JOINT ECONOMIC COMMITTEE

Senator Sam Brownback, Ranking Republican

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ROMER AND BERNSTEIN ANALYSIS OF STIMULUS EFFECTS: JOBS CREATED OR SAVED

Christina Romer (Chair of the Council of Economic Advisors) and Jared Bernstein (Office of the Vice President), recently provided an analysis of possible job effects of a "prototypical recovery package," titled "The Job Impact of the American Recovery and Reinvestment Plan." (available at Romer/Bernstein).

The Romer and Bernstein analysis:

- Provides no useful standard against which to measure results of stimulus.
- Uses rules of thumb and Keynesian-style "multipliers" from economic models that were estimated using historical data to forecast output and employment effects of stimulus in the current environment, which is far different from the environments from which those data were generated.

Save or create at least 3 million jobs: A goal of the administration's American Recovery and Reinvestment Plan is to "save or create" at least 3 million jobs by the end of 2010. To help implement this plan, the House and Senate are considering "stimulus" measures intended to boost economic activity, including employment. Romer and Bernstein offer "…a preliminary analysis of the jobs effects of some of the prototypical recovery packages being discussed." They hope to shed light on whether we can expect such packages to create sufficient jobs to meet the administrations goals of saving or creating at least 3 million jobs by the end of 2010.

Analyzing job effects of stimulus: To analyze possible employment effects of a prototypical stimulus package, Romer and Bernstein proceed as follows:

1. Assume a package of slightly over $775 billion, which includes: substantial investments in infrastructure, education, health and energy; temporary programs including increases in food stamps and expansions of unemployment insurance; state fiscal relief; business investment incentives; and a tax cut along the lines of the Making Work Pay tax cut proposed in President Obama's election campaign.
2. Use Keynesian multiplier estimates, assumed to "represent a consensus of a broad range of economists and professional forecasters," to translate increases in government spending and reductions in taxes into effects on the gross domestic product (GDP).
3. Take the effects on GDP and translate them into employment effects using a "rule of thumb" that a 1% increase in GDP corresponds to an increase in employment of approximately 1 million jobs, or about 0.75%.

The result of the Romer and Bernstein analysis is that the $775 prototypical stimulus package that they consider "is expected to create between three and four million jobs by the end of 2010."

The authors are upfront in identifying that their estimates of job effects of stimulus are subject to errors and that there is a great amount of uncertainty surrounding Keynesian-style multiplier analysis. They identify clearly that: "…all of the estimates presented…are subject to significant margins of error." They also readily admit that "…the uncertainty is surely higher than normal now because the current recession is unusual both in its fundamental causes and its severity."

Even with those caveats, the Keynesian multiplier analysis of GDP effects of stimulus and rule of thumb translation of GDP changes into job changes leaves a lot to be desired. Aside from a number of solid reasons to dismiss, or at least be highly suspicious of, the multiplier plus rule of thumb analysis of Romer and Bernstein, what their results tell us is problematic.

Creating jobs or saving jobs; an impossible goal to verify. If, as Romer and Bernstein conclude, they expect that a stimulus package will create or save three million jobs by the fourth quarter of 2010, what does that mean? It seems to mean that relative to a baseline in which there is no stimulus package, there would be three million more jobs if the stimulus package is enacted. How, then, can we measure whether an enacted package ends up meeting the goal? Unfortunately, there will be no way to tell because, if a package is implemented, we will never know what the counterfactual no-stimulus baseline would have been.

Were the hurdle stated as "the stimulus will create three million jobs on net by the end of the fourth quarter of 2010," then it would be easy to measure if success was realized. We would simply measure employment at the end of the fourth quarter of 2010 and see whether it was three million more than today. But, since the hurdle is stated as "the stimulus will save or create three million jobs by the end of the fourth quarter of 2010," we will never know if the stimulus is a success. No matter what employment at the end of 2010, it can always be claimed that it would or could have been three million (or more) less had we not enacted a stimulus. Consequently, the three million jobs saved or created is a useless and unverifiable metric against which to measure the success or failure of stimulus.