



Policy Memorandum

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KEEPING TEACHERS ON THE JOB COSTS LESS THAN ADVERTISED

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A misplaced obsession with the size of federal budget deficits remains the single biggest obstacle to enacting new measures to create jobs on a scale commensurate with the crisis in the American labor market.

Even assuming that budget scoring rules can't be changed, at the very least policy makers should be aware of the true impact a given piece of legislation will have on deficits when debating new measures aimed at job creation. The congressional budget scoring rules can sometimes grossly distort the apparent impact of legislation on the federal budget deficit.

When an economy is facing unemployment rates that are roughly double what they were just 30 months ago even while the Federal Reserve has cut the interest rates it directly controls to historic lows, deficit-financed legislation aimed at creating jobs can be partially self-financing: as people are put back to work because of the legislation's effects, tax collections rise and the need for safety net spending is reduced. Both of these things reduce the budget deficit.

The degree to which any piece of legislation can partially self-finance by spurring job-growth depends largely on how efficient it is in creating jobs—legislation with higher “bang for buck” (i.e., jobs created per given amount spent) will spur more tax collections and reduce safety net spending more and hence will provide larger offsets to its gross headline costs.

Legislation recently proposed by Sen. Tom Harkin (D., Iowa) would provide \$23 billion in aid to states to keep teachers and other education professionals employed even as state budgets are in crisis. A range of respected macro-economic forecasters have identified fiscal relief to states as one of the quickest-acting and most-efficient forms of stimulus for an ailing economy. This large bang-for-buck means that the \$23 billion *gross* cost of the Harkin education staffing proposal greatly overstates its actual impact on the federal budget deficit.

Mark Zandi of Moody's Economy.com estimates that each dollar of federal aid to states provided during times of high unemployment will lead to a \$1.40 increase in overall economic activity (gross domestic product, or GDP). The Congressional Budget Office has estimated that each 1% increase in *actual* GDP relative to *potential* GDP (for example, the level of economic activity that would have been reached had unemployment been at 5% instead of 10%) leads to a \$0.38 reduction in the federal budget deficit.

Using these two numbers, we can roughly calculate the self-financing of the education staffing proposal: the \$23 billion multiplied by the 1.4 multiplier yields a \$32 billion increase in GDP as a result of the legislation. This extra \$32 billion will then generate extra taxes and reduced safety net spending that will lower the federal budget deficit by \$12.2 billion. With this offset, the net cost of Harkin's proposal will be only \$10.8 billion, or less than *half* the headline price.

Given that obsession with the simple size of the federal budget deficit now (wrongly) dominates the discourse on job-creation strategies, we need to at least get the numbers right. The greater offset to deficits provided by measures with a high "bang for buck" is one more reason to make sure that we direct resources as efficiently as possible in the name of job creation.