Don't Raise Taxes

June 21, 2021

As the summer of 2021 begins, the heat is rising not only around the country with record setting temperatures in the West, but in the Congress with a growing effort to increase taxes on individuals and businesses. The president speaks frequently about his plans to undue the Trump tax rate cuts and make the rich pay their "fair share". Members of Congress are also pushing for a wealth tax. The question we should all be asking is: Why? One idea that has decades of longevity is that we must close the budget deficit. When Tom first started out in this business in 1968, the first economic commentary that he penned pointed out the Nixon Administration's concern about the budget deficit! Over the past 53 years we have had only two occasions when the country had a budget surplus demonstrating that deficits go hand in hand with a growing economy. Nixon's tax rate increases to shrink the deficit preceded the 1974 recession and one of the worst stock market declines in history while Clinton's tax increases led to the Republican "Contract with America" which flipped the House and Senate to the Republicans in Clinton's first mid-term election. Efforts to raise tax rates to reduce the budget deficit have not met with great success. So, we ask again, what is the need to close the budget deficit when history demonstrates that such efforts only cause pain for the average American?

The federal government's response to the pandemic was twofold: (1) a massive increase in liquidity as the Fed poured billions of dollars into the economy and (2) the administration's spending of billions of dollars to keep the economy on a recovery track through the worst part of the pandemic. Trillions of dollars of budget deficits later, where are we? Well, there is some indication of inflationary pressures triggered by an economy that is quickly bouncing back, but the traditional indicators of gloom and doom are not showing signs of hard times ahead. Recently, lumber prices surged then fell back by 40% from the peak. Hoarders did that as they did with toilet paper and hand sanitizer early in the pandemic. Gold, the traditional indicator of inflation, has been flat to down in price so far this year. The big culprit in recent inflation data has been oil prices but they are only recovering from the collapse of last year. In addition, household wealth is at record levels and consumers are paying down their debt. Why would anyone want to raise taxes in such an environment and put the kibosh on a booming economy? And, anyway, the federal and state governments are seeing a surge in tax revenues anyway. Why not leave well enough alone?

One important piece of the puzzle is still missing. In today's world of fiat currencies, the government does not need to tax to spend. The past year demonstrates that fact. The federal government makes money, so they do not need money from an increase in tax collections. The purpose of taxes or tax increases is to slow the economy if growth is too strong. Unfortunately, the drive to raise tax rates seems to be more an indication of envy than of leveling the playing field. Let's hope common sense and historical experience spares us from Congress approving an economic policy that can only end in hard times.