Written by **Ralph R. Reiland** on March 25, 2014

A Winning Strategy for Economic Recovery

There's a commonsense perspective and first-rate line of attack for economic recovery in the ideas quoted below from a major speech by a top U.S. politician.

His policy recommendations reveal a clear comprehension of economic incentives, human nature, and the fundamental fact that people do less of something when it's more penalized, more taxed, and more costly — and do more of something when it's more rewarded, less taxed, and less expensive.

That's why cigarettes are taxed at a higher rate than oranges — so we smoke less and get more vitamin C.

It's also why there's a federal Gas Guzzler Tax on new cars that goes up as fuel economy goes down.

As posted by the Department of Energy at fueleconomy.gov, there's no guzzler tax on cars that get "at least 22.5 mpg city/highway combined," a $3,000 tax on cars that get "at least 16.5 but less than 17.5 mpg," a $6,400 tax on cars with "at least 12.5 but less than 13.5 mpg," and a top tax of $7,700 on cars that get "less than 12.5 mpg."

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As the Department of Energy explains, "The Energy Tax Act of 1978 established a Gas Guzzler Tax on the sale of new cars with particularly poor fuel economy to discourage the production of such vehicles."

Overall, that's the way the world works. Raise the sticker price on gas hogs via taxation and fewer gas hogs will be on the road than would otherwise be the case. Similarly, raise the price of workers to employers via increased taxation, mandates, and regulations and there will be fewer workers on the job than would otherwise be the case.

In understanding these basic economic principles and being adept at applying these fundamental economic insights regarding human behavior and incentives to such issues as tax rates, government revenue, federal budgets, deficits, business incentives, investing, profits, economic growth and job creation, the aforementioned politician, addressing the Economic Club of New York, powerfully and succinctly presented his policy prescriptions for economic recovery, deficit reduction, and job creation.

"It is a paradoxical truth," he asserted, "that tax rates are too high today and tax revenues are too low and the soundest way to raise the revenues in the long run is to cut the tax rates."

Further, he expanded his tax analysis to profit levels and job creation: "An economy constrained by high tax rates will never produce enough revenue to balance the budget, just as it will never create enough jobs or enough profits."

He was explaining, in short, that the slow rate of new business investment, high unemployment rate, low level of job creation, and decline in economic growth — caused by the piling up of more and more taxes and regulations on businesses, investors and "the rich" — had produced a clear economic pathway to lower profits, lower investment, less growth, more joblessness, more poverty, inadequate tax revenues and higher levels of government red ink.

The U.S. tax system, he asserted, imposes “deterrents to private initiative,” “siphons out of the private economy too large a share of personal and business purchasing power” and “reduces the financial incentives for personal effort, investment and risk-taking.”

The solution, he asserted, was “an across-the-board, top-to-bottom cut in personal and corporate income taxes,” including tax cuts for those in the “upper income brackets, who can thereby be encouraged to undertake additional efforts and enabled to invest more capital.”

The aforesaid economic analysis was delivered on Dec. 14, 1962, in an address at the Waldorf Astoria by President John F. Kennedy.

In 1963, faced with a sluggish economy and a 5.7 unemployment rate, Kennedy proposed to cut the marginal federal income tax rates from the existing range of 20 percent at the bottom to 91 percent at the top to across-the-board lower marginal income rates ranging from a bottom rate of 14 percent to a top rate of 65 percent.

Additionally, Kennedy proposed a cut in the corporate tax rate from 52 percent to 47 percent, a cut in the capital gains tax rate, and a cut in the tax rate on dividends.

Kennedy argued that cuts in tax rates would stimulate economic growth, create jobs, and generate more revenue for the government — a pre-Reagan pro-growth, pro-business, supply-side program for economic recovery.

Kennedy’s proposed tax cuts were enacted in 1964, following his assassination, dropping the top marginal tax rate on income from 91 percent to 70 percent, a 23 percent cut, and dropping the lowest rate from 20 percent to 14 percent, a 30 percent cut.

The result, after the Kennedy tax cuts became fully effective in 1965?

Economic growth, adjusted for inflation, i.e. real GDP, jumped from an annual average growth rate of 4.6 percent in the four years prior to the tax cuts, 1961 through 1964, to an annual average growth rate of 5.1 percent in the four years following the tax cuts, 1965 through 1968, report Arthur B. Laffer and Stephen Moore in *Return to Prosperity* (2010, Simon & Shuster).

With this higher growth, correspondingly, the U.S. unemployment dropped from an annual average of 5.8 percent in the four years prior to the Kennedy tax cuts to an annual average of 3.9 percent in the four years following the tax cut, the lowest peacetime level of unemployment in more than three decades.

And as forecasted by Kennedy and his economic advisors, increased growth and more jobs resulted in more government revenues, even with lower rates of taxation. Total inflation-adjusted income tax revenue, personal and corporate, to the federal government jumped from an annual average increase of 2.6 percent in the four years prior to the tax cuts, 1961 through 1964, to an annual average increase of 9.0 percent in the four years following the tax cuts, 1965 through 1968, a 346 percent increase in the growth rate of inflation-adjusted federal revenues.

Bottom line, President Kennedy’s economic policies showed what works in unleashing an economic boom, a lesson that President Reagan understood and implemented and President Obama chooses to deny.

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