Opinion **The Exchange**

The long-term effect of Trump's three-pronged boost

Can the long-term promise of the interventions match the short-term attractions?

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Investing in digital networks could create more growth than physical infrastructure © Getty

Dambisa Moyo 6 HOURS AGO

By many metrics — gross domestic product forecasts, unemployment and still relatively tame inflation — the Trump administration appears to be encouraging America's solid growth recovery nearly 10 years after the financial crisis.

However, while appealing in the short term, the three-pronged policy approach of tax reform, infrastructure boost and regulatory retrenchment has considerable long-term risks. None of the interventions offers a sure path to sustainable growth. Instead, they could well pose a threat.

The hope is, for example, that households will respond to tax cuts by increasing their consumption, in turn boosting demand and economic growth. Indeed, large companies such as Apple and Walmart have said they will boost pay to employees on the back of corporation tax cuts.

But, as the economist David Ricardo argued, the opposite might happen: households may view themselves as intricately connected to future generations and care about the economic fate of their children and children's children. Thus, rather than spend a tax windfall, households would save it, recognising that future governments will have to fund today's cuts with rises to balance their budgets.

If some families decide to save, rather than spend, the windfall, it will blunt the growth impact of the tax cuts. At worst, mass saving could have a negative impact on growth.

Moreover, even before the tax reforms were finalised, the Congressional Budget Office warned about the government's growing debts and deficits, saying in a March 2017 report: "The prospect of such large and growing debt poses substantial risks for the nation."

Second, there is the $1.5tn infrastructure pledge. The American Civil Engineers' report has ascribed America's infrastructure a grade of D+, indicating decades of under-investment. Well-functioning physical infrastructure, including roads, bridges and airports, is a prerequisite for any functioning economy.

Yet, Japan's experience with large-scale infrastructure impetus and its promise for supporting economic growth is cautionary. Japan has invested enormously to spur economic growth, with little positive impact. By some estimates, Japan invested over $6tn to build bridges, highways, airports, trains and roads between 1991 and 2008. While this notable injection — widely termed "bridges to nowhere" and multiples of what President Donald Trump promises — did increase jobs, many economists argue that the higher debts incurred were not offset by growth.

Infrastructure investment has a first-order effect of boosting growth by creating jobs for low-skilled workers, through increasing income and spending. Strong infrastructure is also a foundation for further trade and commerce.

If there is a lesson from Japan's experience on the interplay of infrastructure and economic growth, the type of capital investment matters crucially. Investing in new digital networks could create more growth than building bridges or roads. For now, statements from Trump's administration have focused on traditional infrastructure and, other than a nod to the importance of rural broadband, it remains unclear how much will be earmarked for digital projects..

Finally, Mr Trump has stressed that his administration's plans for regulatory retrenchment are equally as important as tax reform in resetting the US growth prospects and the country's economic resurgence.

But reducing regulation does not necessarily help growth in the long run. For example, environmental deregulation might reduce the cost of production today but it masks its true cost. These higher costs will have to be borne in the future and will therefore act as a drag on growth. Moreover, regulation can support business — for example, competition rules can level the competitive playing field by cracking down on illegal behaviour and monopolistic structures, which can limit growth.

It would be wrong to suggest that this mix of policies does nothing for growth, but there is a lack of evidence that it is a panacea for lack of growth. After all, the global economy faces a slate of structural threats that promise to undermine long-term growth, including a jobless underclass, inadequacy in skills and falling productivity — all of which bear the negative impact of a rapidly digitising world. Resolving these will require more ingenuity than this suite of traditional levers.

The writer is a global economist and the author most recently of 'Winner Take All'. She serves on the boards of Barclays Bank, Barrick Gold, Chevron and Seagate Technology