COVID-19 Federal Rescue Policies

Jan Eberly
James R. and Helen D. Russell Professor of Finance
Faculty Director, Kellogg Public-Private Initiative (KPPI)

Northwestern | Kellogg
Executive Education
COVID-19 Federal Rescue Policies:

Economic Policy in a Pandemic

Professor Janice Eberly

May 7, 2020

Northwestern | Kellogg
What do we see and what is being done?

• Current conditions and forecasts
  – Sharp Q2 decline, less so in Q3 (murky)
  – Labor market deteriorating quickly
• Policy rescue measures – rapid initial phases
• Monetary response
  – Provide liquidity, save business capacity for recovery
• Fiscal response: three phases so far
  – Phase 1 & 2: Safety net, labor, health
  – Phase 3: massive $2T household, business rescue
  – Phase 3.5: top up small business, more for hospitals
  – Next?
Initial Unemployment Claims weekly, January - April 2020

~200,000/week

~3.3 million, 5x highest week in financial crisis

~6.9 million

Data: Bureau of Labor Statistics
Total of 30 million jobless claims is about 18% of pre-pandemic workforce.

- Concentrated in states with
  - larger outbreaks (Michigan, Washington) and
  - more vulnerable industry mix, especially leisure and hospitality (Hawaii, Nevada)

- Claims will also rise as
  - backlog is worked off
  - delay for gig workers ends
  - some state restrictions are eased

chart: McKinsey Global Institute
The increase in unemployed was almost entirely temporary layoffs, defined as < 6 months.

Other unemployed steady at ~ 2 million

The claims numbers tell us that both numbers will rise dramatically for April (to be released Friday, May 8)

Data: Bureau of Labor Statistics

May 7, 2020 (c) Janice Eberly
US output growth: GDP fell by 4.8% in Q1
Pandemic economic impact

• First quarter GDP down 4.8%
  – Not bad? No, just not complete.
  – Only a few weeks of pandemic (late March)
  – Incomplete data – first print has less on services
  – Likely to be 7–8% decline by final estimate
• Q2 starts with April – expect 30% decline (annualized, quarter/quarter)
• Relatively accurate in the short run, because the shock is well-defined
  – Rule of thumb: half of economy is services, 30% (excluding healthcare) of
    that is face to face.
  – 15% of economy is 50% operational over the quarter => -7.5% for quarter,
    or -30% annualized
  – Larger effects as the recovery takes longer, and add “knock on” effects of
    lower income feeding back to lower demand
Gains and losses, but gains are not big enough

- **Jobs**
  - Losses in retail, hospitality, childcare, food service
  - Gains in translators, respiratory therapists, psych, physicians, warehouse stockers
- **Consumption**
  - Losses in personal services, clothing, personal care goods(!)
  - Gains in electronics, food, housewares, prescription drugs
  - Income has been well-supported so far (see fiscal programs)
  - Shortages of toilet paper, yeast, flour; surpluses of restaurant supplies
  - Supply chain will adjust
- **These shifts are larger than other countries that have a “shelter in job” approach**
  - They are designed to keep employees attached to firms during short-lived downturns
  - Not as effective when trend changes, but effective in short cycles
  - How to mimic that in this crisis? – keep employees attached virtually
Federal Reserve tools

- Immediate rate reduction to ZLB (starting from 1.5% rather than 5%)
- Asset purchases $500bn Treasuries + $200 bn Agency MBS, then uncapped
- Liquidity support for Commercial paper, Money Funds, Asset Backed Securities through TALF
Federal Reserve Assets 2008-2020

Pre-financial crisis
$800 billion

2015 max
$4.5 trillion

Post-financial crisis min
$3.8 trillion
August 2019

April 29,
$6.7 trillion

Data: Federal Reserve Board
Federal Reserve tools – new facilities

- New programs to support the flow of credit to employers, consumers, and businesses by providing up to $300bn in new financing. The Treasury, using the Exchange Stabilization fund (ESF) will provide $30bn in equity to these facilities – expanded by Phase 3 fiscal.
- Two facilities to support credit to larger employers:
  - Bridge financing: the Primary Market Corporate Credit Facility (PMCCF) for new bond and loan issuance. Investment grade companies, bridge financing of four years. May defer interest and principal payments during the first six months of the loan.
  - Secondary Market Corporate Credit Facility (SMCCF) to provide liquidity for outstanding corporate bonds. Purchase corporate bonds issued by investment grade US companies and US listed ETFs (broad holdings).
- Establishment of a “Main Street Business Lending Program” to support lending to eligible small-and-medium sized businesses (see fiscal programs, too.)
  - Size thresholds and other features under development.
- Municipal finance facility under development
Fiscal Stimulus – *three phases 1 and 2 focused directly on health & safety net*

- **Stimulus Phase 1**: March 6, $8.3 billion:
  - Extra funding for directly involved agencies: the Centers for Disease Control and Prevention (CDC), Food and Drug Administration (FDA), National Institutes of Health (NIH), the State Department, the Small Business Administration (SBA), and the United States Agency for International Development (USAID).
  - $4 billion for coronavirus tests, and $1 billion in small business loan subsidies.

- **Stimulus Phase 2**: March 18, $100 billion:
  - Free coronavirus testing (also for the uninsured).
  - Two weeks of paid sick and family leave.
  - Increased unemployment insurance benefits.
  - Increased federal funds for Medicaid and food security (SNAP).
Fiscal Phase 3 – March 27
$2 trillion “CARES Act”

1. $290bn in checks to individuals
2. $260bn in expanded UI
3. $377bn small business PPP
4. $500bn capital for business loans
5. $150bn in fiscal aid to states
6. $340bn in direct federal spending, including hospitals/health, tax measures, airlines, employee retention credit

Source WSJ March 2020

May 7, 2020 (c) Janice Eberly
Cash Payments to households

- One-time checks, maximum $1,200 per adult; $500 per child dependent
- Phase-out for upper-income taxpayers, based on 2018 tax returns
  - Single: $75,000 to $99,000
  - Married: $150,000 to $198,000
  - Head of Household: $122,000 to $136,000
- If used direct deposit, IRS deposited in early-mid April
  - This covers roughly half of ~150 million eligible households
- Other tax-filers will receive debit cards starting in early May
  - Fiscal Service can process about 5 million per week – will take through the summer to complete.
- Non tax-filers (other than Social Security recipients) need to file paperwork – system portal crashing.
Unemployment Insurance expansion

- **Extend** duration, offering 39 weeks of unemployment insurance (rather than the standard 26 weeks)
- **Increase** benefit amount by $600/week, roughly half of the worker’s prior weekly pay, providing full wage replacement on average. For some sectors, like leisure and hospitality sector, the average weekly wage is closer to $500, this provides > full wage replacement.
- **Expand** coverage: Pandemic Unemployment Assistance for those not normally covered (self-employed, gig workers)
- Pay cost of first week if waiting period eliminated
- Federal coverage of work-sharing costs
**PPP, first wave (April 16, 2020)**

1,661,367 loans

$342 billion distributed

---

Distributed to all fifty states, average loan size of $206,022

<table>
<thead>
<tr>
<th>By State (largest 9 recipients):</th>
<th>$ millions</th>
<th>Loans, thous</th>
<th>Avg loan size, $</th>
</tr>
</thead>
<tbody>
<tr>
<td>Florida</td>
<td>17863</td>
<td>89</td>
<td>200,708</td>
</tr>
<tr>
<td>Illinois</td>
<td>15973</td>
<td>70</td>
<td>228,186</td>
</tr>
<tr>
<td>California</td>
<td>33414</td>
<td>113</td>
<td>295,699</td>
</tr>
<tr>
<td>Massachusetts</td>
<td>10361</td>
<td>47</td>
<td>220,447</td>
</tr>
<tr>
<td>Michigan</td>
<td>10381</td>
<td>43</td>
<td>241,419</td>
</tr>
<tr>
<td>New York</td>
<td>20346</td>
<td>81</td>
<td>251,185</td>
</tr>
<tr>
<td>Ohio</td>
<td>14109</td>
<td>60</td>
<td>235,150</td>
</tr>
<tr>
<td>Pennsylvania</td>
<td>15698</td>
<td>70</td>
<td>224,257</td>
</tr>
<tr>
<td>Texas</td>
<td>28484</td>
<td>135</td>
<td>210,993</td>
</tr>
</tbody>
</table>

Followed by Georgia, New Jersey and Minnesota

May 7, 2020 (c) Janice Eberly
PPP, first wave (April 16, 2020)

1,661,367 loans
$342 billion distributed

Estimated to be about 50% of eligible payroll – total demand closer to $700b among private firms with <500 employees

<table>
<thead>
<tr>
<th>Sectors (NAICS codes)</th>
<th>Loans (thous)</th>
<th>millions $</th>
<th>average $</th>
</tr>
</thead>
<tbody>
<tr>
<td>Construction</td>
<td>178</td>
<td>44,907</td>
<td>252,287</td>
</tr>
<tr>
<td>Professional, Sci &amp; Tech Services</td>
<td>208</td>
<td>43,295</td>
<td>208,149</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>109</td>
<td>40,922</td>
<td>375,431</td>
</tr>
<tr>
<td>Health Care and Social Assistance</td>
<td>184</td>
<td>39,892</td>
<td>216,804</td>
</tr>
<tr>
<td>Accomodation and Food Services</td>
<td>162</td>
<td>30,500</td>
<td>188,272</td>
</tr>
<tr>
<td>Retail</td>
<td>186</td>
<td>29,418</td>
<td>158,161</td>
</tr>
<tr>
<td>Wholesale</td>
<td>65</td>
<td>19,489</td>
<td>299,831</td>
</tr>
<tr>
<td>Other services</td>
<td>155</td>
<td>17,707</td>
<td>114,239</td>
</tr>
<tr>
<td>Admin, Support, Waste mngmt</td>
<td>72</td>
<td>15,286</td>
<td>212,306</td>
</tr>
<tr>
<td>Real Estate, Rental and Leasing</td>
<td>80</td>
<td>10,743</td>
<td>134,288</td>
</tr>
<tr>
<td>Transport and Warehousing</td>
<td>44</td>
<td>10,598</td>
<td>240,864</td>
</tr>
<tr>
<td>Finance and Insurance</td>
<td>60</td>
<td>8,177</td>
<td>136,283</td>
</tr>
<tr>
<td>Education services</td>
<td>25</td>
<td>8,062</td>
<td>322,480</td>
</tr>
<tr>
<td>Information</td>
<td>23</td>
<td>6,676</td>
<td>290,261</td>
</tr>
<tr>
<td>Arts, Enterntainment, and Recrueation</td>
<td>40</td>
<td>4,939</td>
<td>123,475</td>
</tr>
<tr>
<td>Agriculture, Forestry</td>
<td>46</td>
<td>4,374</td>
<td>95,087</td>
</tr>
<tr>
<td>Mining</td>
<td>11</td>
<td>3,895</td>
<td>354,091</td>
</tr>
<tr>
<td>Public Admin</td>
<td>5.6</td>
<td>1,197</td>
<td>213,750</td>
</tr>
<tr>
<td>Managemnt of Co and Enterprises</td>
<td>3.2</td>
<td>1,171</td>
<td>365,938</td>
</tr>
<tr>
<td>Utilities</td>
<td>3.2</td>
<td>1,028</td>
<td>321,250</td>
</tr>
</tbody>
</table>
Phase 3.5 – $484 billion to top up PPP and provide further health and hospital aid

- $310 billion additional funding for small business PPP program, to total $659 billion
  - $60 billion set aside for small banks
- $60 billion for disaster loans and grants
- $75 billion for hospital and healthcare provider coronavirus reimbursements
- $25 billion for expanded testing

Refill the bucket – or fix the holes?
Phase 3.5 – remaining questions

- SBA announced Sunday May 3 that $175 billion of second wave had been dispersed
  - 2.2 million loans, average loan size of $79,000
- Program effectiveness hampered by
  - Targeting: based on SEC filings, publicly traded companies received more than $1 billion in funds
  - Slow release and lack of clarity on guidelines and requirements for loan forgiveness
- Legislation being considered to loosen payroll requirements, allow more use for overhead, longer spend out
What is to come?

• Current debate on aid to states and local governments
  – States are paying unemployment insurance, other benefits
  – Delay in tax revenue until after July 15, lower anyway
  – Balanced budget amendments – don’t have federal borrowing authority or cost of funds
• Job training, childcare, housing (rent, landlords, buyers)
• Infrastructure: public, supply chain
• *Friday’s jobs report will focus the mind: expect 22 million unemployed (= all of job gains since last crisis), 16-22% unemployment rate (if low, look for falling labor force).*