09 April 2021

Research US

Biden's economic agenda means upside potential for growth in 2022-24

Key takeaways

- President Joe Biden's infrastructure package costs USD2,250bn (USD2,650bn including Clean Energy Tax Credits) over eight years (1.4% of counterfactual nominal 2021 GDP (assuming the pandemic had not hit) per year if spending is equally distributed over the eight years). The package is fully financed over 15 years by higher corporate taxes (USD2,750bn or 0.75% of GDP per year).
- This is the first package out of two. The next one focusing on health care and education is set to be presented soon. We expect the next package will cost in the range USD1,000-2,000bn (likely in the middle of the range), financed by higher taxes on wealthy Americans.
- While Democrats can approve both packages using budget reconciliation requiring only a simple majority, the negotiations are much more difficult than for the relief package, as Democrats have different priorities, which was not the case for the relief package.
- We expect the total size of the two packages to be USD4,000bn only partly financed by higher taxes (approximately USD3,000bn). We expect the spending will be front-loaded in 2022-24 due to midterm elections in 2022 and the presidential election in 2024.
- We see upside potential for US GDP growth in 2022 and onwards compared to our current expectation.

The infrastructure package - the first plan out of two

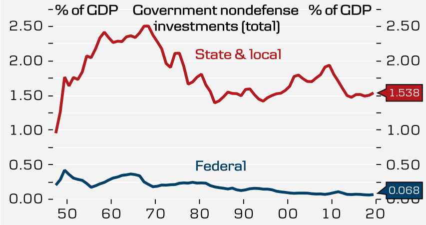
President Joe Biden's infrastructure package

Biden's infrastructure package	8 years	% of GDP per year
Transportation	621	0.3
Manufacturing, R&D, job training	590	0.3
Expand home care services	400	0.2
Housing	328	0.2
Broadband, electrical grid and clean drinking water	311	0.2
Clean Energy Tax Credits	400	0.2
Total spending (over 8 years)	2650	1.4

	10 years	15 years	% of GDP per year
Total corporate tax hikes revenue	1750	2730	0.75

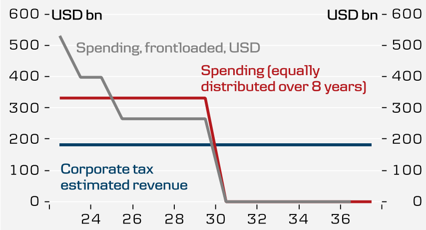
Sources: Committee for a Responsible Federal Budget https://www.crfb.org/blogs/whats-president-bidens-american-jobs-plan

Government nondefense investments have been low compared to GDP for many decades (not as high as from 1947 to 1980)



Sources: BEA, Macrobond Financial

American Jobs Plan is expansionary for the first eight years, contractionary thereafter



Note: In the frontloaded scenario, we have assumed 20% is spent in 2022, 15% in 2023 and in 2024 and 10% onwards

Sources: American Jobs Plan, Danske Bank scenarios

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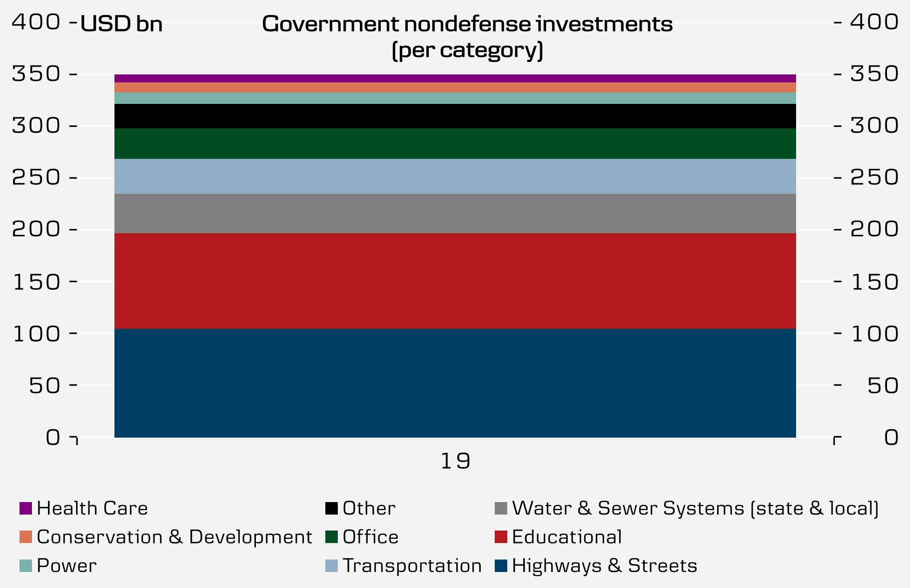
President Joe Biden's American Jobs Plan costs USD2,250bn (USD2,650bn including Clean Energy Tax Credits) over eight years. This corresponds to 1.4% of counterfactual nominal 2021 GDP (assuming the pandemic had not hit) per year if spending is equally distributed over the eight years. The plan focus on five things: 1) Transportation (USD621bn), 2) manufacturing, research & development and job training (USD590bn), 3) expanding home care services (USD400bn), 4) housing (USD328bn) and 5) broadband, electrical grid and clean drinking water (USD311bn).

Government nondefense investments (by category)



Sources: BEA, Macrobond Financial

The Biden administration proposes financing the spending by higher corporate taxes (including a corporate income tax rate hike from 21% to 28% (i.e. not all the way back to the level before former President Donald Trump's tax cuts), a global minimum tax, elimination of deduction for foreign-derived intangible income and a 15% minimum tax on corporate book income). **The plan is only partly financed over the first 10 years (tax hike proposals are estimated to provide a total revenue of USD1,750bn over 10 years or 0.75% of nominal GDP per year) but fully financed over 15 years (total estimated revenue of USD2,730bn)**. **The spending elements are temporary while the tax rate hikes are permanent changes**. We are providing an overview by the end of this piece, otherwise see *The Committee for a Responsible Federal Budget* or *The White House*.

It is worth to keep in mind that this is the first package out of two. President Biden will soon present the second package focusing on education and health care (see *CNBC*). **We expect the next proposal to cost in the range USD1,000-2,000bn, probably in the middle of the range.** In his election campaign, President Biden proposed to hike the top income tax rate from 37% to 39.6% (the level before Trump's tax cuts), repeal deduction for pass-through income for high earners and increase taxation of long-term capital gains and dividends (39.6%, up from 20%). CFRB estimates a total revenue of USD1,400bn over 10 years. This supports our call that the next proposal may cost around USD1,500bn.

President Biden proposes to hike the corporate tax rate from 21% to 28% (35% before former president Donald Trump's tax cuts)

Sources: OECD Tax, Macrobond Financial

Media report that higher taxes on wealthy Americans (with an annual income higher than USD400,000) will finance the second package, see *Bloomberg*. Keep in mind that Biden proposed increasing spending on education and health care for a total of USD4,700bn during the election campaign, which, however, are likely to be watered down, which is also the case for the infrastructure package, see *The Committee for a Responsible Federal Budget*.

Bipartisan deal very unlikely, difficult negotiations ahead

Politically, we think a bipartisan deal is out of the question. The Republicans are not willing to support any corporate tax hikes and also many Republican members of Congress are against most of the green energy stuff. This means that the Biden administration and the Democratic Party would have to use budget reconciliation (enabling them to bypass filibusters in the Senate) once more. **The problem is, however, that it will be tougher for the Biden administration to keep basically all Democrats on board in order to get the bill over the finish line**, as the majority is very slim in both the Senate and the House. The Senate is 50-50 (meaning Vice President Kamala Harris has the tiebreaking the vote) and the Democratic Party can only afford losing three Representatives in the House. **Unlike the relief package, which all Democratic politicians believed was needed, they now all have different priorities depending on which state they are from (and whether they are more leftists or centrists)**. To mention a few problems: Senator Joe Manchin (centrist Democrat) is against hiking the corporate tax all the way to 28%, calling 25% for "fair", see *CNN*. Manchin also mentions that other Democratic Senators are on the same page. In the house, a group of Democrats is pushing for repealing Trump's limit on state and local tax deductions (known as SALT), which raised taxes for high-income earnings in states like New York, see *POLITICO*.

Our base case is that Congress approves both packages eventually but that changes will be made in order to make everyone happy. This implies that the packages will either be smaller, only partly financed or fully financed over even more years than the 15 years in the plan right now. Right now it is too early to tell so we will follow the negotiations closely in coming weeks and months.

According to media (see e.g. *AP News*), House Speaker Nancy Pelosi would like to have the infrastructure package approved by 4 July (although it may slip later into July). This would enable the Senate to approve the deal before the month-long Congressional recess in August. The Biden administration cannot afford to prolong the negotiations for too long. Firstly, they would like to move on to other items on the agenda. Secondly (and more importantly), the Biden administration needs to get it done before politicians start to think too much about the upcoming midterm elections next year. **That said, we are not be surprised if the deal is not approved on this side of summer.**

The good news for the Biden administration and the Democratic Party is that the Senate parliamentarian (an in-house rules expert), Elizabeth MacDonough, has determined that Democrats would be able to do a third budget reconciliation bill this year. The Democratic Party was already able to do it twice this year (one focused on fiscal year 2021 and one fiscal year 2022) but MacDonough has ruled that budget resolutions may contain budget reconciliation instructions giving Democrats more flexibility and room to manoeuvre, see *VOX*.

Economic impact

At the moment, it is difficult to say much about the economic impact. This is due to a combination of tough negotiations, which may alter the package significantly, the second package proposal on its way and the distribution of spending and tax hikes. We would imagine that most of the spending will be frontloaded taking the midterm elections next year and the presidential elections in 2024 into account. Simultaneously, we would not be surprised if the corporate tax rate hike is eventually implemented over some years, as it may not make sense to increase taxation here and now amid the reboot of the economy after the pandemic, where you would like companies to hire and invest. That said, the plan is based on the idea of implementing the tax hikes immediately.

At the moment, we expect the total size of the two packages to be USD4,000bn with most of the spending taking place in 2022-24. We expect the package to be only partly financed by higher taxes (approximately USD3,000bn plus/minus) over 10-15 years. Our reasoning is that Democrats agree on spending but not on financing. There is a tendency for politicians to prefer debt-financing, as “it does not hurt anyone”, at least not near-term. This was also the case when Republicans were in charge and approved Trump’s tax reform.

Given the fiscal multipliers are higher for infrastructure spending than tax hikes (see table below, the package will be expansionary from a growth perspective, meaning upside potential for US GDP growth in 2022-24 compared. At the moment, we are forecasting 7.5% this year and 5.3% next year. How big the growth impact will be also depends on whether the Fed is offsetting the growth impact by tighter monetary policy, as this lowers the fiscal multipliers (see table below).

Assuming that the fiscal multiplier for the spending elements is around 1 and the fiscal multiplier for tax hikes is around 0.25, the total combination of the two packages may add between 2.5pp-4.7pp to total GDP growth in 2022-2024 depending on whether spending is equally distributed or frontloaded. If the final package size is smaller than we anticipate, the growth impact will be lower. The growth impact will not change significantly if tax hikes are higher/smaller, as the fiscal multipliers are low.

Even higher growth would also mean that the Fed is likely to tighten monetary policy sooner (we are currently calling for the first rate hike in H1 2023), which (in addition to higher bond supply as the package is not fully financed near-term) implies upward pressure on US Treasury yields. **This would also reduce the overall growth impact.**

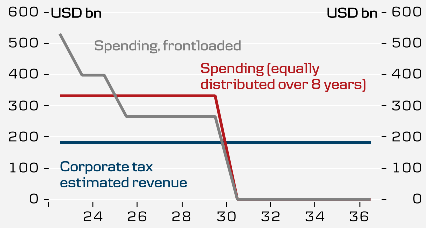
Fiscal multipliers

	Low Estimate	High Estimate
Government consumption	0.5	2.5
Government investments in infrastructure	0.4	2.2
Tax cuts for low- and middle-income earners	0.3	1.5
Tax cuts for high-income earners	0.1	0.6
Corporate tax cuts	0.0	0.4

Note: Low estimates: The Fed offsets expansionary fiscal policy by tightening monetary policy; High estimates: No changes to monetary policy

Source: CBO’s analysis of the American Recovery and Reinvestment Act of 2009

American Jobs Plan is expansionary for the first eight years, contractionary thereafter



Note: In the frontloaded scenario, we have assumed 20% is spent in 2022, 15% in 2023 and in 2024 and 10% onwards

Sources: American Jobs Plan, Danske Bank scenarios

President Joe Biden's American Jobs Plan

Spending proposals	USD bn 8 years	% of GDP per year (equally distributed)
Transportation	**621**	**0.33**
- Electric Vehicles	174	0.09
- Bridges, highways, roads	115	0.06
- Public transit	85	0.05
- Passenger and freight rail service	80	0.04
- Improve infrastructure resilience by safeguarding critical infrastructure and services	50	0.03
Manufacturing, R&D, job training	**590**	**0.32**
- Funding for manufacturing, capital access programs, modernising supply chains etc.	52	0.03
- Additional funding to the National Science Foundation	50	0.03
- Fund investments in the production of critical goods	50	0.03
- Funding for semiconductor manufacturing and research	50	0.03
Expand home care services	**400**	**0.21**
Housing	**328**	**0.18**
- Build energy efficient housing	126	0.07
- Grants to upgrade and build new public schools	50	0.03
Broadband, electrical grid and clean drinking water	**311**	**0.17**
- Funding to build high-speed broadband	100	0.05
- Power infrastructure	100	0.05
- Upgrade and modernise drinking water supplies	56	0.03
Clean Energy Tax Credits	**400**	**0.21**
Total	**2650**	**1.42**

Tax proposals	10 years	15 years	% of GDP per year (equally distributed)
Raise corporate income tax rate from 21% to 28%	850	1300	0.36
Strengthen the global minimum tax for US multinational corporations	500	750	0.21
Eliminate deduction for foreign-derived intangible income	250	400	0.11
Enact a 15% minimum tax on corporate "book" income	100	200	0.04
Prevent US corporations from inverting or claiming tax havens as their residence	25	50	0.01
Eliminate tax preferences for fossil fuels	25	30	0.01
Total	**1750**	**2730**	**0.75**

Sources: Committee for a Responsible Federal Budget https://www.crfb.org/blogs/whats-president-bidens-american-jobs-plan

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This research report has been prepared by Danske Bank A/S ('Danske Bank'). The author of this research report is Mikael Olai Milhøj, Senior Analyst.

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