# The Tax Changes Don’t Do What’s Needed

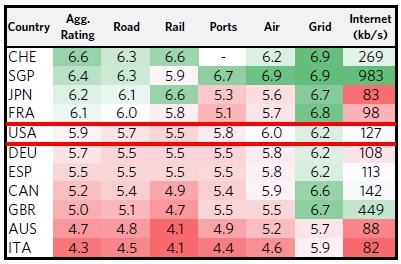
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When we look at the tax plan holistically, it looks to me like it’s a short-term minor boost to the economy that will have some minor positive longer-term impacts, but by and large it doesn’t deal with the impediments that are holding back investment and productivity in the US economy, and it won’t have any notable effect on our biggest economic, social, and political issue, which is the conditions of the bottom 60% and the growing disparity with the top 40% (especially the growing disparity between the bottom 90% and the top 10%).

In the short term, the tax law changes and regulatory reductions will provide a very modest one-time boost to after-tax incomes that will be stimulative.  How “good” the tax law changes are depends on one’s own perspective because some things will benefit and hurt some people more than others—but, net, it won’t be big.  For example, it will typically move after-tax incomes by about 0.5% in total, which will be made up for by a nearly comparable increase in the budget deficit (which doesn’t come at no cost).

The reforms to the structure of corporate taxes at the core of the bill will certainly make the US a more attractive environment to do business, but the impact of those changes is likely to be small relative to the improvement that could be achieved by investing more in things like infrastructure and education, which more directly boost productivity (see [www.economicprinciples.org](http://www.economicprinciples.org/) for our full studies on what makes economies succeed and fail).  To help convey the issue about infrastructure spending, the table below shows how US infrastructure compares to other developed countries (from the World Economic Forum)—i.e., it shows how the US lags significantly in rail and internet speeds, and is more middling in road infrastructure.  Our infrastructure is in desperate need of improvement.



The main impediments to making such investments are the worry over increasing government debt and the desire to make sure spending will pay for itself. While it’s really important that everyone tries to make sure that borrowed money is put into things that produce returns that are large enough to make debt service payments, that is not the most important thing.  In being very cautious about making sure that happens, productivity-enhancing debt-financed investments might not happen.  So, the real question is whether one would rather a) have significant investment development, risking it not fully paying for itself (in which case some of it, such as 20% or 30%, might have to be written off over time), or b) not have significant investment development and avoid that risk.  If one looks at the mechanics and consequences of these two choices, Path A is a better choice than Path B if the debt is denominated in one’s own currency.  For example, if one does the calculations in order to look at the consequences of a) building something like a subway system and having to write off 20-30% over 15 to 20 years or b) not having the subway system, most people would choose Path A.  And, if you look at the consequences for countries that chose Path A versus Path B, most people would prefer the conditions of countries that chose Path A.

For example, China chose Path A, so it has more debt and more and better infrastructure than Russia, which chose Path B.  While there were of course other factors at play that affected some of the differences in how they evolved over the last 20 years (since the old-style communist systems ended), the choice between Path A and Path B was the most important.  By the way, almost 100% of the differences in outcomes were due to this choice and other economic policy choice differences.  They are only two examples among many that show what is consistent with an examination of how the machine works that should lead one to favor Path A over Path B.  For your reference, I say this based on a sample size of about 80 countries.

Right now, we are favoring Path B.

So, while the tax bill will stimulate growth in the short term, we won’t get much long-term mileage out of it in comparison to paths to direct stimulus spending to areas that hit the core issues holding back US productivity.

There’s a tremendous opportunity cost arising from common sense sorts of things not being done or being cut back on—from not investing in infrastructure because of budget concerns and regulatory bureaucracy, to not improving education for similar economic and bureaucratic reasons.  So we’ll do the tax adjustment tweak and the regulatory tweak—a little bit here and a little bit there—but we won’t change things materially.  In other words, the headline is that we’re still not dealing with the bigger issues.

But, to reiterate, there is some economic stimulation coming from changes in the tax law and coming from reductions in regulations.  We will get them, and they will fade as the economy adjusts to them.  They will be relatively small, and they won’t come without costs.

I’d like to digress a moment to talk about the politics surrounding this situation because it’s a big deal in leading to this outcome and the future of our country.  **There’s a war going on**, **and biases are entering into the choices being made so there is not decision-making based on what is good for the whole so much as decision-making based on what one group that has more power wants relative to what the group that has less power wants**.  That’s the case, whether it’s the left/Democrats or the right/Republicans that has more power.  So, right now what we are seeing is policies resulting from those who genuinely believe Path B is better than Path A and who are in the group that has the power to carry its vested interests forward rather than in support of the well-being of the whole.  And we certainly will not deal with the gap and the conditions of the bottom 60% (i.e., the majority).  Once again, I’d love to see a bipartisan commission use metrics of the conditions of the bottom 60% to see if they’re improving or worsening, as well as metrics of the gap between the well-being of the top 40% and the bottom 60% to see if it’s widening or narrowing.  That way, it will be crystal clear whether or not needed changes are being made.  Based on such metrics, we would see that no significant needed changes are being made.  That’s tragic.