

Tax rebates not a quick fix for the economy

January 22 2009

(PhysOrg.com) -- If last year's tax rebates are any indication, one-time payments from the government are a weak economic stimulus, say economists at the University of Michigan.

"The rebates in 2008 provided low bang for the buck as an economic stimulus," said Matthew Shapiro, U-M professor of economics. "Putting cash into the hands of the consumers who use it to save or pay off debt boosts their well-being, but it does not necessarily make them spend."

Using the U-M/Reuters Survey of Consumers, Shapiro and colleague Joel Slemrod asked more than 2,500 Americans what they did with their 2008 federal income tax rebates, which accounted for more than two-thirds of the \$152 billion Economic Stimulus Act of 2008. For the most part, those who filed taxes as single individuals received between \$300 and \$600, while those who filed jointly got between \$600 and \$1,200. In addition, parents with children under 17 received an extra \$300 per child.

The U-M economists found that only 20 percent of U.S. households mostly spent their tax rebates, while about 48 percent used their rebate mostly to pay debt and roughly 32 percent mostly saved their rebate checks.

Americans 65 and older were more likely to spend their rebates, Shapiro and Slemrod say. More than 28 percent of this age group mostly spent the money, compared to only 17 percent of Americans under 65. They found little evidence that spending is related to income, except for those

earning less than \$20,000 a year—58 percent used the rebate to pay off debt, compared with 40 percent of those with incomes above \$75,000.

Shapiro and Slemrod say the overall results are similar to what they found in an earlier study of the 2001 federal income tax rebates, when about 22 percent of Americans mostly spent their rebates.

"In all, adverse shocks to housing and other wealth may have focused consumers on rebuilding their balance sheets in 2008," said Slemrod, professor of business economics at U-M's Ross School of Business and director of the Office of Tax Policy Research. "Given the further decline of wealth since the rebates were implemented, the impetus to save a windfall might be even stronger now."

"Those designing the next economic stimulus package should take into account that much of a temporary tax rebate is likely not to be spent," Shapiro said. "Instead, tax changes that give a sustained boost to purchasing power of households are more likely to be effective."

Provided by University of Michigan

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