCProf (Jan 29, 2004 9:14:32 PM)

Agreed. If you incur debt to invest in productive things you create the means to repay it.

Host: Philip Jefferson '83 (Jan 29, 2004 9:14:34 PM)

We went into a lot of debt to win World War II.

Paul Johnson VCProf (Jan 29, 2004 9:16:00 PM)

Winning was very productive!

Ro Mason '67 (Jan 29, 2004 9:16:02 PM)

At that time, it turned out we owned most of the production in the world, so we paid off the debt by economic growth. I don't think that is likely now, with industrialization and technical knowledge spreading like mad worldwide.

Host: Philip Jefferson '83 (Jan 29, 2004 9:16:08 PM)

We are buying something very valuable for the US economy in Iraq.

Jane Johnson '64 (Jan 29, 2004 9:17:16 PM)

What is the value that you see?

Host: Philip Jefferson '83 (Jan 29, 2004 9:17:26 PM)

Hopefully, peace will lead to prosperity there, which is good for us. But what does this have to do with taxes?

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:17:26 PM)

Hmmm. A silence falls over the chat.

Host: Philip Jefferson '83 (Jan 29, 2004 9:18:09 PM)

Except for the fact that tax cuts here means that we do not get to share in the sacrifice.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:18:09 PM)

How would you define peace?

Host: Philip Jefferson '83 (Jan 29, 2004 9:18:43 PM)

Less killing than would otherwise have taken place?

Host: Philip Jefferson '83 (Jan 29, 2004 9:18:58 PM)

What happens to taxes and jobs?

Paul Johnson VCProf (Jan 29, 2004 9:19:01 PM)

But we could have had peace without starting the war and used the resources for schools, etc., at home.

Ro Mason '67 (Jan 29, 2004 9:19:43 PM)

I am with Paul on that one, but that is political. The economic part though, is that it is a darned costly adventure.

Jane Johnson '64 (Jan 29, 2004 9:19:38 PM)

Ah...the old guns versus butter choice...

Host: Philip Jefferson '83 (Jan 29, 2004 9:20:12 PM)

Especially when there are no tax revenues to pay for it.

Paul Johnson VCProf (Jan 29, 2004 9:20:31 PM)

Yes

Ro Mason '67 (Jan 29, 2004 9:20:23 PM)

It increases the debt, to which I keep returning. The debt is related to the tax cuts.

Paul Johnson VCProf (Jan 29, 2004 9:20:54 PM)

And the increased spending on the war, etc.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:20:55 PM)

Peace? Jobs? Taxes? They are intertwined? Sorry, don't agree. It might be better for the US, but we are members of a larger community.

Host: Philip Jefferson '83 (Jan 29, 2004 9:21:01 PM)

Perhaps the economy started to recover as a result of the war build up à la World War II?

Host: Philip Jefferson '83 (Jan 29, 2004 9:21:39 PM)

A war machine with no job growth? That seems odd!

Paul Johnson VCProf (Jan 29, 2004 9:22:06 PM)

No need for a war to get this. Build schools, roads, hire more teachers; spend on useful things that increase productivity.

Host: Philip Jefferson '83 (Jan 29, 2004 9:22:14 PM)

Where is Rosie the Riveter?

Ro Mason '67 (Jan 29, 2004 9:22:57 PM)

Maybe Rosie is in China?

Ro Mason '67 (Jan 29, 2004 9:22:16 PM)

We did not count the servicemen's and women's jobs. They got work.

Host: Philip Jefferson '83 (Jan 29, 2004 9:22:55 PM)

Productivity is not the problem. It is very high.

Paul Johnson VCProf (Jan 29, 2004 9:22:58 PM)

They were already employed. Besides the employment stats just record civilian employment.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:23:10 PM)

Have we increased the military since the Iraq "war"?

Paul Johnson VCProf (Jan 29, 2004 9:23:10 PM)

In some sectors.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:23:29 PM)

That is, the folks who have volunteered?

Host: Philip Jefferson '83 (Jan 29, 2004 9:23:38 PM)

Yes, and they want to expand the military further.

Jane Johnson '64 (Jan 29, 2004 9:24:02 PM)

Perhaps the "war machine" is so high-tech this time that it tends to create few or no new jobs. Are we fighting a new kind of war now?

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:24:17 PM)

I agree, Jane.

Paul Johnson VCProf (Jan 29, 2004 9:24:22 PM)

If you have a good education your productivity and income is rising. If not, you are staying at the same place or going backwards.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:24:46 PM)

And agreed, Paul.

Jane Johnson '64 (Jan 29, 2004 9:24:52 PM)

Spoken like a true academic, Paul. But of course you're right.

Host: Philip Jefferson '83 (Jan 29, 2004 9:25:07 PM)

That is a problem. Educational attainment is crucial.

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:25:38 PM)

Another subject — the cost of education.

Jane Johnson '64 (Jan 29, 2004 9:25:45 PM)

Yes, liberal arts or something else. Now we're getting into a fascinating issue, but perhaps quite far from the original topic.

Host: Philip Jefferson '83 (Jan 29, 2004 9:25:59 PM)

Funding of education is the issue.

Ro Mason '67 (Jan 29, 2004 9:26:09 PM)

Yes, but I read that new-hatched computer scientists can't find work because the jobs have gone abroad. Education, too, is worth what the market will pay.

Host: Philip Jefferson '83 (Jan 29, 2004 9:26:51 PM)

Which brings us back to taxes. Lower taxes. Lower funding for public schools?

Host: Philip Jefferson '83 (Jan 29, 2004 9:27:22 PM)

More take home pay. Worse schools for your children.

Jane Johnson '64 (Jan 29, 2004 9:27:43 PM)

I really wonder, though, if the absolute funding level really determines the outcomes of public schools?

Pat Duane Lichtenberg '90 (Jan 29, 2004 9:27:56 PM)

Yes, you can buy more amusements for them, but you can't give them a future.

Ro Mason '67 (Jan 29, 2004 9:27:47 PM)

I have computer scientist friends, and they say keep the schools and, after graduation, move to India!

Host: Philip Jefferson '83 (Jan 29, 2004 9:28:20 PM)

As we wind down. I thank all of you for signing on.

Jane Johnson '64 (Jan 29, 2004 9:28:44 PM)

Thanks for hosting.

Ro Mason '67 (Jan 29, 2004 9:29:01 PM)

Yes, thank you.

Host: Philip Jefferson '83 (Jan 29, 2004 9:29:16 PM)

I have enjoyed it. Taxes are a complicated subject. Certainly, we could not resolve all of the issues. But it important to think about.

Jane Johnson '64 (Jan 29, 2004 9:29:33 PM)

Yes, much food for thought!

Host: Philip Jefferson '83 (Jan 29, 2004 9:29:53 PM)

Thank you, AAVC, for setting this up!

AAVC (Jan 29, 2004 9:30:13 PM)

We are out of time. Thank you for joining us. A transcript of this chat will be online next month at www.aavc.vassar.edu/vq. Look for more of these events from AAVC in the future. Thanks again.