To Reduce Inequality, Run a Hot Economy

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Wiener Center Five Big Ideas Series
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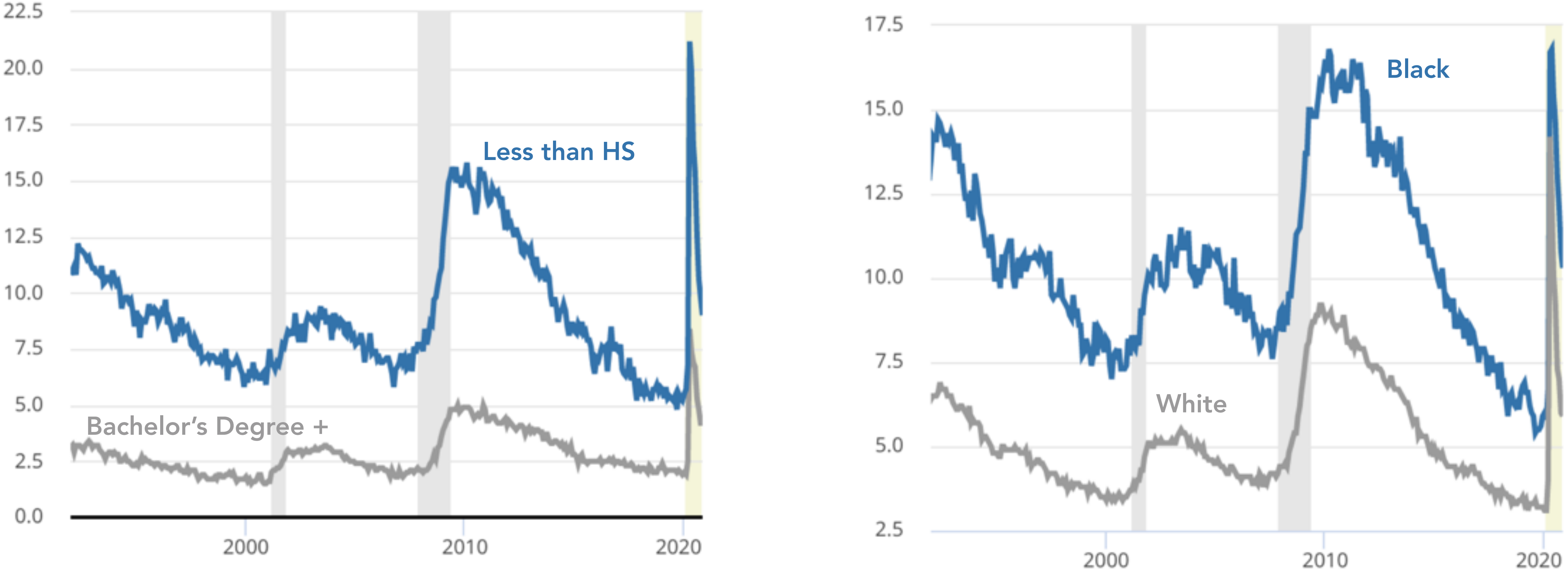
1. Recessions are costly, with the burden falling disproportionately on already struggling populations
2. Effective countercyclical macroeconomic policy can make a big difference
3. Implication for right now—go big with additional fiscal stimulus
4. Implication for later—keep policy supportive until the recovery is complete <u>for everyone</u>

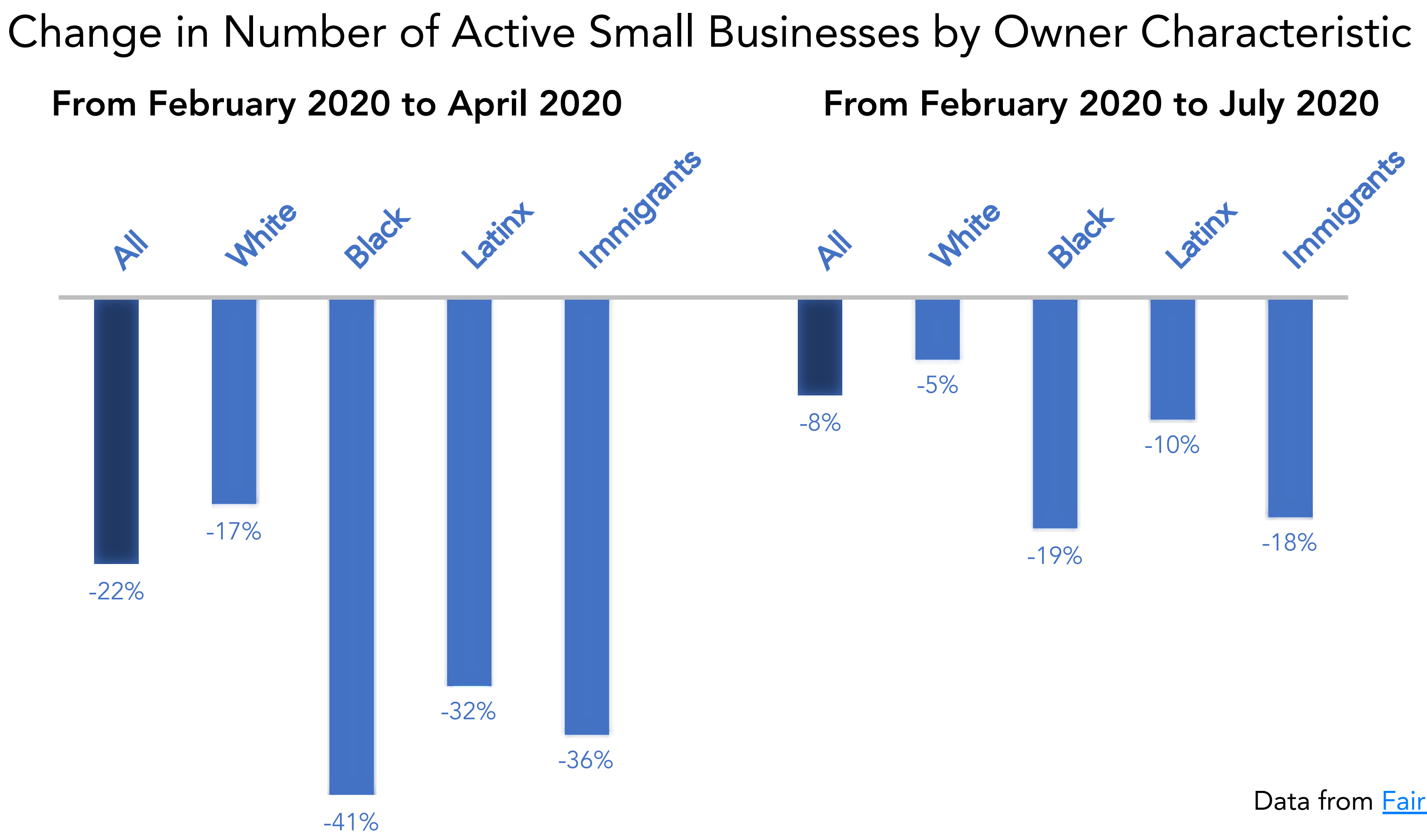
1. Recessions are costly, with the burden falling disproportionately on already struggling populations

Large disparities in rates of job loss over the cycle

Unemployment Rates: Selected Education and Race Groups
(percent of labor force)



Large disparities in rates of small business distress



Data from Fairlie (2020)

Other costs of recessions

Large reductions in lifetime earnings for those laid off in bad recessions [Davis and von Wachter, 2011]

Harms to children [see, for example, Oreopoulos, Page, and Stevens (2008), Stevens and Schaller (2011), Schaller and Zerpa (2019)]

Unemployment's toll on physical and mental health [McKee-Ryan, Song, Wanberg, Kinicki (2005)]

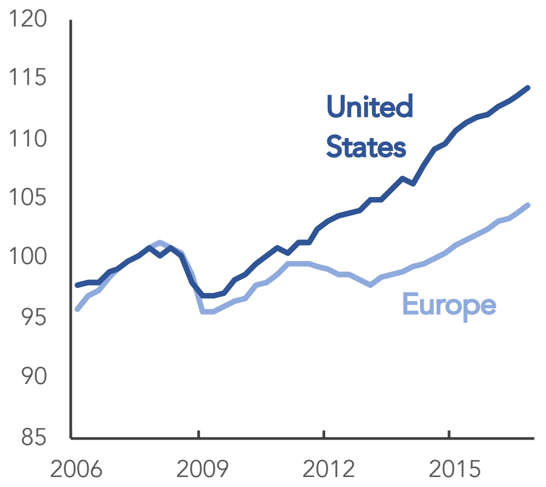
Scarring of earnings for those entering a weak labor market [see, for example, Oreopoulos, von Wachter, and Heisz, 2012]

2. Effective countercyclical macroeconomic policy can make a big difference

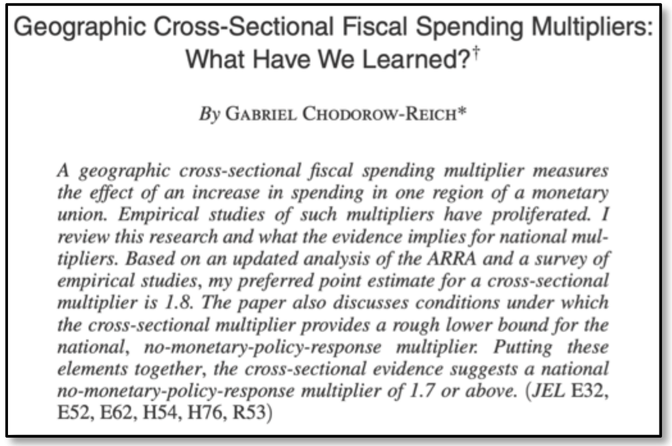
The Great Recession experience

Stronger recovery in the United States than in Europe

Real GDP (2007=100)



Academic studies



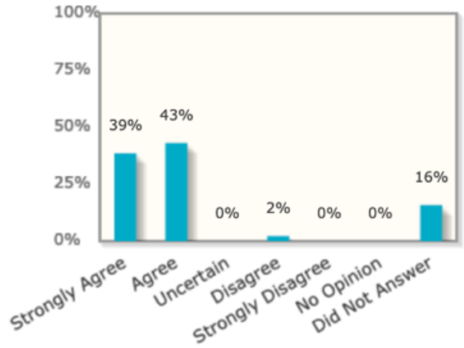
Geographic Cross-Sectional Fiscal Spending Multipliers: What Have We Learned?†

By Gabriel Chodorow-Reich*

A geographic cross-sectional fiscal spending multiplier measures the effect of an increase in spending in one region of a monetary union. Empirical studies of such multipliers have proliferated. I review this research and what the evidence implies for national multipliers. Based on an updated analysis of the ARRA and a survey of empirical studies, my preferred point estimate for a cross-sectional multiplier is 1.8. The paper also discusses conditions under which the cross-sectional multiplier provides a rough lower bound for the national, no-monetary-policy-response multiplier. Putting these elements together, the cross-sectional evidence suggests a national no-monetary-policy-response multiplier of 1.7 or above. (JEL E32, E52, E62, H54, H76, R53)

Polls of economists from the left and the right

Because of the American Recovery and Reinvestment Act of 2009, the U.S. unemployment rate was lower at the end of 2010 than it would have been without the stimulus bill.



IGM Survey (2014)

The COVID Recession experience

Staggering US job loss—at the low point, jobs were down by 22 million relative to the pre-pandemic level

The job loss has been **concentrated among lower-income workers** (especially that which has been persistent—trackthere recovery.org shows that employment rates are nearly back to normal for high-wage workers)

Significant early fiscal policy response—$2.6 trillion (12 percent of GDP) including expanded and more generous unemployment benefits, stimulus checks, support for businesses, money for states and the health care system

Household finances have held up remarkably well considering the job loss

Consumption has held up for lower-income households

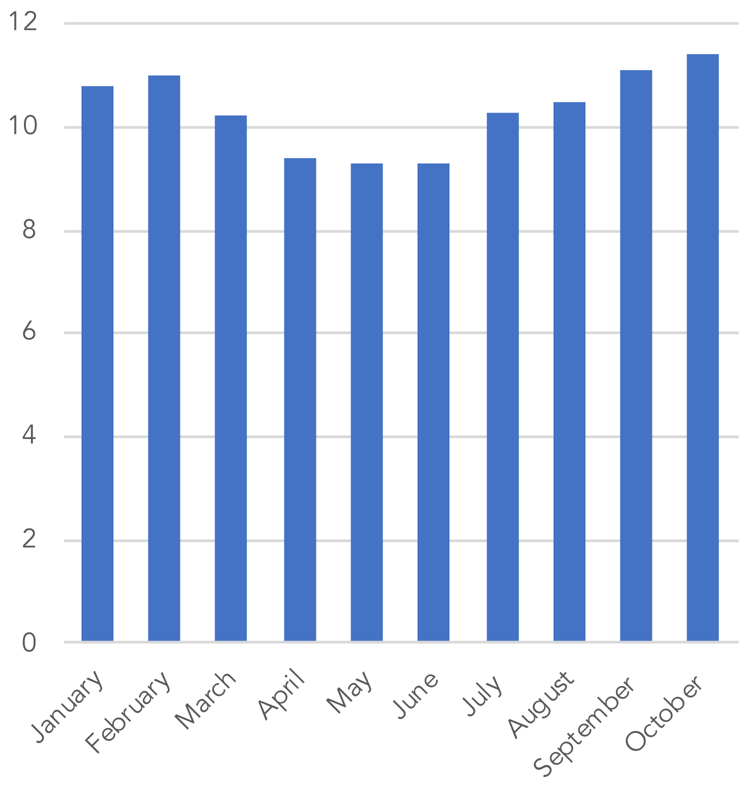
Percent Change in Consumer Spending since January 2020

Screenshot from tracktherecovery.org

Poverty actually declined (for a time)

Real-Time Poverty Estimates

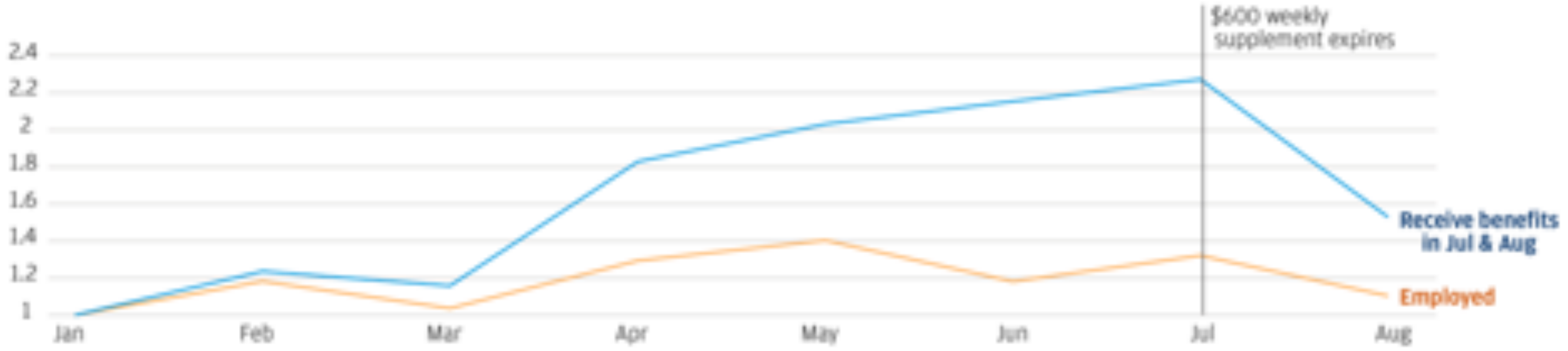
Percent



Data from Han, Meyer, and Sullivan (2020)

Job losers were actually able to save money (for a time)

Median Checking Account Balance (Jan. 2020=1.0)

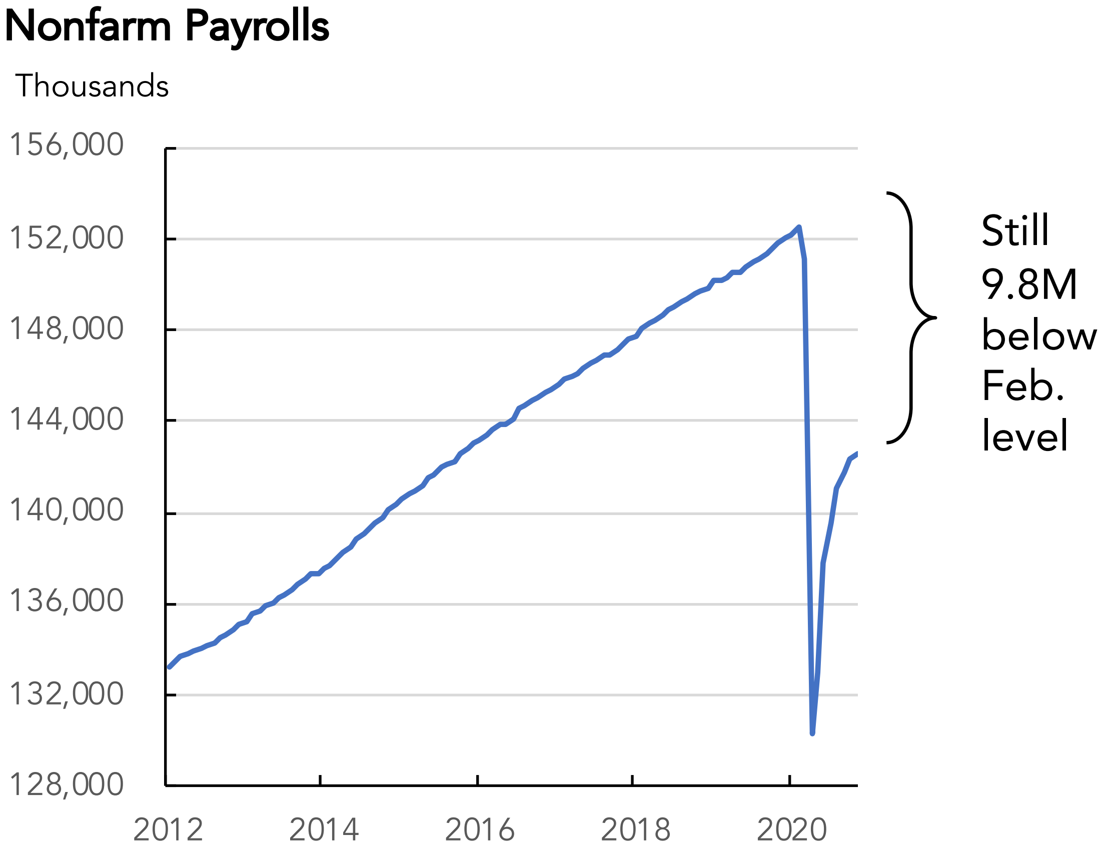


Screenshot from [JPMC Institute]

3. Implication for right now—go big with additional fiscal stimulus

We should be concerned about what's ahead

The economy remains in poor shape



The pace of improvement has slowed waaay down

Change in Nonfarm Payrolls (Thousands)	
Jun	4781
Jul	1761
Aug	1493
Sep	711
Oct	610
Nov	**245**

Source: Department of Labor via FRED

Prescription

Support households' incomes, sustain businesses' operations, and reduce state and local governments' budget gaps

The needed amount of stimulus is uncertain, but the risks are asymmetric—**doing too little would be much more costly than doing too much**

- An additional $1-2 trillion

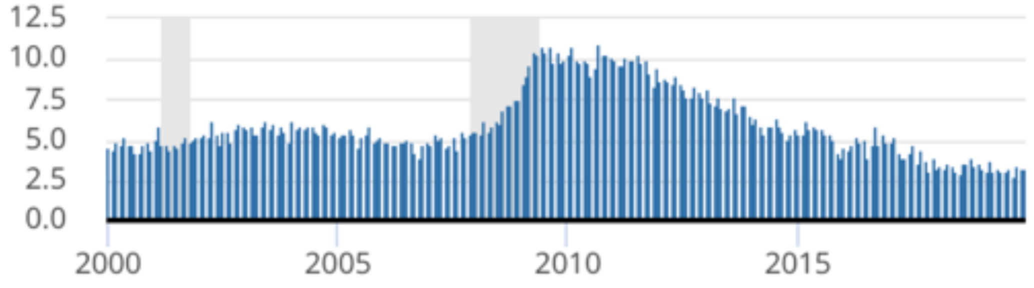
- The **goal is to provide enough support to reach everyone in need**—to reduce suffering now, power a stronger recovery, and prevent destructive long-term scarring

4. Implication for later—keep policy supportive until the recovery is complete <u>for everyone</u>

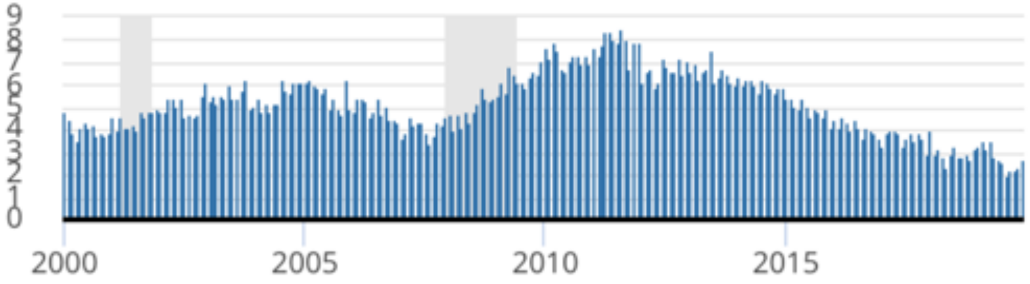
Huge distributional benefits to keeping monetary policy easy through the end of the 2010s

Employment gaps were closing for everyone—and everywhere

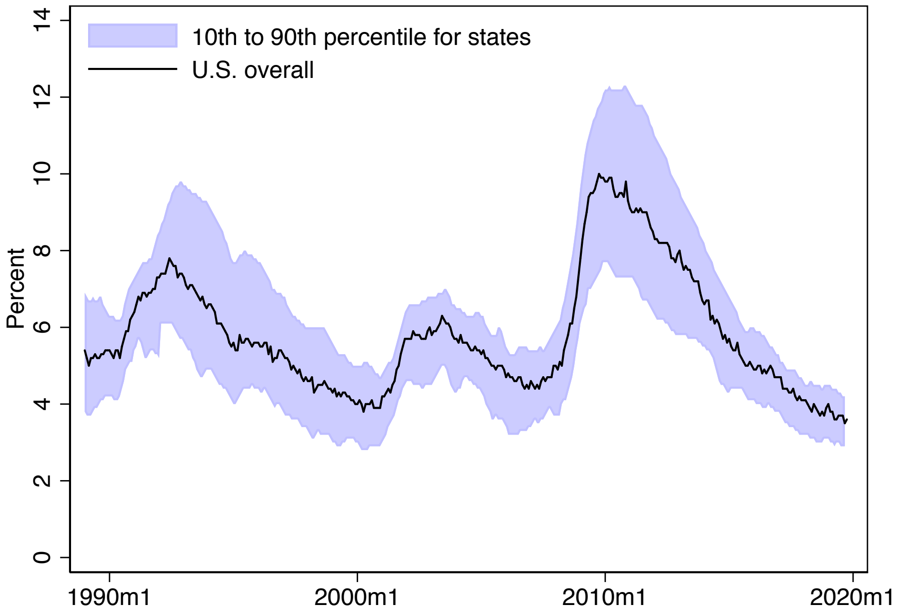
Gap between < High School Unemployment Rate and Bachelor's + Unemployment Rate (through 2019)



Gap between Black Unemployment Rate and White Unemployment Rate (through 2019)



Variation in Unemployment Rates across States (through 2019)

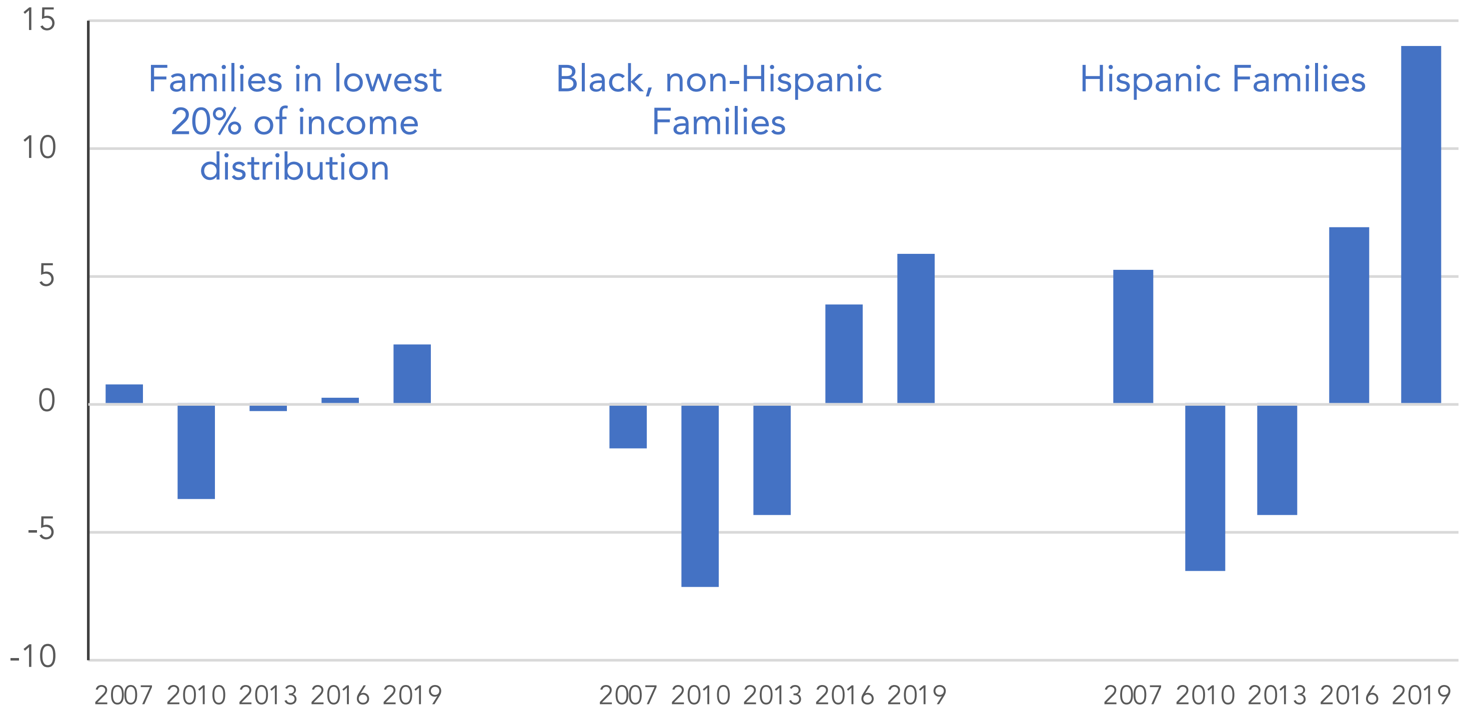


Screenshot from [Dynan and Elmendorf] (2020)

Wealth was rebounding for traditionally low-wealth groups

Median Net Worth

Change in from 3 years earlier, 2019 dollars



Data from Survey of Consumer Finances

Prescription

Let the Federal Reserve **continue to emphasize job creation**

Put policies in place that will help for next time

- **Create employment-based triggers** for federal tax cuts and spending increases so that strong countercyclical policy is more automatic
- **Fill holes in the safety net** so that people are protected from recession-related (and idiosyncratic) job losses