BBB's Supply-side Gamble

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Eakinomics: BBB's Supply-side Gamble

As the nation heads toward a vigorous fall debate over the president's Build Back Better (BBB) plan (aka "the reconciliation bill"), one should be prepared for heated rhetoric on the enormous cost of the plan (true), the enormity of the tax increases (true), the fact that the plan is "paid for" (false), and the overall consequences for economic growth. On the latter, the jury is still out, although there are two strikes against it.

Strike one is the research AAF released on the economic consequences of raising the proposed $3.3 trillion in taxes and spending it exclusively on productive infrastructure. The upshot? The economy shrinks instead of grows, as the negative effects of the taxes outweigh even a disciplined focusing on productive spending. Since the actual BBB is anything but such a disciplined approach, the real-world impacts will be even more negative.

Strike two is the fact that even though the Senate-passed infrastructure bill avoided the damaging tax hikes, it did not fully pay for the outlays by cutting non-investment federal spending. As discussed in a previous Eakinomics, the Congressional Budget Office has released its analysis that suggest a partially or fully deficit-financed investment program has more short-lived beneficial impacts.

But the case is not yet ironclad for reasons highlighted by the president in his recent remarks on the BBB: "And the same time, it's true that long-term investments that bring down the biggest costs that families face — housing, childcare, education, and healthcare — these investments will lower out-of-pocket expenses, not raise them. *They will spur more people to work* by helping ease the burdens of childcare and senior care that parents, especially mothers, bear — keeping them out of the job market" (emphasis added).

The gamble in the BBB is whether the constellation of child tax credit, paid family leave, child care subsidies, earned income tax credit expansion, home health care, and health insurance subsidies will raise the labor force participation rate (LFPR) – particularly for women. Suppose, for example, the BBB were to instantaneously raise the LFPR for U.S. females to that of western Europe (taken from Isabel Soto's recent research). That would mean a LFPR of 72.1 percent instead of 68.9 percent, or roughly 3.3 million more workers (as of the end of June). That corresponds to a 2.3 percent increase in the labor input in the economy. If productivity is (roughly) the same for the new workers, this means a 2.3 percent increase in gross domestic product.

Is 2.3 percent big? Well, it is roughly one year of trend economic growth or $520 billion. I'll let you decide if that is "big" enough. I would just emphasize that it is hardly a lock. First, much of the benefit – child credit, health insurance subsidies, home health care, child care subsidies – is not work-contingent. Moreover, as Soto concluded: "Data from European countries that have implemented country-wide paid-leave programs do not support the argument that a state-sponsored paid-leave system increases female labor force participation. There have also been attempts to create paid leave programs in the United States at the state level, but since the creation of these programs, female labor force participation has not seen significant change."

No change in labor force participation means no change in supply-side growth. If so, strike three.