Posted on Wed, Sep. 14, 2011

Ignore costly, unneeded plan

By Jagadeesh Gokhale

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President Obama hopes that his jobs plan will be passed quickly by Congress. It shouldn't be passed at all.

The president's speech centered on two key ideas: additional spending on construction projects and hiring incentives, and a tax cut for low- and middle-class families through an extension and expansion in the temporary payroll tax cut scheduled to expire this year.

The total package is expected to cost about $450 billion - about half the size of the stimulus enacted in 2009. However, a quick look at statistics on domestic investment, trade, and consumption suggests that this new stimulus is not needed. Indeed, it would be a mistake to pass it if the objective is to create sustainable job growth.

The president linked his spending proposals to the need to put construction workers back to work. These workers are the largest group among those who lost jobs during the 2007-09 recession, initially from the housing-sector bust and later because of a steep decline in investment spending by firms that ditched plans to add to their production capacity. But data from the U.S. Bureau of Economic Analysis shows that both private and total domestic investment spending (mostly the former) are already recovering from the decline they suffered during the recession.

Growth in investment spending, which cratered after the first quarter of 2008, is now back to its prerecession level. That means the lack of progress in reducing the unemployment rate is not because firms are not spending to increase capacity, but because there is a mismatch in jobs available and worker skills. Increasing government spending on additional construction projects is therefore misguided: It will simply slow the change in skills and training that workers must undergo to be successful in a changing economy. We might want to "out-educate, out-invest, and out-innovate the rest of the world," but doing so by siphoning away resources that private firms could invest, while encouraging a stagnant skill pool, is the wrong direction.

That brings us to the payroll-tax cuts that are intended to stimulate consumption spending. Again, however, BEA data show that private consumption growth is already on the mend. The steep decline in consumption growth during 2008-09 has already been restored.

Consumption growth averaged 1.3 percent per year from 2002 to '07 and this growth has already recovered back to above 1.0 percent per year since the second quarter of 2009. This is consistent with a recovery in firms' expectations of sustained growth in demand and should lead to continued recovery in domestic investment spending. Adding a stimulus to consumption spending does not appear justified, except to purchase an insurance policy for Obama's reelection bid at taxpayer expense.

Foreign trade is the one sector where BEA data show the balance of trade and income has worsened since early 2009. A renewed push to expand trade agreements and markets is the only economically sound element in the president's speech to Congress on job creation.

Obama said that every dollar of the new spending and tax cuts will be paid for. The question is, who will pay and when? The clear answer is that the election insurance policy the president is demanding will be deficit financed. The only payment mechanisms Obama identified was a one-line exhortation for the super-committee to "do more" and a vague reference to working on Medicare reform.

Finally, cutting payroll taxes but keeping the Social Security and Medicare trust funds whole by transferring IOUs to them shifts the burden of funding entitlements to taxes on capital income. Warren Buffet notwithstanding, taxing capital income is well known to degrade economic incentives to save and invest - a policy contradictory to the president's objective of creating sustainable job growth. Such a policy may deliver a bang, in terms of jobs, that the president wishes today, but it will demand more bucks and induce more job losses in the future.

Congress should ignore Obama's repeated calls to pass his domestic policy proposals.

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