



The Daily Dish

The Case Against Bigger Automatic Stabilizers

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Eakinomics: The Case Against Bigger Automatic Stabilizers

Automatic stabilizers are the elements of federal programs that automatically lean against the business cycle. For example, as the economy slows or enters a recession, incomes decline, moving people into lower tax brackets (or out of the income tax entirely) and giving them a greater fraction of their earnings available to spend. As layoffs occur, payments for unemployment insurance (UI) rise and bolster the spending power of the household sector. As the economy recovers and accelerates, the programs work in reverse. Automatic stabilizers are often presented as the alternative to discretionary fiscal policy — tax cuts or stimulus spending enacted by Congress — because they will happen in a timely fashion, whereas a Congress may not.

The stylized proposals to expand stabilizers is to have a trigger (e.g., a 0.5 percent increase in the unemployment rate) that causes, e.g., taxes to be lowered or unemployment insurance to get richer and last longer. Since the logic of automatic stabilizers is impeccable, it is tempting to conclude that bigger is better. But having been asked to [testify](#) on the topic, after thinking about it a bit I came down against expanding the automatic stabilizers. Here's the short version why.

First, I have seen no rigorous analysis that makes the case that the existing automatic stabilizers are inadequate. From that perspective, the discussion is getting ahead of itself.

Second, automatic stabilizers would be more mandatory spending — that is, it is automatic. Mandatory spending is the federal budget problem (70 percent of spending is done on automatic programs such as Social Security, Medicare, and so forth), so it is unwise to add to this problem. One could, of course, cut other mandatory spending to have no net expansion, but I have not seen any proposals on that front.

Third, I do not know how one can set the specifics of the proposals. What should be the trigger? A rise in unemployment of 0.5 percentage points? 0.4 percentage points? Unemployment above 5.0 percent? Similarly, how much more should one get in UI? How much longer should it last? Since we have no idea about the nature of the onset or depth of a future recession, there is no scientific answer to these questions.

Fourth, I'm worried that a future Congress will ignore the presence of the automatic stabilizers on steroids and enact a discretionary policy in addition. It is hard to go to a town hall when the economy is headed south and get away with: "Our predecessors took care of this. It's all good. I'm not planning on doing anything." Good luck. The likely outcome is that we augment the fiscal response by a factor of two.

Finally, if Congress wants to do something now to enhance the resiliency of the economy in the future, it should focus on those things — permanent, structural reforms — that enhance the long-run trend rate of growth. The reality is that there will always be a natural disaster, a strike like that at General Motors, or negative shock like the grounding of Boeing airplanes. Economic bad news is inevitable. If the economy is growing at 0.5 percent or 1.0 percent when the bad news hits, it may very well end up in negative territory. But if the trend growth rate is 2.5 percent, the chances of having an actual recession are much lower.

Promising to spend more and tax less when things go bad seems appealing, but it is better to set fiscal policy now to grow rapidly and avoid the bad times in the future.