Reaganomics
Name of economic program espoused by President Ronald Reagan.

When Ronald Reagan was elected president in 1980, largely on the basis of his economic program, the U.S. economy had been plagued with "stagflation" (a combination of high unemployment and high inflation) since the early 1970s. Reagan planned to restore growth and boost employment by cutting income taxes across the board, reducing nondefense spending, easing federal regulation of business and increasing the money supply slowly but steadily. He also promised to increase military spending and balance the federal budget within a few years. "Reaganomics," as it was called, thus would build on two elements of the economic program of the late 1970s under the previous administration of President Jimmy Carter—deregulation and monetary restraint—while adding aggressive new conservative measures. Most economists endorsed Reagan's monetary policy but doubted the overall feasibility of the program.

During his presidential campaign, Reagan increasingly claimed that tax cuts need not be offset fully by spending cuts. He was inspired in this view by an economic theory from economist Arthur Laffer, whose "Laffer curve" postulated that total federal tax revenues actually would increase if tax rates were reduced, because workers would be encouraged to work, save, and invest more. This notion—along with the idea that tax cuts would motivate the wealthy to invest in new plants and equipment (a theory known as trickle-down), thereby creating new jobs for middle- and working-class Americans—were central tenets of supply-side economics. The promise of lower taxes without greater sacrifice greatly appealed to stagflation-weary voters, who ushered Reagan into the White House by a wide margin.

Reagan followed through on most of his economic campaign promises by cutting taxes, easing economic regulation, and moderating economic growth. Following a severe but brief recession in the early 1980s, inflation plummeted. By that time, several of Reagan's top economic advisers, most notably Budget Director David Stockman, had resigned because they doubted the feasibility of Reaganomics. However, the president held firm, claimed his program was beginning to work, and won reelection in 1984. His successor and former vice president, George H. W. Bush, sustained Reagan's fundamental economic policies through 1992.

In retrospect, Reaganomics posted a mixed record. Inflation was controlled and economic growth rose moderately. Economic regulation was scaled back, boosting competitiveness in some sectors including the savings and loan industry, where this competitiveness led some individuals to engage in fraud to gain profits. Nondefense spending cuts were far outweighed by continually rising Medicare, Medicaid, and social security spending and by heavy defense spending. Nor did supply-side tax cuts prove effective; the largest (the Economic Recovery Tax Act of 1981) yielded an average annual net loss of roughly $250 billion per year from 1985 to 1991. Taken together, revenue losses and spending hikes boosted the national debt from 23 percent of GDP in 1981 to 69 percent in 1992. Reaganomics also increased the economic disparities between rich and poor; the income and wealth of the former rose dramatically while middle-class economic status changed little and the poor grew poorer. Under the administration of President Bill Clinton (1992–2000), many of Reagan's policies were reversed; military spending was reduced and social programs were expanded. Reaganomics enjoyed a renaissance after the 2000 election of George W. Bush, who made a large income tax cut and deregulation central to his economic program.

—David B. Sicilia

References

See also Volume 1: Reagan, Ronald; Supply-Side Economics.

Recession
Downturn in aggregate output, income, and employment.

The National Bureau of Economic Research defines a recession as any period in which gross domestic product (GDP) has dropped for two consecutive quarters. The distinction between recession and depression is imprecise and depends on the severity of the unemployment increase and the length of the downturn of real GDP. In the post–World War II period, recessions occurred in 1945, 1949, 1958, 1961, 1970, 1975, 1980, 1982, 1991, and 2001 and usually lasted for one to two years.

In a “growth recession,” there is a downturn in the rate of growth of real GDP, but the growth rate has not yet turned negative. Conditions for growth recession include a large decline in exports and a significant decrease in private expenditure relative to income. Most recently, these conditions became noticeable between the third quarter of 2000 and the second quarter of 2001. The government budget surplus plus the trade deficit equals the private-sector deficit—so if the government spends less than its income (tax revenue), thereby maintaining its surplus, and if the country buys more from abroad than it sells (spending more than its foreign income and thereby increasing its trade deficit) to keep GDP from falling, the private sector must also spend more than its income, thereby incurring a deficit. Thus, when the growth rate declines, a budget surplus cannot lead to a rise in private investment and a healthy long-run rate of profit.

Although the Federal Reserve may cut interest rates considerably in the face of excess capacity, the incentives to build more capacity remain few, even with cheap financing. Thus, increasing government spending and lowering taxes becomes necessary. Otherwise profits drop even farther than prices, while output shrinks and unemployment grows, and as a result the economy cannot run at or near full capacity. With reduced growth of disposable income, firms and households find it difficult to meet their payment commitments. Defaults and bankruptcies grow, and deflationary pressures occur.

—Zdravka K. Todorova and Mathew Forstater