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NEW ZANDI ANALYSIS FINDS REBATES MORE EFFECTIVE AS STIMULUS IF THEY INCLUDE LOWER-INCOME WORKERS

Food Stamps and Unemployment Benefits Get the Highest Ratings

A new analysis by Mark Zandi, chief economist of Moody's Economy.com, examines the effectiveness of various stimulus options that policymakers are now discussing. (The analysis can be found at http://www.economy.com/home/article_ds.asp?cid=102598.) Zandi's findings, which cover both tax and spending options, include the following:

- A temporary increase in food stamp benefits is the most effective stimulus measure on the table; it would generate $1.73 in increased economic activity for each $1.00 in cost.

- Extending unemployment benefits so that workers' benefits don't run out before they can find a new job would be the second most effective measure, generating $1.64 in increased activity per dollar of cost.

- A tax rebate that includes low- and moderate-income working families that don't earn enough to owe income tax would be 24 percent more effective as stimulus than a rebate that leaves these families out (generating $1.26 in increased economic activity per dollar of cost, as compared to $1.02 in activity for a rebate that excludes the lower-income workers).

- In contrast, the principal business tax cut under discussion by Members of Congress and the Administration — a proposal to accelerate the depreciation write-offs that firms take — would be of little value. It would generate only 27 cents in increased economic activity per dollar of cost.

- Zandi's analysis also gives a high rating to temporary fiscal relief for state governments, finding that this would generate increased economic activity of $1.36 for each dollar of cost, because it would lessen state and local government budget cuts that "are sure to become a substantial drag on the economy later this year and into 2009." (See the box on the next page.)

Zandi on State Fiscal Relief

"Because most state governments are required by their constitutions to quickly eliminate their deficits, most are already drawing up plans to cut funding for programs ranging from healthcare to education and cutting grants to local government. Local governments are having their own financial problems; most rely on property-tax revenues, which are slumping with house prices. Cuts in state and local government outlays are sure to become a substantial drag on the economy later this year and into 2009.

"Additional federal aid to state governments would fund existing payrolls and programs and so provide a relatively quick economic boost. States that receive a check from the federal government will quickly pass on the money to workers, vendors and program beneficiaries.

"Arguments that state governments should be forced to cut spending that has grown bloated and irresponsible are strained at best. State government spending and employment are no larger today as a share of total economic activity and employment than they were three decades ago. Moreover, arguments that helping states today would encourage more profligacy in the future also appear overdone. Apportioning federal aid to states based on their size (either by GDP or population), rather than on the size of their budget shortfalls, would substantially mitigate this concern."