

August 25, 2010

Do your schools have dance studios and pizza ovens? We get a report on [LA's \\$578 million school](#). That's right, LA has built a K-12 school for 4,200 students that cost \$578,000,000. Maybe the president will want to send California some more bail-out cash. *LOS ANGELES – Next month's opening of the Robert F. Kennedy Community Schools will be auspicious for a reason other than its both storied and infamous history as the former Ambassador Hotel, where the Democratic presidential contender was assassinated in 1968.*

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The \$578 million school is quite an example of what is wrong with public school system priorities. A report on the school from [ABC News](#).

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*The money troubles come on top of the district's serious academic shortfalls. With a dropout rate upwards of 35 percent, LA Unified is one of the lowest-performing school districts in America. ...*

There is some hope, though. Virginia shows how to make some tough decisions. The [WSJ editors](#) comment on another Republican governor who didn't raise taxes and still balanced his state's budget.

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*The usual suspects—the big business lobbies, the Washington Post—thought a major tax increase was needed. So did the previous Governor, Democrat Tim Kaine, who proposed a \$2 billion tax hike before he left town, on top of two major Virginia tax increases in the previous eight years.*

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*In the Corner, [Veronique de Rugy](#) alerts us to an article by Tad DeHaven about higher pay for government workers; pay that comes from taxes on productive citizens and sectors of the economy.*

*In the debate over the [difference in pay](#) between private and federal employees, the Cato Institute's Tad DeHaven makes [some very good points](#) that I hadn't heard before:*

*...In the private sector, an employee's compensation is a reflection of his or her value in the market. For instance, one may not like that LeBron James makes [millions of dollars](#) playing [basketball](#), but that's what the market for professional basketball players says his production is worth. It's no different for a considerably lower-paid employee in the restaurant industry.*

*What's a federal employee worth? How does one measure a government employee's production? Government isn't subject to market disciplines. It can't go out of business. It has no competitor. It doesn't need to earn a profit or even break even. It doesn't receive its revenue from voluntary transactions – its revenues are obtained via taxation, which is paid by individuals under compulsion and force. ...*

*...Federal and private employees are apples and oranges because the former is dependent on the latter for its existence. ...*

**[Ed Morrissey](#)** has excellent commentary on the lack of real-world experience in the administration as the reason for its abject failure.

*Wonder how Recovery Summer turned into Wreckovery Bummer? How an administration ginned up its entire economic strategy into one stimulus bill and has done nothing since, even as the economy disintegrated? Marty Robins advises his readers to [check the CVs](#) of the people in charge in Washington to understand just how incompetence has triumphed — and not just Barack Obama's:*

*If Washington seems out of ideas on how to get the private-sector jobs machine running again, there's a pretty straightforward reason — the people in government have virtually no experience in business. ...*

*...This increasing disconnect between the government and the business world is a big, if unrecognized, problem, if for no other reason than that it deprives government officials of the knowledge and experience that successful business leaders can bring to solving difficult problems.*

*...Obama stuck with ideological allies heavy on academics and with no real-world experience, reflecting his own profile rather than complementing it as an experienced executive would have known to do. Obamanomics is the result. It's a classic command-economy approach that works on every university campus where it's discussed — and in no real-world setting where it's ever been tried. ...*

**Robert Samuelson** discusses government policies that led to the housing bubble and what changes could be made to those policies and to the government-sponsored enterprises that administrate them.

*...In an ideal world, we would discard failed policies. We would trim or end the mortgage-interest tax deduction. We would curtail the GSEs' loans and guarantees (the promise to repay mortgages that default). The consequences need not be dire. The homeownership rate, already down to 67 percent from its 2004-06 peak of 69 percent, would probably stabilize in the mid-60s. People would save more for down payments. Mortgage rates might rise a bit.*

*The irony is that, in failure, the GSEs have become more important than ever. Private lenders, which once regarded a mortgage secured by a home as a highly safe investment, now see it as highly risky. Few new mortgages are made without government guarantees. The GSEs continue to operate and, along with other government agencies, guaranteed about 95 percent of new mortgages made in 2009, reports *Inside Mortgage Finance*, an industry newsletter. Since 1990, the government guarantee share had fluctuated between 30 and 50 percent.*

*This means that sudden withdrawals of support might deepen housing's depression. Economists Phillip Swagel of Georgetown University and Donald Marron of the Tax Policy Center, among others, have made sensible [proposals to scale back Fannie and Freddie](#). But done too quickly, they could backfire. ...*

**Peter Schiff** gives us a great lesson in economics that liberal politicians don't understand. He explains why government policies that encourage spending do not help the recovery. In a CNBC debate last week, former Labor Secretary Robert Reich presented a set of contradictory beliefs that unfortunately reflect the conventional wisdom of modern economists. ...

*...Reich called for lowering taxes on working Americans and raising taxes on the rich. He argued that middle-income Americans are more likely to spend additional dollars while the rich are more likely to save and invest. As a "demand-side" economist, Reich made clear that spending is superior to savings and investing as a catalyst for growth.*

*To put it simply: Reich believes that the cart pushes the horse. In his worldview, businesses produce goods and services simply because consumers spend. Therefore, anything that increases spending fuels growth. Unfortunately, he fails to see what should be strikingly obvious: capital formation must precede production, which then allows for consumption.*

*In a complex society like ours, those relationships are hard to see. However, if we break it down to a simpler level, it becomes more obvious (as I try to accomplish in my new book: [How an Economy Grows and Why it Crashes](#)). For example, let's take a look at a simple barter-based economy consisting of only three people: a butcher, a baker, and a candlestick maker. ...*

Kudos to the **Washington Examiner editors!** The editors are challenging Republicans to come up with a plan to reign in government.

*...Those Bush years too often displayed little difference between Republicans and Democrats in Washington. Much of the vast expansion of the federal government by Democrats was previewed by the Bush-led Republicans. Obamacare's overreach? Don't forget the Republicans' entitlement-expanding and budget-busting Medicare Part D. In fact, Republicans were off the reservation long before Bush ever*

entered office. The 1994 Republican revolution marked the first time in more than 40 years that Republicans held a congressional majority. They won while pledging specific policy goals in their Contract with America, including term limits, a balanced budget amendment, and welfare reform. Some significant progress was made but in a few years the revolution was all but abandoned. The Cato Institute's Ed Crane recently noted that the "combined budgets of the 95 major programs that the Contract with America promised to eliminate ... increased by 13 percent."

Today, most Americans are ready as never before to shrink government and stop the spending madness. This presents the GOP with an opportunity it didn't have in 1994: an electorate exhausted by Washington politicians and their doubletalk. But the GOP so far seems unwilling to lay out specifics about how it plans to respond to what Americans are saying if they restore the party to majority status in the House and perhaps the Senate. House Minority Whip Eric Cantor, R-Va., boasts of the Republican "YouCut" Web site that solicits ideas from voters, but that effort barely rises above window dressing. Rep. Paul Ryan, R-Wis., has proposed a "Roadmap to Economic Recovery" as a serious program for entitlement reform, yet the party leadership has not embraced it. Similarly, the Heritage Foundation has compiled 128 policy recommendations across 23 major policy areas for shrinking government and making it work better. The Examiner will be offering a number of ideas on this page in coming days as well. Republican leaders risk squandering a historic opportunity by ignoring such recommendations. The voters are waiting.

In [Volokh Conspiracy](#), [David Kopel](#) says, stop giving Obama grief for golf.

*In this polarized period of American politics, many people on the Right have been taking cheap shots at President Obama because he plays golf so much.*

*...Of American Presidents since World War II, the one President who is now almost universally regarded as highly successful and constructive, by persons of all political persuasions, is President Dwight D. Eisenhower. While serving eight years as President of the United States, Eisenhower may have [played](#) over eight hundred rounds of golf. In other words, about twice a week. ...*

*...However, President Eisenhower demonstrated beyond any doubt that there is no inherent contradiction between being a good President and being an avid golfer. Indeed, golf helps clear the mind, and hardly any sport is better at fostering humility in participants. So unless President Obama's critics are willing to state that President Eisenhower golfed too much, they should stop carping about President Obama's golfing.*

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## **Yahoo News**

### [LA unveils \\$578M school, costliest in the nation](#)

by Christina Hoag

LOS ANGELES – Next month's opening of the Robert F. Kennedy Community Schools will be auspicious for a reason other than its both storied and infamous history as the former Ambassador Hotel, where the Democratic presidential contender was assassinated in 1968.

With an eye-popping price tag of \$578 million, it will mark the inauguration of the nation's most expensive public school ever.



The K-12 complex to house 4,200 students has raised eyebrows across the country as the creme de la creme of "Taj Mahal" schools, \$100 million-plus campuses boasting both architectural panache and deluxe amenities.

"There's no more of the old, windowless cinderblock schools of the '70s where kids felt, 'Oh, back to jail,'" said Joe Agron, editor-in-chief of *American School & University*, a school construction journal. "Districts want a showpiece for the community, a really impressive environment for learning."

Not everyone is similarly enthusiastic.

"New buildings are nice, but when they're run by the same people who've given us a 50 percent dropout rate, they're a big waste of taxpayer money," said Ben Austin, executive director of Parent Revolution who sits on the California Board of Education. "Parents aren't fooled."

At RFK, the features include fine art murals and a marble memorial depicting the complex's namesake, a manicured public park, a state-of-the-art swimming pool and preservation of pieces of the original hotel.

Partly by circumstance and partly by design, the [Los Angeles Unified School District](#) has emerged as the mogul of Taj Mahals.

The RFK complex follows on the heels of two other LA schools among the nation's costliest — the \$377 million Edward R. Roybal Learning Center, which opened in 2008, and the \$232 million Visual and Performing Arts High School that debuted in 2009.

The pricey schools have come during a sensitive period for the nation's second-largest school system: Nearly 3,000 teachers have been laid off over the past two years, the academic year and programs have been slashed. The district also faces a \$640 million shortfall and some schools persistently rank among the nation's lowest performing.

Los Angeles is not alone, however, in building big. Some of the most expensive schools are found in low-performing districts — New York City has a \$235 million campus; New Brunswick, N.J., opened a \$185 million high school in January.

Nationwide, dozens of schools have surpassed \$100 million with amenities including atriums, orchestra-pit auditoriums, food courts, even bamboo nooks. The extravagance has led some to wonder where the line should be drawn and whether more money should be spent on teachers.

"Architects and builders love this stuff, but there's a little bit of a lack of discipline here," said Mary Filardo, executive director of 21st Century School Fund in Washington, D.C., which promotes urban school construction.

Some experts say it's not all flourish and that children learn better in more pleasant surroundings.

Many schools incorporate large windows to let in natural light and install energy-saving equipment, spending more upfront for reduced bills later. Cafeterias are getting fancier, seeking to retain students who venture off campus. Wireless Internet and other high-tech installations have become standard.

Some pricey projects have had political fallout.

After a firestorm over the \$197.5 million Newton North High School in Massachusetts, Mayor David Cohen chose not to seek re-election and state Treasurer Timothy Cahill reined in school construction spending.

Now to get state funds for a new school, districts must choose among three designs costing \$49 million to \$64 million. "We had to bring some sense to this process," Cahill said.

In Los Angeles, officials say the new schools were planned long before the economic pinch and are funded by \$20 billion in voter-approved bonds that do not affect the educational budget.

Still, even LA Unified Superintendent Ramon Cortines derided some of the extravagance, noting that donations should have been sought to fund the RFK project's talking benches commemorating the site's history.

Connie Rice, member of the district's School Bond Oversight Committee, noted the megaschools are only three of 131 that the district is building to alleviate overcrowding. RFK "is an amazing facility," she said. "Is it a lot of money? Yes. We didn't like it, but they got it done."

Construction costs at LA Unified are the second-highest in the nation — something the district blames on skyrocketing material and land prices, rigorous seismic codes and unionized labor.

James Sohn, the district's chief facilities executive, said the megaschools were built when global raw material shortages caused costs to skyrocket to an average of \$600 per square foot in 2006 and 2007 — triple the price from 2002. Costs have since eased to \$350 per square foot.

On top of that, each project had its own cost drivers.

After buildings were demolished at the site of the 2,400-student Roybal school, contaminated soil, a methane gas field and an earthquake fault were discovered. A gas mitigation system cost \$17 million.

Over 20 years, the project grew to encompass a dance studio with cushioned maple floors, a modern kitchen with a restaurant-quality pizza oven, a 10-acre park and teacher planning rooms between classrooms.

The 1,700-student arts school was designed as a landmark, with a stainless steel, postmodernistic tower encircled by a rollercoaster-like swirl, while the RFK site involved 15 years of litigation with historic preservationists and Donald Trump, who wanted to build the world's tallest building there. The wrangling cost \$9 million.

Methane mitigation cost \$33 million and the district paid another \$15 million preserving historic features, including a wall of the famed Cocoanut Grove nightclub and turning the Paul Williams-designed coffee shop into a faculty lounge.

Sohn said LA Unified has reached the end of its Taj Mahal building spree. "These are definitely the exceptions," he said. "We don't anticipate schools costing hundreds of millions of dollars in the future."

## ABC News

### [Los Angeles Public School Named After Robert Kennedy Costs \\$578 Million](#) *Most Expensive Public School in Nation's History Set to Open Next Month*

by David Wright and Bradley Blackburn

The most expensive public high school in the nation's history will open its doors to students next month in Los Angeles, but critics say the \$578 million school is already teaching a [lesson on wasteful spending](#).

The Robert F. Kennedy Community Schools will house 4,200 students from kindergarten through 12th grade. The complex is built on the site of the Ambassador Hotel, where Kennedy was assassinated by Sirhan Sirhan on June 5, 1968.

The new campus between Wilshire Boulevard and 8th Street in Los Angeles preserve pieces of the historic hotel, but it's the stunning new architecture that's drawing eyes and plenty of wagging fingers.

The soaring, unusually shaped buildings are clad in glass and metal, and the interiors are just as slick. The facility boasts a state-of-the-art swimming pool, fine art murals, an ornate auditorium suitable for hosting the Oscars, and a faculty dining room that the superintendent says is "better than most restaurants."

### **More Expensive Than China's Olympic Stadium**

All those amenities add up to an enormous price tag, which works out to about \$250,000 per pupil. That \$578 million cost is more expensive than the Bird's Nest stadium built for the 2008 Olympic Games in Beijing, China, which cost \$500 million. It's also significantly more expensive than the \$400 million home of the Denver Broncos, Invesco Field at Mile High.

Critics say the school is a luxury that the Los Angeles Unified School District cannot afford. The district has a \$640 million budget shortfall, and over the past two years, 3,000 teachers have been laid off. The district has even proposed shortening the school year by six days to save money.

The money troubles come on top of the district's serious academic shortfalls. With a dropout rate upwards of 35 percent, LA Unified is one of the lowest-performing school districts in America.

### **School District: Budget Covered by Voter-Approved Bonds**

But Los Angeles school district officials say it's not an "either-or" proposition. The money for school construction comes from voter-approved bonds, an account that is totally separate from what is budgeted for textbooks and teachers.

"The money can only be spent for that building," LAUSD Superintendent Ramon Cortines said. "That's what the voters said."

The new facility is just the latest so-called "Taj Mahal" school in LA. There's also a \$377 million Roybal Learning Center, and there's the new \$232 million Visual and Performing Arts High School.

The superintendent confessed he's embarrassed by the price tag of the project. "Yes," he said, "it bothers me." He insists the project was commissioned by school officials years ago, in a different economic climate.

"I'm not sure it's my place to cut the ribbon," he said, preferring to leave that task to others.

"Welcome to the Alice in Wonderland world of education politics in Los Angeles," said Ben Austin, executive director of Parent Revolution. "Up is down, down is up, and none of these decisions has anything to do with kids."

### **"Taj Mahal" Schools a Nationwide Trend**

But Los Angeles is hardly alone in its taste for expensive schools. In New York City, there's a \$235 million campus. In Brunswick, N.J., \$185 million was spent for a high school, and Newton, Mass., topped that figure with a \$197 million for a new high school.

Not everyone thinks that big construction budgets make for better teaching.

"What goes on inside the classroom is a lot more than the four walls that go around the classroom," Austin said. "Whether you have a Taj Mahal or a broom closet, make sure you have a 'kids first' agenda."

Back on Wilshire Boulevard, future generations may appreciate the school now built there in Kennedy's name. But the taxpayers now are finding it tough to justify.

### **WSJ - Editors**

#### **Virginia Is for Surpluses**

#### ***Erasing red ink without a tax increase.***

Here's something you don't see often these days: a government running a budget surplus. Governor Robert McDonnell announced last week that Virginia closed fiscal 2010 some \$400 million in the black. That's a radically improved financial picture from a year ago when the state faced a \$4.2 billion two-year budget hole.

The usual suspects—the big business lobbies, the Washington Post—thought a major tax increase was needed. So did the previous Governor, Democrat Tim Kaine, who proposed a \$2 billion tax hike before he left town, on top of two major Virginia tax increases in the previous eight years.

Mr. McDonnell has proved otherwise. The newly elected Republican put a freeze on hiring and took the knife even to such politically sensitive programs as school aid, police and Medicaid to cut hundreds of millions of dollars. Total state spending has been reset more or less to 2007 levels. If Congress were to do that, the federal deficit could fall by more than \$900 billion, or two-thirds.

It's true that Richmond used too many budget tricks to make the surplus appear larger than it really is. Sales tax payments were accelerated by one month to count in 2010 rather than 2011. Several hundred million dollars were borrowed from the public-employee pension reserve—money the Governor

promises to repay by 2013. Most fiscal experts think the real surplus is closer to \$87 million. But given the lousy economy, Virginia's budget achievement is laudable.

From his first day in office, Mr. McDonnell took a tax increase off the table because he says "it will injure our economy, slow the recovery, and cost us jobs." His strategy to cut spending across most categories stands in contrast to Washington's, where everything except defense gets branded as "stimulus" to get more money. The feds could do worse than employ the Virginia strategy to close its deficit chasm—and they almost certainly will.

## The Corner

### What's a Federal Employee Worth?

by Veronique de Rugy

In the debate over the [difference in pay](#) between private and federal employees, the Cato Institute's Tad DeHaven makes [some very good points](#) that I hadn't heard before:

I think the most valid criticism [defenders](#) of federal pay offer up is that we're comparing "apples and oranges." However, although they have a point, it's not for the reasons they suggest.

In the private sector, an employee's compensation is a reflection of his or her value in the market. For instance, one may not like that LeBron James makes [millions of dollars](#) playing [basketball](#), but that's what the market for professional basketball players says his production is worth. It's no different for a considerably lower-paid employee in the restaurant industry.

What's a federal employee worth? How does one measure a government employee's production? Government isn't subject to market disciplines. It can't go out of business. It has no competitor. It doesn't need to earn a profit or even break even. It doesn't receive its revenue from voluntary transactions – its revenues are obtained via taxation, which is paid by individuals under compulsion and force.

Therefore, federal employee compensation is a function of the political process. Government employees are plugged into a pay scale, and can move up the scale by simply sticking around. President Obama proposed in his fiscal year 2011 budget that federal civilian employees receive an arbitrary across-the-board 1.4 percent pay increase. What does that figure have to do with a federal employee's worth?

Federal and private employees are apples and oranges because the former is dependent on the latter for its existence.

More [here](#).

## Hot Air

### Obama's Washington: No experience necessary

by Ed Morrissey

Wonder how Recovery Summer turned into Wreckovery Bummer? How an administration ginned up its entire economic strategy into one stimulus bill and has done nothing since, even as the economy disintegrated? Marty Robins advises his readers to [check the CVs](#) of the people in charge in Washington to understand just how incompetence has triumphed — and not just Barack Obama's:

If Washington seems out of ideas on how to get the private-sector jobs machine running again, there's a pretty straightforward reason — the people in government have virtually no experience in business.

In a major departure from prior administrations, you'd be hard-pressed to find anyone in the current administration with any real business experience. Even offices such as treasury and commerce secretary, which have traditionally been occupied by successful business people, are occupied by a career central banker (with his own tax-compliance problems) and a lawyer/politician.

The situation is little different in Congress, where the "barons" — Pelosi, Frank, Dodd, Waxman, Reid, Rangel — are all career "public servants."

This increasing disconnect between the government and the business world is a big, if unrecognized, problem, if for no other reason than that it deprives government officials of the knowledge and experience that successful business leaders can bring to solving difficult problems.

Of course, they're led by the least experienced President in modern times, in the private sector sense (non-existent), executive experience (non-existent), and political senses (only three-plus years in national politics). Incompetence should have been expected under the circumstances, and certainly was by Obama's critics.

The answer to those arguments during the election was that presidential experience mattered less than the people hired to do the actual work. Obama's supporters pointed to Ronald Reagan as an example of this, but they forgot that Reagan spent two terms as California Governor (and a term running the Screen Actors Guild before that), learning how to hire qualified people for posts in his administration. By the time he got to the Oval Office, Reagan understood how to pick and then run a team, and how to get the best performance out of them once in harness.

The results have been as dismal as anyone could have predicted. Obama stuck with ideological allies heavy on academics and with no real-world experience, reflecting his own profile rather than complementing it as an experienced executive would have known to do. Obamanomics is the result. It's a classic command-economy approach that works on every university campus where it's discussed — and in no real-world setting where it's ever been tried.

After February 2009 and the establishment of Porkulus, Obama and his team haven't deflected from its trajectory an iota, mainly because no one on his team has the experience to know *how* to change course. None of them, as Robins points out, has ever had to run a business and reconsider strategies on the fly. None of them have been responsible for managing stockholder assets nor held accountable for the real-world implications of their actions. In short, this administration is a one-trick pony on economics, and now has no clue on how to formulate a Plan B.

The entire administration reflects incompetence. They need a massive change in leadership, or more accurately, we need a massive change in leadership.

## **Washington Post**

### **[How a homeownership fetish hurt the American dream](#)**

by Robert J. Samuelson

The question of what to do about Fannie Mae and Freddie Mac -- the two government-created enterprises that have backed massive loans to the housing market -- involves much more than finance

or real estate. It marks the end of an era. The relentless promotion of homeownership as the embodiment of the American dream has outlived its usefulness.

Historically, the pursuit of homeownership dates to the Great Depression of the 1930s, notes historian A. Scott Henderson of Furman University. In some ways, it's a great success story. In 1940, 44 percent of households owned a home; by 1985, the rate was 64 percent. The size and quality of homes have increased dramatically. Owning a home contributes to neighborhood stability and encourages property improvement.

Unfortunately, we let a sensible goal become a foolish fetish. Not everyone can become a homeowner. Some are too young and footloose; some are too old and dependent; some are too poor or irresponsible. Some don't want a home. Even with these gaps, [homeownership is virtually universal among the middle-aged middle class](#): almost three-quarters of Americans ages 45 to 54 and four-fifths ages 55 to 64.

Government subsidizes homeownership in two ways: through tax and spending policies and through credit markets. Tax breaks for homeowners (mainly the deductions for mortgage interest and property taxes, plus preferential treatment of capital gains on homes) exceeded \$120 billion in 2009, [reports the Congressional Budget Office](#). These benefits go heavily to higher-income borrowers, who are encouraged to buy bigger and more expensive homes that generate larger tax savings. This is both unfair and unnecessary. By contrast, government subsidies for lower-income renters are skimpier, totaling about 25 percent of the support for homeowners.

The cheap credit subsidy operates mainly through Fannie Mae and Freddie Mac. These government-sponsored enterprises (GSEs) were economic mongrels: profit-making companies that were given goals of expanding homeownership among poorer buyers. The GSEs could borrow at interest rates barely above the U.S. Treasury's, because investors regarded Fannie and Freddie bonds as backed by the government.

It seemed a perfect marriage: The GSEs would do well by doing good. They'd earn profits and pass along the benefits of cheaper credit by financing or guaranteeing mortgage loans. Congress could promote homeownership outside budget constraints. By 2009, Fannie and Freddie had [lent or guaranteed almost \\$5.5 trillion in home mortgages](#), roughly half of the U.S. total. But the marriage between private profit and public purpose failed. In September 2008, the Bush administration took over Fannie and Freddie, which faced huge losses from bad mortgages.

There's a ferocious debate as to whether these losses stemmed from unrealistic "housing affordability goals" or lax lending in pursuit of higher profits. The correct answer is: probably both. Regardless, the [GSE bailouts](#) have cost almost \$150 billion, with more to come.

In an ideal world, we would discard failed policies. We would trim or end the mortgage-interest tax deduction. We would curtail the GSEs' loans and guarantees (the promise to repay mortgages that default). The consequences need not be dire. The homeownership rate, already down to 67 percent from its 2004-06 peak of 69 percent, would probably stabilize in the mid-60s. People would save more for down payments. Mortgage rates might rise a bit.

The trouble is that the ideal solution may be temporarily undesirable. The housing market, as everyone knows, has collapsed. New home starts are running at about a [quarter](#) of the [2005 rate of 2.1 million](#). Sales of existing homes, though up slightly this year, [remain weak](#). Home prices have dropped sharply.

The irony is that, in failure, the GSEs have become more important than ever. Private lenders, which once regarded a mortgage secured by a home as a highly safe investment, now see it as highly risky. Few new mortgages are made without government guarantees. The GSEs continue to operate and,

along with other government agencies, guaranteed about 95 percent of new mortgages made in 2009, reports Inside Mortgage Finance, an industry newsletter. Since 1990, the government guarantee share had fluctuated between 30 and 50 percent.

This means that sudden withdrawals of support might deepen housing's depression. Economists Phillip Swagel of Georgetown University and Donald Marron of the Tax Policy Center, among others, have made sensible [proposals to scale back Fannie and Freddie](#). But done too quickly, they could backfire.

"This is not a good time to make permanent solutions for housing," says Guy Cecala, publisher of Inside Mortgage Finance. The single-minded promotion of homeownership failed and, paradoxically, undermined the American dream. It contributed to the housing "bubble" and favors housing investment over new industries and technologies. But to end it, we need to make haste slowly.

## **Euro Pacific Capital** **Carts and Horses**

by Peter Schiff

In a CNBC debate last week, former Labor Secretary Robert Reich presented a set of contradictory beliefs that unfortunately reflect the conventional wisdom of modern economists. In a discussion with Wall Street Journal columnist Stephen Moore, Reich correctly and comprehensively listed the reasons why American consumers could spend so lavishly before the crash of 2008 and why they can no longer keep up the pace. But instead of making the logical conclusion that former levels of spending were unsustainable and that spending should now reflect current conditions, he advocated that government take on *additional debt* so that tapped out consumers can spend like they used to.

To achieve this, Reich called for lowering taxes on working Americans and raising taxes on the rich. He argued that middle-income Americans are more likely to spend additional dollars while the rich are more likely to save and invest. As a "demand-side" economist, Reich made clear that spending is superior to savings and investing as a catalyst for growth.

To put it simply: Reich believes that the cart pushes the horse. In his worldview, businesses produce goods and services simply because consumers spend. Therefore, anything that increases spending fuels growth. Unfortunately, he fails to see what should be strikingly obvious: capital formation must precede production, which then allows for consumption.

In a complex society like ours, those relationships are hard to see. However, if we break it down to a simpler level, it becomes more obvious (as I try to accomplish in my new book: [How an Economy Grows and Why it Crashes](#)). For example, let's take a look at a simple barter-based economy consisting of only three people: a butcher, a baker, and a candlestick maker.

If the candlestick maker wants cake, he can't simply demand that the baker hand it over. The cake needs to be produced, and the baker has to expend labor and material to produce it. Unless the candlestick maker offers the baker something of value in exchange, the cakes won't get baked. The ability of the candlestick maker to demand cake from the baker is a function of his ability to supply candles to trade. Without production, consumption can't occur.

What if the candlestick maker gets sick and produces no candles? As the baker would be unwilling to give his cakes away, he would likely stop baking cakes for the candlestick maker. Economic activity would naturally contract until the candlestick maker recovers.

But according to Reich, if the candlestick maker doesn't have anything to trade, the government should step in and give him candles. But where will the government get them? It could take them from the candlestick maker; but if he is not making candles, how will he pay the tax? Even if there were a few candles left to tax, any that the government took would simply transfer demand from the candlestick maker to the government. No new demand is created.

Alternatively, if the butcher is still healthy, the government could tax him, and give his steaks to the candlestick maker to buy cakes. However, this doesn't create new demand either. It simply transfers demand from the butcher to the candlestick maker.

Some may feel that a barter-based metaphor doesn't hold water because the ability to expand the money supply and create credit gives an economy far more flexibility. This is a deceptive argument. Although money is more efficient than barter, it doesn't change the dynamic between production and consumption.

But Reich suggests that printed money can stimulate demand just as effectively as real candlesticks. But what good will the paper offer the baker if there are no candlesticks to buy? All the baker can do is bid up the prices of those goods, like steaks, that continue to be produced. Similarly, if the government simply prints money and gives it to people to spend, no new production occurs. Prices merely rise to reflect the increase in the supply of money relative to the supply of consumer goods.

In a more complex economy, the relationship between production (supply) and spending (demand) still holds. Every consumer either lives off his own productivity or the productivity of someone else. When individuals work, the wages earned result from the productivity of labor. The ability to consume is directly related to the production of goods or services that result from one's efforts. However, if people waste their labor in unproductive jobs, little real demand is created.

In the Soviet Union, everyone had a job, yet workers had to stand in line for hours for basic necessities. Although everyone worked (for the government), production was too low. This lack of production meant wages delivered relatively little in the way of purchasing power.

Since production cannot be created by government stimulus, neither can demand. To the extent that there are savings, demand can be brought forward by stimulus – but only at the cost of future demand, plus interest. If stimulus *could* produce demand, then no nation would be poor. Taken to its logical end, Reich's argument suggests that African poverty would be wiped out if African governments simply printed money more freely. In reality, Africans are not poor because they lack currency to spend; they are poor because their corrupt and inept governments inhibit production by soliciting bribes, denying property rights, abrogating contracts, preventing the accumulation of capital, and nationalizing profits.

Reich is correct about one thing: Americans are indeed broke. But rather than encouraging the country to spend itself deeper into debt, he should call for greater savings so that we have the means to invest in new businesses and new industries. That is the true road back to solvency, but it will only work if we have less government spending, fewer regulations, lower taxes (particularly on those with the highest propensity to save and invest), and higher interest rates.

Unfortunately, Reich and his allies are calling the shots in Washington. The country cannot recover until the only thing politicians stimulate is demand for new economic leadership.



*Senate Minority Leader Mitch McConnell, left, confers with Republican senators John McCain and Jon Kyl of Arizona*

Republicans enjoy a 50 percent to 43 percent advantage over Democrats among registered voters, the highest yet in Gallup's weekly tracking of the 2010 midterm elections. But a Republican victory in November will mean nothing if it means more GOP business as usual. That is why it is critically important for congressional Republicans to put forward a concrete agenda before the election as an alternative to that of big-spending congressional Democrats. Instead, Republicans appear satisfied to fall back on a one-plank platform: "We're not the Democrats." That won't cut it because, as pollster Scott Rasmussen recently told the Wall Street Journal, the GOP will benefit from voters' desire to oust the party in power, but "75 percent of Republicans say their representatives in Congress are out of touch with the party base. Should they win big this November, they will have to move quickly to prove they've learned lessons from the Bush years."

Those Bush years too often displayed little difference between Republicans and Democrats in Washington. Much of the vast expansion of the federal government by Democrats was previewed by the Bush-led Republicans. Obamacare's overreach? Don't forget the Republicans' entitlement-expanding and budget-busting Medicare Part D. In fact, Republicans were off the reservation long before Bush ever entered office. The 1994 Republican revolution marked the first time in more than 40 years that Republicans held a congressional majority. They won while pledging specific policy goals in their Contract with America, including term limits, a balanced budget amendment, and welfare reform. Some significant progress was made but in a few years the revolution was all but abandoned. The Cato Institute's Ed Crane recently noted that the "combined budgets of the 95 major programs that the Contract with America promised to eliminate ... increased by 13 percent."

Today, most Americans are ready as never before to shrink government and stop the spending madness. This presents the GOP with an opportunity it didn't have in 1994: an electorate exhausted by Washington politicians and their doubletalk. But the GOP so far seems unwilling to lay out specifics about how it plans to respond to what Americans are saying if they restore the party to majority status in the House and perhaps the Senate. House Minority Whip Eric Cantor, R-Va., boasts of the Republican "YouCut" Web site that solicits ideas from voters, but that effort barely rises above window dressing. Rep. Paul Ryan, R-Wis., has proposed a "Roadmap to Economic Recovery" as a serious program for entitlement reform, yet the party leadership has not embraced it. Similarly, the Heritage Foundation has compiled 128 policy recommendations across 23 major policy areas for shrinking government and making it work better. *The Examiner* will be offering a number of ideas on this page in coming days as well. Republican leaders risk squandering a historic opportunity by ignoring such recommendations. The voters are waiting.

## Volokh Conspiracy

### [Stop Criticizing President Obama for Playing Golf](#)

by David Kopel

In this polarized period of American politics, many people on the Right have been taking cheap shots at President Obama because he plays golf so much.

These golf-related criticisms are at least factually accurate, in contrast to the [lies](#) that Michael Moore told about George Bush supposedly vacationing much of the time. However, the criticisms of President Obama are misguided.

Of American Presidents since World War II, the one President who is now almost universally regarded as highly successful and constructive, by persons of all political persuasions, is President Dwight D. Eisenhower. While serving eight years as President of the United States, Eisenhower may have [played](#) over *eight hundred* rounds of golf. In other words, about twice a week.

Like President Obama, President Eisenhower was [criticized](#) by partisan opponents for his avid interest in golf.

Obviously there are many differences between President Eisenhower and President Obama. To begin with, the former came into office with demonstrated success in a very difficult executive job, Supreme Allied Commander Europe, defeating Hitler and Mussolini. By contrast, Obama was apparently successful as President of the *Harvard Law Review*, but was a [failure](#) at his only latter significant executive position, [Chairman of the Board](#) of the Chicago Annenberg Challenge, which attempted unsuccessfully to improve education in selected Chicago schools.

However, President Eisenhower demonstrated beyond any doubt that there is no inherent contradiction between being a good President and being an avid golfer. Indeed, golf helps clear the mind, and hardly any sport is better at fostering humility in participants. So unless President Obama's critics are willing to state that President Eisenhower golfed too much, they should stop carping about President Obama's golfing.



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