The latest jobless figures show America's economy is stuck in the doldrums. The US urgently needs a new stimulus injection

The latest jobless figures show America's economy is stuck in the doldrums. The US urgently needs a new stimulus injection

- 

  - Dean Baker
  - guardian.co.uk, Monday 6 July 2009 19.00 BST

The June US employment report should convince even the determinedly ignorant that the time has come for another round of stimulus for the American economy. The economy is continuing to shed jobs and work hours at a very rapid pace. The unemployment rate is virtually certain to cross 10% by the end of the summer and will likely hit 11% before we are very far into 2010. This is a scenario much worse than the Obama administration had expected when it crafted its stimulus package. It is time for it to adjust its plans accordingly.

When the Obama administration put together its stimulus package in January, it was projecting that, in the absence of any stimulus, the unemployment rate would peak at just over 9% early in 2010. With the unemployment rate reaching 9.5% in June, they clearly underestimated the size of the downdraft hitting the US economy.

The June data showed the economy shedding 465,000 jobs – but even more striking was the fact that hours worked fell by 0.8%. This rate of decline in hours worked is the same as in the period of economic free fall from October to April. It's good that employers cut back hours per worker, rather than lay people off, but it still means that the demand for labour is plummeting. If hours per worker did not change, this would be equivalent to a loss of more than 900,000 jobs in June.

While few would argue that the economy is already turning, some economists maintain that we have to wait longer to feel the full effects of the stimulus package. To refute this argument we need only look at the size of the package.

More than 60% of the stimulus package ($480bn out of $790bn) was in the form of either tax cuts or mandatory spending such as expanded unemployment benefits. These tax cuts and spending measures have already fully kicked in. While most of the money has not yet been spent, we are already paying taxes at a lower rate, due to the tax cut, and collecting higher benefits as a result of the stimulus package.

Consumption in April, May, and June was undoubtedly higher as a result of these stimulus measures, but there is no reason to believe that they will provide further additional boost in July, August, and September. In other words, we are now feeling the benefits of this stimulus, and we will continue to feel the benefits. But it is just not sufficient to offset the downward momentum from the collapse of the housing bubble.

If we expect a further boost from the stimulus, then it has to come from the direct spending portion. As many commentators have rightly noted, most of this money has not yet gone out the door. However, the amount at issue is too small to have much impact.

The Congressional Budget Office projects that we will spend $110bn from this portion of the stimulus package in the fiscal year beginning in October. However, almost $30bn of this spending is designated as a state and local fiscal stabilisation fund. This money will prevent cutbacks at the state and local level. This is very useful spending, but this money is just preventing further contraction, not pushing the economy forward.

That leaves us with just $80bn as a net stimulus for 2010 compared with current tax and spending levels. This is just a bit more than 0.5% of GDP. It is less than one-fifth as large as the falloff in housing construction from its peak at the height of the bubble. It is only a bit more than one-tenth as large as the falloff in consumption due to the disappearance of housing bubble wealth. In short, it cannot possibly be large enough to turn the economy around.

This is why we badly need a third stimulus package. There is nothing on the horizon to prevent the unemployment rate from staying high long into the future. As I have written before, the obvious form for a third stimulus would be an employer tax credit to give workers paid time off.

This "pay for play" tax credit would give employers an incentive to shorten work time with paid family leave, paid sick days, paid vacations and/or shorter workweeks. It is likely to have an impact very quickly, since employers would be throwing money away by not moving as quickly as possible to take advantage of the tax credit. As a result, it would both put more money into the economy and also redistribute employment so that fewer workers are unemployed. If we all worked five per cent fewer hours, then seven million more workers could have jobs at the same level of demand.

The people who make economic policy gave us this recession because they were too bullheaded to see an $8,000bn housing bubble right in front of their face. There are ways to get us out of the mess they created, if our leading economic policymakers could finally start to open their eyes and think seriously about the economy.

http://www.guardian.co.uk/commentisfree/cifamerica/2009/jul/06/us-economy-obama-stimulus