Should North Carolina Refuse Stimulus Funds?

By: Andrew Brod

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Article:

The Civitas Institute, a conservative think tank in Raleigh, recently released a study on the economic impact of the federal stimulus package on the North Carolina economy. The study's main result was striking. Whereas the Obama administration expects the stimulus to create or save more than 100,000 jobs in North Carolina, the Civitas study claims that it will cost the state nearly 70,000 jobs.

That's a 170,000job difference of opinion, which is roughly the difference between an 8 percent and a 12 percent unemployment rate.

Should North Carolina really refuse stimulus money? Mainstream economists are clearly bullish on the benefits. Fortunately or unfortunately (depending on your politics), this study doesn't come close to making the case for a negative impact.

The study's conclusions are less surprising when one looks at its byline. It was produced by the consulting firm founded by Arthur Laffer, the economist best known for his Reagan-era support of "supply-side economics," and more recently for his apparent belief that Medicare and Medicaid are not government programs.

The direction taken by the Laffer study is made clear early on. It claims that "increasing federal spending does not stimulate the economy." Really? Not under any circumstances? Not even in the midst of the worst recession since the 1930s? Many economists have studied when and what types of federal spending stimulate growth. But for Laffer and his associates, there's no room for complexity.

The explanation for the no-stimulus assumption is another bald assertion, that government spending "crowds out" private spending. To be sure, crowding out is an important concern in policy analysis. But as a blanket statement, this is silly. It appears to apply to all government spending.

Consider education spending. Sure, we'd have more private schools if there were no public schools. So yes, private spending on schools has been crowded out. But so what? The real issue isn't crowding out, it's efficiency. Most activities are more efficiently performed by the private sector than by government. A few aren't. Ignoring the exceptions may lead to a consistent belief system, but it's bad economics.

A more serious problem with the crowding-out claim is that it only makes sense if the private sector is ready to spend but is prevented by the intrusion of government money. But in a deep recession, there is very little private spending to crowd out. That's the whole problem right now! Did Laffer and his associates not notice this?

After making a few more questionable assumptions and misapplying an overly simple statistical model, the Laffer study eventually pops out its prediction of nearly 70,000 lost jobs. All in all, it's a pretty dubious piece of work.

But the blanket statements don't stop there. In promoting the Laffer study, a Civitas analyst has said that "government does not create wealth." Clearly, the analyst has never driven on a government-built highway or visited a government-funded business incubator. Either that or, like Laffer, his ideology has blinded him to common sense.

Federal spending isn't the solution to every problem, or even most problems. But it's silly to pretend that it's never the solution, especially during a recession as deep as this one. There's evidence that Europe and China are leading us out of the recession partly because of their more aggressive fiscal policies during the downturn. North Carolina doesn't have to emulate them, but the last thing we should do is follow the advice of Civitas and Laffer.