International Monetary Fund revises down US growth predictions

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The International Monetary Fund (IMF) has poured cold water on the idea that the Trump administration can lift the US economic growth rate either through tax cuts or an infrastructure stimulus package.

This assessment of the core economic agenda on which Trump won the election was contained in the IMF's annual assessment of the US economy issued earlier this week. It not only called into question Trump's stated policies but pointed to deeper problems within the US economy.

In the short term the IMF decided to remove the increase in growth from any stimulus package contained in its assessment of the US economy made in April. It lowered the expected growth rate for 2017 from 2.3 percent to 2.1 percent and for 2018 from 2.5 percent to 2.1 percent as well. It also predicted a lower rate in the medium term, forecasting that it would subsequently converge to the underlying potential rate of 1.8 percent by around 2020.

The IMF began its assessment by noting that the US economy was in its third longest period of economic expansion since 1850, with real gross domestic product some 12 percent higher than its pre-recession peak. But this fact only serves to point to deep-rooted structural changes because the present "recovery" is not bringing any real improvement in the position of the working population.

As the assessment noted, "relative to historical performance, post-crisis growth has been too low and too unequal."

It said that, like other advanced economies, the US was confronted with "secular shifts on multiple fronts."

These include technological change that is reshaping the labour market and low productivity growth, combined with a divergence in wages between more skilled and less skilled sectors of the workforce and an aging population.

"Despite having high per capita income and being one of the most flexible, competitive, and innovative economies in the world, the US model appears to be having difficulties adapting to the secular changes."

The shifts were having real consequences for people's livelihood.

"[H]ousehold incomes are stagnating for a large share of the population (in inflation-adjusted terms, more than half of US households has a lower income today than they did in 2000); job opportunities are deteriorating with many workers too discouraged to remain in the labour force (since 2007, the labour force participation rate has fallen from 66 to below 63 percent…); prospects for upward mobility are waning; and the poverty rate (at 13.5 percent) is one of the highest among advanced economies."

IMF assessments of individual economies are generally conducted in close discussion with treasury and other officials of the country concerned and so often reflect the views of the particular government.

In this case there has been something of a departure from that procedure with the IMF offering critical comments on the Trump administration's policies.

It stated that, as currently framed, "the budget implies significant cuts to discretionary spending that, in the staff's view, would seem to place a disproportionate share of the adjustment burden on low- and middle-income households. This would appear to counter the budget's goal of promoting safety and prosperity for all Americans."

If the IMF is voicing such criticisms, it is not because it has suddenly become concerned about the social and economic position of the majority of the working population—its role in enforcing austerity in Greece demonstrates that. Rather, it is another expression of the growing divergence between Europe and the US over the future economic agenda.

The IMF assessment pointed to “policy uncertainties” surrounding the Trump administration which contained “downside risks” to the growth forecast. A medium-term fiscal consolidation, “such as proposed in the budget”, would result in a growth rate below the IMF’s baseline protection.

And in a criticism of the administration’s trade agenda it said that a “retreat from cross-border integration would represent a downside risk to trade, sentiment and growth.”

While speaking in what might be called the language of economic diplomacy, the IMF essentially poured scorn on the assertions by the Trump administration that its policies can lift the US economic growth rate by at least a percentage point from its present historically low level of around or below 2 percent.

It said that even with “an ideal constellation of pro-growth policies”, potential growth in the US would be lower than that projected in the budget. “The international experience and US history would suggest that a sustained acceleration in annual growth, as projected by the administration, is unlikely. Indeed, since the 1980s there are only a few identified cases among the advanced economies where this has happened. These episodes mostly took place in the mid to late 1990s against a backdrop of strong global demand and many of them were associated with recoveries from recessions.”

The only case in the US where growth increased by a percentage point was the recovery from the deep recession of the 1980s under conditions of increased labour force participation, an expansion of the federal fiscal deficit and increased growth in the trading partners of the US. “These tailwinds are unlikely to recur today.”

The IMF assessment also made an explicit reference to the upcoming decision to be made by Trump on whether to invoke national security considerations in imposing restrictions on steel imports into the US.

In April Trump announced a special investigation into US steel imports under section 232 of the 1962 Trade Expansion Act which allows the US president to limit imports, without reference to Congress, if they are deemed to be a threat to national security.

The IMF warned that the US “ought to be judicious in its use of import restrictions on national security grounds and avoid measures that inadvertently weaken, rather than strengthen, the overall economy.”

The invocation of section 232, which has been described as the “nuclear option” on trade, would represent a major escalation of tensions and possibly lead to other countries invoking retaliatory measures. Last week US trade representative Robert Lighthizer, who has previously worked as a lawyer for the steel industry, said it was a “legitimate use of the statute if the president decides to go in that direction.”

Reports over the past days have suggested that Trump could announce a decision sometime next week in the lead-up to the summit meeting of G-20 leaders to be held in Germany on July 7-8. Invocation of the statute would increase the already significant divisions between the major powers.