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The full expensing of business investment is expected to contribute to the laws's near-term growth boost. RYAN COLLERD/ AGENCE FRANCE- PRESSE/ GETTY IMAGES

Economic Fallout Will Be Muted at First

Trump's policy law promises a modest economic tailwind, with long-term risks

BY PAUL KIERNAN

For all the fireworks over President Trump's \$3.4 trillion policy measure, the economic impact will be modest at first—too little for most people to notice, economists predict.

Starting this year, more money will be spent on the military and border enforcement. Many people who earn tips, work overtime or are over 64 will pay lower taxes as soon as this year. The bill also reduces projected spending on Medicaid through provisions that will disqualify several million people from benefits starting in 2027, as well as food stamps.

But the vast majority of the bill's price tag comes from extending provisions of the 2017 Tax Cuts and Jobs Act slated to expire Dec. 31. Those extensions aren't going to change the behavior of individuals and firms the way the tax cuts did when first implemented, or the way President Joe Biden's 2021 stimulus did.

That is a macroeconomic plus: Averting a tax increase is one less drag on an economy facing headwinds from Trump's trade and immigration policies.

"The vast majority of it is a continuation of current policy, and everything else that's being battled about is, you know, not big numbers," said Michael Feroli, chief U.S. economist at JPMorgan Chase. "If you're going to talk about GDP and macro things, you need big numbers to make it matter."

* Baseline 8

The legislation's cost and economic effects depend on what baseline is used for comparison. Compared to a scenario in which the 2017 tax cuts were allowed to expire, the new law means gross domestic product, adjusted for inflation, will be 1% to 1.2% larger by 2027, said Kent Smetters, faculty director of the Penn Wharton Budget Model.

But most economists thought complete expiration unlikely since both Republicans and Democrats had long supported extension of most of the tax cuts for individuals. Once Trump was re-elected and Republicans took control of both chambers of Congress, near-total extension became a *fait accompli*.

Versus a baseline in which the 2017 tax cuts were extended, the new bill should add between 0.2 and 0.5 percentage point to GDP growth in 2026, said Josh Hirt, senior U.S. economist at Vanguard.

The benefit from the law could be significantly offset by Trump's tariff increases. Goldman Sachs expects GDP to be about 1% smaller in the first quarter of 2026 as a result of the tariffs.

Among the provisions contributing to the law's nearterm growth boost are temporary deductions for tip income, overtime pay and senior citizens; and full expensing of business investment. Increased spending on defense and border security are also expected to push up growth in the near term. The deduction for state and local taxes, which was significantly pared back in the 2017 law, will be expanded through 2029, at a cost of \$142 billion.

Except for investment expensing, those provisions phase out after several years. Meanwhile, cuts to Medicaid and other spending only take effect after the midterm elections next year. Thus, the tax cut stimulus is frontloaded while the drag from spending cuts is backloaded.

"In the out years, [the bill] flips from fiscal expansion to fiscal contraction as the temporary tax cuts expire and as the planned spending cuts ramp up," said Wells Fargo economists Michael Pugliese and Aubrey Woessner. *

Backloading the spending cuts raises the risk that, in the future, Congress will vote not to implement them at all.

The short-term benefits of the law must be weighed against the potential for trillion-dollar deficits as far as the eye can see, pushing up interest rates and crowding out private investment.

"Our big way of thinking about this bill is, will the deficit impacts overwhelm the potential growth impacts?" Hirt said.

The Committee for a Responsible Federal Budget, which advocates for smaller deficits, estimates if the law's various tax cuts and spending increases are made permanent, it would add \$5.5 trillion to deficits through 2034, pushing debt to 127% of GDP.

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