



The Daily Dish

Uncharted Territory Redux

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Eakinomics: Uncharted Territory Redux

With the arrival of the coronavirus pandemic in March 2020, the U.S. economy entered uncharted territory. Never before had the United States lost 20 million jobs in a month, as it did in April (the previous record was 2 million), nor had it ever before gained 2.5 million jobs as it did in May. Never before had the unemployment rate risen by over 10 percentage points, nor had it fallen by the 2.2 percentage points it declined in May. Gross domestic product (GDP) fell 9 percent in the 2nd quarter – a record. GDP rose by 7.5 percent in the 3rd quarter – a record. Oil futures prices fell into negative territory, the federal deficit ballooned to 3.3 trillion (16 percent of GDP), and the Federal Reserve (Fed) balance sheet expanded by \$3 trillion. All records.

Federal policy was an integral part of converting the large negative numbers into subsequent positive territory. The Fed lowered rates to zero and flooded markets with liquidity. It continues to do so. The Coronavirus Aid, Relief, and Economic Security (CARES) Act provided over \$2 trillion of support to households (checks, unemployment insurance), governments (state, local, and school aid), and businesses (the Paycheck Protection Program distributed \$500 billion in one month). This enormous transfer of cash flow permitted large swaths of the private sector to bunker down and survive the initial surge in COVID-19 cases. As the virus threat moderated, the economy recovered quickly (if not quite entirely).

We are experiencing another round of the same dynamics. As cases soar nationwide, once again households are sheltering from the virus at the expense of labor supply and economic commerce. In the absence of a policy response, one could expect a decline in household spending (especially on services that involve personal contact), small business closures, and a reduction in employment.

The good news is that the support of the Fed is ongoing and that over the past 10 months households and businesses alike have learned better how to operate in the presence of the virus. As a result, the initial downdraft is likely to be far less severe. Also, Congress has passed another \$900 billion of CARES-like support in the form of unemployment insurance, one-time checks, and Paycheck Protection Program funding. This sum amounts to over 4 percent of annual GDP. If it is disbursed over the next 2 quarters, that will be tantamount to an 8 percent of GDP cash-flow support for the economy. That is an enormous fiscal boost.

That is not a lot of history, but there is a good chance to expect that the economy can arrive in the 2nd quarter prepared to shake off the virus-induced interruptions in activity and grow of its own accord. The key this time is to take advantage of the breathing room and genuinely address the spread of the virus.