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**RESCINDING TAX CUTS WOULD BENEFIT U.S. ECONOMY MORE THAN  
ENACTING BUDGET CUTS, ACCORDING TO NEW LEVY INSTITUTE STUDY**

**Unemployment Would Rise and GDP Growth Would Drop under Spending-Cut Scenario  
Favored by Bush Administration, Levy Macro Team Says**

ANNANDALE-ON-HUDSON, N.Y.—Though recent economic reports have been more optimistic about U.S. economic growth and unemployment, both the Congressional Budget Office (CBO) and International Monetary Fund have warned recently that a surging budget deficit and record trade deficit threaten to spur higher interest rates and undermine future growth. As pressure mounts for policymakers to address the budget deficit, a new study from The Levy Economics Institute of Bard College argues that—in opposition to the Bush administration's plan to slash government spending—rolling back recent tax cuts would bring substantially higher growth rates and substantially lower unemployment rates.

In their Strategic Analysis, *Is Deficit-Financed Growth Limited? Policies and Prospects in an Election Year*, the Levy Institute's Macro Modeling Team—President Dimitri B. Papadimitriou, Senior Scholar Anwar M. Shaikh, and Research Scholars Claudio H. Dos Santos and Gennaro Zezza—argue that the current twin deficits are unsustainable. They explore two scenarios, curtailing spending and rolling back recent tax cuts, for reducing the government deficit by half over five years. They contend that it would be better to reduce the deficit by repealing the tax cuts, and, furthermore, that the sharp rise in actual GDP growth from 2001–2003 had more to do with the jump in government spending than with the reduction in tax rates.

Starting from a baseline of 4.1 percent growth and a 6 percent unemployment rate in 2003, the authors find that halving the budget deficit by cutting government spending would cause the growth rate to fall to 2.6 percent in 2005 and to about 2 percent by 2008. Furthermore, unemployment would rise to about 8 percent over the same interval. Looking at the scenario in

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which the deficit would be cut in half by rescinding recent tax cuts, the authors find that GDP growth would fall only slightly, to 3.8 percent in 2005 and to 3.1 percent by 2008, while the unemployment rate actually falls to 5.1 percent in 2006 before rising back to 5.5 percent in 2008. "The latter scenario also produces less troublesome increases in foreign and government debt burdens, precisely because it gives rise to higher growth rates," the authors write.

The Levy Macro Modeling Team raises two other issues that could affect the outcome of their models. Should the devaluation of the dollar continue, the current account balance would improve and growth would accelerate, the authors maintain, provided that interest rates did not rise in response to the decline in the dollar. However, if interest rates rise, the outlook deteriorates. "If interest rates were to rise in the future as projected by the CBO and others, the prospects of the U.S. economy would significantly worsen," the authors write. "It would create rising interest burdens for the private sector, which would likely slow down its demand for loans and hence its growth in spending. It would also increase the government's interest payments, which would largely benefit foreign holders of government debt, leading to larger income flows out of the country."

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Strategic Analysis, *Is Deficit-Financed Growth Limited? Policies and Prospects in An Election Year*

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