

# Comments on “Taxes and Wages”

by Hasset and Mathur

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## Overview: Strengths

- Clear and plausible set of linkages between taxes, investment, productivity, and wage levels in manufacturing.
- Lots of interesting data with enough variation to generate useful findings.
- Exhaustive sensitivity tests.

## But...

- Reasons to be concerned re all the links in the chain of events.
- Tremendous data challenges.
- Econometric questions re specification and time-series properties of the series.
- Sole manufacturing focus limits policy implications.
- Productivity/wage split: a fundamental challenge when inequality wedge is in play.

## Paul O'Neill from his confirmation hearing:

Senator Murkowski: "...what areas of the tax code do you think would best encourage more business investment?

Changing the depreciation schedule? Cutting the corporate rate or a combination of both?"

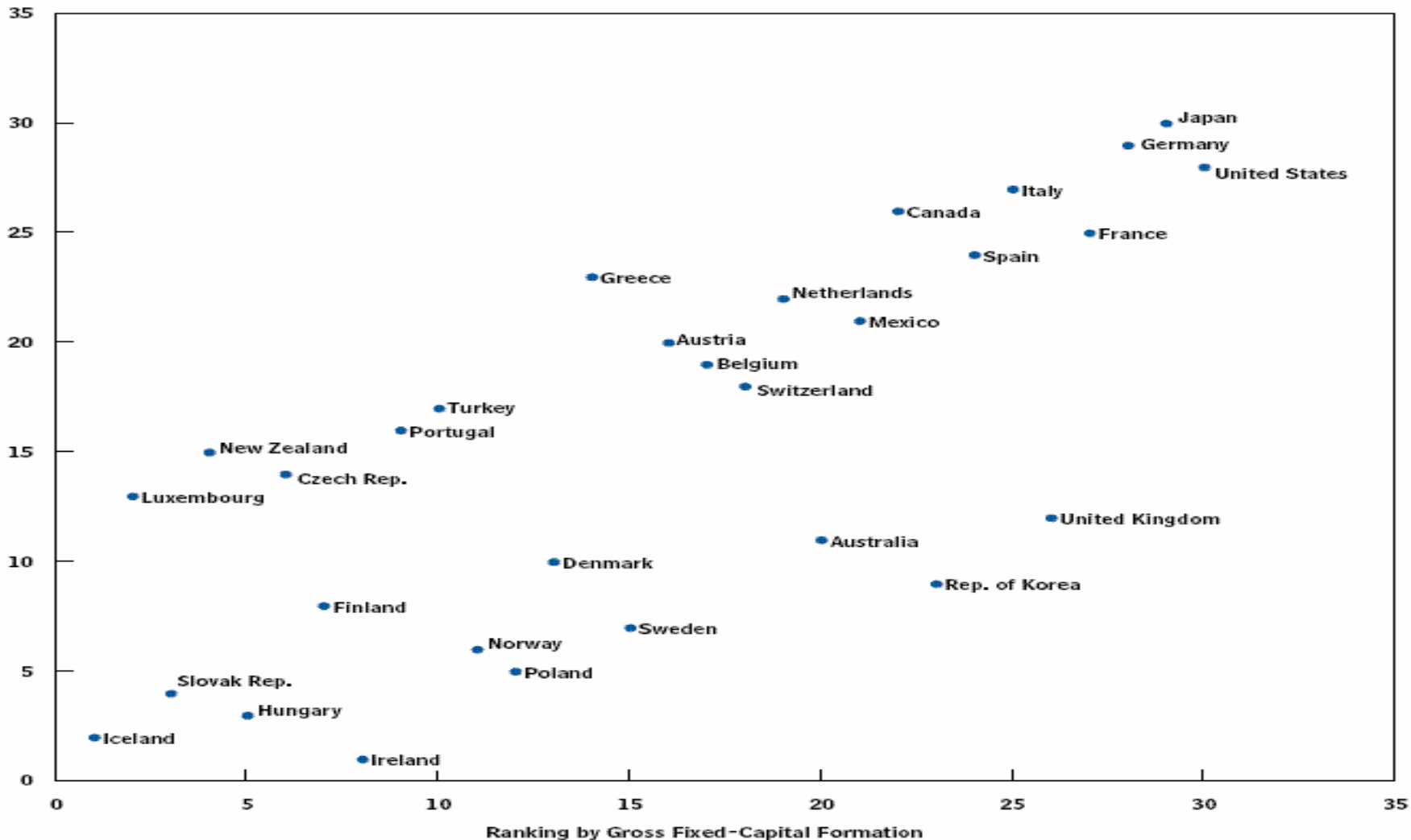
Paul O'Neill: "Let me answer you this way. I guess I will be a maverick for the moment and tell you what I think about this. I never made an investment decision based on the Tax Code."

How much do we know about relationships between:

- corp tax rates and investment?
- investment and productivity?
- productivity and wages?

# OECD Countries' Top Statutory Corporate Tax Rates Relative to Total Investment, 2003

(Ranking by top statutory corporate tax rate)



Source: Congressional Budget Office based on data from M.P. Devereux, R. Griffith, and A. Klemm, "Corporate Income Tax Reforms and International Tax Competition," *Economic Policy*, vol. 35 (October 2002), pp. 451-495; and Organization for Economic Cooperation and Development, *Main Economic Indicators* (Paris: Organization for Economic Cooperation and Development, 2005).

Note: Top statutory corporate tax rates include both national and subnational taxes.

# Econometrics

- Nominal wages have unit roots, even in short panels; add lag of DV but hard to do with 5-yr averages.
- Long averages (5 observations over 72 countries; no lag structures) and lack of instruments make it hard to assert causation (though 2SLS model is persuasive).
- If tax changes work through Inv and Prod, why is contemporary tax variable in model?
- Non-independence: CBO: “The history of corporate tax rates between 1982 and 2003 suggests that countries do not change their corporate tax rates independent of one another.”

## Econometrics, cont.

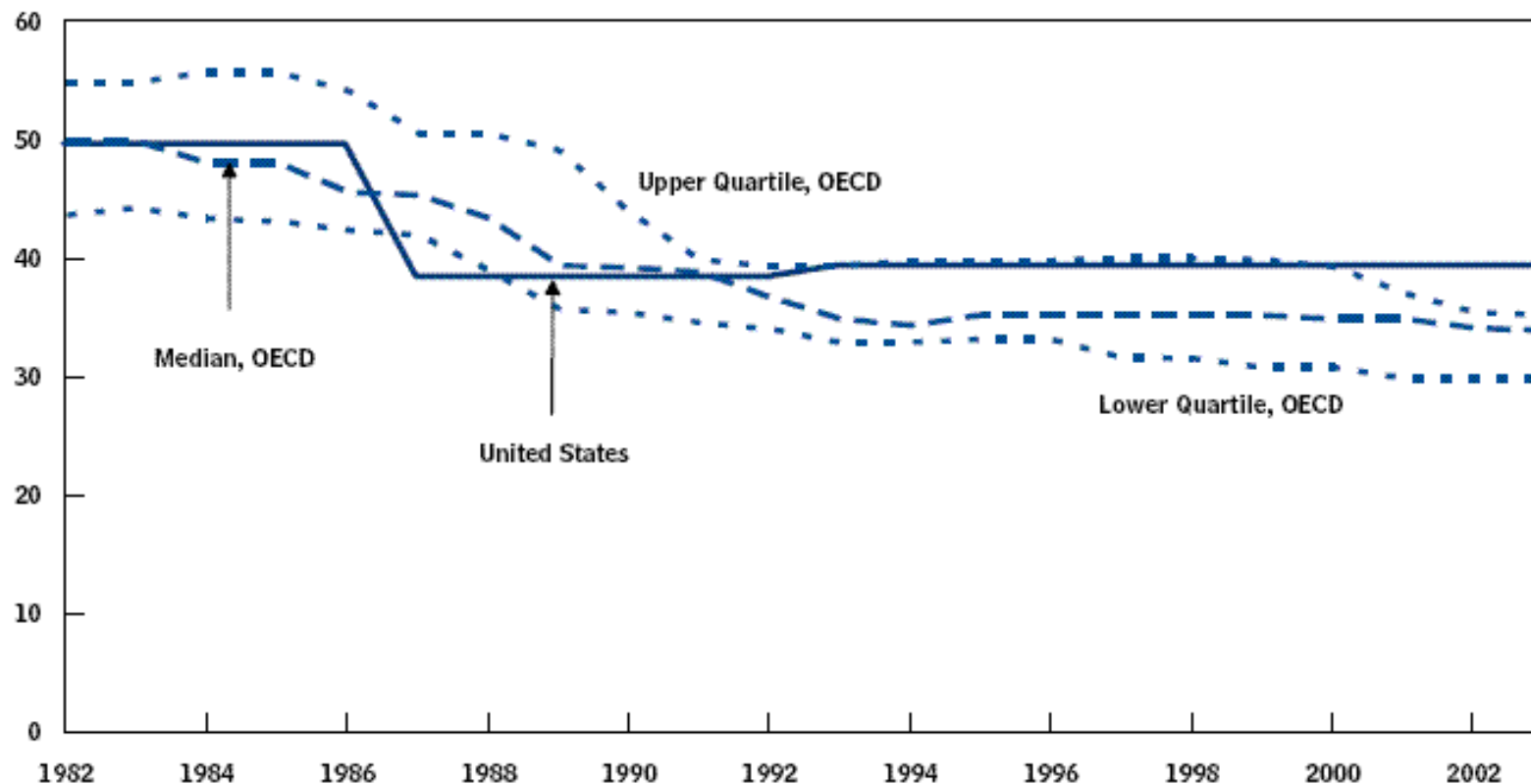
- Enough within country variation of key DV?
- To what extent do high corp tax countries pay lower wages but provide high levels of services through tax system?

2004 OECD avg relative to GDP: 2.5%

US: 1.8%, Norway: 8.2%, Canada: 3.4%, Denmark: 2.9%, UK: 2.9%, etc...

## Top Statutory Corporate Tax Rates in the United States Compared with Summary Measures of Top Statutory Rates for Selected OECD Countries

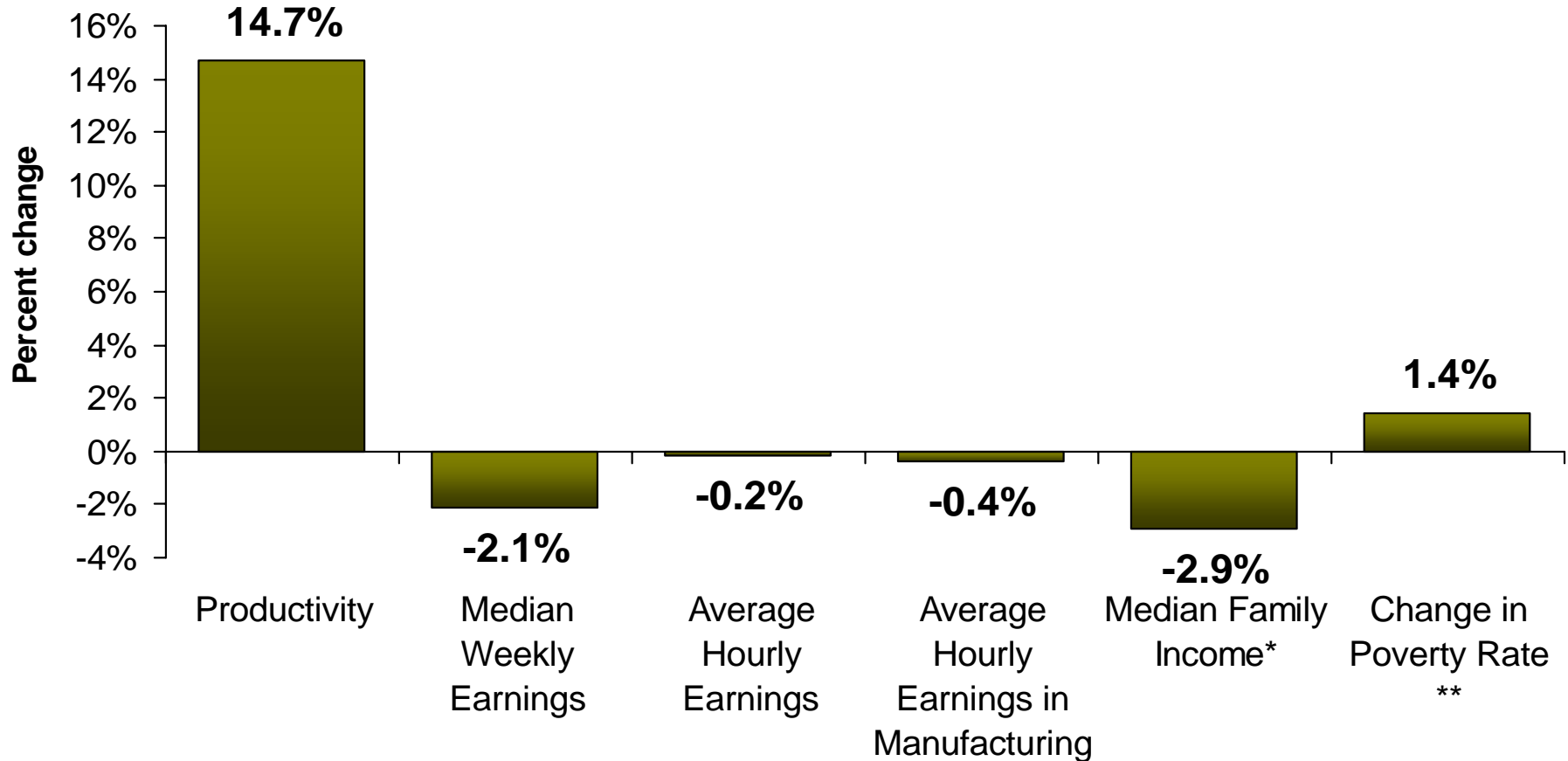
(Top statutory corporate tax rate)



Source: CBO, 2005

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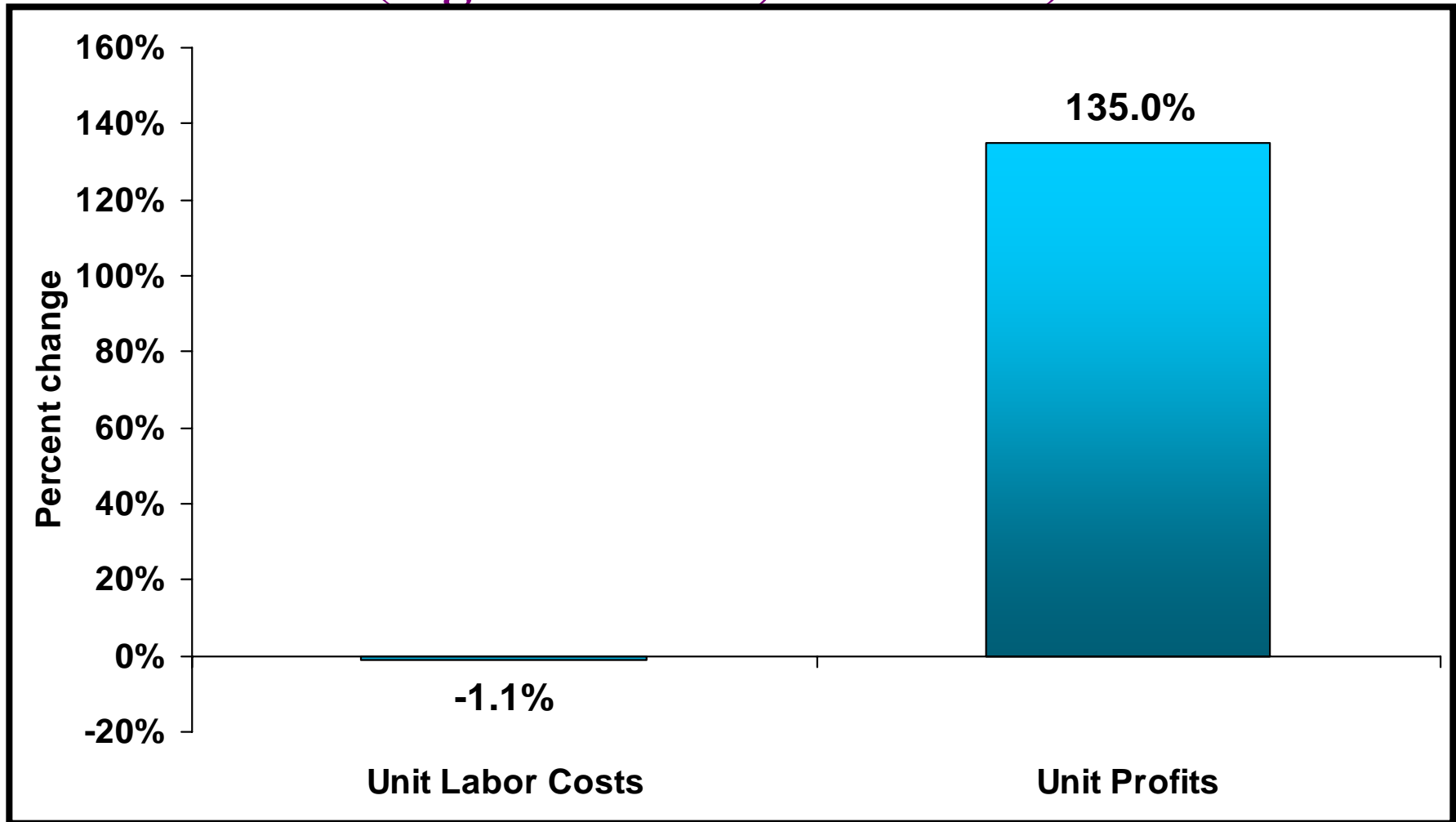
# Productivity and Living Standards 2001q4 – 2006q1



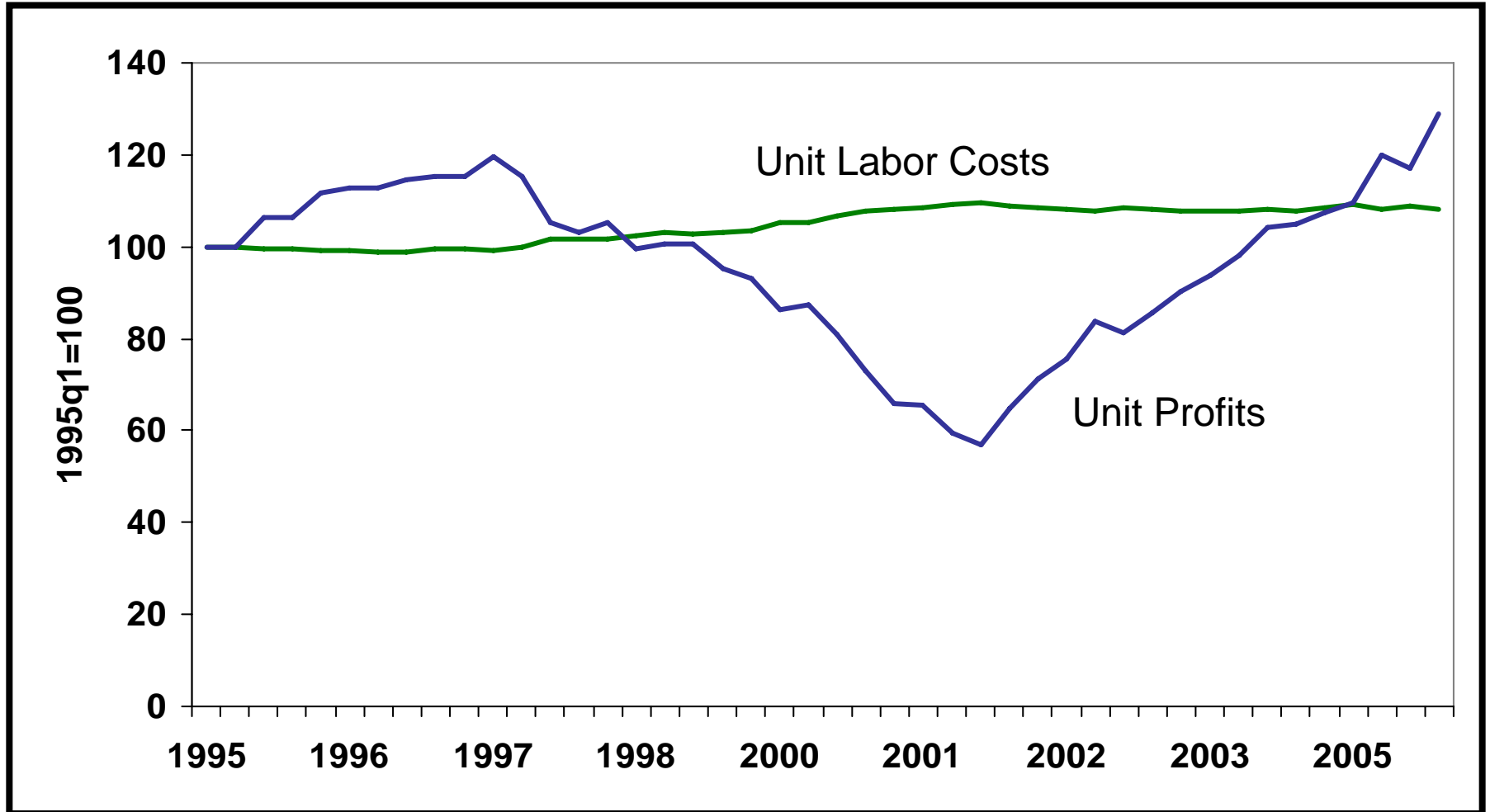
\* Median Income and Poverty are for 2000-04

\*\* Percentage point change

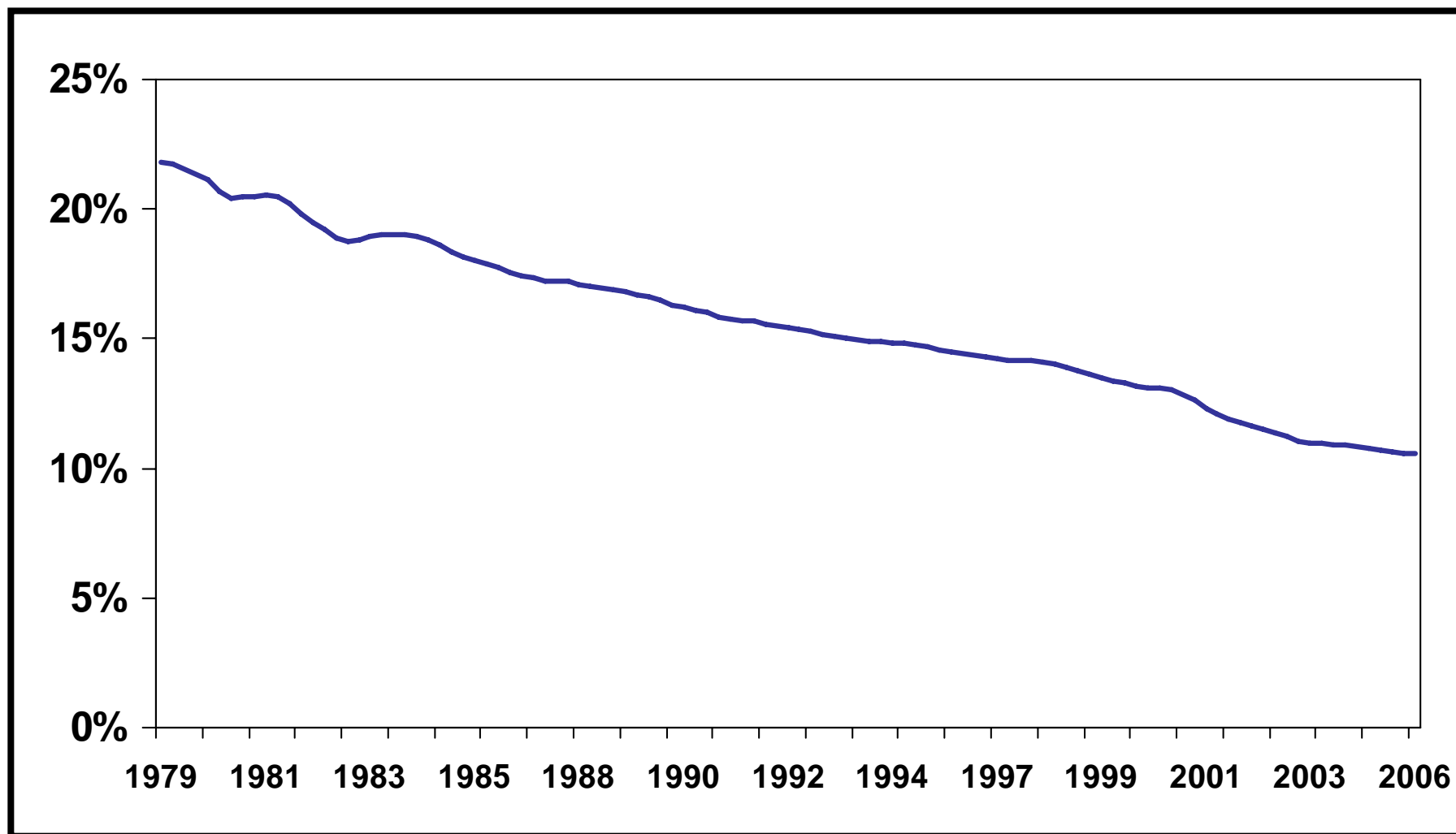
# Unit Costs, Nonfinancial Corporations 2001q4 – 2006q1 (big correction, but still...)



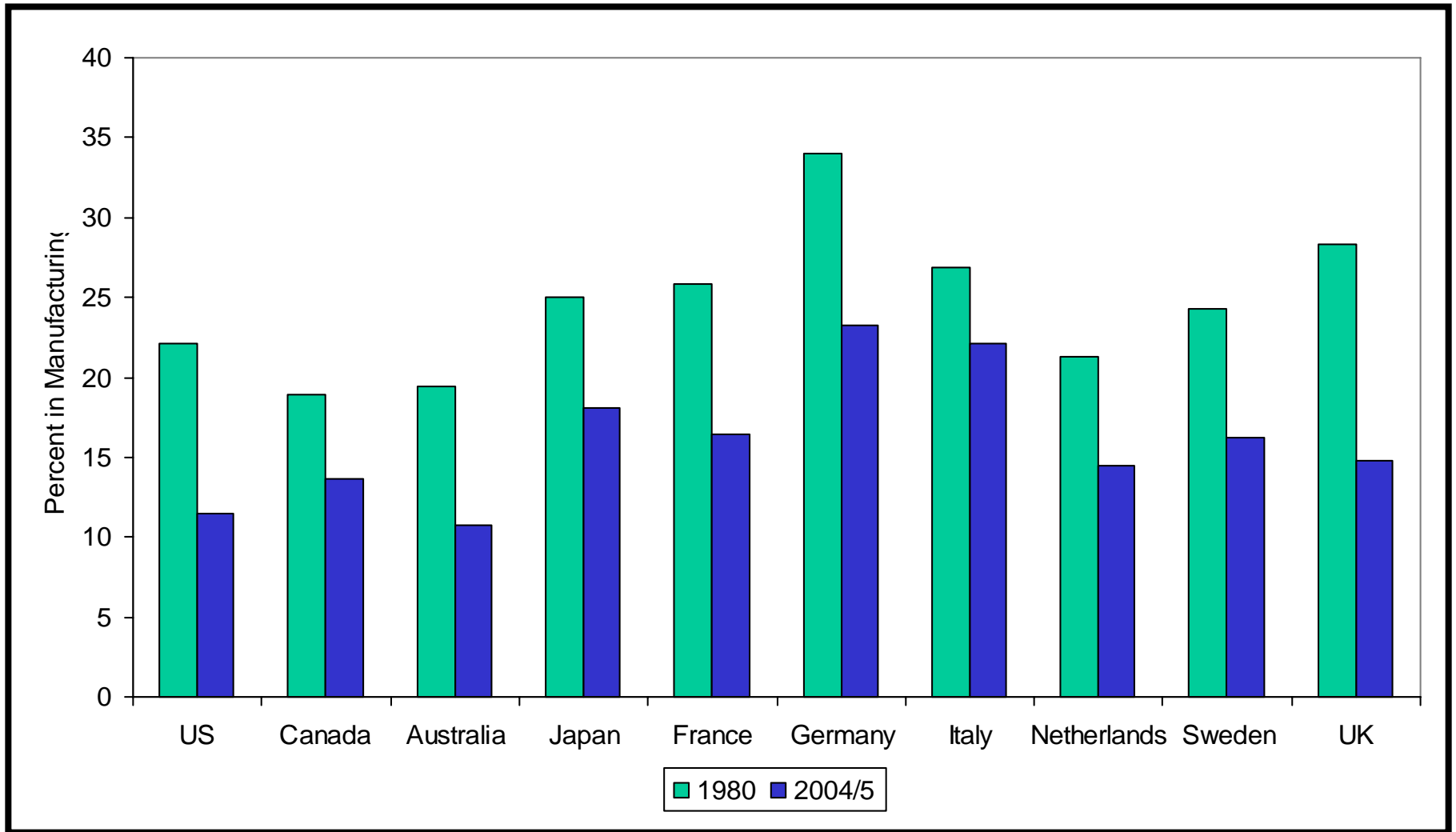
# Unit Labor Costs and Unit Profits, Non-Financial Corporations, 1995-2005



# Manufacturing share of employment, US



# Manufacturing Share of Emp, 1980-2004/5



Source: BLS

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