Funding the Future

Myths vs evidence: Tax cuts for the 10%

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With the election out of the way it's time to look at research again. This [was a highlight of recent publications, coming from Alex Cobham at Tax Justice Network](), with permission:

How do tax cuts targeted at different parts of the income distribution affect job creation? This is the question addressed in a new NBER paper by Owen Zidar, an economist at Chicago (not *[known historically]() for progressive analysis). But the paper (see the [ungated version](); and [slides]()) has had a good deal of US media coverage, largely because of the progressive tax implications. First, some graphs:*

[caption id="attachment_344" align="aligncenter" width="584"] ***The paper's main innovation is to overcome the scarcity of time series data by exploiting US data on state-level income distributions, to view each state-year response to a national tax policy change as a separate observation.***[/caption]

The main result is not, intuitively, surprising: but it is not a question that has been commonly posed, nor this well answered before. The result is that ***tax cuts are least likely to generate benefits when targeted to the top 10% of households; and most likely to generate benefits when targeted to the bottom 90% - or as in figure 5, the bottom 50%***. As Zidar puts it:

"*Overall, tax cuts for the bottom 90% tend to result in more output, employment, consumption and investment growth than equivalently sized cuts for the top 10% over a business cycle frequency.*"

the top 10% drive the economy;Why would we ever cut taxes for the top 10% as a stimulus, I hear you ask? Because they're in charge, say the cynics. Or perhaps because policymakers and/or the public have bought a series of economic myths, such as:

* the top 10% spend all their time worrying about things like tax cuts rather than broader factors like aggregate demand, or the availability of sound infrastructure and a

healthy, well-educated workforce;

* progressive taxation is bad for growth, and ultimately bad for the poor as well as the rich.

One fairly clear implication of the findings is: the opposite seems to be the case.

A tax change for the top 10% seems to have pretty much no impact on job creation, so a revenue-neutral change in tax structure that deliberately reduces the ***Palma measure of inequality*** ***(that is, the ratio of incomes of the top 10% to the bottom 40%) will not only be progressive but will have the effect of boosting jobs growth. Zidar's next chart shows this:***