Written by Brian Koenig on February 14, 2011

Economic Stimulus and Economic Stress

The AP Economic Stress index gives a score from 1 to 100 (the higher the score the more stress), basing criteria on unemployment, bankruptcies, and foreclosures; counties with a stress level over 11 are deemed to have "stressed" economies, and over the past couple of months, many have surpassed this unfortunate mark.

One aspect of the economy that has recently shown signs of restoration is unemployment. The unemployment rate has plunged over the past two months, from 9.8 percent in November to 9 percent in January, the sharpest two-month decline since the Eisenhower administration. (The Bureau of Labor Statistics' U-6 rate, its broadest unemployment measure, which includes short-term discouraged and other marginally-attached workers as well as those forced to work part-time because they cannot find full-time employment, puts unemployment at about 16 percent. And if we add long-term discouraged workers, as does economist Walter Williams at Shadow Government Statistics, unemployment is about 22 percent.) Some claim that this "great news" is proof that President Obama's stimulus plan is finally showing a heartbeat, while others applaud the extension of the Bush tax cuts, as it has assured businesses of a barrier to future tax increases.

The current discussion among analysts, and the economic predictions for the rest of 2011 and beyond, will concentrate on whether or not the Bush tax cuts extension will spur the growth that fiscal conservatives anticipate. The question also lies with whether or not the Economic Stimulus of 2009 will drive economic growth, which up to this point has been dormant.

Harvard professors Alberto Alesina and Silvia Ardagna co-authored a paper on adjustments in fiscal policy and their impact on expansionary and recessionary economies. The analysis observed 107 fiscal adjustments in 21 Organization for Economic Cooperation and Development (OECD) countries between 1970 and 2007. Their goal was to determine the relationship between government spending and economic growth and to analyze the "stimulus vs. tax cut" paradigm.

Alesina and Ardagna defined an expansionary fiscal adjustment as when a country's rate of GDP growth, during the year of the adjustment, was in the top 25 percent of the OECD. Conversely, a recessionary period was when a country's GDP growth was in the bottom 75 percent. Professor Alesina declared in the *Wall Street Journal*, "Our results were striking," adding,

> Over nearly 40 years, expansionary adjustments were based mostly on spending cuts, while recessionary adjustments were based mostly on tax increases. And these results would have been even stronger had our definition of an expansionary period been more lenient (extending, for example, to the top 50 percent of the OECD). In addition, adjustments based on spending cuts were accompanied by longer-lasting reductions in ratios of debt to GDP.

Indeed, the researchers concluded that *spending-based stimuli actually contributed to reduced economic growth*. One need not be an acclaimed economist with a Ph.D. to realize that stimulus spending takes money from one sector of the economy and transfers it to another. This is not distribution; it is redistribution. A transfer of wealth from one segment of the populace to another, whether it is businesses or individuals, does not pump money into the economy — assuming the Fed keeps its hands off the printing press.

Many analysts predict substantial economic growth in 2011, largely due to the Bush tax cuts extension, which will save millions of Americans thousands of dollars in taxes while decreasing Social Security taxes for employees. Naturally, the extension leaves more money for consumers to purchase goods and services and, more importantly, eliminates the fear of a deepened tax burden for investors and business owners.

John Cochrane of the University of Chicago explained this phenomenon: "Every dollar of increased government spending must correspond to one less dollar of private spending. Jobs created by stimulus spending must correspond to one less dollar of private spending." He further advised that created jobs from stimulus spending are "offset by jobs lost from [a] decline in private spending," and "stimulus jobs" are generally less productive than private sector jobs.

Because there is no crystal ball to reveal the next 10 months, the only way to soundly predict economic growth is through historical analysis, and the recent exposure of American government activity provides all the history needed to reach a conclusion.

Over the past few years, during both the Bush and Obama administrations, Congress passed three separate stimulus packages totaling roughly $1 trillion. The first stimulus was hatched in February 2008 under the Bush administration, and included a $600 individual tax rebate, loan guarantees for housing, and other miscellaneous "stimuli"; at the time, the unemployment rate stood at 4.9 percent.

Then in September 2008, as the recession progressed, a $61 billion stimulus was passed, which went primarily to infrastructure projects and unemployment extensions; a month later the unemployment rate rose to 6.5 percent.

In February 2009, President Obama passed the mother of all stimulus packages, a $787-billion pork-barrel spending spree; when the bill passed, the unemployment rate had climbed to 8.1 percent. Since the legislation was enacted, billions of dollars are now wasted every month on frivolous spending programs and congressional pet projects.

So over the past couple of years, the government has spent hundreds of billions of dollars to "create jobs" — the premise of Obama's drive for stimulus legislation — and to revive the economy. But has it worked?

Let’s take a look: Today the official unemployment rate stands at 9 percent, 4 percent higher than it was before $1 trillion of taxpayer-funded spending was legislated.