Forget a ‘Second’ Stimulus. Stop the First One!

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The economy has gotten worse than the Obama administrationhad predicted it would be even if Congress had spent nothing on “fiscal stimulus.” Although some are arguing that this gap is proof that more stimulus is needed, it really shows that the cost of the American Recovery and Reinvestment Act of 2009 — and laws like it — far exceed their benefits in the form of economic stimulus.

By June 2009, the unemployment rate had reached 9.5 percent, as compared to the 7.6 percent it was in January 2009 when Congress passed, and President Obama signed, the $787 billion stimulus bill.

The Obama administration had predicted that the June 2009 unemployment rate would be less than 8 percent — almost a half of a percentage point bigger than it would have been without a stimulus bill. The Obama team had predicted that the stimulus law’s effect would always be less than two percentage points, even at its peak potency.

We cannot blame the Obama administration for failing to predict June’s 9.5 percent unemployment rate. That result just shows the size of the shocks hitting the economy: Even the best forecasters can miss the unemployment rate by almost two percentage points, even when forecasting fewer than six months ahead.

Some of us thought that the fiscal stimulus would doessentially nothing to improve the economy. But even stimulus advocates admitted that economic improvements coming from the stimulus law — about a half a percentage point (by their estimates) — would be small when compared to the shocks hitting the economy.

Based on this comparison, a few economists have suggested that the stimulus bill should have been larger. Their logic is that a half of a percentage point improvement could have been one percentage point if we have spent twice as much, and two percentage points if we had spent four times as much. An even more massive stimulus, they say, would actually have effects that we could notice, and that we need.

But fiscal policy is not merely a dial that can be turned to any desired amountIf it were just a dial, then those of us who thought the stimulus bill would have a tiny effect would be supporting an even larger stimulus than the Obama administration proposed! An impotent fiscal policy dial would have to be turned a lot to have a given effect.

This faulty logic comes from ignoring the costs of fiscal stimulus, and failing to ask whether the costs are commensurate with even the most optimistic estimate of the benefits.

The Obama administration had said that the stimulus bill would “save or create” 3.5 million jobs while adding $787 billion to the federal budget. Admittedly, some of this money went to taxpayers and to some worthwhile public works, but it also created additional economic burdens in the process of collecting the taxes and issuing the debt to pay for it. To an order of magnitude, the promise of those 3.5 million jobs cost a quarter of a million dollars per job promised.

If instead the fiscal stimulus “save or created” just one million jobs, that doesn’t mean that the stimulus should have been 350 percent bigger. Rather, it means that each job promised cost almost $1 million each!

Congress needs to ask the stimulus advocates why just one job promised is worth hundreds of thousands of taxpayer dollars, and why they are so sure that the promised jobs will turn into actual ones.

Even better, they should consider turning off the first stimulus before more tax dollars are wasted.

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