

Economic Policy

When Reagan took office the economy was one of the double-digit inflation and high interest rates. During the campaign Reagan promised to restore the free market from excessive government regulation and encourage private initiative and enterprise.

Reagan's economic policies came to be known as "Reaganomics," an attempt, according to Lou Cannon, to "balance the federal budget, increase defense spending, and cut income taxes." The President vowed to protect entitlement programs (such as Medicare and Social Security) while cutting the outlays for social programs by targeting "waste, fraud and abuse." Reagan embraced the theory of "supply side economics," which postulated that tax cuts encouraged economic expansion which in turn increased the government's revenue at a lower tax rate.



During his first year in office, Reagan engineered the passage of \$39 billion in budget cuts into law, as well as a massive 25 percent tax cut spread over three years for individual, and faster write-offs for capital investment for business. At the same time, he insisted on, and for the most part, was successful in gaining increased funding for defense.

Although inflation dropped from 13.5% in 1980 to 5.1% in 1982, a severe recession set in, with unemployment exceeding 10% in October, 1982 for the first time in forty years. The administration modified its economic policy after two years by proposing selected tax increases and budget cuts to control rising deficits and higher interest rates. After the 1982 downturn, the reduced inflation rate (under 5% for the remainder of the administration) sparked record economic growth, and produced one of the lowest unemployment rates in modern U.S. history (unemployment hit a 14 year low in June of 1988). As Reagan left office, the nation was experiencing its sixth consecutive year of economic prosperity.

The economic gains, however, came at a cost of a record annual deficit and a ballooning national debt. The budget deficit was exacerbated by a trade deficit. Americans continued to buy more foreign-made goods than they were selling. Reagan, however adhered to his free trade stance, and signed an agreement to that effect with Canada. He also signed, reluctantly, trade legislation designed to open foreign markets to U.S. goods.