

Box 6 Creating 2.4 million jobs and 7 million job-years in the United States through private investment

With the ongoing reduction in fiscal stimulus measures and increased austerity being enacted by governments in many developed economies, increasing private investment is an essential catalyst for forging a sustained jobs recovery. Investment in new plants and equipment could help pick up the slack of reduced public-support measures, boosting payrolls and providing a much-needed jolt to economic activity.

Yet, there is evidence that many companies are holding large amounts of excess cash reserves relative to historical patterns, rather than investing towards productive ends. This is perhaps not surprising, given the highly uncertain economic environment in which firms are currently operating, but the consequence of this behaviour when aggregated across companies and economies is a “paradox of thrift” – oversaving by large numbers of companies leads to low levels of investment, which, in turn, reduces prospects for economic growth and job creation and makes a further downturn more likely.

In the United States, there has been a great deal of media attention on the large cash reserves that have been built up by non-financial corporations. In aggregate, around US\$2 trillion was held by non-financial companies in the United States at the end of June 2011. As this amounts to more than 13 per cent of total US GDP, it is expected that investment of even a fraction of the total cash reserves could provide a substantial boost to growth of output and employment.

To assess the potential impact of such an increase in investment, the ILO and the Interindustry Forecasting Project at the University of Maryland (Inforum) produced a series of scenarios using the Long-term Interindustry Forecasting Tool (LIFT), a 97-sector dynamic general equilibrium representation of the US national economy. Estimates and projections of impacts on output, employment and a number of other labour market and macroeconomic variables were generated for two scenarios:

- Scenario 1: Investment of a portion of each company's excess cash on hand in the industry in which the company operates, with funds being invested starting in 2012.
- Scenario 2: Introduction of an "Infrastructure Bank" into which companies would invest a portion of their available cash. Funds through the bank would support infrastructure investment projects throughout the economy starting in 2013.

It was estimated that there was a total of US\$508 billion in *excess* cash holdings among US non-financial corporations averaged over the period from Q3 2010 and Q2 2011. This figure was derived utilizing Flow of Funds data published by the US Federal Reserve by calculating the ratio of liquid assets to current liabilities over this period and comparing this with the historical average ratio over the period from 2002 to 2007. The current ratio was found to be more than 14 percentage points greater than the historical average. Reversion back to the historical average gives the US\$508 billion estimate of excess cash holdings.

Scenario 1

Utilizing annual non-financial corporate balance sheet data for 230 non-financial firms listed in the S&P 500 stock index and distributed across 37 industries, the proportion of total excess cash held by each industry was calculated as industry excess cash divided by total excess cash for all industries, where the total was calculated from balance sheet data. The aggregate excess cash calculated from the Flow of Funds data was then distributed accordingly across industries.

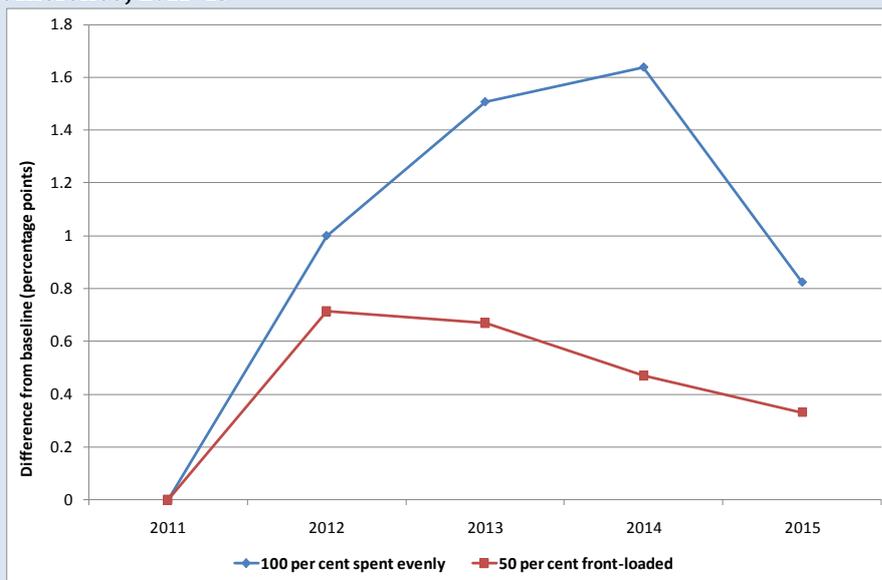
The impact of increased investment across the industries on overall GDP growth and employment was then estimated through simulations using the LIFT model. The results from two scenarios are presented in the figures below: (1a) expenditure of 100 per cent of the excess cash (US\$508 billion), spread evenly over three years (2012–14); and (1b) expenditure of 50 per cent of the excess cash (US\$254 billion), front-

loaded with 50 per cent spent in 2012, and 25 per cent spent in both 2013 and 2014.

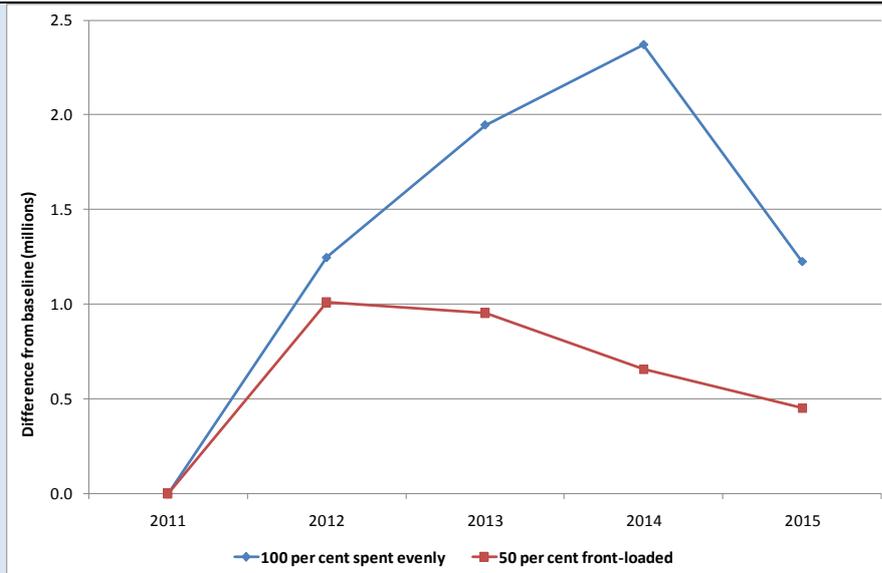
According to the results of the LIFT model scenarios, expenditure of 100 per cent of the estimated excess cash reserves spread evenly across the three years 2012 to 2014 would result in an increase in the U.S. Real GDP level of 1 per cent in 2012, 1.5 per cent in 2013 and 1.6 per cent in 2014 compared with the baseline scenario, in which excess cash reserves would not be spent. In terms of employment impacts, under scenario 1a the employment impact would peak in 2014, whereby an additional 2.4 million jobs would be created relative to the baseline scenario. Aggregating the additional employment generated due to the increased investment over the period 2012 to 2015 results in an estimated 6.8 million job years created (total additional employment in excess of the baseline scenario over the period). This would result in a 0.8 percentage point reduction in the unemployment rate in the country in 2012 compared with the baseline scenario, with a peak effect of a 1.5 percentage point reduction in the unemployment rate in 2014. According to the results, effective incentives to companies to deploy their excess capital into productive investment could yield large-scale benefits for growth and employment in the United States.

Even a more conservative assumption of expenditure of half of the excess cash reserves, with spending front-loaded in 2012 (scenario 1b), is projected to result in a large stimulus to growth and employment, with an estimated 1 million jobs created in 2012 and more than 3 million job years created between 2012 and 2015. The boost to output under this scenario would be around 0.7 per cent in both 2012 and 2013, with a smaller boost in 2014 and 2015.

Impact of increased investment on the level of Real GDP in the United States, percentage difference, 2011–15



Impact of increased investment on Employment in the United States, millions of jobs, 2011–15



Scenario 2

The second scenario introduces an “infrastructure bank” into which companies will invest a portion of their cash holdings. The basis for this scenario is a hypothetical introduction of a tax amnesty programme for companies’ overseas cash, enacted with a requirement that companies invest repatriated funds in an infrastructure bank for three years. The bank will allocate its resources to a variety of public infrastructure improvement projects throughout the economy, starting in 2013. The assumption is that investment in state, local and federal structures would increase by a total of US\$250 billion between 2013 and 2016, with US\$50 billion spent in 2013, US\$75 billion in 2014 and 2015 and US\$50 billion in 2016.

This investment is projected to boost GDP by around 0.8 per cent in 2014 and 2015, with additional employment of around 1.1 million relative to the baseline scenario in each year. In aggregate, the infrastructure bank scenario would result in 3.9 million job-years created between 2013 and 2017.

Source: Casselman and Lahart, 2011; Inforum, 2011.