Trickle-Down Economics

Walter E. Block*
Loyola University New Orleans
United States of America

Abstract
Trickle-down economics is the hypothesis that when the rich get wealthier, this will positively impact the poor. The rich will lift up the poor into a less poverty-stricken situation. This hypothesis has been widely excoriated in the literature. Sometimes it has been conflated with the Laffer curve. The present paper makes the case that there is more to trickle-down economics than the critics allow.

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Trickle-down economics has had bad press as of late. Critics have been piling on.[1]

According to Hope (2020), in the view of the International Monetary Fund (Dabla-Norris et al. 2015) "a rising income share of the top 20 percent results in lower growth—that is, when the rich get richer, benefits do not trickle down." And the Associated Press (2017) maintains that "history shows [trickle-down economics] has a spotty record of delivering on its promises."[2] The entire Keynesian edifice bitterly opposed this concept, on the grounds that the rich spend a disproportionately smaller percentage of any additional revenue they are able to garner than the other income groups.

What is trickle-down economics? It is the view that the poor will gain in welfare if there are more rich people around. The metaphor sometimes bandied about is that the tables of the rich are heavily laden with food, and they sit back as they eat so that crumbs drop onto the floor, there to be picked up by the poor, starving wretches.

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[1] This is not allowed in football, but all is fair in this regard in political economy.

[2] The Associated Press characterizes the matter as follows: "Does money roll downhill?" But this is a problematic way of looking at the matter. It implies that the rich donate money to the poor. But this hardly exhausts the manner in which the wealthy, by gaining even more wherewithal, are able to help the poor.

This way of benefiting the poor not only is rather insulting but is thought, also, to be erroneous by the critics. The rich are far more careful than that, and they keep the goodies to themselves, all of them. There is no trickle down, at least not from any such source.[3] Further, the rich get rich by impoverishing the poor—not by helping them, directly or indirectly. Certainly all Marxists in good standing would support this criticism (Gordon 1990; Raico 1977; Roemer 1982, 1988; Zwolinski 2007).

What are the facts of the matter?

Yes, the rich often trickle down wealth to the poor, directly.[4] They do so not at all by allowing crumbs to fall onto the floor and the poor to gather them up, but rather via charity, often very generous charity (Fuss and Li 2022; Hayman 2016; Priday 2020).

But they help them to a far greater degree indirectly via the free marketplace. How did Ray Kroc first become wealthy?[5] He did so by enriching himself—and pretty much everyone else who purchased one of his burgers, and this certainly included the impecunious. This took place every time anyone visited his emporium, McDonald's. Assume the price of a Happy Meal was $10. How much did the buyer value that offering? Not less than that amount—for example, at $9, he would have lost $1. Nor precisely $10. For at that valuation, why would he have bestirred himself to get off his couch and make the trip to visit Ronald McDonald? No, there would have then been nothing in it for him; he would not have earned a profit. He would just have broken even. If he purchased the burger, he expected its value to himself would be more than that $10—for example, $12. In that case, there would have been a $2 profit in it for him. So, yes, Ray Kroc made a profit on the deal. The meal might have cost him $7, in which case he pocketed $3. But in so doing he enriched every purchaser, including the poor ones. He did not exploit them, as the Marxists would have it.

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[3] Rich farmers allow gleaners, but this is because it is thought that it would cost them more to pick up the grain they missed than its value to themselves.

[4] Here is a statement by a referee of this journal: "I'm not convinced TDE is anything other than an intellectually lazy slander. Who actually defends it? Who are its chief advocates, according to its detractors?" I have no idea who are its chief advocates, according to its detractors. The critics do not condescend to mention this point. But there are plenty of scholars who defend this theory, apart from the present author—for example, North (2018), Anderson (2015), Matthews (2021), Cordato (2018).

[5] He did not start out that way.

What are the effects of investment on wages? It all depends upon whether the investments are profitable. If they are, wages inevitably rise since marginal revenue product will increase, and wages, at least in equilibrium,[6] are equated with that variable. However, if the investment is misallocative, then, depending upon the degree to which it is not integrated with consumer and producer desires, it may or may not improve wage levels. However, the good news in this regard is that those who engage in malinvestments tend to lose money and have less control of resources subsequently.

Even the Keynesians are on board with trickle-down economics.[7] They, in sharp contrast, emphasize aggregate demand. Who do you think has much demand for goods and services if not the well-to-do? I thus applaud their support for trickle-down economics. However, I do so with great misgiving: the Keynesians are wrong about pretty much everything they say about the dismal science.[8] I comfort myself with the fact that even a broken clock is correct twice per day. It cannot be denied that these economists claim that the rich allot all too much of their funding to saving, which in their mistaken view hurts the economy.[9] But at least the rich, given that they do not take any money away from the poor in the first place as we have seen, add their mite to aggregate demand.

Here is yet another piece of support for trickle-down economics. This one concerns immigration. Authorities in charge of whom to admit to the recipient nation, if they want to improve the domestic economy, are forever looking for rich people, including entrepreneurs who can create employment slots, or investors, who amount to something similar (Frank 2017; Shaw 2022; Singer 2019). They rarely put floor sweepers at the top of their list of desired newcomers. Why? Trickle-down economics, of course. The top 1

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[6] Which we never reach, but we are always tending in that direction.

[7] At least they can be interpreted in that manner, although they would scarcely agree.

[8] One of the most powerful objections to the Keynesian enterprise is Say's law. It states that production, not consumption (as Keynes would have it), is the driving force of the economy. The former makes the latter possible, not the other way around. For further elucidation of this law, see Anderson (2009), Bylund (2017), Hazlitt (2010), Hutt (1974), Mises (2022), Rothbard (2012), Say ([1880] 1971), Sowell (1972).

[9] How else do we get capital that enhances labor productivity and hence wages apart from saving, from both domestic and foreign sources? For a defense of saving, see Garrison (1994, 2001), Hayek (1931), Hazlitt (1959, 1983), Mises ([1949] 1998), Murphy (2008), Rothbard (1963, 1993).

percent of the income distribution consists of people from whom trickles can come down, not those from the other end of the distribution of wealth, from whom no trickles whatsoever emanate.

Trickle-down economics is sometimes confused with supply-side economics and the Laffer curve. It is correctly maintained that the poor do not always see an improvement in their standards of living after a tax cut for the rich. True enough. But one reason is that in reality when taxes are lightened for the rich, hundreds of other variables are changing as well. It is no easy task to tease out the effects of this one alteration, in the midst of all these other goings-on. Further, the thesis of trickle-down economics is not at all implicated when the lowest decile fail to see an improvement in their well-being subsequent to this alteration in taxes.[10]

All Laffer is saying (Laffer 2004; Laffer, Domitrovic, Sinquefield. 2022; see also Barnett and Block 2005; Block 2010; Murphy 2004; Salerno 2013) is that if the government sets a tax rate of 100 percent, it will collect no taxes since no one would work, on the books at least, if they could not earn a single dime thereby. Similarly, if the tax rate were zero, again no taxes would be garnered, for obvious reasons. This means, necessarily, that the tax take would rise as the rate fell from 100 percent and rise as it increased from zero. It also logically follows that there is some inversion point from which, when rates rise or fall, tax revenues are constant. Another logical implication is that if tax rates were above this point, a reduction in them would imply more revenue, and, if below, then less. This is all a matter of pure mathematical logic, and those who reject this are necessarily in error. Of course, it by no means follows that if tax revenues rise, this will benefit the poor. All too likely, the government will give this additional money to corporate capitalists,[11] in an orgy mislabeled "rent-seeking."[12]

As for the International Monetary Fund, trickle-down economics says nothing about "a rising income share" for the rich. When this occurs, the lot of the poor necessarily declines, for, at any given time, the size of the pie is fixed; there is a zero-sum game in operation

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[10] We should not overlook that, ceteris paribus, cuts in, for example, corporate income taxes result in benefits for shareholders, employees, and customers.

[11] It is surely no accident that most of the richest counties in the US are clustered around Washington, DC. See on this Morello and Mellnik (2012).

[12] What is so wrong with innocent rent? On rent-seeking see Bhagwati (1982), Block (2000, 2002, 2015), Buchanan (1983), Henderson (2008), MacCallum (2015), Pasour (1986), Wenzel (2016a, 2016b).

(Sowell 2000). If the share of the rich rises, of course, others, including the poor, have less. No, trickle-down economics is predicated upon the wealthy becoming even richer as part and parcel of the operation of economic freedom, not at the expense of the poor.

So, the next time you hear criticism of trickle-down economics, take it not with a grain of salt, but with a whole bucketful.[13]

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[13] For a more sensible perspective on this issue, see Anderson (2015), Cordato (2018), Galles (2016), Kowalski (2023), Matthews (2021).

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