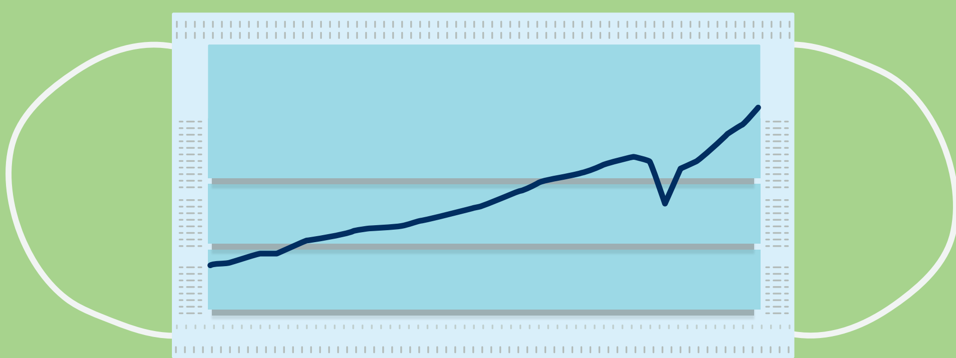
RECESSION REMEDIES

Lessons Learned from the U.S. Economic Policy Response to COVID-19



Edited by

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THE HAMILTON PROJECT

Hutchins Center
on Fiscal & Monetary Policy
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Overview

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Introduction

The worst global pandemic in a century took a devastating human toll, threatening lives and livelihoods nearly everywhere. More than six million people around the world had died from COVID-19 as of April 2022, nearly 1 million of them in the U.S. (Johns Hopkins 2022a). Figure 1 shows the course of the pandemic through the number of deaths associated with COVID-19 in the U.S.

COVID-19 hit certain racial and ethnic groups particularly hard. As Figure 2 illustrates, adjusted for age and compared to the rate for white, non-Hispanic people, the death rate associated with COVID-19 among American Indian/Alaska Native people was about 2.5 times higher, and the rate among Black people was almost twice as high, while the rate among Hispanic people was slightly higher.

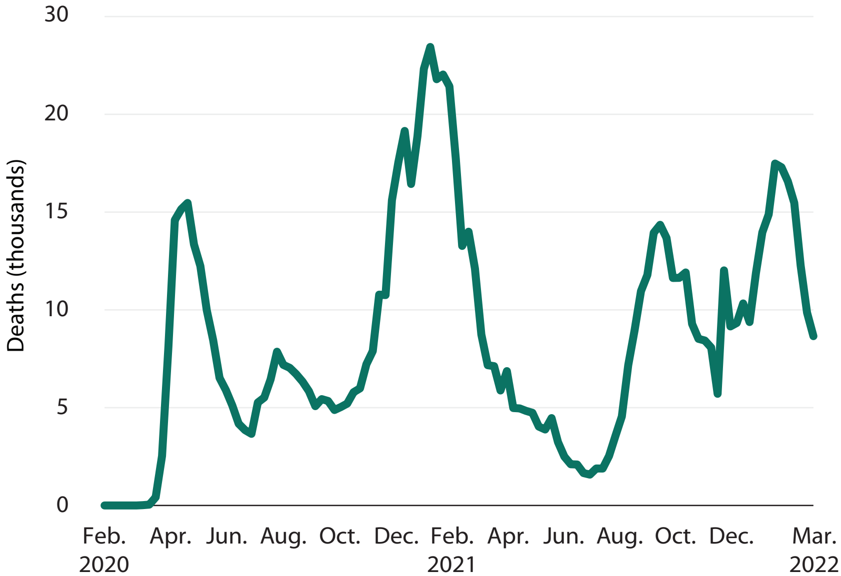
Vaccine development exceeded expectations in both timing and efficacy (Boyle 2021; Klein and Tufekci 2022). Vaccines were made available for high-risk groups in December 2020, just 11 months after the first COVID-19 case was detected in the United States. As constraints on vaccine eligibility loosened, average daily vaccinations peaked in April 2021 (New York Times 2022). In January 2022 fully vaccinated people were 2.4 times less likely to test positive for COVID-19 and 9 times less likely to die from it (Centers for Disease Control and Prevention [CDC] 2022b). As of early April 2022, about three-quarters of Americans had received at least one dose of the COVID-19 vaccine, two-thirds had received two doses, and nearly half had received a booster (New York Times 2022).

COVID-19 and the Economy

The pandemic posed an extraordinary threat to the economy. President Trump declared a nationwide public health emergency in March 2020. Around that time, many states and localities began to order lockdowns—closing schools, shutting bars and restaurants, and suspending public gatherings. Many people dramatically reduced their face-to-face interactions, and businesses closed or told employees to work from home.

FIGURE 1

Weekly Deaths from COVID-19 in the U.S.



Source: Johns Hopkins 2022b.

Note: Weekly deaths are plotted through the week ending March 20, 2022.

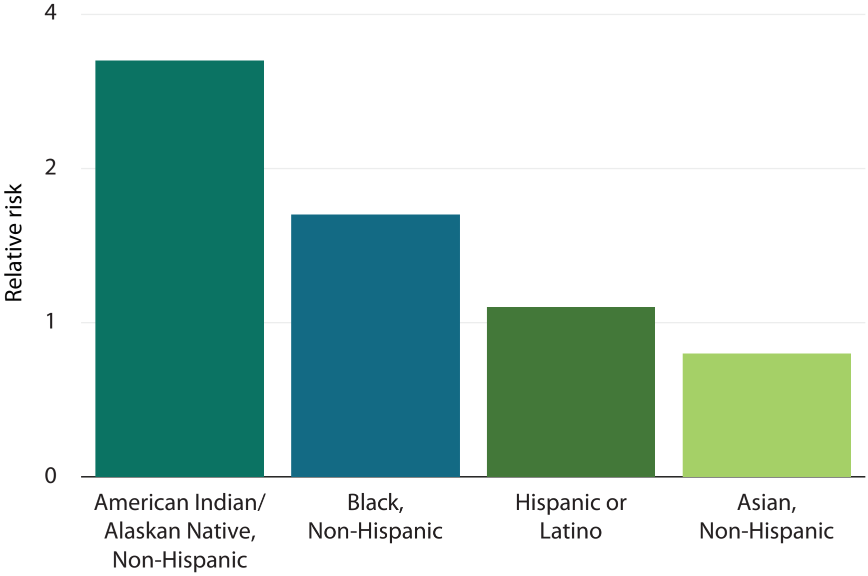
In the U.S., the COVID-19 downturn was sharp. In April 2020 the unemployment rate shot up to 14.7 percent, and there were steep declines in labor force participation and the employment-to-population ratio (Bureau of Labor Statistics [BLS] 2022). In May 2020, about one-third of all those employed were teleworking, and a quarter of those in the labor force were unable to work because an employer had closed or lost business due to the pandemic.

The ensuing economic recovery was faster and stronger than nearly any forecaster anticipated. For example, although expectations were generally for the unemployment rate to continue rising and output to continue falling, the economy began to recover by May 2020. In part that is because of the swift, aggressive, sustained, and creative response of U.S. fiscal and monetary policy.

As described in more detail in subsequent chapters, Congress responded forcefully to the pandemic and economic downturn—notably by passing the $1.7 trillion Coronavirus Aid, Relief, and Economic Security (CARES) Act in March 2020, the $1.9 trillion American Rescue Plan in March 2021, and several other smaller pieces of legislation. In all, Congress allocated more than $5 trillion to the fiscal response—substantially more than it allocated during the Great Recession of 2008–9 (for details, see Table 1 in Chapter 1).

FIGURE 2

Relative Risk for COVID-19 Death by Race/ Ethnicity, Compared to White, Non-Hispanic Persons



Source: Center for Disease Control and Prevention (CDC) 2022a.

Note: Estimates are age-adjusted.

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Households received substantial support through three rounds of Economic Impact Payments (EIPs) totaling $3,200 per eligible adult and $2,500 per eligible child, expanded Unemployment Insurance (UI), eviction moratoriums, and forbearance on mortgages and student loans. Businesses received more than $1 trillion in subsidies and forgivable loans, and state and local governments received almost $1 trillion dollars in grants. The Federal Reserve cut its key short-term interest rate to zero in March 2020 and held it there for two years, bought about $5 trillion of Treasury and mortgage-based securities, and, with the encouragement of Congress, expanded its emergency lending beyond financial institutions to businesses and state and local governments.

Questions That Will Be Asked When the Next Recession Arrives

When the next recession arrives, it most likely won't be triggered by a pandemic. So when policymakers ask how best to respond to that recession, they will want to know: What did we learn from the economic policy responses to COVID-19? What should we consider repeating, perhaps with modifications? What should not be repeated?

The Hamilton Project and the Hutchins Center on Fiscal & Monetary Policy at the Brookings Institution gathered scholars with deep expertise to help answer these questions to the fullest extent possible with the available evidence. We know that the evidence is still incomplete, and scholars will be debating these questions for years to come. But we also know that the next recession may arrive before the answers are fully resolved. Indeed, assessing what we still don't know is as important as assessing what we do know. We asked the scholars to describe specific economic policy responses to the pandemic, summarize the available evidence about the outcomes of those policies, and analyze the lessons learned for future recessions. We asked them to try, as much as possible, to analyze the extent to which outcomes were pandemic specific and hence likely not applicable to the next recession. This project does not evaluate the public health response to the pandemic, as important as that was: we focus exclusively on the economic policy response.

In Chapter 1, Wendy Edelberg, Jason Furman, and Timothy F. Geithner trace the macroeconomic impact of the breadth of the economic policy responses that produced a recovery that was both stronger than generally anticipated and stronger than those of other advanced economies but has also been accompanied by an unwelcome increase in inflation.

This volume covers the expansion of UI (Chapter 2), the provision of EIPs (Chapter 3), loans and grants to businesses (Chapter 4), assistance to renters and mortgage holders (Chapter 5), and aid to state and local governments (Chapter 6). Subsequent chapters examine the efforts aimed specifically at children (Chapter 7); the reasons, including but not limited to Federal Reserve policy, that the U.S. Treasury was able to borrow trillions of dollars without pushing up interest rates (Chapter 8), and the use of nontraditional data to monitor the economy and guide policy (Chapter 9).

Overarching Lessons for the Next Recession

The authors of each chapter draw specific lessons learned from the economic policy responses to the pandemic. Looking across the variety of ways the government addressed the economic challenges posed by the pandemic, we (the three editors) draw a few overarching conclusions.

1. ***A strong, broad, and inclusive social insurance system provides effective relief to households as well as macroeconomic stimulus.***

Beneficiaries, like those who lose wages and receive UI benefits, tend to spend promptly much of what they receive. Sufficiently generous social insurance benefits can reduce the need for other sorts of assistance including aid to businesses, homeowners, renters, and even state and local governments.

2. ***The sizable fiscal and monetary policy response helped stabilize the economy.***

The U.S. has enjoyed a stronger economic recovery than other advanced economies: remarkably few businesses failed, few people lost their homes or were evicted, and state and local government budgets are still in good shape. Despite a surge in federal borrowing, long-term interest rates remain low, in part because of accommodative monetary policy. However, the combined fiscal and monetary policy response, particularly in the spring of 2021, was a factor behind the surge in inflation. Of course, inflation also was boosted by other factors such as disruptions to global and domestic supply chains and, more recently, by the spike in energy prices following Russia's invasion of Ukraine. It is too soon to know how history will judge the size of the fiscal and monetary policy response. If the uncomfortably high inflation rate is brought down over the next couple of years without too much pain, then the responses to the pandemic will likely be viewed as a significant economic policy success.

3. ***Generous Unemployment Insurance may have smaller disincentive effects than previously thought.***

During periods when demand for labor is low, even significantly enhanced UI appears to only modestly discourage recipients from returning to work. This suggests that boosting UI benefits would likely be worthwhile, particularly during recessions and probably in regular periods. In addition, the pandemic showed it is feasible to extend UI to many who previously have been ineligible and that the benefits of doing so seem greater than the costs.

4. ***Because standing up new programs quickly and targeting them is difficult, preparation is key.***

Federal and state governments should improve their administrative capacity *now*—including modernizing computer systems, improving communications across agencies and levels of government, and investing in data systems—to be better prepared to respond quickly to changing economic conditions. In addition, if it is deemed desirable to make some aspects of the novel pandemic-era policies permanent features of the response to recessions—such as the extension of UI to the self-employed—such policies should be designed and legislated now rather than waiting until the next recession.

5. ***Sufficiently reliable, representative, and timely data on too many aspects of the economy are lacking.***

Slow-to-materialize and incomplete economic indicators made it difficult to assess needs during the pandemic and the lack of such data continues to make it difficult to fully evaluate the economic consequences of COVID-19. There are no comprehensive and timely data on renters, nor are there reliable, timely data on state and local expenditures. One argument for distributing EIPs so widely was to be sure to reach people who were hurt by the pandemic and weren't reached by targeted programs. However, it is almost impossible to know what fraction of EIP recipients had significant financial needs that were unmet by targeted programs or how many people, despite EIPs, nonetheless fell through the cracks. Merging administrative data with survey data and increasing the size of household and business surveys would help in real time as well as after-the-fact evaluations. Privately gathered data did help guide policy during the pandemic, but those data can be hard to interpret without consistent historical comparisons.

6. ***Although Congress reacted quickly to provide generous relief in the spring of 2020, such prompt action may not occur in the future.***

Without such prompt, wide-reaching action to support the household sector, support for other sectors would be more critical than it was during the last two years (such as support for the business sector, state and local governments, and the housing market). More broadly, Congress should not assume that the swift recovery after March 2020 is a template for future recoveries. The pandemic was—we hope—a very unusual episode. Although we didn't know it initially, the pandemic was, economically, much more like a natural disaster—a devastating but brief disruption to economic activity followed by a rebound—than like the Great Recession and its protracted recovery. The strength of the economy in 2021 and the resilience of the labor market and the business sector reflect not only substantial fiscal and monetary stimulus but also the remarkably rapid development of and administration of vaccines that allowed businesses, workers, and consumers to begin to resume normal activities. In addition, the strength of the stock market and of house prices contributed to the vigor of the recovery; rising house prices and home equity were one reason that programs to help mortgage holders worked as well as they did and mostly seemed to support households who needed the help. However, rising wealth isn't a feature of every recession and recovery.

7. ***Next time, support for the business sector should be better targeted.***

In the next recession we would not repeat the broad Paycheck Protection Program, the (largely forgivable) loans to businesses that were intended to prevent layoffs. Much of that money went to businesses that didn't need it and wouldn't have laid off employees in its absence. As a result, it largely resulted in a transfer to the business sector that did little to boost the economy. Nonetheless, in the future a more targeted program in a recession could reduce the number of bankruptcies of otherwise viable businesses, as described in Chapter 4.

8. ***Next time, support for households should better reflect the state of the economy and the needs of households.***

Congress allowed programs to lapse prematurely in the summer and fall of 2020 and probably provided too much stimulus in the winter and spring of 2021. For example, the value of UI benefits swung wildly, with little connection to the state of the labor market. Most households received a sizable Economic Impact Payment in the spring of 2021 when perhaps more targeted and persistent support was warranted. Congress, therefore, should develop policies that respond automatically as economic conditions warrant, particularly when economic outcomes are so uncertain; for detailed proposals on such policies, please see The Hamilton Project and Washington Center for Equitable Growth volume *Recession Ready* (2019). Also, relative to what was done in the CARES Act in March 2020, we would make sure that increases in Supplemental Nutrition Assistance Program benefits be targeted at the poorest households and we would allow state and local governments more flexibility in using federal aid. Subsequent legislation was improved to these ends.

Assessing the Specific Economic Policy Responses

Unemployment Insurance

In Chapter 2, Peter Ganong, Fiona Greig, Pascal Noel, Daniel Sullivan, and Joseph Vavra review the substantial expansion of UI—supplementing state-provided benefits, expanding eligibility to those not traditionally eligible, and extending the duration of benefits at a cost to the federal government of roughly $700 billion. They draw five conclusions. First, UI expansions were highly progressive in that they offset income losses and delivered the most benefit to lower-income workers. Second, UI benefits provided a powerful stimulus to the macroeconomy by boosting consumption. Third, work disincentive effects from UI benefits were small during the pandemic, especially when compared to history. Fourth, Congress increased access to benefits for workers on the margins of the labor market, and there is no clear evidence of greater work disincentive effects for them than for other workers. Fifth, the rapidly expanded UI programs faced a range of administrative challenges in meeting the surge in UI demand, including delays, unnecessary red tape, and overpayments, all of which were costly in terms of consumer welfare and government expense.

Economic Impact Payments

In Chapter 3, Michael Gelman and Mel Stephens examine the more than $800 billion in cash that was distributed to all but the highest-income households in the three rounds of EIPs. Although there were delays in getting the money to some vulnerable, low-income households, electronic disbursement allowed the Treasury to make payments quickly—about two weeks after the initial legislation was signed and even more quickly in the subsequent rounds. The available evidence suggests that the payments led to a rapid increase in spending; consumers spent about the same or a smaller fraction of these payments than they did in similar payments in past downturns. The payments were not, of course, well targeted. Some households that weren't adversely affected by the pandemic received the money, but other recipients were adversely affected but weren't eligible for or didn't promptly receive more targeted benefits (such as UI or rental assistance) and were greatly aided by the EIPs.

Support for Business

In Chapter 4, Gabriel Chodorow-Reich, Ben Iverson, and Adi Sunderam survey the new federal subsidies and loans provided to businesses in the first year of the pandemic —including the Paycheck Protection Program (PPP), the Economic Injury Disaster Loan (EIDL) program, and aid targeted at specific industries such as airlines and restaurants—and also examine the additional lending and corporate bond purchases by the Federal Reserve. They observe that businesses overall fared much better during the pandemic recession and recovery than had been expected at the outset. In sharp contrast to past recessions, for instance, business bankruptcies fell during the pandemic. Many large firms continued to have access to private credit markets. They conclude that policies to support small businesses could have achieved their objective at a much lower cost to the federal government had the programs been more targeted. They find no credible evidence that the largest PPP loans had any substantial positive effect on employment. Loans through the EIDL program, which unlike the PPP loans were not forgivable, were better targeted. The Federal Reserve's support for bank lending to business had little direct impact, in large part because banks were in much better shape than they were during the Great Recession. However, the Fed's interventions in the corporate bond market had an important stabilizing effect in the early months of the pandemic in 2020. The authors caution policymakers against blindly deploying the 2020 tool kit, judging that the resiliency of the business sector reflects the unusual nature of the lockdown and reopening, and the substantial fiscal aid to households, more than it does the aid targeted directly at businesses. They also question the wisdom of providing federal aid to some large firms, such as airlines, that have a history of successful bankruptcy resolution.

Housing

Chapter 5 is divided in two. In the first part, Kristopher Gerardi, Lauren Lambie-Hanson, and Paul Willen review the aid offered to the roughly 50 million homeowners with mortgages included in a forbearance program (on top of EIPs and UI) and the Federal Reserve's actions that pushed down mortgage rates, allowing many mortgage holders to reduce their monthly payments by refinancing (Census Bureau n.d.). They deem these policies to be quite effective in relieving financial distress and allowing homeowners to stay in their homes, especially in contrast with the policies pursued during the Great Recession. They emphasize that these policies in part worked because of rising housing prices and home equity, before and during the pandemic, and note that such conditions might not hold in future downturns. They observe that minority mortgage borrowers were much more likely to miss mortgage payments, so forbearance was particularly important to them. Black and Hispanic borrowers, however, were less likely to refinance than white or Asian borrowers.

In the second part, Laurie Goodman and Susan Wachter evaluate aid offered (again on top of EIPs and UI) to the 44 million renting households. These include federal, state, and local eviction moratoriums and the two rounds of Emergency Rental Assistance (up to $25 billion allocated by Congress in December 2020 and up to $21.55 billion more allocated in March 2021). However, the distribution of financial assistance was distressingly slow. Data on renters are unfortunately skimpy, a major impediment to precisely measuring the effects of these policies. General income replacement might have sufficed if policymakers were concerned only with the negative effect of the recession on renters' finances, but the eviction moratoriums and Emergency Rental Assistance were particularly important to those struggling to make their rental payments before the recession. Eviction moratoriums, while particularly justified in a pandemic, impose hardships on landlords.

Aid to State and Local Governments

In Chapter 6, Louise Sheiner looks at the nearly $1 trillion that the federal government provided to state and local governments. The federal aid was more than sufficient to offset the declines in state and local revenues, which were not nearly as severe as initially feared, in part because the relationship between economic conditions and state and local revenues during the pandemic differed significantly from historical experience. Nevertheless, state and local government employment declined sharply, and the decline has been quite persistent: employment at state and local governments in February 2022 was 3 percent below the pre-pandemic level, accounting for roughly one-quarter the shortfall in total employment in the U.S. from its pre-pandemic trend. She concludes that much of the decline in employment reflected the unique nature of the pandemic rather than tight budgetary conditions. However, she also argues that had state and local policymakers known about the full extent of forthcoming aid, had the aid been more flexible, and had it been provided directly to more local governments, the layoffs likely would have been somewhat smaller. Finally, she cautions against using the unique pandemic experience as a reason to discard the lesson of the Great Recession that aid to state and local governments is critical to ensure a strong economic recovery.

Children

In Chapter 7, Anna Aizer and Claudia Persico examine the impact of the pandemic and related policy responses on children. In 2020 the combined effect of several government programs—EIPs, UI, and the expansion of the Supplemental Nutrition Assistance Program—reduced the percentage of children living in poverty (measured by the Supplemental Poverty Measure) from 12.6 percent in 2019 to 9.7 percent. Child poverty likely fell again in 2021 because of continued support for households and the expansion of the Child Tax Credit. The authors note that the pandemic hit child-care providers particularly hard; child-care employment fell much more sharply than in typical recessions, and many child-care centers closed despite billions in federal aid and forgivable loans. Much of that aid came too late to avoid closures, a mistake that should not be repeated. Federal efforts to prevent a decline in health insurance coverage, including through Medicaid and Affordable Care Act exchanges, were largely successful. The expansion of SNAP benefits reduced food insecurity. The provision of debit cards to purchase groceries for students eligible for free or reduced-price lunch (including the undocumented) while schools were closed was slow to roll out but ultimately very successful. While some elements of the pandemic were unique, such as the suspension of in-person schooling, available evidence underscores the importance of cash and near-cash transfers in reducing poverty as well as housing and food insecurity among families with children.

Interest Rates and Monetary Policy

In Chapter 8, Robin Brooks and Jonathan Pingle examine the role of monetary policy in keeping interest rates low in the wake of a surge in federal borrowing to assess whether a similar increase in borrowing could be repeated in future recessions. They note that despite the huge increase in federal borrowing, some traditional buyers of U.S. Treasury debt—including foreigners and domestic investors—did not increase their holdings on net outside of accounts that had a regulatory incentive to hold Treasurys. It's too soon to know if the pre-pandemic trend toward lower global interest rates will persist or be reversed. During the pandemic, the upward pressure on interest rates from substantial U.S. borrowing was offset by factors other than monetary policy that keep rates from rising. Policymakers should not assume that will always be the case. They conclude that the Federal Reserve's purchases of more than $3.3 trillion in U.S. Treasury debt helped dampen rates and estimate that the yield on 10-year Treasury notes would have been 0.70 percentage points higher if not for the Fed's purchases. Whether the Fed can and will repeat this in future downturns depends, in large part, on whether it can tame the current surge of inflation and on the inflationary environment when the next recession arrives.

Nontraditional Data

In Chapter 9, Tomaz Cajner, Laura Feiveson, Christopher Kurz, and Stacey Tevlin examine the use and value of nontraditional data sources, such as private payroll service providers and restaurant reservation services. They identify three main benefits of such data. First, these data are often available much earlier than the data provided from government surveys, an important feature at times like March 2020, when the economy was changing direction abruptly. Second, these data are often more granular—covering particular geographies or demographic groups, for instance—and that can allow for faster evaluations of the cost of shocks or the benefits of policies, which, in turn, can help fine-tune policies. And, third, nontraditional sources can provide information unique to a particular crisis. But the cost to the government of nontraditional, privately gathered data can be substantial. Historical time series are not always available, which can make interpreting the data challenging. Privately gathered data are not always representative or gathered with the same methodological rigor as government economic indicators. Still, the benefits of nontraditional data are greater than the costs.

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The COVID-19 pandemic posed an extraordinary threat to lives and livelihoods. In the United States, the pandemic triggered a sharp downturn. Yet, the ensuing economic recovery was faster and stronger than nearly any forecaster anticipated due in part to the swift, aggressive, sustained, and creative response of U.S. fiscal and monetary policy. But when the next recession arrives, it most likely won't be triggered by a pandemic.

Recession Remedies examines and evaluates the breadth of the economic-policy response to COVID-19. Chapters address Unemployment Insurance, Economic Impact Payments, loans and grants to businesses, assistance to renters and mortgage holders, aid to state and local governments, policies that targeted children, Federal Reserve policy, and the use of non-traditional data to monitor the economy and guide policy. These chapters provide evidence and lessons to apply to the next recession.

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