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Ms. Kate Stanley, Chair
Legislative Federal Economic Stimulus Program Oversight Commission
Hawaii State Capitol
415 South Beretania Street, Room 206
Honolulu, Hawaii 96813

Aloha,

You have requested that I review the Fourth Quarterly Report from the Council of Economic Advisors (CEA) entitled The Economic Impact of the American Recovery and Reinvestment Act (ARRA) of 2009 (Report) and provide you and the rest of the Commission members with my impressions. This letter will summarize some of my impressions and those of others that I have found.

In releasing the 51 page Report, Vice President Joe Biden and CEA chair Christina Romer (who has since resigned) noted that:

The Recovery Act has had a significant impact on employment and economic growth:

- As of the second quarter of 2010, the Recovery Act has raised employment by between 2.5 and 3.6 million jobs. This puts us well on track to reach the 3.5 million jobs benchmark by the end of this year.
- CEA estimates that the Recovery Act has raised the level of GDP as of the second quarter of 2010 by between 2.7 and 3.2 percent. These estimates are very similar to those of a wide range of other analysts, including the Congressional Budget Office.
- Outlays in areas such as infrastructure, clean energy, and communications technology increased by roughly 50 percent between the first and second quarters of 2010.

The Recovery Act is making investments that benefit the economy today and far into the future:

- $319 billion in the Act is dedicated to "public investments" that are not only "helping the economy to recover and put Americans back to work today, they are also making investments in areas such as clean energy, health information technology, roads, and the skills of our workers that will benefit the economy far into the future." To date, two-thirds of these funds have been obligated and more than one-quarter have been outlayed. CEA estimates that the $86.3 of outlays has already created or saved more than 800,000 jobs as of the second quarter of 2010, an increase of 30 percent over the first quarter.

The Recovery Act is leveraging significant investment from private companies and other entities:

- A subset of these public investments, $95 billion, is leveraging external funds from private companies and other entities. For each of these dollars invested, $4.00 of economic activity is supported – meaning $286 billion of external investments are partnering with Recovery Act funds to support $382 billion into total project activity.

  The benefits of this "co-investment" include:
- Jump-starting private investment: With credit markets still recovering from the financial crisis, the Recovery Act is directly stimulating $153 billion in private sector investment alone.
- Aligning economic incentives: As private investors use significant amounts of their own money in Recovery Act projects, they put "skin in the game" and have more incentive to use funding responsibly.
- Increasing overall support: The federal government has a responsibility to use tax dollars as effectively and efficiently as possible. Taxpayers get more value when those dollars are leveraged by private investment.

The positive spin by the Obama administration is not echoed by much of the business community if a recent article in the Wall Street Journal reflects their view. The Journal article states that:

Americans say they are underwhelmed by the economic recovery, and yesterday's report of 2.4% growth in the second quarter met their expectations. A recovery that should be accelerating after the long and deep recession has instead downshifted into slower growth.

About the best that can be said is that the report showed no signs of a looming "double dip" recession. Domestic demand was strong enough to suck in a burst of imports, which rebuts the Keynesians who are predicting another depression. Investment and business spending were strong, thanks to inventory rebuilding and some comeback in housing and commercial real estate. Disposable income also grew at a 4.4% annual rate, with less than half of it coming from government transfer payments.

Savings by households also increased again, to above 6%, which is back to the range of the early 1990s and is a healthy sign. The great deleveraging that began with business last year is now continuing with consumers. While some economists fret that this is bad for consumer "demand," savings don't vanish from the economy. They are recycled into lending and investment that can drive future growth if businesses see the right opportunities and have enough confidence. The irony is that businesses and consumers have been fixing their balance sheets even as the government has been doing the opposite. States and localities have deficits of nearly $100 billion, while the federal hole will be close to $1.4 trillion for the second year in a row.

This implies higher taxes, which Democrats in Washington are promising to deliver on January 1, and that's only the first installment. So just as Americans are putting themselves in the financial condition to start investing and spending more robustly, the Obama Administration will suck tens of billions out of the private economy. This is not the way to nurture a recovery that is weaker than it should be.

The 2.4% growth rate is especially disappointing coming after the previous two quarters of 5% and 3.7% growth. Yesterday's report also contained the government's annual historic GDP revisions, and growth was revised downward for the last three years. This means the U.S. is $130 billion, or 1%, poorer than previously thought and that growth will have to be that much faster to catch up.

A robust recovery would be building momentum, especially with historically easy monetary policy continuing. Instead this one is plodding along at a rate that won't create enough new jobs to sharply reduce the 9.5% unemployment rate. The Obama Administration, in its Keynesian confusion, is simultaneously saying the economy is so weak it needs more spending "stimulus" but also strong enough to absorb a huge tax increase.

The message of 2.4% second quarter growth is closer to the opposite: The epic government stimulus has failed to produce the robust expansion the White House promised, and the prospect of higher taxes and more regulation is inhibiting the private animal spirits needed for growth to accelerate. Americans may have to wait for November for Washington to get that message.

Hawaii was recently reported to have the third highest debt per capita of any state (Connecticut was first and Massachusetts was second) and that Honolulu had the fifth highest debt per capita of major cities (behind Harrisburg, Detroit, San Francisco and New York City).

As Chair of the Commission, you have repeatedly asked presenters “What happens after the ARRA funds are expended?” It seems obvious that neither the State nor the City and County of Honolulu should rely on continued Federal support. Anticipated changes in the makeup of Congress in November will likely reduce Federal expenditures. More State or County bonds would also seem out of the question in light of our heavily indebted status.

Raising taxes would also be counterproductive if our small business community is to survive. It would seem that some reduction in expenditures by State and local governments would be inevitable. Therefore, the question of what happens after ARRA is an important one.

A controversial report by Senators John McCain and Tom Coburn on waste under ARRA listed some 100 projects that were questionable, in their opinion. Fortunately, none of those projects, as far as I know, was located in the State of Hawaii.

Based on the Appendix included in the July 14^{th} Report, the Jobs Impact in 2010:Q2, for Hawaii, was 13,000. It is somewhat unclear as to how less than 3,600 jobs reported to the Commission, becomes 13,000 jobs. Although some effort is made to explain the process, the Report concludes that:

> measuring what a policy action has contributed to growth and employment is inherently difficult because we do not observe what would have occurred without the policy. Therefore, it must be understood that our estimates are subject to substantial margins of error. The results, however, are strong enough and clear enough that we are confident that the basis conclusions are solid. That a wide range of private and government analysts concur with our estimates adds a reassuring check on our analysis.

I hope this brief summary of various comments concerning the ARRA program is useful to you and the rest of the members.

For me, personally, I'm worried that the borrowed money for the stimulus adds an additional amount to our huge national debt which must be repaid at some point, by our kids, grandkids and future generations.

Spending public and private money we did not have on things we could not afford and in many cases did not need, is what many believe got us into this financial mess. Spending more money that we do not have seems an unlikely way to resolve the problem.

Sincerely,

Eddy N. Kemp

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Member