Another Testimonial for Supply-Side Economics

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We have not heard too much about the school of Supply-Side economics recently, but the evidence continues to role in that the principle of this approach makes sense. One important economic data series provides a case study in how the supply-side story works: Reduce tax rates and regulation and you get a surge in revenues. As the Wall Street Journal recently pointed out, recent corporate tax reform resulted in positive (and better than expected) results. The evidence is that the forecasts of corporate tax revenues by the Congressional Budget Office (CBO) have fallen far short. Here are the forecasts in the billions of dollars for 2021 through 2023 both before and after Covid compared with the actual results.

	2021	2022	2023
Actual:	$372(b)	$454(c)	N/A
CBO estimate after tax reform:	$327(a)	$353(d)	$388
CBO estimate before 2017 tax reform:	$383	$389	$395

The pessimistic corporate tax forecast for 2021 did not use the dynamic supply side model and ended up with an estimate (a) that fell $45 billion short of the actual number (b). For 2022, the Tax Foundation is estimating that corporate tax collections will amount to $454 billion (c), over $100 billion higher in corporate tax collections than the current CBO estimates (d). Even in the face of this surge in corporate tax collections, Congress and the President are moving ahead with plans to increase taxes on corporations. So, given this model, what might the outcome be if the government substantially increases taxes? The CBO model that will project higher tax revenues because of higher tax rates will fall flat on its face.

According to the Laffer Curve, the government should continue to lower tax rates until they reach a point where tax revenues are no longer increasing. As we have said over the past few months tax revenues at all levels of government are soaring. According to the Journal, “individual tax revenues rose by $300 billion, or 36%, in the fiscal year through March from the same period in 2021.” We still have not seen the 12-month number through April, but it should be a very favorable report for federal government tax collections. Even with these rapidly rising numbers, politicians are bent on raising taxes at the higher end of the spectrum to include a tax on unrealized capital gains that is the equivalent of a wealth tax. Note that the French election ended with the current president Macron getting 58.5% of the vote vs. his adversary Marine Le Pen getting 41.5%. One reason Macron is so popular is that he abolished the wealth tax!

On the downside is the fact that the surge in tax revenues is taking wealth out of the private economy and giving it to the government. While Wall Street rages about the impact of tight money as being practiced by the Federal Reserve, we cannot count out the negative effect of tight fiscal policy.

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