JOINT ECONOMIC COMMITTEE

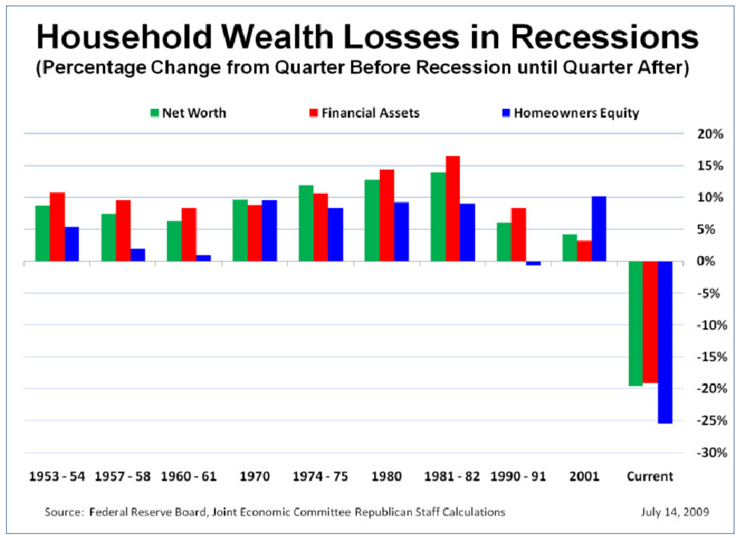
Senator Sam Brownback, Ranking Republican Member

July 16, 2009

CURRENT STIMULUS = THE WRONG MEDICINE

Focus Needed on Job Creation and Household Wealth

In February Congress rushed an unprecedented $787 billion "stimulus" package to the President's desk with the promise that the package would stem the tide of rising unemployment and place the economy back on firm footing. The package has not delivered the promised relief, in part, because it was premised on faulty Keynesian economic assumptions. While supporters point out that little of the "stimulus" money has been delivered, critics correctly respond that the failure to deliver stimulus dollars supports their criticism that the package wasn't stimulus in the first place because it did not meet the test of being "timely, targeted, or temporary." Even though "stimulus" spending has not reached full swing, the nation's debt-spending for this fiscal year is already over $1 trillion and there is still a whole quarter left in the year for spending to rise.



One distinguishing feature of the current recession is the massive loss of wealth by American households. Not since the Federal Reserve's flow of funds data series began in 1952 have there been declines in household wealth that approach the losses experienced in the current recession, nor has there been a period of such prolonged decline.

Since the 4th quarter of 2007, net worth of households and nonprofit organizations has declined by more than $12 trillion or 19.5%, household equity in real estate has declined by $2.5 trillion or 25.4%, and financial assets have declined by $9.5 trillion or 19.1%. Even these massive declines, however, fail to describe adequately how recent economic turmoil has battered household balance sheets compared to prior recessions.

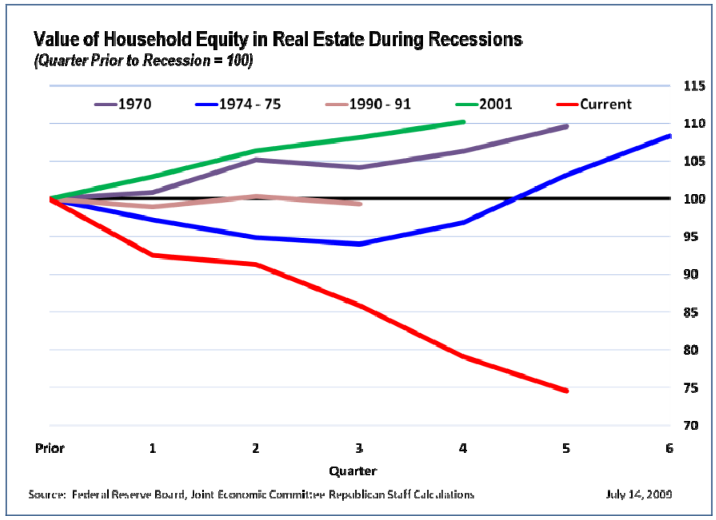
BOTH net worth and the value of financial assets have declined for six consecutive quarters. Prior to this, declines in both measures during the same single quarter have only occurred ten times out of 222 quarters since 1952 – only once have they declined together for two consecutive quarters (2nd and 3rd quarters 1974).

Net Worth

Since peaking at $64.25 trillion in the 2nd quarter 2007, net worth has declined by $13.9 trillion or 21.5%, and has set a record seven consecutive quarters of net worth decline for households and nonprofit organizations. Net worth has never declined for more than two consecutive quarters since the data series began in 1952, and the greatest previous decline in household wealth during a recession was 2.3%, or about one-tenth that which we've already experienced in the previous recession(4th quarter 1969 to the 2nd quarter 1970).

No prior recession has come to an end with net worth of households and nonprofit institutions lower than the levels recorded in the quarter before it began.

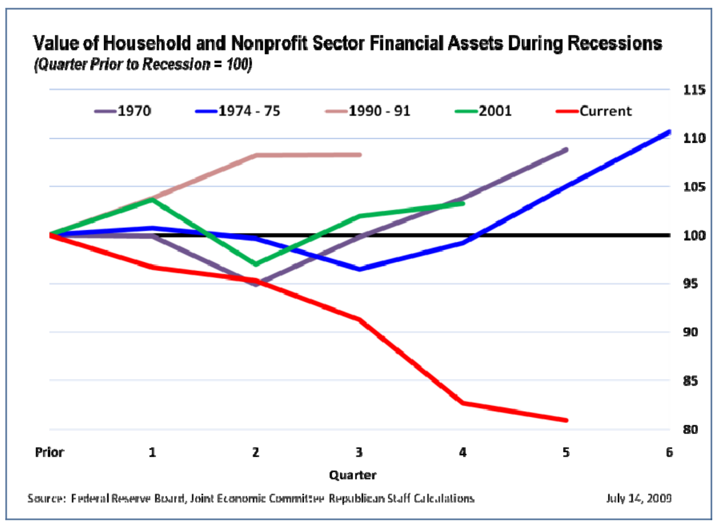
Owner's Equity in Real Estate Owned



The decline in the value of homeowners' equity in real estate is also unprecedented during the life of the Flow of Funds data series. Homeowners' equity has declined for nine consecutive quarters and in 12 of the last 13 quarters. Since its peak at \$12.5 trillion in the 4th quarter 2005, homeowners' equity has plunged \$5.1 trillion or 40.8% to \$7.4 trillion – a level not seen since the 1st quarter 2001.

To put this in perspective, 6.0% was the largest prior decline, during the 1974-75 recession. The only recession to end with homeowner's equity below its pre-recession quarter level was the 1991-92 recession—lower by 0.7%.

Value of Financial Assets



The value of household and nonprofit financial assets has declined by \$10.2 trillion or 20.2% in six consecutive quarters of decline. This is unprecedented during the life of the data series. The most similar declines occurred for only three consecutive quarters (4th quarter 1969 – 2nd quarter 1970) and were down by only 5.1%. As is the case with total net worth, no recession has ended with the value of household and nonprofit financial assets below their value in the quarter prior to the recession's beginning.

"Fixing" Wealth and Jobs Critical to Ending Recession

With household wealth battered in an unprecedented manner, it should come as no surprise that households and businesses have been reluctant to respond to Keynesian inspired stimulus. Consumer spending, which accounts for 70% of the economy, cannot directly "fix" household balance sheets. While prior recessions have ended with labor markets still in decline, in none of those cases was household net worth still declining or at a level below what existed before the recession's beginning. Unfortunately, the present stimulus package does little to rebuild household wealth. Uncertainty surrounding health care reform, cap and trade environmental legislation, and anticipated higher taxes serve to discourage the kind of investments in labor and capital that are necessary to rebuild the economy.