Contact: Mark Primoff
845-758-7412
primoff@bard.edu

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GOVERNMENT INVESTMENT IN RESEARCH AND DEVELOPMENT OFFERS OPPORTUNITY FOR U.S. ECONOMY TO REGAIN COMPETITIVENESS CRUCIAL FOR GROWTH AND EMPLOYMENT, NEW LEVY STUDY SAYS

ANNANDALE-ON-HUDSON, N.Y.— If recent Congressional Budget Office projections for government revenues and outlays come to pass, the U.S. economy will not grow fast enough to bring down the unemployment rate between now and 2016, a new study from the Levy Economics Institute of Bard College argues. Both government and household sector deficits are expected to decline from present levels and endanger the sustainability of the recovery. A new Levy Institute Strategic Analysis shows, however, that a public sector stimulus of a little over 1 percent of GDP per year focused on investment in export-oriented research and development would increase U.S. competitiveness through export-price effects, resulting in a rise in net exports, and slowly lower unemployment to less than 5 percent by 2016. The improvement in net export demand would allow the U.S. economy to enter a period of aggregate-demand rehabilitation—with very encouraging consequences at home.

"Accelerated economic growth and increased aggregate demand will not come about from private expenditures while the household sector continues its deleveraging trend," write the Levy Institute's Macro-Modeling Team, President Dimitri B. Papadimitriou and Research Scholars Greg Hannsgen, Michalis Nikiforos, and Gennaro Zezza, in their Strategic Analysis, *Rescuing the Recovery: Prospects and Policies for the United States.* "Rescuing the recovery will require using expansionary fiscal and monetary policies."

Using the Levy Institute's U.S. macro model, the scholars provide medium-term projections of employment and economic growth through 2016 under three different scenarios. In their baseline run, using current CBO projections for growth and unemployment, they find that, with fiscal consolidation expected to continue, there will be an extension of the weak labor market recovery, with unemployment at only slightly less than 7 percent and GDP growth remaining near 3.5 percent.

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In their second scenario, the Levy team simulates the effects of a $160 billion increase in government infrastructure spending, or approximately 1 percent of GDP, which results in GDP growth of 5 percent and a drop in unemployment to below 6 percent by 2016. Their third scenario, in which the scholars simulate the same increase, $160 billion, in government R & D spending (or sparing such expenditures from sequester cuts), results in GDP growth of 5.5. percent and an unemployment rate of less than 5 percent by 2016, largely achieved by raising productivity in industries catering to export markets and stimulating export growth.

The Levy team concludes by arguing that the business-as-usual case they analyze in their baseline shows anemic growth and unemployment for the years ahead, that the congressional debt ceiling stalemate and government shutdown will have enormously detrimental consequences, and that a change in the government's fiscal policy stance is necessary to create an outlook for stronger growth and employment.

"Our scenario considering increases in R & D expenditures convinces us that restoring US price competitiveness, especially long overdue in the high-technology manufacturing sector, will increase export demand at a relatively small cost of about 1 percent of GDP in new stimulus annually to 2016," writes the Levy team. "The range of strategic policy options for the United States is limited. Bringing down the stubbornly high unemployment rate and reversing the decline of household fortunes are urgent priorities."

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Strategic Analysis: *Rescuing the Recovery: Prospects and Policies for the United States*

To read the full text of this policy paper or to learn more about the Levy Economics Institute of Bard College, please visit http://www.levyinstitute.org/publications/?docid=1909.

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