Trickle-down Government: A Primer (of sorts)

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Likewise there is no generally accepted economic theory that claims redistributing income or wealth from poor to rich stimulates economic growth or employment. In some quarters this last statement is often pejoratively referred to as The Trickle Down Theory (TDT). One is hard pressed to find an economic text that even mentions the term much less defines or describes it. The reason is because the TDT is not an economic term but a *political* one.

From whence does the TDT term emanate? Some claim from the Reagan Era—the era of Supply-Side and Voodoo economics—while others suggest the John F. Kennedy tax cuts in the aftermath of his assignation. Neither is correct. The term is a bastardization of John M Keynes ideas first put forth in his *The General Theory of Employment, Interest and Money* (1936).

Keynes believed that a slow growing or depressed economy is caused by inadequate aggregate demand for newly produced final goods and services. Because consumers and businesses were generally depressed in those circumstances only government could be reasonably expected to fill the void. Keynes suggested that either increasing government expenditures or cutting taxes would stimulate aggregate demand by the creation of larger government deficits.

Keynes showed that an autonomous increase in government expenditure would produce a multiplied increase in GDP. It did not matter what the government purchased so long as it was newly produced final goods or services. Progressives and liberals alike warmly embraced this policy as it provided theoretical support for any and all government expenditures. A number of modern theories, however, cast serious doubt on Keynesian policies.

If the increased government expenditures benefited mainly the poor or lower middle classes then the expenditures would eventually "trickle-up" to the upper classes or so some left leaning policy wags seem to suggest. However, producers of the goods and services would still receive the lion's share of the increased largesse. Recall, government produces very little in relation to the total economy, e.g., the postal service, the weather service, armed forces, police and fire protection, education, etc. Private contractors sometimes working for government produce most every thing else including military hardware.

Keynes did not include government transfer payments because by their very nature they consist solely of taking funds (income) out of some people's pockets and placing them in other people's pockets. The fiscal impact of that policy is null because no production or exchange of goods or services is involved. Spending power is simply transferred from one individual/group to another with little or no net effect. Post-Keynes theories of consumption and lack of empirical evidence suggests that redistribution of income or wealth alone produces little or no net macroeconomic effect.

Secondly, Keynes believed that cutting taxes (reducing government revenues) could also lead to a restoration of the maximum sustainable level of employment (*formally called full employment*). Herein lies the probable source of the trickle down label. Taxes are not borne equally throughout the population. Those with higher incomes pay a disproportionate share of all taxes whether in income or consumption taxes. Thus, if taxes are reduced the benefits naturally fall primarily on those paying the taxes. The idea is to provide businesses and individuals with incentives to increase expenditures on hard goods, i.e., housing, autos, appliances, etc. for households and capital goods, i.e., plant and equipment for businesses. In the production of these goods people are employed and incomes rise.

Those that benefit the most from these policies are those who find employment or have their employment restored. After all going from little or no income to some or higher levels represents a larger percentage increase than a worker going from one six-figure income to a higher six-figure income. Higher levels of private investment expenditures lead to growing employment and incomes. Keynes showed us that much. If GDP and employment are not growing sufficiently it is because of insufficient private investment.

The lack of businesses investment is the primarily culprit for the current (2015) deficit (3 percent) in the labor force participation rate. Imagine how much GDP growth and personal income would be enhanced if only the missing labor participants (3 million) were found and employed. Could it be that confiscatory taxes and burdensome government regulations have reduced private investment to only a trickle?