COVID MACROECONOMICS: THE CURRENT STATE OF AFFAIRS

what does REMI say? ™

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Overview

- A One-Minute History of COVID-19 Recession
- Whither Stimulus 2.0?
- Measuring the Economic Impact of State and Local Budget Deficits
- Conclusions and Future Measures

COVID Recession

- "Happy families are all alike; every unhappy family is unhappy in its own way."
- Recessions:
  - Demand shock (loss of consumer confidence, financial crisis)
  - Supply shock (oil shocks of the 70's)
- COVID Recession is both:
  - Demand shock (loss in confidence, fear of consumption activities)
  - Supply shock (supply chain, government-mandated shutdowns)

The Grand Response

- Monetary Policy: Add 3 Billion to the Fed Balance Sheet
- Fiscal Policy: 2.2 Trillion of Spending, Deficit Financed
- Why both?
  - With simultaneous demand and supply shock, need both fiscal and monetary expansion
  - Monetary alone: without demand, or business and consumer confidence that demand will hold up, access to capital even at a low interest rate will be not be enough to move forward "pushing against a string"
  - Fiscal alone: expansionary fiscal policy without monetary accommodation will tighten access to capital
- In concert, monetary and fiscal expansion stemmed a vicious economic circle.

Whither Stimulus 2.0?

- March 2020: 2 Trillion Dollar CARES Act
- Summer 2020: continuing negotiations for additional relief
- October 26: Senate adjourned until November 9, postponing further action
- November 3: What is the outcome of the election? Uncertain political dynamics in lame duck session
- January 2020: Our New Government, expectation for stimulus, but many unknowns

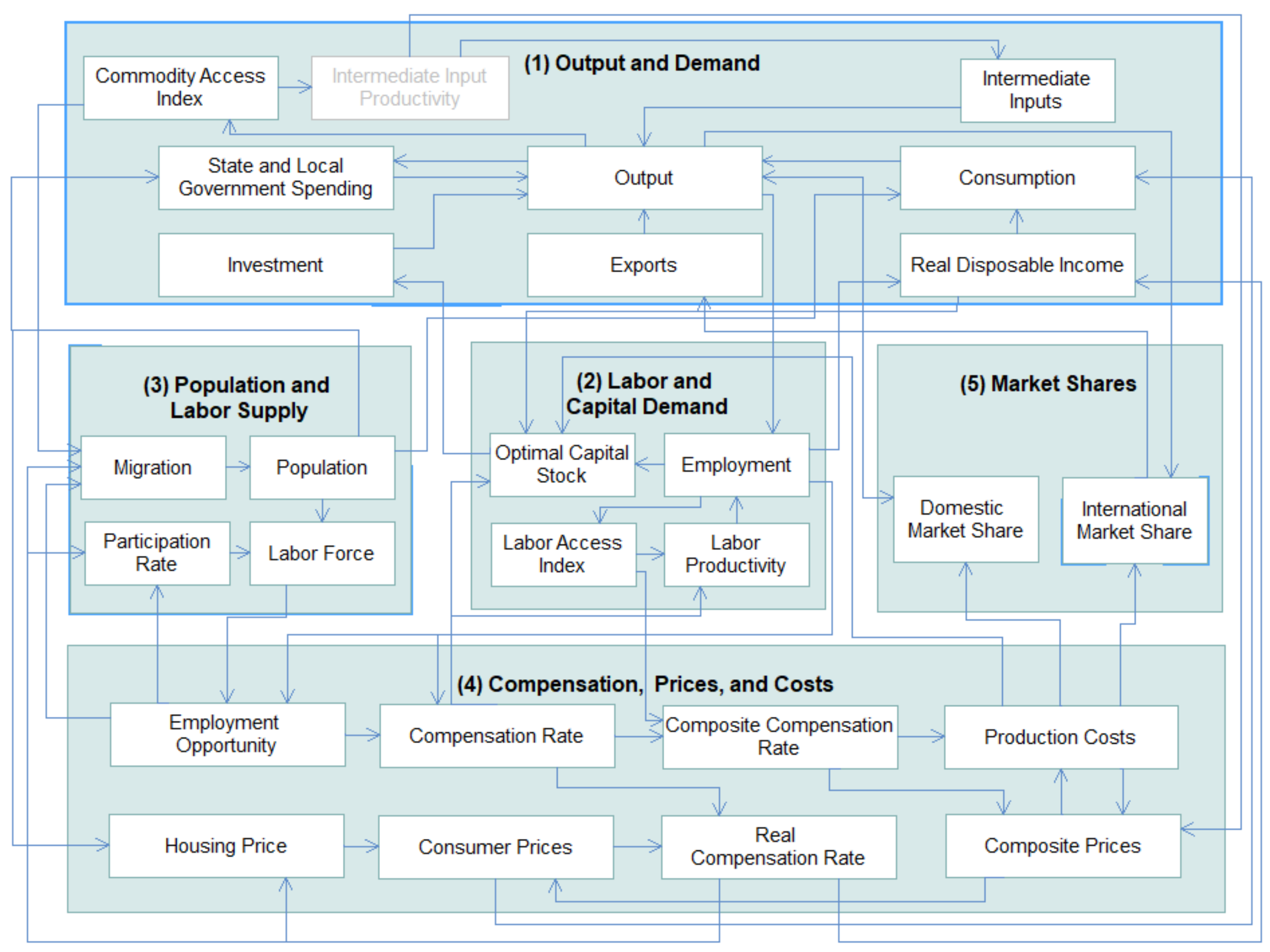
Why do states matter?

- Collectively, state and local governments outspend the federal government and make up 11% of GDP[1]
- States make up vast majority of transportation and education spending, items that make the US globally competitive
- States in a bind: diminished revenue from curtailed economic activity, lowered value of pension funds, but increased spending on social welfare and public health
- States cannot easily borrow money, unlike the federal government

Methodology & Assumptions

- REMI IQ+ and REMI PI+
- Baseline: May RSQE update (includes predicted stimulus)
- Experiment: May RSQE update with state and local spending cuts and pre-COVID federal spending figures
- Predicted state revenue shortfalls collected from the Center on Budget and Policy Priorities[2]
- If a state has a range of projections, the average is used
- Missing state data (Alabama, North Dakota, and South Dakota) filled in with group average
- Two tests:
  - Short-term cut from Q4 2020 to Q2 2021
  - Long-term: cuts extended from 2021 to 2030

Model Outline



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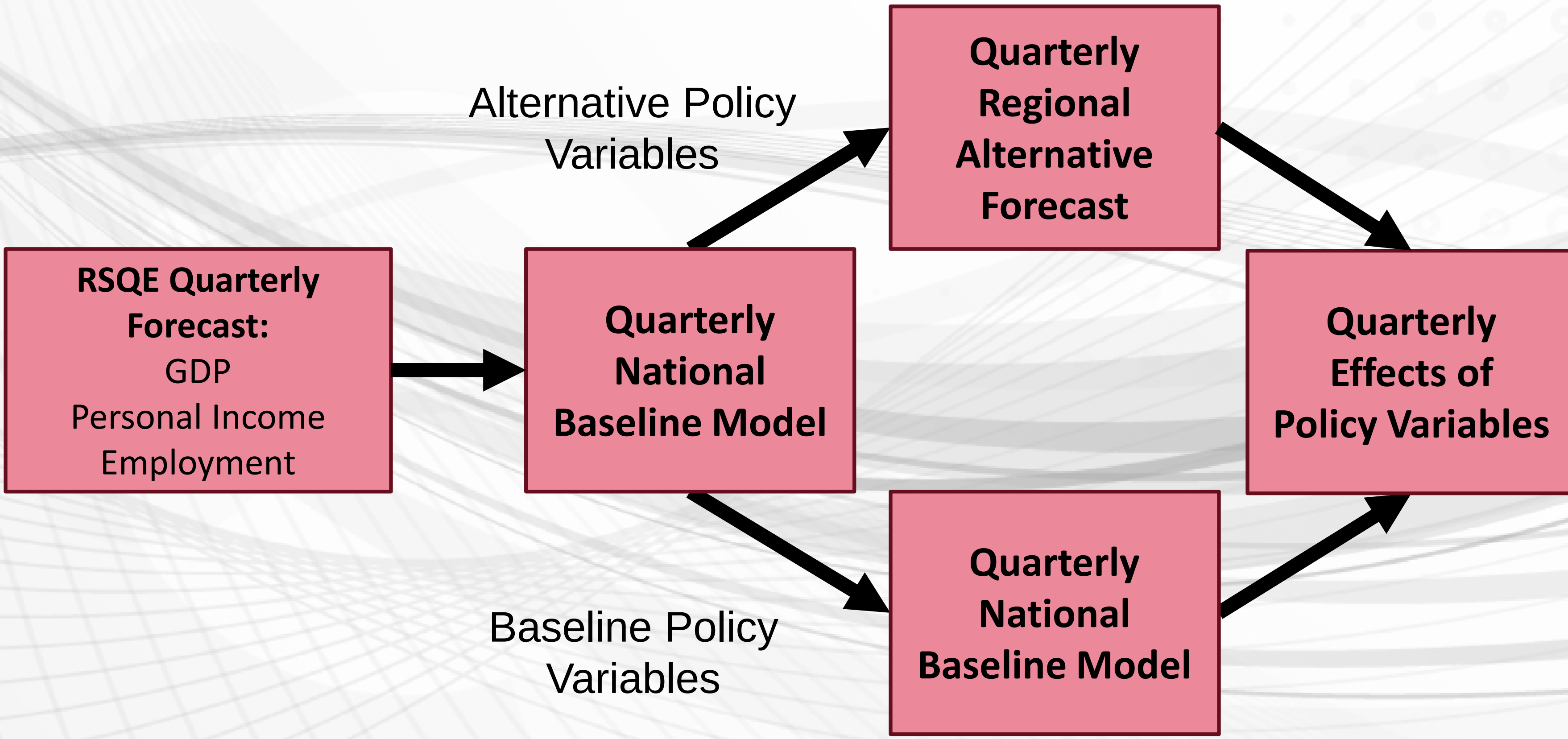
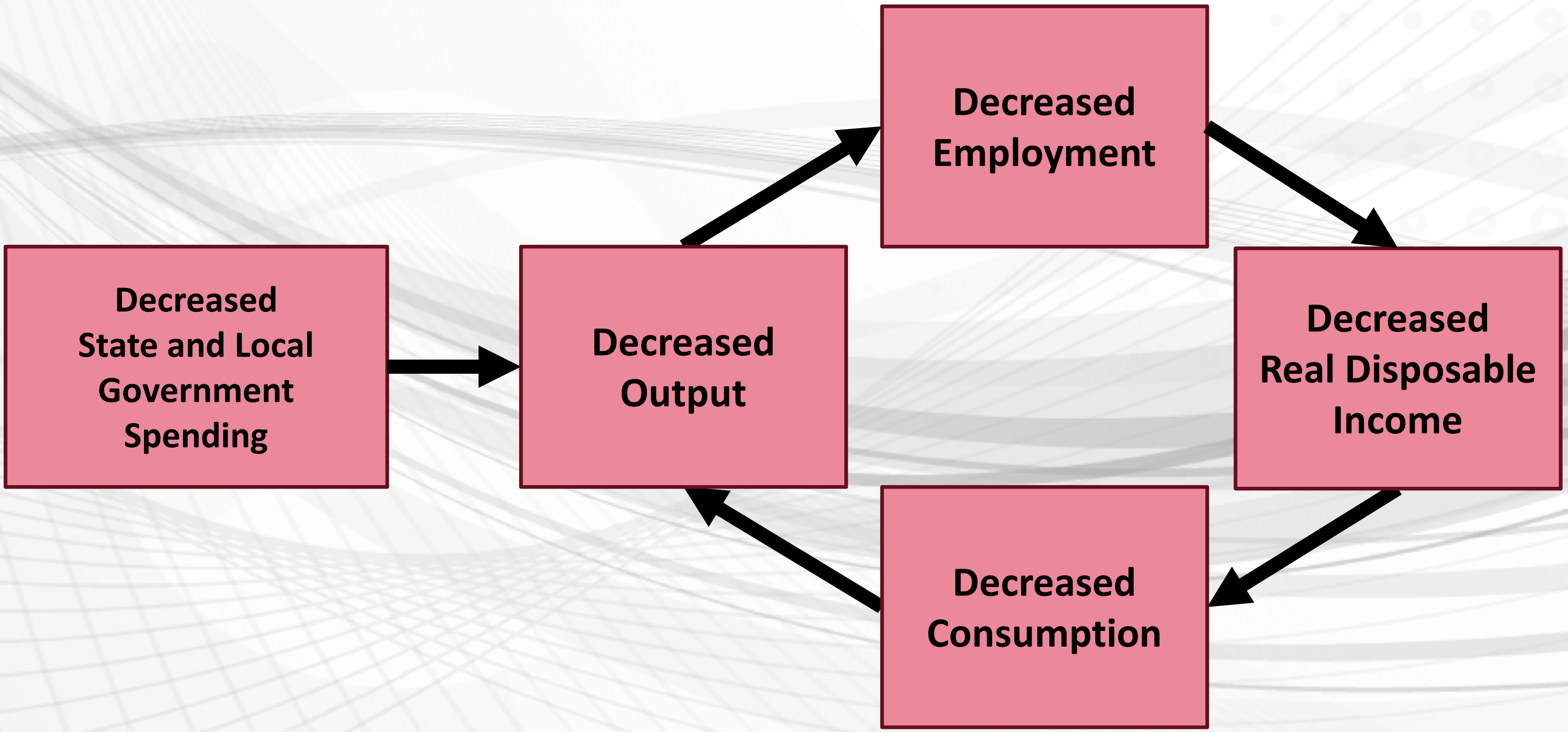
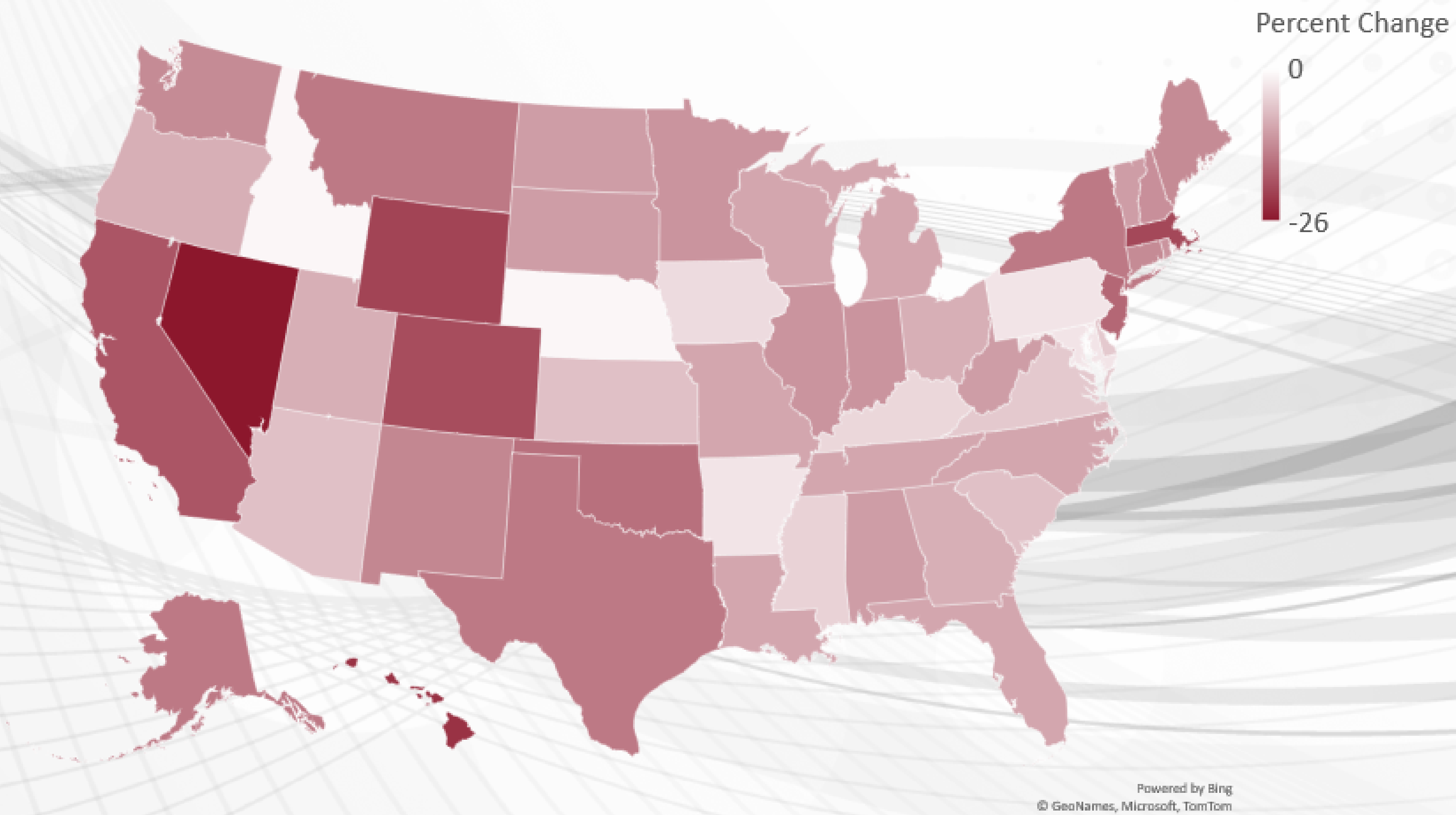
Model Outline (Simplified)



Avenues of Change (Consumption)



State Revenue Shortfalls



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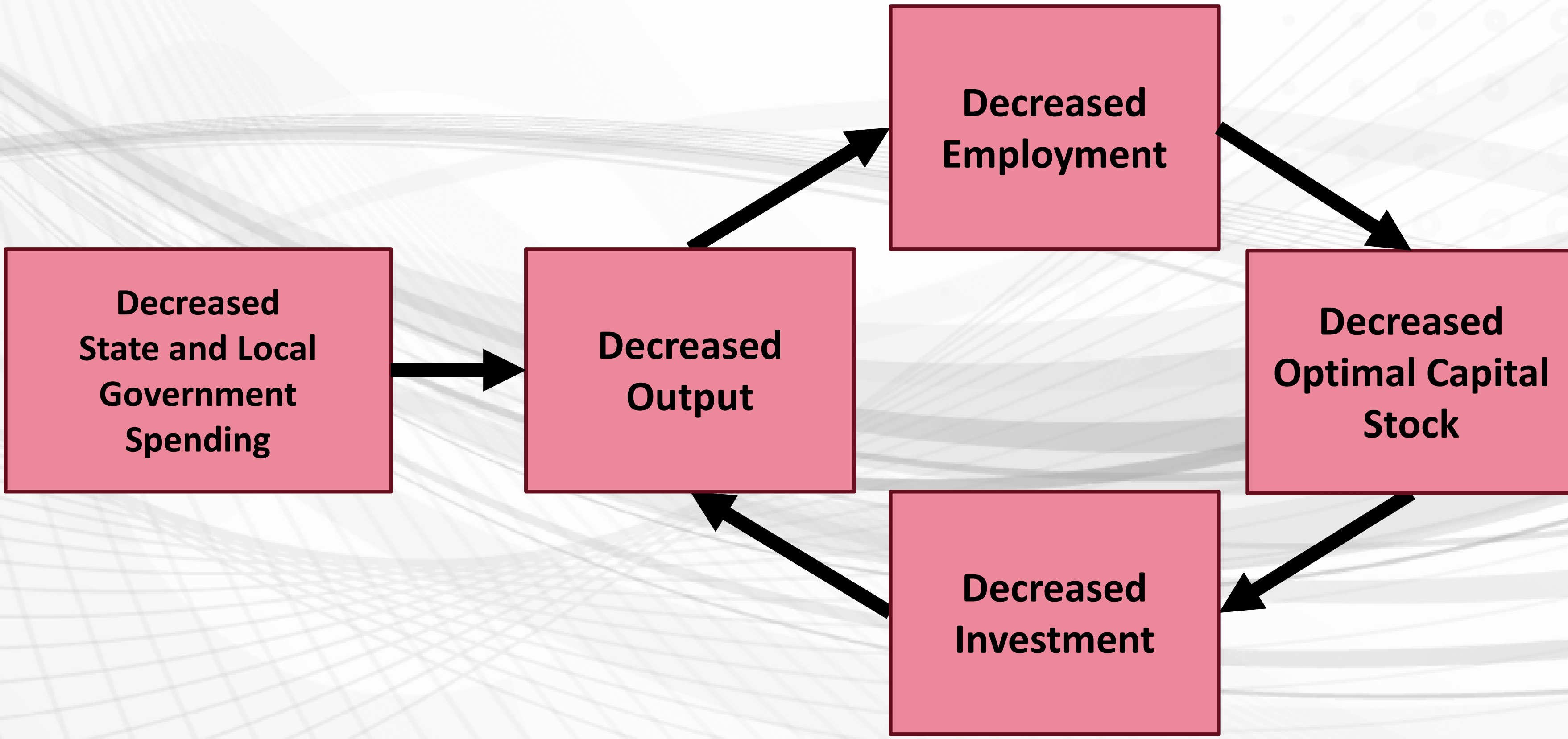
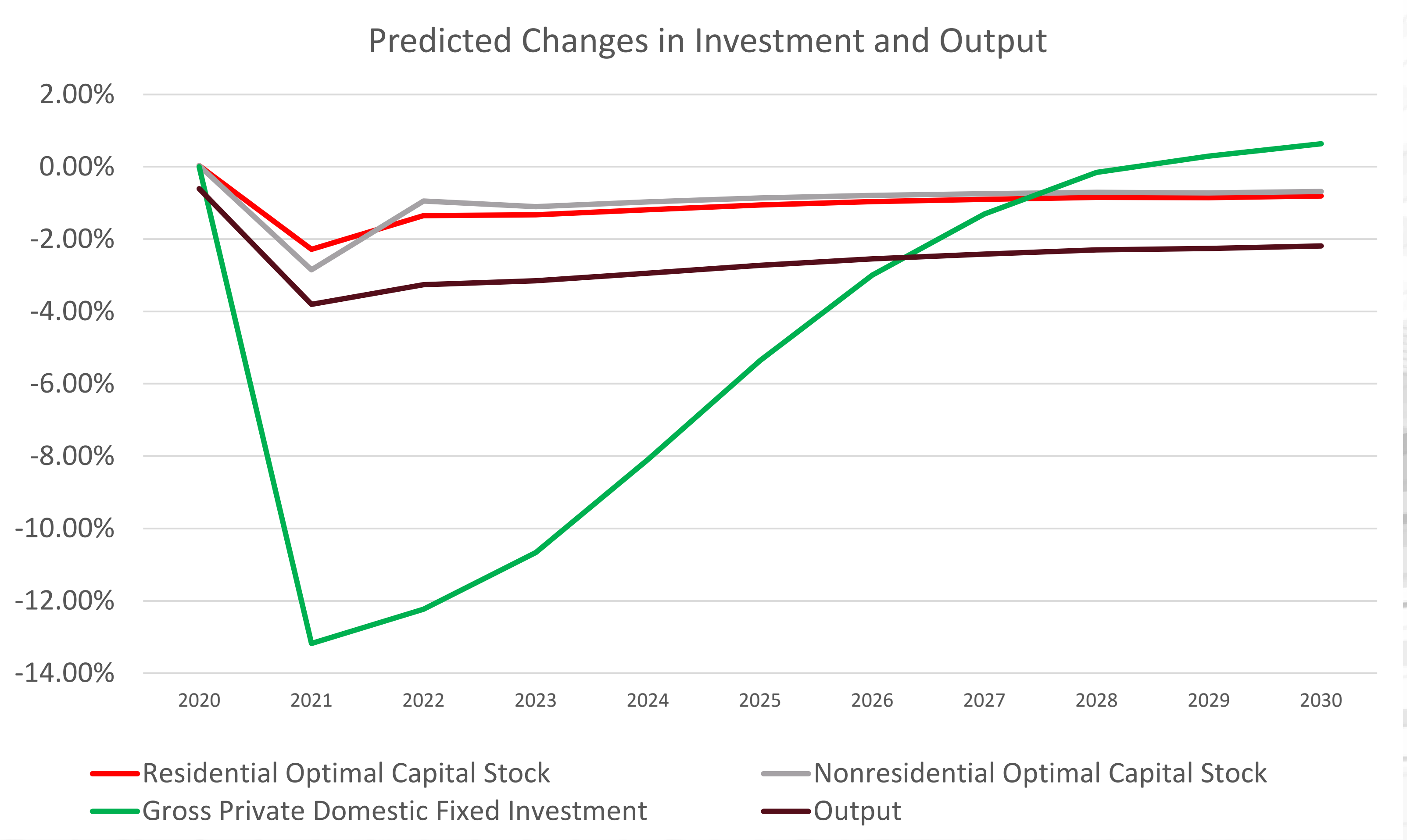
Q2 2021 Results

Category	Losses	Percent Change
Employment	6.5 million jobs	-3.49%
Consumption (Durables)	55 billion fixed (2012) dollars	-2.86%
Consumption (Non-Durables)	47 billion fixed (2012) dollars	-1.61%
Consumption (Services)	158 billion fixed (2012) dollars	-1.83%
Output	1,055 billion fixed (2012) dollars	-3.03%
GDP	599 billion fixed (2012) dollars	-3.08%

Avenues of Change (Investment)



The National Picture



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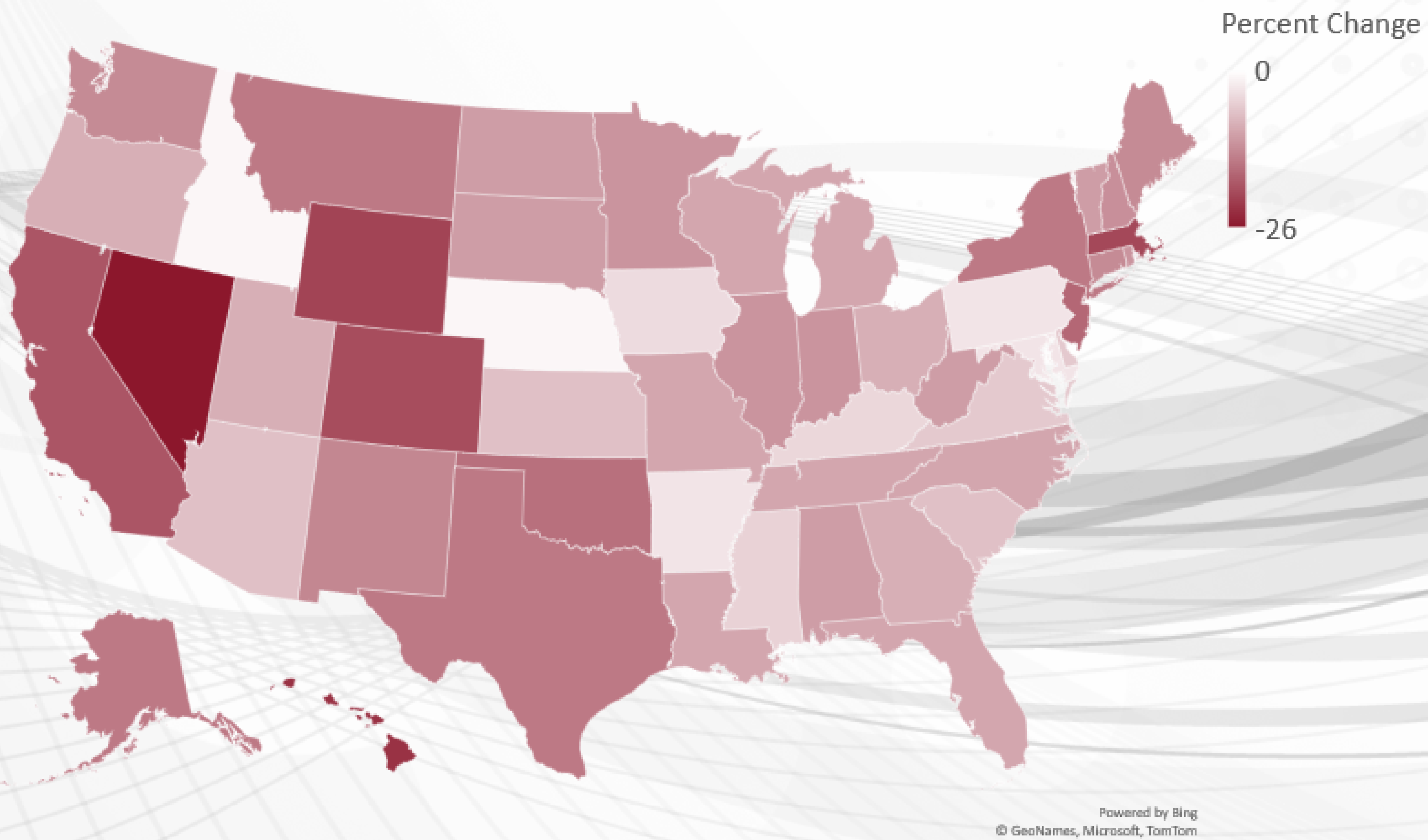
State Revenue Shortfalls



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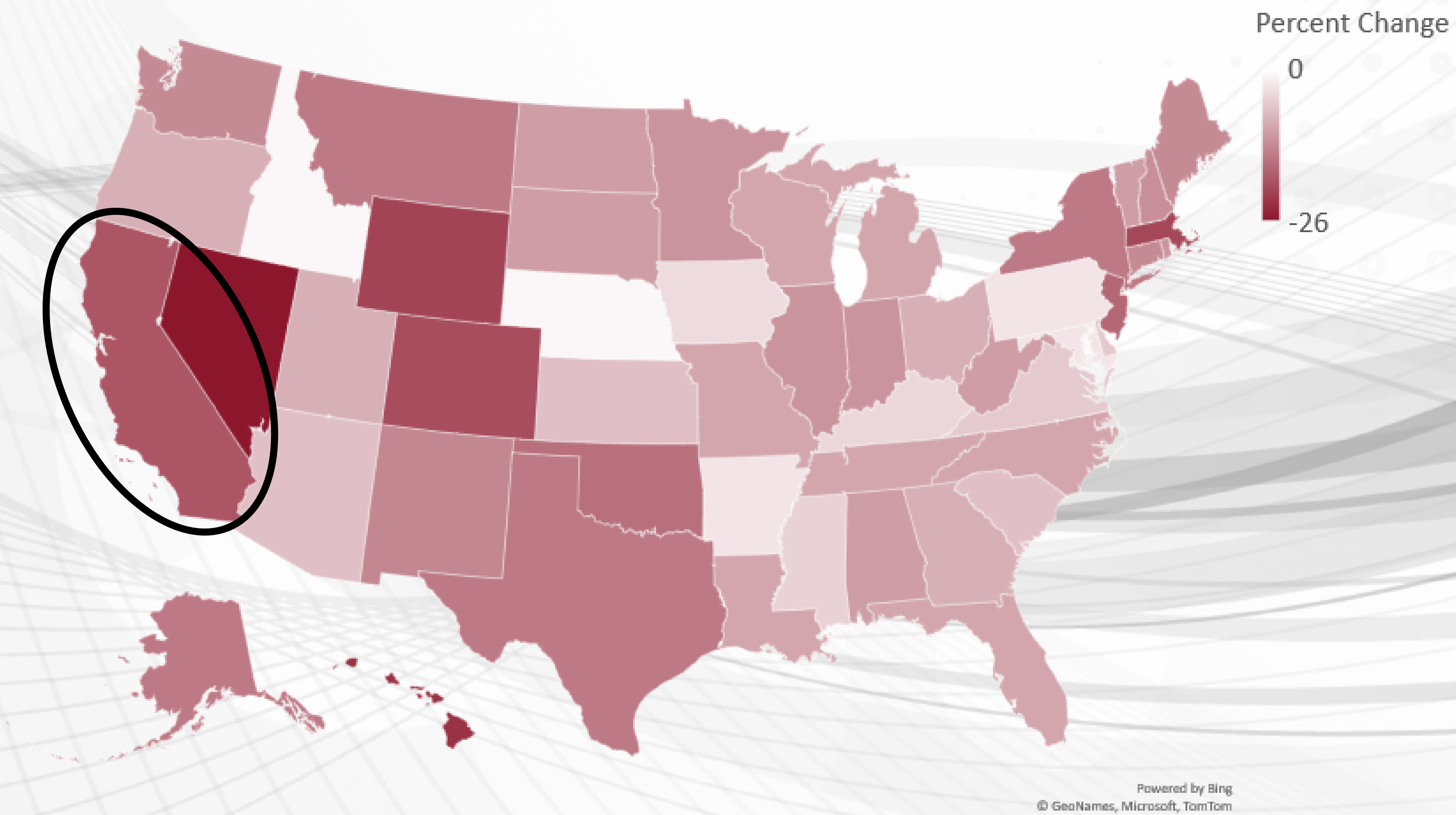
State Revenue Shortfalls



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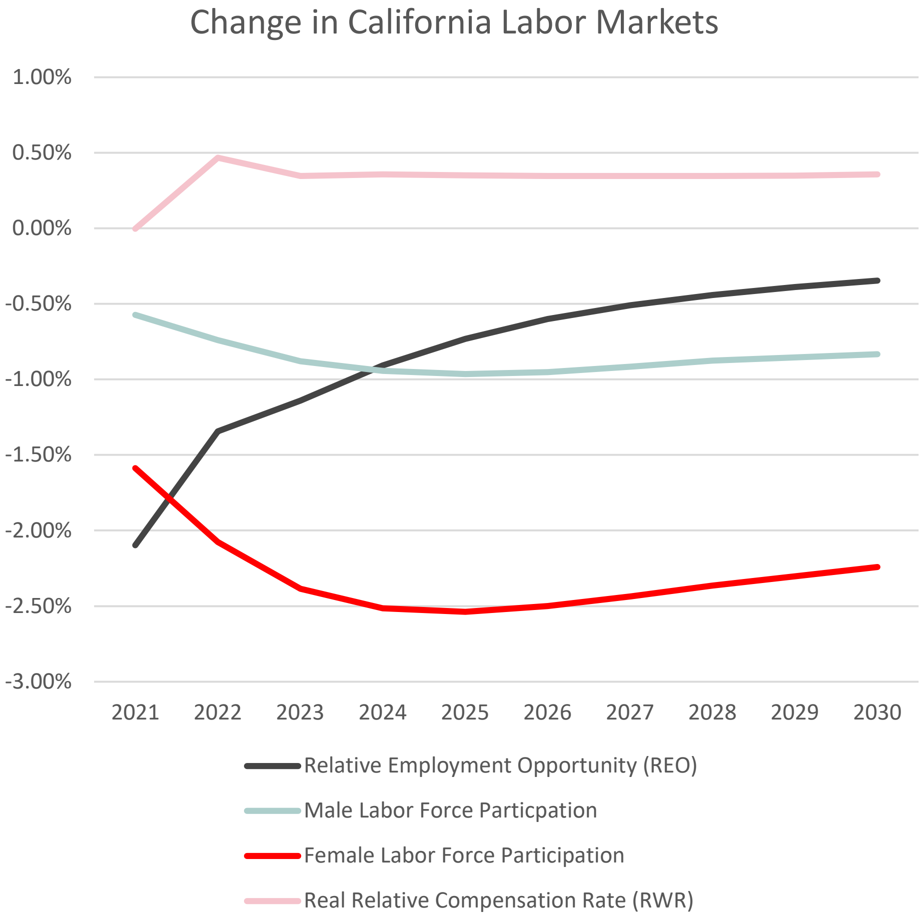
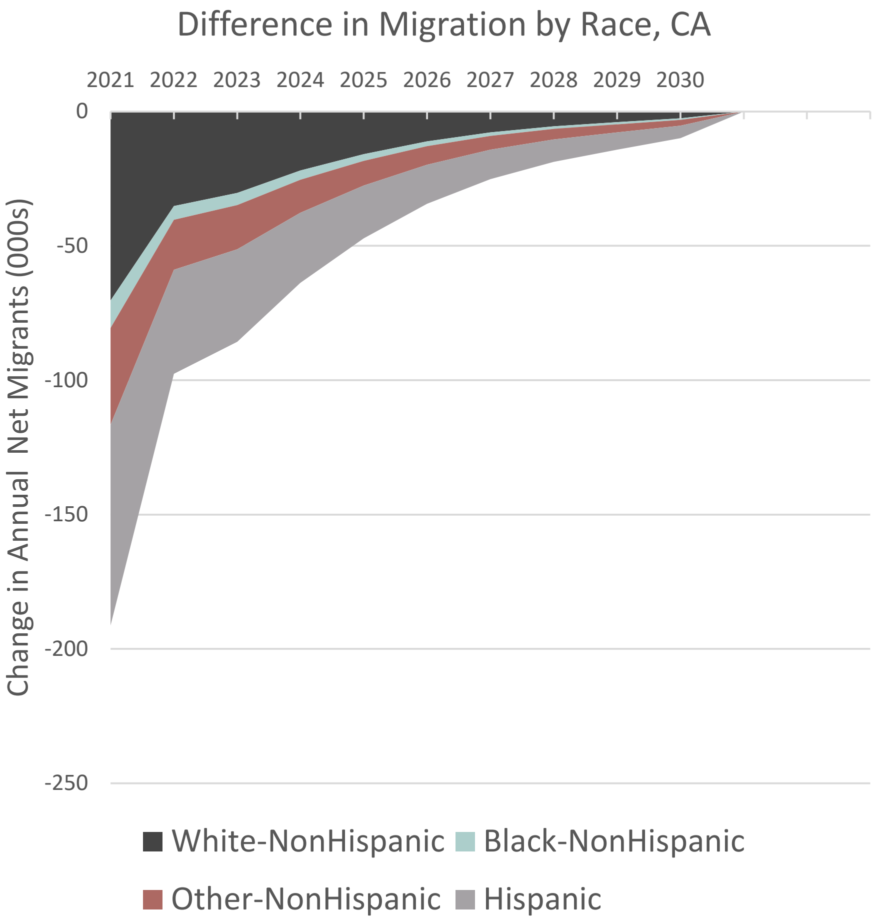
Labor Force





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Policy: what's next?

- Ongoing stimulus discussions include additional support of businesses, stimulus checks, unemployment benefits; ranging from 1.8 to 2.2 trillion
- Yet, the economy rebounded in Q3 in absence of additional stimulus
  - Though still 3% below its pre-COVID peak[3]
- May be difficult to get broad consensus on stimulus as economy recovers and financial markets stable.

Is there a “right” way for economic stimulus?

- Extended unemployment, stimulus check: economic rationale is consumer spending (“induced”); but consumers may just bank money, pay off debts, subsidizing economically unproductive activity
- State and local stimulus subsidizes productive work
- Other stimulus, such as infrastructure, benefits the entire supply chain, (direct, indirect, induced); long-term productivity benefit (broadband, transportation costs)

Conclusion

- Stimulus 2.0 is big (2 trillion in a 20 trillion economy)—massive economic effect.
- We model state and local spending cuts as one component: could reduce Q2 2021 jobs by over 3%
- New stimulus “baked-in” to many macro forecasts; breaking the deadlock may need to be triggered by job losses and financial market disruption.

Citations

- 1. Siripurapu, Anshu, and Jonathan Masters. "How the Coronavirus Will Harm State and City Budgets." *Council on Foreign Relations*, Council on Foreign Relations, 15 May 2020, www.cfr.org/backgrounder/how-coronavirus-will-harm-state-and-city-budgets.
- 2. "States Grappling With Hit to Tax Collections." *Center on Budget and Policy Priorities*, 5 Oct. 2020, www.cbpp.org/research/state-budget-and-tax/states-grappling-with-hit-to-tax-collections.
- 3. Pickert, Reade. "U.S. Economy's Path Less Certain After Record Quarterly Growth." *Bloomberg.com*, Bloomberg, 29 Oct. 2020, www.bloomberg.com/news/articles/2020-10-29/u-s-economy-expands-at-record-33-1-pace-after-covid-plunge.

Q&A Session