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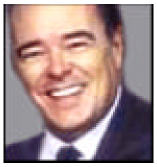

West Wing Airing: Tax Cut a Good Thing

By John Rutledge
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Talk about *deja vu*. This week I had the chance, along with a dozen other investment strategists, to brief President Bush and Treasury Secretary John Snow on the impact of the dividend tax cuts on growth, interest rates and stock markets.

I sat in the same chair, in the same room in the West Wing of the White House discussing the same subject, as I did 22 years ago in 1981 when we were putting together the Reagan economic plan. The only difference is that I had black hair then.

The consensus of the group was that the economy is much weaker today than it was when the president announced the plan. We need a growth boost more than ever.

The strategy group advised President Bush that ending the double taxation of dividends is the single greatest thing he can do to bring back growth to the economy, improve governance in our companies, and restore confidence among investors. In our discussion it became very clear that the White House is going to fight very hard for the congressional support to get the largest stimulus plan possible, and that the administration believes the dividend tax cut is the cornerstone of the plan. Don't expect them to fold under pressure on this one.

The tax cuts in the president's jobs and growth plan will be the biggest event to hit the U.S. economy and asset markets since the Reagan plan in 1981. The most important element of the plan is ending the double taxing of dividend income that has given America the highest taxes on capital in the industrialized world. It would work by raising the after-tax return on capital by nearly two-thirds.

This approach would increase equity values by 10% initially, with the potential for another 10% to 20% down the road as companies adapt to the new tax rates. The plan would add $1 trillion to $3 trillion to net worth initially. It would make capital available to companies to buy new tools and equipment to make workers more productive.

Worker Benefits

The dividend tax cut is a Main Street policy, and it will work by increasing the capital stock, which will raise productivity and real incomes. The benefits will be enjoyed by working people, not coupon-clippers, both by increasing the value of their pension funds and by increasing their incomes.

U.S. workers have the highest productivity in the world. They're productive because they have the best training and the most modern tools. The dividend tax cut will bring more tools to workers to create more high-paying jobs, just as the 1981 tax cuts did.

The increased dividend payments will exert powerful discipline on managers, will help to restore proper governance to businesses and improve confidence among investors.

The revenue lost to the government totals about $30 billion a year, even before thinking about any new tax revenue that would accompany growing incomes and higher capital gains. This number isn't material to our $10 trillion-plus economy, still less so for our $100 trillion-plus asset markets. It would have no measurable impact on interest rates. But the benefits of the tax cut will be enormous.

We have a once-in-a-generation opportunity to correct such a destructive element of the tax system. We can't afford to miss this opportunity. We must end the double-tax on dividends now.

Dr. John Rutledge is the chairman of Rutledge Capital, a Greenwich, Ct.-based private equity investment firm, and of Rutledge Research, a Virginia-based economic advisory firm. He also publishes The Rutledge Report, a weekly investment newsletter, and serves as chairman of the advisory boards of the B.V. Group, a venture capital, hedge fund and real estate investment firm, and Saugatuck Capital, a middle-market private equity firm. Rutledge serves as partner at Kudlow & Co. At the time of publication, he had no positions in any of the securities mentioned in this column, but holdings can change at any time. Under no circumstances does the information in this commentary represent a recommendation to buy or sell stocks. While he cannot provide investment advice or recommendations, he invites you to send your feedback.