The American Recovery and Reinvestment Act of 2009

Introduction

The American economy is in a recession - the most recent of many in our long history. America's GDP declined at an annualized rate of 3.8% in the fourth quarter of 2008, the largest decline since 1982. In December the national unemployment rate was 7.2%, higher than average but far below the 10.5% rate faced by president Reagan when he first took over the Oval office in 1981. In his campaign the president Obama ran on the slogan "Hope not Fear" but within three weeks of taking office, he told the citizens of Elkhart, Indiana that "Economists from across the spectrum have warned that if we don't act immediately, millions of more jobs will be lost. The national unemployment rates will approach double digits not just here in Elkhart, all across the country. More people will lose their homes and their health care. And our nation will sink into a crisis that at some point we may be unable to reverse."

By pursuing this strategy of fear mongering, the president seems to be continuing the political strategy of his Chief of Staff, Rahm Emanuel who proclaimed at his press conference November 20, 2008 "You never want a serious crisis to go to waste. And what I mean by that, it's an opportunity to do things that you think you could not do before." The president relentlessly hammered out a few simple points. 1) America is in a terrible mess; 2) Only government can solve the problem: and 3) If we don't hurry, things will get much worse; 4) But if we act now, we can "save or create" up to four million jobs.

It worked! Similar versions of a so-called "stimulus package" were cobbled together in the House of Representatives and the Senate after more than 200 amendments to the bills had been submitted to the rules committee for consideration The U.S. congress quickly agreed and the president signed a 1,073 page gargantuan piece of legislation - the single most expensive appropriation and spending piece of legislation that has ever been enacted in the history of the world. It greatly increases the role of our Federal government in our economy and effectively legalizes "generational theft" by obligating our children to pay off the immense debts that will be incurred to pay for the misconduct of our Federal government today.

The non-partisan Congressional Budget Office predicts that even if the Act boosts the economy in the short term, by 2019 it will actually make America poorer than it would otherwise have been had the federal government done nothing to intervene during this recession and simply allowed market forces to bring about the necessary adjustments in the allocation of our scarce resources.

The stock market is a good indicator of public sentiment. Investors in the American equity markets have been demonstrating their displeasure with the Act – the Dow Jones Industrial Average closed at 7114 today (February 23, 2008), the lowest it has been since October 1997 and has lost approximately 44% in value just within the past 12 months.

But there is a remote possibility that Obama - the Chosen One and his cadre of tax cheats can hire enough new bureaucrats (who mostly vote Democratic) to manipulate our economy though the current recession - even though it would have most likely ended through normal market forces - and come out smelling like a rose claiming credit for a minor miracle just in time for the next election cycle. But enough pleasantries – lets consider the Act itself.

Obama's New - New Deal

The information and much of the actual language used in this paper was obtained from the Cato Institute Website and from the Congressional Budget Office (CBO) and the Joint Committee on Taxation (JCT).

The full name for this Act is "Making Supplemental Appropriations for Job Preservation and Creation, Infrastructure Investment, Energy Efficiency and Science, Assistance to the Unemployed, and State and Local Fiscal Stabilization, for the Fiscal Year Ending September 30, 2009, and for Other Purposes." The short name is "American Recovery and Reinvestment Act of 2009."

The Act specifically states that it has the following purposes:

1. To preserve and create jobs and promote economic recovery.
2. To assist those most impacted by the recession.
3. To provide investments needed to increase economic efficiency by spurring technological advances in science and health.
4. To invest in transportation, environmental protection, and other infrastructure that will provide long-term economic benefits.
5. To stabilize State and local government budgets, in order to minimize and avoid reductions in essential services and counterproductive state and local tax increases.

The Act states that the president and the heads of Federal departments and agencies shall manage and spend the funds made available in this Act as quickly as possible consistent with prudent management.

The Act specifies appropriations for a wide range of federal programs and would increase or extend certain benefits payable under the Medicaid, unemployment compensation, and nutrition assistance programs. The legislation also reduces individual and corporate income tax collections through a variety of changes to tax laws; those changes include instituting a tax credit of up to $500 for each worker in both 2009 and 2010, and raising the exemption amount allowed against an individual's income for the alternative minimum tax (AMT) for tax year 2009.

Major provisions of the legislation and key factors affecting estimates of spending are summarized, by title, below. The act separates the outlays into two categories: appropriations (Division A) and discretionary/direct spending (Division B).

Division A—Increased Spending Amounts for Appropriation Provisions

Title I—Agriculture, Rural Development, Food and Drug Administration, and Related Agencies. CBO estimates that title I of Division A would increase spending by the Department of Agriculture (USDA) by $21.6 billion over the 2009-2019 period.

Title II—Commerce, Justice, Science, and Related Agencies. Title II of Division A would appropriate $21.5 billion for science and criminal justice programs as well as initiatives to expand the commercial use of technology.

Title III—Defense. Title III of Division A would provide $3.4 billion to the Department of Defense for the repair, maintenance, and renovation of its facilities; for energy efficiency projects at those facilities; and for the leasing of alternative-energy vehicles. The title also would provide $0.2 billion for energy-related research and development and $0.1 billion for the procurement of components to be used in vehicles that utilize alternative-energy technologies. CBO expects that more than 80 percent of those funds would be spent in fiscal years 2009 and 2010.

Title IV—Energy and Water Development. Title IV of Division A would provide $53.8 billion in budget authority over the 2009-2019 period for programs related to energy and water resources. That amount includes $47.8 billion for the Department of Energy (DOE), $4.6 billion for the Army Corps of Engineers and $1.4 billion for the Bureau of Reclamation. Most of the funding provided to DOE would promote activities related to energy supply and conservation.

Title V—Financial Services and General Government. Title V would appropriate $10.7 billion primarily to promote energy efficiency and conservation at federal facilities and in the federal motor fleet. Most of that amount—$9.0 billion—would be appropriated to the General Services Administration's Federal Buildings Fund to construct and repair federal facilities.

Title VI—Homeland Security. Title VI would appropriate $5.1 billion for a variety of programs administered by the Department of Homeland Security.

Title VII—Interior and Environment. Title VII would appropriate a total of more than $11.6 billion, including $6.0 billion for the Clean Water and Drinking Water State Revolving Funds (SRFs). Under both programs, EPA provides grants or "seed money" to all 50 states plus Puerto Rico to capitalize state loan funds used by local governments to build water infrastructure projects.

Title VIII—Department of Labor, Health and Human Services, and Education and Related Agencies. CBO estimates that title VIII would increase funding by $89.3 billion over the 2009-2019 period for a variety of programs. That amount includes:

- $23.4 billion for programs administered by the Department of Health and Human Services;
- $3.8 billion for employment and training programs administered by the

Department of Labor;
● $26.5 billion for grants to elementary and secondary schools, including funding for special education and Title I;
● $17.1 billion to renovate elementary and secondary schools, fund educational technology, and support homeless students;
● $13.9 billion for Pell grants and other student financial assistance; and
● $4.2 billon for other education programs, including $3.5 billion to renovate facilities at post-secondary institutions.

Title IX—Legislative Branch. The legislation would provide $20 million for activities of the Government Accountability Office.

Title X—Military Construction and Veterans Affairs, and Related Agencies. Title X would appropriate $4.0 billion to several accounts in the Department of Veterans Affairs.

Title XI—State, Foreign Operations, and Related Programs. Title XI would provide about $1 billion to the Department of State and related agencies.

Title XII—Transportation and Housing and Urban Development. Title XII would appropriate $60.6 billion for programs administered by the Department of Transportation (DOT) and the Department of Housing and Urban Development (HUD). That amount includes:
● $27.1 billion for highway construction;
● $18.4 billion for other transportation programs administered by DOT;
● $12.9 billion for housing assistance programs administered by HUD; and
● $2.3 billion for grants to states and cities for community development.

Title XIII—State Fiscal Stabilization Fund. Title XIII would appropriate $79.0 billion to the Department of Education to create a fiscal stabilization fund to provide grants-in-aid to states. All of the funds will be made immediately available.

Division B—Other Provisions

Division B of the Act contains provisions that would increase direct spending for unemployment insurance, health care, fiscal relief for states through the Medicaid program, and literally hundreds of other programs and earmarks – too many to even attempt to summarize in this brief paper.

The CBO and JCT estimate that of the total spending increase of $884 billion for the combined Division A and Division B provisions in the Act, the latter category accounts for $253 billion of the total over the 2009-2019 period.

Time is of the Essence – Hurry up and Wait

Even though the stated purpose of the bill that was rushed through congress was to produce immediate jobs and spend the money “as quickly as possible”, CBO expects that the rate of spending in 2009 for many programs funded in the legislation would be considerably slower than historical rates of spending for a full year of funding because the bill would be enacted almost halfway into the fiscal year.

Although some programs would receive funding that is significantly above (double, triple, or more), the amounts provided for existing or similar programs in recent years, CBO expects that federal agencies, along with states and other recipients of that funding, will find it difficult to properly manage and oversee a rapid expansion of existing programs. It will not be possible to spend the added funds as quickly as they expend the resources provided for their ongoing programs because of the need to draft plans, solicit bids, enter into contracts, and conduct regulatory or environmental reviews.

Brand new programs pose additional challenges. Developing procedures and criteria, issuing the necessary regulations, and reviewing plans and proposals would make distributing money quickly even more difficult. Throughout the federal government, spending for new programs has frequently been slower than expected and rarely been faster.

What Will Happen? - Thinking Beyond Stage One

An army of new bureaucrats will need to be hired to administer the multitude of provisions in the Act who will never be sacked and will mostly vote Democratic.

In their February 2, 2009 report, the nonpartisan Congressional Budget Office (CBO) and the Joint Committee on Taxation (JCT) estimated that enacting this legislation would increase budget deficits by $694 billion over the 2009-2010 period (about 19 months) and by a total of $884 billion over the 2009-2019 period.

Within 2 days of their initial report, the CBO concluded, in a letter to Sen. Judd Gregg, New Hampshire Republican, who was originally selected by Mr. Obama to be Commerce Secretary, that president Obama's economic recovery package will result in so much government debt that within a few years it would crowd out private investment, actually leading to a lower Gross Domestic Product over the next 10 years and likely hurt the economy more in the long run than if the government had done nothing. CBO estimates that by 2019 the Act would reduce GDP by 0.1 percent to 0.3 percent on net. CBOs basic assumption is that, in the long run, each dollar of additional debt crowds out about a third of a dollars worth of private domestic capital.

In coming years the spending on entitlements – the main ones being Social Security, Medicare (health care for the elderly) and Medicaid (health care for the poor) – will dramatically increase deficits and consequently the national debt. According to the CBO, publicly held debt will increase from 41% of GDP last year to 54% next year and, if current policies continue, the debt would theoretically reach 400% of GDP by 2050.

Cato Ad

The Cato Institute recently paid for a full page ad (inserted at the end of this paper) that ran in several major newspapers to dispute the following proclamation issued by president-Elect Barack Obama January 9, 2009 “There is no disagreement that we need action by our government, a recovery plan that will help to jumpstart the economy.”

More than 200 economists signed the following statement that was contained in the ad.

> Notwithstanding reports that all economists are now Keynesians and that we all support a big increase in the burden of government, we the undersigned do not believe that more government spending is a way to improve economic performance. More government spending by Hoover and Roosevelt did not pull the United States economy out of the Great Depression in the 1930s. More government spending did not solve Japan’s “lost decade” in the 1990s. As such, it is a triumph of hope over experience to believe that more government spending will help the U.S. today. To improve the economy, policymakers should focus on reforms that remove impediments to work, saving, investment and production. Lower tax rates and a reduction in the burden of government are the best ways of using fiscal policy to boost growth.

FDRs New Deal Revisited

Let’s consider what happened during the last “New Deal.” Although Time magazine proclaimed in their January 15, 2009 issue that “we all really do seem to be Keynesians now”, there are many reputable economists who strongly disagree. They feel that spending is not stimulus. Bigger government and disproportionately higher levels of spending, with respect to GDP, did not work for FDR, LBJ, Gerald Ford, the Japanese during the 1990s or Bush #2 and it will not work for Obama.

Perhaps Time Magazine should have examined why Keynesian policies failed to rescue the United States economy in the 1930s – leading president Roosevelt’s own Treasury Secretary Henry Morgenthau, Jr. to conclude that “we have tried spending money. We are spending more than we have ever spent before and it does not work.”

Perhaps Time magazine should have asked why Japan’s ten Keynesian stimulus bills in the 1990s failed to rescue their sluggish economy.

Or, perhaps they should have looked into why the alternative approach of reducing marginal tax rates did help to bring and end to the 1980-1982 recession, and created a surge of economic growth after the 2003 tax cuts.

But the answers to those questions wouldn’t support the goal of liberals to confiscate scarce resources from the private sector and redistribute these resources in accordance with the anti-capitalist, collectivist utopian visions held by our political and academic elite.

But let us return to Keynes.

Keynesian economics was built on the belief that people are slow-witted and couldn't be trusted to make rational economic decisions. Keynesians feel that the politicians and bureaucrats in our central government must intervene in our individual economic decisions because they possess superior intelligence compared to those in the private sector of our economy. Their actions indicate a conviction that the combined intelligence contained by those in the central government is superior to the combined intelligence of millions of individuals in the private sector, each making their own economic decisions at the micro economic level.

The combined intelligence and the immediacy of their knowledge of the hundreds of thousands of entrepreneurs and workers in America is far superior than the limited intelligence possessed by the much smaller number of politicians and bureaucrats in government with their vague understanding of what is best for every single person in our country.

Keynesian policies result in taking the economic decision making process out of the hands of individual entrepreneurs and workers since Keynesians are convinced that these individuals are too dim to get right on their own.

During the 1930s, Keynes and his disciples argued that the economy could be boosted if the government borrowed money and spent it. According to the theory, this new spending would put money in people's pockets, and the recipients of the funds would then spend the money and "prime the pump" as the money began circulating through the economy.

The Keynesians also said that some tax cuts—particularly lump-sum rebates—could have the same impact since the purpose is to have the government borrow and somehow put the money in the hands of people who will spend it.

Keynesian theory suffers from a rather glaring logical fallacy. It overlooks the fact that, in the real world, government can't inject money into the economy without first taking money out of the economy. Any money that the government puts in the economy's right pocket is money that is first removed from the economy's left pocket. There is no increase in what Keynesians refer to as aggregate demand since every dollar that is spent on a stimulus package is a dollar that the government first must borrow from private credit markets. Keynesianism doesn't boost national income, it merely redistributes it.

Real-world evidence does not support the Keynesianism perspective. In his four years, Herbert Hoover increased taxes dramatically, including a boost in the top tax rate from 25 percent to 63 percent. He imposed harsh protectionist policies. He significantly increased intervention in private markets. Most importantly, at least from a Keynesian perspective, he boosted government spending by 47 percent in just four years. And he certainly had no problem financing that spending with debt. He entered office in 1929, when there was a surplus, and he left office in 1933 with a deficit of 4.5 percent of GDP.

Unfortunately, other than being a bit more reasonable on trade, Roosevelt followed the same approach. The top tax was boosted to 79 percent and government intervention became more pervasive. Government spending, of course, skyrocketed—rising by 106 percent between 1933 and 1940. This big-government approach didn't work for

Roosevelt any better than it did for Hoover. Unemployment remained very high, averaging more than 17 percent throughout the 1930s, and overall output did not get back to the 1929 level until World War II. According to recent research by economists at UCLA, New Deal policies extended the Depression by seven years.

During the Bush years, so-called stimulus legislation based on "Keynesian" theory was enacted in both 2001 and 2008. It was hoped that putting money in people's pockets would lead to more consumer spending and thus give the economy a positive jolt. Those episodes of Keynesian policy were ineffective, but that has not dimmed enthusiasm for the approach.

The Obama economic team is pushing a similar approach, but on a much bigger scale—more than $800 billion of new spending, a figure that climbs above $1 trillion when interest costs are included. And that may be just the starting point since the promise of additional spending has set off a feeding frenzy on Capitol Hill.

Doing more of a bad thing is not a recipe for growth. Government spending generally is a burden on the economy. Whether financed by debt or taxes, government spending requires a transfer of money from the productive sector of the economy. Moreover, most forms of government spending result in the misallocation of labor and capital, causing even further damage.

Although many factors influence economic performance, the negative impact of government spending is one reason small-government jurisdictions such as Hong Kong have higher growth rates than nations that have medium-sized government, such as the United States. The same principle explains in part why the United States enjoys faster average growth than a big-government country such as France

Other Keynesian episodes generated similarly dismal results, though fortunately never as bad as the Great Depression. Gerald Ford did a Keynesian stimulus focused on tax rebates in the mid-1970s. The economy did not improve. But why would it? After all, borrowing money from one group and redistributing it to another does nothing to increase economic output. As mentioned above, George W. Bush gave out so-called rebate checks in 2001 and 2008, yet there was no positive effect either time. And he certainly was a big spender, yet that didn't work either.

International evidence also undermines the case for Keynesianism. The clearest example may be Japan, which throughout the 1990s tried to use so-called stimulus packages in an effort to jump-start a stagnant economy. But the only thing that went up was Japan's national debt, which more than doubled during the decade and is now even far more than Italy's when measured as a share of GDP. The Japanese economy never recovered, and the 1990s are now known as the "lost decade" in Japan.

Alternative Plan – Get Off Our Back!

Even though liberals often launch into a well-rehearsed rant anytime conservatives suggest a reduction in taxes, even the renowned economist Christina Romer, Chair of

Obama's Council of Economic Advisors, has herself written that tax increases, even if they are made to reduce inherited budget deficits, reduce economic growth. Conversely, tax reductions increase economic growth by putting more money into the hands of individuals and businesses so that they can make their own economic decisions, manage their own economic affairs and more efficiently utilize our nation's scarce resources.

Interestingly, Romer also puts to rest the fiction that continues to be perpetuated in public-school propaganda that FDRs New Deal helped to end the economic depression of the 1930s; rather she documents the fact that when the inevitability of war became obvious to Europeans, it was the massive flight of European capital to the relative safety of America that ended our depression. Today we seeing a repeat of this same phenomenon caused by the flight of foreign capital from shaky economies into U.S. treasury instruments. This tremendous inflow of capital could, by itself, end our recession and this observation may be a main reason that Obama chose to rush through his massive spending proposals before our economy actually improved on its own without any government intervention.

Ironically, John Maynard Keynes stated that the maximum tolerable proportion of taxation is 25 percent of GDP. America is now well past that stage and a further expansion of government will make the United States more like a stagnant, European-style welfare state.

Most people hate paying taxes and often hang on to appreciated assets (resources) that could be put to better uses. Quite often owners refuse to sell these assets (that have better alternative uses) because that economic decision would require them to pay a significant amount of the gain to the government. It is not unusual for this writer to see individuals staying in much larger homes than they need (or want) but resist selling simply because the sale would require them to pay a large sum in taxes. This behavior throttles our economy and the logical solution is both simple and easy – reduce or eliminate taxes on capital gains.

A reduction in or elimination of the capital gains tax would **immediately** stimulate our economy. If our government eliminated taxes capital gains, there would be an incredible flurry of economic activity and our scarce resources would be more efficiently allocated according to the rules of basic economics.

Furthermore, the president's package of increased spending is exactly the wrong thing to do. However, since no one wants to bear the political cost for appearing to be uncaring by favoring a policy of "doing nothing" during an economic slowdown, out of political cowardice and disdain for American entrepreneurial spirit, the federal government has foisted a solution upon America that conforms to their goal of usurping even more power from the states and from the people even though it will make our country poorer in the long run.

You can't solve an excessive spending problem by spending more. We are making the crisis worse. We have been down this road before. But again and again, the politicians and intelligentsia presume a Keynesian cause and a Keynesian cure.

The free-market solution to dealing with recessions is to allow the various marketplaces to respond to the changed economic environment through the normal pricing system that will result in an appropriate reallocation of scarce resources that have alternative uses. The very idea that companies or individuals cannot be allowed to fail is absurd. In free societies and in capitalism there is the understanding that all of us have the right to pursue our own individual dreams and accept individual responsibility for our actions - the alternative economic systems have various names: communism, socialism and fascism.

If an individual or company makes decisions that result in failure, we already have the well-tested system of bankruptcy that efficiently re-allocates those scarce resources to more productive uses – our country doesn't need a stinking bailout!

Conclusion

Monetary policy, trade policy, taxation, labor markets, property rights, and competitive markets all have some impact on an economy's performance. But one of the key variables is government spending. Once government expands beyond the level of providing core public goods such as the rule of law, there tends to be an inverse relationship between the size of government and economic growth. This is why reducing the size and scope of government is one of the best ways to improve economic performance. Unfortunately, policy moved in the wrong direction during the Bush years, and proposals for so-called stimulus indicate a continuation of those failed policies during the Obama years.

However, there is a major conflict between the need to spend quickly and the desire to spend well. Much emphasis has been made about "shovel-ready" projects; however, everyone with a shovel will now claim to be shovel-ready. Projects that were long ago dismissed as unnecessary will suddenly spring to life. Rather than spending funds on unexciting projects such as repairing infrastructure and fixing the potholes, politicians will most certainly direct the money to more spectacular structures that they can celebrate with high profile ribbon cutting ceremonies and impressive media coverage that can be re-run during their next election campaign.

Bush brought the Age of Reagan to a close; now Obama has gone further. During the roughly three decades since Reagan made big government the enemy and "liberal" an epithet, our economy grew and the growth of government as a percentage of GDP remained relatively constant. government growth did not shrink. But for the past five years or so, it has borne a suspicious resemblance to Bernie Madoff's stock fund. Americans have been living high on borrowed money (the savings rate dropped from 7.6 percent in 1992 to less than zero in 2005).

According to the Organization for Economic Cooperation and Development, 10 years ago U.S. government spending was 34.3 percent of GDP, compared with 48.2 percent in the euro zone—a roughly 14-point gap,. In 2010 U.S. spending is expected to be 39.9 percent of GDP, compared with 47.1 percent in the euro zone—a gap of less than 8 points.

If entitlement spending rises over the next decade, we will become even more like the socialist countries in Europe and more government intrusion in the economy will almost surely limit growth (as it has in Europe, where a big welfare state has caused chronic high unemployment). Growth has always been America's birthright and saving grace.
Government is not the solution – government is the problem!

"There is no disagreement that we need action by our government, a recovery plan that will help to jumpstart the economy."

—PRESIDENT-ELECT BARACK OBAMA, JANUARY 9, 2009

With all due respect Mr. President, that is not true.

Notwithstanding reports that all economists are now Keynesians and that we all support a big increase in the burden of government, we the undersigned do not believe that more government spending is a way to improve economic performance. More government spending by Hoover and Roosevelt did not pull the United States economy out of the Great Depression in the 1930s. More government spending did not solve Japan's "lost decade" in the 1990s. As such, it is a triumph of hope over experience to believe that more government spending will help the U.S. today. To improve the economy, policymakers should focus on reforms that remove impediments to work, saving, investment and production. Lower tax rates and a reduction in the burden of government are the best ways of using fiscal policy to boost growth.

Burton Abrams, *Univ. of Delaware*
Douglas Adie, *Ohio University*
Lee Adkins, *Oklahoma State University*
William Albrecht, *Univ. of Iowa*
Ryan Amacher, *Univ. of Texas at Arlington*
J.J. Arias, *Georgia College & State University*
Howard Baetjer, Jr., *Towson University*
Charles Baird, *California State University, East Bay*
Stacie Beck, *Univ. of Delaware*
Don Bellante, *Univ. of South Florida*
James Bennett, *George Mason University*
Bruce Benson, *Florida State University*
Sanjai Bhagat, *Univ. of Colorado at Boulder*
Mark Bils, *Univ. of Rochester*
Alberto Bisin, *New York University*
Walter Block, *Loyola University New Orleans*
Cecil Bohanon, *Ball State University*
Michele Boldrin, *Washington University in St. Louis*
Donald Booth, *Chapman University*
Michael Bordo, *Rutgers University*
Samuel Bostaph, *Univ. of Dallas*
Donald Boudreaux, *George Mason University*
Scott Bradford, *Brigham Young University*
Genevieve Briand, *Eastern Washington University*
Ivan Brick, *Rutgers University*
George Brower, *Moravian College*
Phillip Bryson, *Brigham Young University*
James Buchanan, *Nobel laureate*
Richard Burdekin, *Claremont McKenna College*
Richard Burkhauser, *Cornell University*
Edwin T. Burton, *Univ. of Virginia*
Jim Butkiewicz, *Univ. of Delaware*
Henry Butler, *Northwestern University*
William Butos, *Trinity College*
Peter Calcagno, *College of Charleston*
Bryan Caplan, *George Mason University*
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Dustin Chambers, *Salisbury University*
Emily Chamlee-Wright, *Beloit College*
V.V. Chari, *Univ. of Minnesota*
Barry Chiswick, *Univ. of Illinois at Chicago*
Lawrence Cima, *John Carroll University*
J.R. Clark, *Univ. of Tennessee at Chattanooga*
Gian Luca Clementi, *New York University*
R. Morris Coats, *Nicholls State University*
John Cochran, *Metropolitan State College at Denver*
John Cochrane, *Univ. of Chicago*
John Cogan, *Hoover Institution, Stanford University*
Lloyd Cohen, *George Mason University*
John Coleman, *Duke University*
Boyd Collier, *Tarleton State University*
Robert Collinge, *Univ. of Texas at San Antonio*
Peter Colwell, *Univ. of Illinois at Urbana-Champaign*
Michael Connolly, *Univ. of Miami*
Lee Coppock, *Univ. of Virginia*
Mario Crucini, *Vanderbilt University*
Christopher Culp, *Univ. of Chicago*
Kirby Cundiff, *Northeastern State University*
Antony Davies, *Duquesne University*
John Dawson, *Appalachian State University*
A. Edward Day, *Univ. of Texas at Dallas*
Clarence Deitsch, *Ball State University*

Allan DeSerpa, *Arizona State University*
William Dewald, *Ohio State University*
Arthur Diamond, Jr., *Univ. of Nebraska at Omaha*
John Dobra, *Univ. of Nevada, Reno*
James Dorn, *Towson University*
Christopher Douglas, *Univ. of Michigan, Flint*
Floyd Duncan, *Virginia Military Institute*
Francis Egan, *Trinity College*
John Egger, *Towson University*
Kenneth Elzinga, *Univ. of Virginia*
Paul Evans, *Ohio State University*
Frank Falero, *California State University, Bakersfield*
Eugene Fama, *Univ. of Chicago*
W. Ken Farr, *Georgia College & State University*
Daniel Feenberg, *National Bureau of Economic Research*
Hartmut Fischer, *Univ. of San Francisco*
Eric Fisher, *California State Polytechnic University*
Fred Foldvary, *Santa Clara University*
Murray Frank, *Univ. of Minnesota*
Peter Frank, *Wingate University*
Timothy Fuerst, *Bowling Green State University*
B. Delworth Gardner, *Brigham Young University*
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Rick Geddes, *Cornell University*
Aaron Gellman, *Northwestern University*
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Otis Gilley, *Louisiana Tech University*
Stephan Gohmann, *Univ. of Louisville*
Rodolfo Gonzalez, *San Jose State University*
Richard Gordon, *Penn State University*
Peter Gordon, *Univ. of Southern California*
Ernie Goss, *Creighton University*
Paul Gregory, *Univ. of Houston*
Earl Grinols, *Baylor University*
Daniel Gropper, *Auburn University*
R.W. Hafer, *Southern Illinois University, Edwardsville*
Arthur Hall, *Univ. of Kansas*
Steve Hanke, *Johns Hopkins University*
Stephen Happel, *Arizona State University*
Richard Hart, *Miami University*
Thomas Hazlett, *George Mason University*
Frank Hefner, *College of Charleston*
Scott Hein, *Texas Tech University*
Ronald Heiner, *George Mason University*
David Henderson, *Hoover Institution, Stanford University*
Robert Herren, *North Dakota State University*
Gailen Hite, *Columbia University*
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Brian Jacobsen, *Wisconsin Lutheran College*
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Jason Johnston, *Univ. of Pennsylvania*
Boyan Jovanovic, *New York University*
Jonathan Karpoff, *Univ. of Washington*
Barry Keating, *Univ. of Notre Dame*
Naveen Khanna, *Michigan State University*

Nicholas Kiefer, *Cornell University*
Daniel Klein, *George Mason University*
Paul Koch, *Univ. of Kansas*
Narayana Kocherlakota, *Univ. of Minnesota*
Marek Kolar, *Delta College*
Roger Koppl, *Fairleigh Dickinson University*
Kishore Kulkarni, *Metropolitan State College of Denver*
Deepak Lal, *UCLA*
George Langelett, *South Dakota State University*
James Larriviere, *Spring Hill College*
Robert Lawson, *Auburn University*
John Levendis, *Loyola University New Orleans*
David Levine, *Washington University in St. Louis*
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Dean Lillard, *Cornell University*
Zheng Liu, *Emory University*
Alan Lockard, *Binghampton University*
Edward Lopez, *San Jose State University*
John R. Lott, Jr., *Univ. of Maryland*
John Lunn, *Hope College*
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