CONGRESS OF THE UNITED STATES

JOINT ECONOMIC COMMITTEE

CONGRESSMAN KEVIN BRADY

RANKING REPUBLICAN HOUSE MEMBER

NEWS RELEASE

For Immediate Release
February 26, 2010

Press Release #111-29
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STATEMENT OF CONGRESSMAN KEVIN BRADY

The Road to Economic Recovery: Prospects for Jobs and Growth

I am pleased to join in welcoming Dr. Berner, Mr. Joerres, and Dr. Hassett before the Committee this morning.

This is not a good time for American workers and their families. While there are some positive signs in the labor market—the rate of job losses has slowed and temporary services firms have begun to hire more workers in recent months—the unemployment rate is elevated and job openings remain scarce.

President Obama signed the *American Recovery and Reinvestment Act* on February 17, 2009, promising that it would jump start economic growth, create jobs, and reduce the unemployment rate. At the time, two of the Administration's top economists predicted that Obama's stimulus plan would keep the unemployment rate below 8.0 percent.

A year later, the Administration's rosy predictions remain unfulfilled. Since the Obama stimulus plan passed, the United States has lost more than 3 million payroll jobs. The unemployment rate is 9.7 percent.

At first, Administration officials tried to claim Obama's stimulus plan was creating or saving hundreds of thousands of jobs based on reports filed by stimulus fund recipients. However, the news media uncovered so many errors in the tabulation of these "jobs created or saved" that Administration claims became the butt of jokes by late night television comedians.

On Tuesday, the Congressional Budget Office entered the fray with its estimates of how much the Obama stimulus plan contributed to real GDP growth and employment during the fourth quarter of 2009. The CBO used fiscal multipliers to make these estimates. Unfortunately, the CBO's methodology prejudges the outcome and causes it to overstate the likely economic benefits from Obama's stimulus plan.

First, the CBO derived its fiscal multipliers from three macroeconomic forecasting models that use historical relationships among demand-side factors to predict the near-term performance of the U.S economy. These models ignore many supply-side factors. For example, business investment is treated largely as a function of aggregate demand and the real interest rate. Thus, a business tax cut does not affect directly investment by reducing the cost of investing and increasing the after-tax return on capital. Instead, a business tax cut affects investment indirectly through higher aggregate demand as business owners consume a portion of the payouts received from their businesses.

The CBO even acknowledges that the models' demand-side orientation biases its calculation of fiscal multipliers. Quoting from the CBO report, "Because they emphasize the influence of aggregate demand on output in the short run, the macroeconomic forecasting models tend to predict greater economic effects from demand-enhancing policies such as ARRA than other types of models."

Second, two of three macroeconomic forecasting models used by the CBO are “old Keynesian” models that do not allow for rational expectations. This creates a strong upward bias in the CBO’s calculation of fiscal multipliers. Consequently, the CBO ignores what I see occurring in my district in Texas: people are saving more and businesses are investing less in anticipation of paying higher taxes in the near future to service the enormous debts from stimulus spending, “cap and trade,” and new health care entitlements. Last year, John Cogan, Tobias Cwik, John Taylor, and Volker Wieland found that about 5/6ths of the real GDP growth benefits and almost all of the net job creation benefits of stimulus spending disappear when a “new Keynesian” model that allows for rational expectations is used.

For these reasons, the CBO’s fiscal multipliers are biased. The CBO simultaneously overstates the likely economic benefits from stimulus spending and temporary tax rebates and understates the likely economic benefits of business tax cuts designed to reduce the after-tax cost of making job-creating business investments. Therefore, we should take the CBO’s claims that Obama’s stimulus plan increased real GDP by between 1.5 percent and 3.5 percent and increased the number of people employed by 1.0 million to 2.1 million with a pound of salt.

I am interested in hearing what the private sector experts here today have to say about job creation. I look forward to hearing their testimony.

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