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Massive Tax Cuts Cleared U.S. Congress for Signing by President Trump

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On December 20, the U.S. House of Representatives voted 224 to 201 to pass massive tax cuts bill, a presidential campaign promise to which President Donald Trump has given priority. Earlier, the Senate passed the tax bill with a vote of 51 to 48. Following the passage through the two chambers, the bill was to be sent to President Trump for his signing to enact the largest tax reduction in three decades.

The tax bill will lower the corporate tax rate from 35% to 21% permanently from 2018. It also includes temporary measures to cut the maximum personal income tax rate from 39.6% to 37% and the inheritance tax and expand tax credits for children. Tax cuts are estimated to total $1.5 trillion (about 17 trillion yen) in 10 years, representing the largest tax reduction since the tax overhaul under the Reagan administration in the 1980s.

In response to the congressional passage of the bill, President Trump in his address at the White House emphasized that the tax reform would greatly contribute to boosting the economy, businesses and employment. The tax cut initiative has been positioned as one of the most important campaign promises since the presidential campaigns. Since its inauguration, however, the Trump administration has had difficulties dealing with Congress, failing to win the enactment of any bill to realize key campaign promises or policies. Therefore, the incoming enactment of the tax reform bill will be the Trump administration’s first major domestic policy achievement.

President Trump may be willing to take advantage of the achievement for halting a fall and winning a rebound in his approval ratings to shore up his administration in consideration of the midterm congressional elections in 2018. However, there are uncertainties about whether he can do so. The tax bill is criticized for favoring large companies and wealthy people too much and is estimated to expand federal budget deficits by more than $1 trillion in 10 years, even with the tax cuts’ economy-boosting effects taken into account. The tax reform’s macro and micro effects are attracting attention.

At least, however, the Trump administration won points by leading its domestic economic policy as a key presidential campaign promise to clear Congress for enactment. The tax reform is expected by a majority to have positive effects on economic growth. Hopes on the massive tax cuts, as well as the robust U.S. economy, have contributed to leading the Dow Jones industrial average on the New York Stock Exchange to rewrite a record high close to 25,000. In a sense, the tax cuts have been discounted into the stock market. Nevertheless, I would like to pay attention to the tax cuts' effects on future stock prices and GDP growth.

Given that U.S. economic growth sustained or accelerated through the tax cuts is expected to have positive effects on the global economy, such effects in 2018 will attract attention. Global economic trends are the most important factor for energy demand and a key point for analyzing the supply-demand environment for the international energy market.

However, tax cuts' effects are not simple. They influence the economy through various complicated paths. If the massive tax cuts accelerate economic growth and push up stock prices, for example, it may have some impact on future interest rate hikes. The Federal Open Market Committee announced 2017's third policy interest rate hike of 0.25 percentage points on December 13 and maintained a plan to raise interest rates three times in 2018. However, the FOMC noted that it would closely watch future U.S. economic growth and inflation. It may pay attention to the impact of the massive tax cuts.

If the tax cuts exert any impact on the timings and degrees of interest rate hikes, it may cause various effects not only on the United States but also on the global economy and the energy market. This is because U.S. interest rates greatly influence global fund flows. Under generally accommodative monetary policy, abundant money is available in the international financial market. U.S. interest hikes may prompt money to go back to the United States and fly away from emerging economies.

Emerging economies, though continuing to grow, have some destabilizing factors including financial risks to which attention must be paid. As the global economic growth center shifts to emerging countries and Asian developing nations, how U.S. interest rate hikes would impact the growth center and how such impact would affect global energy demand growth are key points.

Interest rate changes' impact on fund flows could influence not only economic growth but also flows into risk assets. In this sense, changes in fund flows into crude oil and other commodity futures markets would influence commodity prices. While fundamental supply and demand factors are basically important for commodity prices, financial effects on these prices cannot be ignored. In this sense, we may have to pay attention to U.S. interest rate changes' effects on the dollar's exchange rates. As the dollar's depreciation structurally causes crude oil price hikes or its appreciation triggers oil price drops, I would like to watch future U.S. interest rate hikes' contribution to the dollar's appreciation.

How the key domestic policy achievement the Trump administration made at last one year since its inauguration would influence the U.S. economy, the global economy and the international energy market is a great matter of interest for me.

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