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Budget Model

Short-Term Economic Effects of the Trump $1 Trillion Infrastructure Plan

Summary: We estimate that the anticipated Trump administration bill to invest $1 trillion in infrastructure would increase GDP up to $720 billion through June 2022.

Introduction

This week, reports indicate that the Trump administration is preparing a proposal to invest $1 trillion in public infrastructure to stimulate the U.S. economy. Public infrastructure spending can boost long-run GDP by making the economy more productive. However, these long-run effects on productivity would not materialize quickly enough to change economic conditions during this recession. Nonetheless, PWBM estimates that states could spend up to $300 billion of this infrastructure aid per year, which would stimulate short-term demand and increase GDP by as much as $720 billion through June 2022.

Federal Aid and State Infrastructure Spending

Given states' current fiscal challenges, their infrastructure spending is likely to fall quickly. Because state and local governments are faced with very large revenue shortfalls, they are going to act more like the "distressed areas" discussed in our previous analysis of federal infrastructure aid, and total infrastructure spending will increase by as much as a dollar for each dollar in federal aid.

PWBM previously estimated that state and local governments would be able to spend up to $300 billion per year in federal infrastructure aid over the next two years, accounting for the availability of shovel-ready projects and the likelihood of project delays due to the virus. Therefore, up to $300 billion per year in federal infrastructure aid will lead states to spend up to $300 billion on infrastructure investment that otherwise would have been cut. This spending will keep workers employed during the recession and increase GDP.

Infrastructure Spending on Output

While the productivity-boosting effects of infrastructure investment are too slow to effectively fight recessions, in times of economic distress, federal infrastructure aid can provide a significant short-term boost to demand. When GDP is below so-called "potential GDP," defined as the maximum sustainable output of the economy, federal aid to states for infrastructure projects effectively stimulates demand and thus increases short-term GDP.

Based on PWBM's recent analysis of the effectiveness of fiscal stimulus in the CARES Act, we estimate that current federal aid to state and local government for infrastructure spending would have a fiscal multiplier of about 1.2, which is the dollar increase in GDP from each new dollar of total infrastructure investment.[1]

Therefore, a $300 billion per year increase in federal infrastructure aid to states would increase GDP by up to $360 billion per year while the recession lasts. If the Trump administration's plan allocates $300 billion to infrastructure aid in each of the next two years through June 2022, GDP will increase by a total of $720 billion over those two years.

When the recession is over, and actual GDP recovers to a level close to its potential, the multiplier will fall to close to zero and so additional infrastructure spending will have roughly zero additional effect on GDP. Moreover, federal aid beyond $300 billion in each 12-month period would likely go towards non-shovel-ready projects and so its effects on short-term demand would be hindered by slow spending rates.

This analysis was conducted by Jon Huntley with writing support from Kody Carmody.

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1. The transportation support provision of the CARES Act includes spending besides transfers to state and local governments for infrastructure and so has a different multiplier than what we apply here. These other categories include transfers to persons, business tax provisions primarily affecting cash flow, and a one-year tax cut for higher-income people. ↩