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KC Fiscal Focus: President Obama's Jobs Plan Bolder Than Expected, But Not Likely to Have a Significant Lasting Positive Impact on Economy

By [David Kersten](#)

President Barack Obama stood before a joint session of Congress earlier this month to roll out his \$447 billion jobs act. An analysis by Kersten Communications reveals that the package contains some positive elements but is unlikely to have a significant and lasting positive economic impact on the nation's economy.

The President is supposed to lay out how he will plan for the plan and pay down the nation's debt on Monday September 19th, according to a White House press release.

Perhaps more importantly, the President's speech and proposal of his plan shows that he is serious about the jobs issue and challenges Republicans to either work with him to restore national employment or propose their own ideas on the jobs issue.

President Obama criticized Congressional Republicans for their belief that the only way to improve the economy is to cut government spending and eliminate most government regulations.

The following policy white paper presents a detailed analysis of the President's jobs plan, highlights its positive impacts as well as where it is deficient, and makes some suggestions about what really needs to be done to restore the nation's long term economic health.

Kersten Communications plans to continue to evaluate jobs proposals proposed at both the national, state and local levels of government to provide analysis and commentary on economic development strategies.

Overview of President's \$447 Billion Jobs Proposal

The chart below provided by the White House summarizes the \$447 billion in spending included in the President's four point jobs proposal (White House 18).

As indicated below, a majority of the spending, some \$245 billion (sections #1 and #4), consists of temporary tax cuts for businesses and workers. Another \$140 billion is spent on retaining teachers, modernizing schools, and much needed infrastructure. The remaining \$62 billion is spent to try to help Americans looking for jobs, primarily through reforming and extending unemployment insurance.

The President said that all of the proposals had generated bipartisan support in the past. He said the plan would be fully paid for through the work of the long-term debt relief committee that is considering tax changes and spending cuts. As mentioned previously, he is planning to provide additional details on his funding plan on Monday September 19.

Summary of Spending in President Obama's Jobs Act

<p>1. Tax Cuts to America's Small Businesses</p> <p>--Cut employer payroll taxes in half and bonus payroll cut for new jobs/wages --Extend 100% expensing to 2012</p>	<p>\$70 billion total</p> <p>\$65 billion \$ 5 billion</p>
<p>2. Putting Workers Back on the Job While Rebuilding and Modernizing America</p> <p>--Teacher rehiring and first responders --Modernizing schools --Immediate surface transportation --Infrastructure bank --Rehabilitation/repurposing of vacant property --National wireless initiative --Veterans hiring initiative</p>	<p>\$140 billion total</p> <p>\$ 35 billion \$ 30 billion \$ 50 billion \$ 10 billion \$ 15 billion \$ 0* N/A</p>
<p>3. Pathways Back to Work for Americans Looking for Jobs</p> <p>--Unemployment insurance reform and extension --Jobs tax credit for long term unemployed --Pathways back to work fund</p>	<p>\$ 62 billion total</p> <p>\$ 49 billion \$ 8 billion \$ 5 billion</p>
<p>4. More Money in the Pockets of Every American Worker and Family</p> <p>--Cutting employee payroll taxes in half in 2012</p>	<p>\$175 billion total</p> <p>\$175 billion</p>
Total	\$447 billion

*Proposal has a gross cost of \$10 billion, but a net deficit reducing impact of \$18 billion because of spectrum auction proceeds.

Source: White House

President's Plan Contains Some Positive Elements That Will Aid Economic Growth and Help Nation's Unemployed

President Obama's proposal contains a number of good ideas that have been proven to either generate immediate economic growth or lay the foundation for future economic growth.

As noted in the chart on the previous page, the plan proposes to spend \$140 billion on putting workers back to work and rebuilding and modernizing America's infrastructure (section #2) (White House 18).

This includes \$35 billion to prevent teacher layoffs and keep police and firefighters on the job, which is estimated to save up to 280,000 jobs. Another \$30 billion will be spent to modernize at least 35,000 public schools. Some \$50 billion will be spent on infrastructure projects which include immediate investments for highway, transit, passenger rail and aviation projects (White House 5-7).

A total of \$10 billion would go toward the creation of a national infrastructure bank to prioritize national infrastructure projects and \$15 billion would go to rehabilitating homes, businesses and communities impacted by the housing downturn (White House 8).

A consensus of economic studies show that investing infrastructure has significant positive short and long term economic effects (Schweke 1-10). Retaining teachers and public safety officials will have the immediate impact of saving jobs, and therefore increasing consumer spending, while improving education and public safety.

Investing in infrastructure projects creates construction jobs immediately, and lays the ground work for future economic growth by improving education and transportation, which are two essential drivers of economic prosperity.

Section #3 in the chart on the previous page shows that \$62 billion will be invested to help Americans who are currently looking for jobs. This includes \$49 billion for the reform and extension of unemployment insurance, \$8 billion for a jobs tax credit for the long term unemployed, and \$5 billion to expand employment opportunities for low income youth and adults.

The \$8 billion jobs tax credit will be addressed later, but the remainder of this \$62 billion in spending to help the unemployed will have an immediate positive economic and social impact. "Households receiving unemployment benefits tend to spend the additional benefits quickly, making this option both timely and cost-effective in spurring economic activity and employment," according to the 2010 CBO report "Policies for Increasing Economic Growth and Employment in the Short Term," (7).

The unemployment insurance reform and other provisions included in this section will provide increased job search assistance and reemployment services that will help Americans find jobs.

Despite these positive aspects of the President's jobs proposal, a majority of the spending is not likely to have a significant lasting economic impact as will be discussed in the next section.

Weakness of President's Jobs Plan: Majority of \$447 Billion in Spending Will Not Have a Significant Lasting Economic Impact

Put simply, a majority of the package's \$447 billion in spending funds tax cuts and programs that are unlikely to have a significant and lasting economic impact.

As the chart on page 2 illustrates, more than half of the proposal's \$447 billion in spending, some \$245 billion, is spent on tax cuts including cutting employer payroll taxes in half and providing a bonus payroll cut for new jobs/wages (\$65 billion), cutting employee payroll taxes in half in 2012 for every American worker (\$175 billion), and extending the 100% expensing allowance to 2012 for business equipment purchases (\$5 billion) (White House 18).

Another \$8 billion is spent to provide a special bonus tax credit of up to \$4,000 for businesses that hire the long-term unemployed.

Employer Payroll Tax Breaks Will Not Generate Economic Growth

The President's plan would extend the payroll tax cut to firms by cutting their payroll roll taxes in half, from 6.2% to 3.1%, on the first \$5 million in payroll (to target the break toward small businesses). This tax break is estimated to cost \$65 billion and would only apply to the 2012 tax year (White House 2).

For example, "a construction firm with 50 workers earning an average of \$50,000 per year—for a total of \$2.5 million—would receive a payroll tax cut of 3.1% of its total payroll, or about \$80,000," according to the White House (2).

This is a very marginal tax break, only 3.1% of the costs of employing an employee, and unlikely to provide an incentive to hire any additional workers, particularly since it is only for the 2012 calendar year. Businesses would gain additional tax savings, yet the trend in the current economy is for businesses to hold onto additional money as reserves (see recent Wall Street Journal reports), as opposed to spending it and thereby generating economic growth. Thus, the employers' payroll tax break is unlikely to generate little, if any, economic growth and merely represents a tax windfall for businesses.

The President's plan also provides a complete payroll tax holiday for employers creating new jobs or increasing wages.

A strong public policy case can be made that the payroll tax cut for businesses creating new jobs or enacting wage increases for current workers is an inefficient use of taxpayer dollars. Specifically, the plan completely refunds payroll taxes paid on added workers or wage increases for current workers above the level of last year's payroll. To focus the benefit on small business, this payroll tax relief would be capped at \$50 million in new wages.

The economic reality is that businesses will create new jobs when it makes economic sense to do so. Eliminating the payroll tax of 6.1% on new jobs or wage increases is a marginal reduction in an employer's cost of hiring or increasing wages that is unlikely to entice employers to do so unless it makes economic sense to do so otherwise. For a \$50,000 per year job, this tax break would provide \$3,050 in tax relief, but the employer still would have to pay the \$46,950 in increased wage expenses for the new employee's salary.

During these economic times, there is little incentive for employers to increase wages due to the high unemployment rate and the relative abundance of labor. A marginal 6.1% reduction in the cost of wage increases will do next to nothing to encourage wage increases that do not make economic sense otherwise.

The employers that are hiring in today's economy, such as the high-tech sector, require highly skilled workers and will be forced to pay higher wages as more workers are needed or to entice existing workers to stay put. The President's tax break will merely reward these firms for something that already makes economic sense to do.

Similarly, a special bonus tax credit of up to \$4,000 for firms that hire the long-term unemployed will not likely serve its intended goals of creating jobs for the long-term unemployed. The tax break represents a small portion of the cost of hiring these workers.

Employee Payroll Tax Break Would Provide Limited Short-Term Economic Stimulus

The President's plan also proposes cutting employee payroll taxes in half for 2012, which would cost the federal government \$175 billion. Similar to the employer proposal discussed above, this tax break would cut the amount that employees have deducted from their payroll from 6.2% to 3.1% for 2012 (White House 16).

These tax cuts are largely targeted toward the middle-class and will put more money in people's pockets but will only provide a limited and short term economic stimulus, similar to President Bush's \$500 tax refund for every taxpayer. The workers' payroll tax cut will provide approximately \$1,500 in tax relief for the typical household earning \$50,000, according to the White House.

Middle-class households are more likely than the rich to spend a larger portion of this money, thereby generating economic growth, but this marginal amount of extra spending will be minimal compared to the overall economy and only last for the 2012 calendar

year. Moreover, as UC Berkeley Professor Robert Reich has noted, such taxpayers have a tendency to use this extra money to pay down debt or save during distressed economic times.

Notwithstanding the above policy arguments, this \$175 billion represents a tax cut for the lower and middle-classes that will provide some immediate economic stimulus.

“The Congressional Budget Office wrote last year that a payroll tax cut for employees has a larger immediate impact on job creation than most other tax cuts it evaluated, including across-the-board income tax cuts,” according to the White House (16). This 2010 CBO report, titled “Policies for Increasing Economic Growth and Employment in the Short Term,” is available by [clicking here](#).

Jobs Act Is a Positive First Step But Much More Needs to Be Done to Restore Long Term Economic Growth

As mentioned previously, most analysts agree that the President’s jobs package is a positive first step, but is not large enough to put America’s estimated 14 million employed back to work and provide a strong enough jolt to the nation’s economy.

Harvard economist Paul Krugman has observed, “President Obama’s hair may not be on fire, but it’s definitely smoking; clearly and gratifyingly, he does grasp how desperate the jobs situation is” (2).

The President’s proposal of a jobs plan, and the Republican reaction or a lack of a reaction to it, sets the stage for the economic policy debate going into the 2012 election season.

“I don’t pretend that this plan will solve all of our problems,” Obama said, noting that there is a need to listen to all proposals, regardless of what party proposes them.

“Doing nothing is not an option,” Obama said. Obama urged Congress to do something now because most Americans do not have the luxury of waiting 14 months until the next election.

Unfortunately, it does not appear that anything significant will be done on the jobs issue in the near future absent a significant uproar by the American people or a major shift in Washington’s political environment.

Many Economists Believe that Government Policy Has Significant Impact on Economic Growth

Economists disagree on the impact of government policy on economic growth, but “many have argued that competitiveness is most strongly influenced by government policy,” according to Harvard Professor Michael E. Porter, a leading expert on economic competitiveness (Porter 4). A convincing case can be made from the economic literature,

based on a review by Kersten Communications, that the nation's political environment can have a significant, and either positive or negative impact, on a national economy.

A survey of the economic literature shows that the deterioration in the nation's political climate, characterized by increased partisan polarization and gridlock, is one of the major underlying causes of America's decline in economic competitiveness in recent years. This literature will be reviewed in greater detail in future KC analyses and is beyond the scope of this current analysis due to time constraints.

Global Competitiveness Report Indicates Decline in United State's Economic Competitiveness Due To Increasing Political and Economic Weaknesses

The Global Competitiveness Report 2010-11, which ranks the competitiveness of 139 of the world's economies based on 100 indicators, found that "the United States continues a decline that began last year, falling two more places to 4th position.," (World Economic Competitiveness Report 2010-11, WECR 2010-11, 14). The U.S. was formerly number 1. The report is the most comprehensive and highly regarded assessment of its kind. The full report, which is published by the World Economic Forum in Geneva, Switzerland, is available for download by [clicking here](#).

The report found that "many structural features make its economy extremely productive" but "a number of escalating weaknesses have lowered the U.S. ranking over the past two years" such as a decline in public institutions, distrust of politicians, the functioning of the private financial markets and a lack of macroeconomic stability (WECR 2010-11 23).

The Global Competitiveness Report 2011-12 finds that the competitiveness of the United States dropped another rank, from 4th to 5th, due to the same weaknesses (WECR 2011-12 14).

"A lack of macroeconomic stability continues to be the United States' greatest area of weakness (90th). Over the past decade, the country has been running repeated fiscal deficits, leading to burgeoning levels of public indebtedness that are likely to weigh heavily on the country's future growth," states the report (WECR 2011-12 24).

"The business community continues to be critical toward public and private institutions (39th). In particular, its trust in politicians is not strong (50th), it remains concerned about the government's ability to maintain arms length relationships with the private sector (50th), and it considers that the government spends its resources relatively wastefully (66th)," states the report (WECR 2011-12 24).

An even closer examination of what the report says are the 12 pillars of economic growth shows that the recent decline of the United States economy may only be the beginning of a steep decline, absent a significant change in the way the United States supports economic growth.

Summary of Twelve Pillars of Economic Growth

For more than three decades, the World Economic Forum's annual competitiveness reports have examined the many factors enabling national economies to achieve sustained economic growth and long-term prosperity.

“Since 2005, the World Economic Forum has based its competitiveness analysis on Global Competitiveness Index (GCI), a highly comprehensive index for measuring national competitiveness, which captures the macroeconomic foundations of national competitiveness,” states the 2010-11 report (4).

The GCI is regularly put through a rigorous analysis by the Joint Research Centre of the European Commission (JRC), which is widely recognized as the holding the world's leading expertise on composite indicators (10). The index is also largely based on a one of a kind regular survey of corporate CEOs and executives.

“We define competitiveness as the set of institutions, policies, and factors that determine the level of productivity of a county...In other words, more competitive economies tend to be able to produce higher levels of income for their citizens,” (4).

Pillar #1: Institutions: The institutional environment is determined by the legal and administrative framework within which individuals, firms, and governments interact to generate income and wealth in the economy. The importance of a sound and fair institutional environment has become even more apparent during the economic crisis, given the increasingly direct role played by the state in the economy of many countries. This also includes government attitudes towards markets, efficiency of operating, and management of public finances.

Pillar #2: Infrastructure: An extensive and efficient infrastructure is critical for ensuring the effective functioning of the economy, as it is an important factor determining the location of economic activity and the kinds of activities or sectors that can develop in a particular economy. This includes transportation infrastructure, communications, energy, etc.

Pillar #3 Macroeconomic Environment: The stability of the macroeconomic environment is important for business and, therefore, is important for the overall competitiveness of a country. Although it is certainly true that macroeconomic stability alone cannot increase the productivity of a nation, it is recognized that macroeconomic disarray harms the economy.

Pillar #4 Health and Primary Education: A healthy workforce is vital to a country's competitiveness and productivity. Workers who are ill cannot function to their potential and will be less productive. Poor health leads to significant costs to business, as sick workers are often absent or operate at lower levels of efficiency. In addition, this pillar takes into account the quantity and quality of basic education received by the population, which is increasingly important in

today's economy. Basic education increases the efficiency of each individual worker.

Pillar #5 Higher Education and Training: Quality higher education and training is crucial for economies that want to move up the value chain beyond simple production processes and products. In particular, today's globalizing economy requires countries to nurture pools of well-educated workers who are able to adapt rapidly to their changing environment and the evolving needs of the production system.

Pillar #6 Goods Market Efficiency: Countries with efficient goods markets are well positioned to produce the right mix of products and services given their particular supply-and-demand conditions, as well as to ensure that these goods can be most effectively traded in the economy. Healthy market competition, both domestic and foreign, is important in driving market efficiency and thus business productivity, by ensuring that the most efficient firms, producing goods demanded by the market, are those that thrive. The best possible environment for the exchange of goods requires a minimum of impediments to business activity through government intervention.

Pillar #7 Labor Market Efficiency: The efficiency and flexibility of the labor market are critical for ensuring that workers are allocated to their most efficient use in the economy and provided with incentives to give their best effort in their jobs. Labor markets must therefore have the flexibility to shift workers from one economic activity to another rapidly and at low cost, and to allow for wage fluctuations without much social disruption.

Pillar #8 Financial Market Development: The recent financial crisis has highlighted the central role of a sound and well-functioning financial sector for economic activities. An efficient financial sector allocates the resources saved by a nation's citizens, as well as those entering the economy from abroad, to their most productive uses. Business investment is critical to productivity.

Pillar #9 Technological Readiness: In today's globalized world, technology has increasingly become an important element for firms to compete and prosper. The technological readiness pillar measures the agility with which an economy adopts existing technologies to enhance the productivity of its industries, with specific emphasis on its capacity to fully leverage information and communication technologies (ICT) in daily activities and production processes for increased efficiency and competitiveness.

Pillar #10 Market Size: The size of the market affects productivity since large markets allow firms to exploit economies of scale. Traditionally, the markets available to firms have been constrained by national borders. In the era of globalization, international markets have become a substitute for domestic

markets, especially for small countries. There is a vast empirical evidence showing that trade openness is positively associated with growth.

Pillar #11 Business Sophistication: Business sophistication is conducive to higher efficiency in the production of goods and services. This leads, in turn, to increased productivity, thus enhancing a nation's competitiveness. Business sophistication concerns the quality of a country's overall business networks as well as the quality of individual firms' operations and strategies.

Pillar #12 Innovation: The final pillar of competitiveness is technological innovation. Although substantial gains can be obtained by improving institutions, building infrastructure, reducing macroeconomic instability, or improving human capital, all these factors eventually seem to run into diminishing returns. In the long run, standards of living can be enhanced only by technological innovation. Innovation is particularly important for economies as they approach the frontiers of knowledge and the possibility of integrating and adapting exogenous technologies tends to disappear. This requires an environment that is conducive to innovative activity, supported by both the public and the private sectors.

Source: GCI Report 2010-11

Review of 12 Pillars Shows Competitiveness of United States Will Likely Continue to Decline Absent a Change in the Current Political Environment

As one reviews the 12 pillars of economic competitiveness, it becomes clear why the competitiveness of the United States has declined in recent years. The ability of a nation to achieve a competitive position in many of the 12 pillars rests in the policy arena, namely the nation's political institutions.

To illustrate, the lack of Washington's ability to reach a consensus on major economic issues such as the debt ceiling, domestic spending, and the jobs issue, has led to a less favorable institutional environment (Pillar #1), poorer infrastructure (Pillar #2), a deteriorating macroeconomic environment (Pillar #3), and a decline in health and primary education and higher education and training (Pillars #4 and #5), among other things.

The nation's political environment appears to be getting worse which is likely to encourage a further deterioration in the nation's pillars of economic competitiveness.

President's Jobs Plan Not Nearly Enough According to Experts

Acclaimed analysts such as UC Berkeley Professor Robert Reich and Harvard Economist Paul Krugman have pointed out that the jobs plan is much bolder than expected but not likely to put a significant and lasting dent in national unemployment.

Similar to the stimulus plan proposed earlier in his term, Obama's jobs plan represents an attempt by the administration to craft a modest proposal that stands some chance of passage in a Republican-controlled Congress.

Reich argues that the President has fallen into a trap similar to the stimulus proposal in that he tried to propose something that stands some chance of passage, yet is too modest to have a significant impact on the economy even if it is approved in its entirety (2).

"This isn't a job plan. It's a reelection plan," said Republican Senate leader Mitch McConnell. Reich said that is precisely the problem (Reich page 2).

"McConnell and company have stated publicly that their number-one objective is to unseat Obama and regain the presidency in 2012. They don't want to give the President anything he could possibly claim as a victory. And they're not terribly worried if the economy stays awful through Election Day because that's the best way to fulfill their number-one objective," Reich wrote (2).

Reich concludes that "the President would have done better with a plan that was big enough to make a real difference. And then, when Republicans rejected it, campaign on it" (2).

Harvard Economist Paul Krugman finds that the proposal is too small to have a real impact (1-3).

"It calls for about \$200 billion in new spending—much of it on things we need in any case, like school repair, transportation networks, and avoiding teacher layoffs—and \$240 billion in tax cuts. That may sound like a lot, but it actually isn't. The lingering effects of the housing bust and the overhang of household debt from the bubble years are creating a roughly \$1 trillion per year hole in the U.S. economy, and this plan—which wouldn't deliver all its benefits in the first year—would only fill part of that hole. And it's unclear, in particular, how effective the tax cuts would be at boosting spending," Krugman wrote in the New York Times (2).

"Still, the plan would be a lot better than nothing," Krugman concludes (2).

Reich reaches a similar conclusion, noting that the new boost to the economy out of the \$447 billion plan is closer to \$300 billion because "some of this merely extends current spending (unemployment benefits) and tax cuts (in Social Security taxes), so it doesn't add to aggregate demand" (1).

"The net new boost to the economy is closer to \$300 billion. That doesn't approach even half the gap between what the economy is now producing and what it could produce at or near full employment," Reich notes (1).

Conclusion: Those Who Live in Glass Houses Should Not Throw Stones

This analysis has sought to show why President Obama's jobs initiative would only have a limited and short-term impact on the nation's economy. Moreover, economists agree that much more needs to be done to stimulate the economy over the long run, and employers say the jobs plan will not significantly impact hiring.

A September 11, 2011 New York Times article concluded that "the dismal state of the economy is the main reason many companies are reluctant to hire workers, and few executives are saying that President Obama's jobs plan—while welcome—will change their minds any time soon," (Motoko 1).

But a strong case can be made that something is better than nothing and the President's push on the jobs issue initiates an important political debate over the future of the nation's economy.

Most economists, including Federal Reserve Chairman Ben S. Bernanke and Treasury Secretary Timothy Geithner, have pointed out that what is really needed to restore economic health is significant relief for homeowners who are underwater on their mortgages. Only very modest attempts have been made by the Administration to address this issue (Applebaum 1-3).

Media articles have noted that Republicans have been cautious in how they have responded to the Administration's proposal because they have faced increasing complaints from constituents on the jobs issue (Steinhauer 1-3).

It is unclear and doubtful in the current political environment that the President will be able to muster the political support in the Republican-controlled Congress to pass his jobs proposal. Yet those who criticize him should not do so without taking an inventory of their own jobs proposals.

As the age-old expression goes, those in glass houses should not throw stones. Republicans should take note that they have collectively failed to propose any credible jobs proposals apart from the dismantling of government programs and tax cuts for the rich and business interests--hardly a viable economic package.

Kersten Communications will continue to monitor and evaluate job creation proposals at both the federal, state and local levels of government so keep an eye out for future analyses.

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