How to Make Joe Biden's Budget Better

Part I: Send Money Now!

By Max B. Sawicky*

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Center for Economic and Policy Research
1611 Connecticut Ave. NW
Suite 400
Washington, DC 20009

Tel: 202-293-5380
Fax: 202-588-1356
https://cepr.net

*Max B. Sawicky is a writer and economist in Virginia. He has worked for the Economic Policy Institute and the US Government Accountability Office.

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Introduction

A new day in public policy beckons with the election of Joe Biden and Kamala Harris. There is much to do. Popular attention tends to focus on taxes and spending, but the Biden Administration will have additional, powerful tools at its disposal. These include regulations, mandates applying to state and local governments, executive orders, judicial appointments, and the administration of federal agencies. This paper confines itself to fiscal policy – the use of public spending and taxation. It will be released in three installments.

The first focuses on the urgency of immediate expenditure to deal with the financial crises afflicting families and state and local governments. The second will turn to longer-term considerations on public investment, including the Green New Deal. The third will discuss the roles that defense spending cuts and tax reform should play going forward.

The objective is to provide a guide for advocates, decision-makers, and the interested public. The hope is to lay out boundaries and guideposts that can be mutually recognized by the diverse interests that are clamoring for action by the incoming administration.

Our approach depends only on the fact that Joe Biden will be the next president. Some Democratic senators willing to vote for Democratic control of the Senate may not be willing to support important proposals coming from a Democratic White House. The hope is that this framework can be used to exert pressure on the new Congress as well as lay the basis for advocacy in the run-up to the 2022 midterm elections.

The popular demands are obvious and were reflected in President-Elect Biden's speech in Wilmington, Delaware on the night of November 7th: action to end the pandemic, restore the economy, combat climate change, and promote racial justice. There is no reason to quibble with these priorities. It should be understood, however, that they leave *everything* to the imagination when it comes to specifics. Beyond Biden's speech, his website fills out the picture of his proposals. In this paper, we try to peel a few more layers of the onion.

We begin by setting out the longer-term economic background for budget policy and trends within the budget itself. We then turn to the economic collapse of 2020, the use of relief measures, and the case for further, immediate action. Our intention is to discuss how ambitious, long-term policy ideas pertain to the current context for policy. We hope that readers find it useful, not only to press for better legislation in the coming year, but also to provide a vision for challenging current incumbents of both parties in future elections.

A Look Back: Economic Trends Since the Great Recession of 2007–2008

Ultimately, the source for public spending is the productive capacity of the economy as a whole. The potential for public sector expansion is often understated for ideological reasons, but there is no economics that does not recognize limits on public spending. The government can't buy more than the economy can produce.

In considering historic trends we choose December 2019 as an endpoint to avoid the distorting effects of the pandemic and the ensuing economic collapse in 2020. To avoid the confounding effect of very large numbers, we try to scale them appropriately and use relevant comparisons.

At the close of 2019, the US Gross Domestic Product (GDP) stood at over $19 trillion. (We rely on inflation adjustments that measure everything in 2012 dollars.) GDP growth after 2009 was consistent and significant. Employment rose from 130 million in December of 2009 to 152 million by 2019. But there are good reasons to think GDP could have been higher and grown more rapidly, with more aggressive policies following the financial meltdown of 2008. The post-2008 period acquires particular salience due to its similarity to the current moment, with another Democratic president taking office to oversee a difficult recovery from the disastrous policies of his predecessor.

The Obama Administration launched significant stimulus spending when it came into office in 2009, but its plans proved to be hampered by several erroneous assumptions.

One was that stimulus ought to be "timely, targeted, and temporary." This mantra presumed that a rapid V-shaped recovery was in store. It was not to be. The two prior downturns, from July 1990 to March 1991 and from March 2001 to November 2001, each lasted for eight months. The 2007-2009 slump began in December 2007 and did not abate until June of 2009, after 18 months.

In January of 2010, the Economic Report of the President forecast real growth rates for 2011–2013 exceeding four percent. The actual rates were 1.6, 1.5, and 2.6 percent, respectively.

By 2016, real GDP reached levels 17 percent higher than the depths of the recession in 2009, but only after seven years. The axioms of "timely and temporary" implied too narrow a window for fiscal activism. The vaunted benefits of targeting understated how widespread the slowdown became.

The second misconception was understating the determination of the Republican Congress to ensure the failure of all administration proposals. To be sure, discredit is also due to the Republicans themselves, who abandoned all traditions of bipartisanship. But part of the blame can be ascribed to the Obama administration, which continuously held out unfulfilled hopes for bipartisan collaboration.

How much more GDP might have been seen by 2019? Compared to the actual growth of 17 percent, the Congressional Budget Office projected a potential increase of 25 percent (comparing actual GDP in 2009 with the CBO estimate of "potential GDP," meaning GDP at full employment, in 2019). This could be regarded as a conservative estimate due to overstatement of the unemployment rate at full employment. Both the Congressional Budget Office and the Obama administration shared this error, projecting a long run unemployment rate of 5.2 percent.

Actual experience has shown the unemployment rate can be much lower. Moreover, under alternative assumptions about the structure of employment, it is possible to imagine workers under full employment being shifted to more productive jobs, making possible still higher GDP. In a similar vein, if unemployment rates for women, Black, and Hispanic workers matched those for white men, GDP would be higher still.

If we assume GDP returned to its trend prior to 2008, as indeed the Obama Administration and the Congressional Budget Office assumed in 2009 (it never did), and we apply the GDP growth rate from 2000 to 2008 to the level of GDP prior to the 2008 collapse, we could have seen $21 trillion by the end of 2019, rather than the actual level of roughly $19 trillion.

(There is no important change in GDP growth from its 2008–2016 trend for the first three years of Donald Trump's time in office. He really did inherit the Obama recovery.)

By the same token, we could compare the employment-population ratio (EPOP) of 61 percent in 2019 for the entire population to its prior peak of 64.7 percent in 2000. There is no reason it could not have exceeded 61percent. (The increased average age of the population, which means more retirees, does not explain the fall in the EPOP, admittedly a smaller one, for prime-age (25–54) workers.)

As noted above, the mere number of employed workers may also understate the growth potential of the economy since it is possible that under different policies, workers might be in more productive jobs. We will return to this in Part II, in our discussion of public investment and the Green New Deal.

The COVID Cliff

At the start of 2020, GDP was $19 trillion (in 2012 dollars) and national employment peaked in February at almost 152 million. The most recent figures are a GDP of about $18.6 trillion and employment of 143 million. In other words, a ballpark estimate of slack in the economy suggests roughly half a trillion dollars or nine million jobs. We have elaborated above why these could be very conservative estimates.

Elise Gould estimated that absent the COVID-19 crisis, by November of 2020, employment could have been obtained by an additional thirteen million workers.[1] In the same vein, we could have expected growth beyond the $19 trillion level over the course of 2020. Now the public sector can and should make up the difference. The means to accomplish this is deficit spending.

By now it is well understood that umbrage over budget deficits is selectively taken by Republicans, depending upon which party occupies the White House. The incoming Biden Administration can look forward to a claque of born-again deficit hawks who were nowhere

1 Gould 2020.

to be found in the face of burgeoning defense budget growth and tax cuts proposed by Republican presidents.

For their part, some Democrats may be conflicted over their assigned role of budget clean-up brigade and their apprehensions over the genuine harm that deficits might eventually bring. The usual fear is that higher borrowing causes interest rates to rise and discourages business investment. This fear has been decisively refuted by the past 40 years of experience, as higher budget deficits were accompanied by steadily falling interest rates. Still, some Democratic economists who might serve in the Biden Administration may harbor a fondness for the old canards.

For example, the well-regarded Janet Yellen, former head of the Federal Reserve Board of Governors, will be nominated by Biden for Secretary of the Treasury. Well before the economic slowdown of 2020 was visible, she was forthright about the dangers, as she saw them, of the long-term trajectory of the national debt. (Like many economists, she is also adamant about the need for deficit spending in the near term.)

It is certainly the case that in long-term projections of the economy and budget, federal debt grows to unprecedented levels. There are good reasons to ignore such projections.

- As Yogi Berra may or may not have said, "Predictions are hard – especially about the future." The long-term projections are utter speculation. A very small change in assumptions on parameters whose future values are unknown can radically alter imagined outcomes. Furman and Summers (2020) note that predictions of deficits even within a decade's passing by the Congressional Budget Office have been repeatedly wrong.
- These days, the recession tends to quiet any talk of deficit reduction. However, the purported specter of long-run insolvency tends to exaggerate expectations of rapid economic recovery and make more urgent the onset of austerity measures. In other words, the long-term debt story centers a dark cloud over current initiatives to expand public investment. This explained some of the attenuation of stimulus fervor on the part of the Obama Administration in 2010 and thereafter.
- It is widely recognized, if not as widely acknowledged, that the US government cannot go bankrupt due to debts incurred in its own currency. Once the insolvency bugaboo is dismissed, the remaining concerns about excessive US borrowing causing interest rates to spike are decisively debunked by the historical record.

Currently, interest rates are at historic lows. These levels, which prevailed prior to the onset of the pandemic, signal a high savings level as well as a dearth of private investment opportunities. By contrast, these same low interest rates point to a plethora of productive investments in the public sector. As Biden adviser Jared Bernstein points out, cheaper capital signifies the profitability (in terms of benefits exceeding costs) of a higher volume of public investment.[2]

Notwithstanding the new opportunities for profitable public investment, it is not the most important consideration of the moment. Tens of millions of families are suffering from lost income, lack of health insurance coverage, and threats of eviction or mortgage foreclosure. The immediate priority for them, and for the country, is money and other financial assistance.

There is a second emergency building – the fiscal crisis in state and local governments. They suffered a triple impact in 2020, first in the loss of routine revenues due to the economic downturn, second from the added public expenses associated with the pandemic response, and third from the added spending needs during a recession for anti-poverty programs, particularly Medicaid. These problems afflict all states alike. There is no foundation to charges from the president and Senator McConnell that budget problems are confined to "Democrat states."

Failure to respond to the immediate crises of families and state and local governments drives the economy into a deeper hole and prolongs the span of recovery. The first step in "building back better" is providing sufficient, immediate stimulus. Furman and Summers suggest $3.5 trillion, phased in over three years.[3]

The current economic downturn will not be the last. When it comes to both aid to individuals or to state and local governments, the institution of automatic stabilizers would ensure timely responses to the next crisis. Prior agreement on such provisions would also eliminate the need for time consuming debates on when to begin and withdraw the additional support.

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2 Bernstein 2020.
3 Furman and Summers 2020.

Initial Responses to the Recession

The federal government acted with unusual speed to address the economic downturn, beginning on March 6th by enacting the Coronavirus Preparedness and Response Supplemental Appropriations Act, and just 12 days later, the Families First Coronavirus Response Act, and again on March 27th with the Coronavirus Aid, Relief, and Economic Security Act (CARES). The legislation included an expansion of unemployment benefits, cash payments to families (excluding some immigrants), a fund for aid to state and local governments, and additional funds to programs relevant to the pandemic.

The Center on Budget and Policy Priorities pointed out that the largest of the three measures, the CARES Act, with a cost exceeding $2 trillion, allotted limited assistance for those with health costs stemming from the virus, among other shortcomings, an odd oversight in the teeth of a pandemic.[4] Its shortcomings aside, the act did increase GDP, by one estimate in the amount of five percent. It also provided significant cash relief. As of this writing, much of that relief was due to expire at the end of 2020.

Remembering "The Poor"

Poverty is not a dilemma for a narrow slice of the population. We need a different understanding of the concept, one that departs from the sympathetic, landmark treatment by Michael Harrington (1962) in "The Other America." Ever since, there has been a tendency to think of poor people as "other," a group apart from mainstream, middle-class America. (The poor are "them," while those reading about the poor are "us.")

People falling under the conventional classification of poverty, as defined in the US as an outdated, simplistic annual income threshold, is a dynamic, constantly changing group, especially in this year of deep recession. Being poor, if only briefly, can happen to almost anybody. The number of those who move in and out of poverty greatly exceeds the number

4 Parrott et al. 2020.

classified as poor at any moment. A brief passage through poverty can have seriously negative long-term consequences. Even temporary poverty can give rise to bankruptcy, eviction, mortgage foreclosure, or failure to obtain necessary medical treatment, among other maladies.

It makes more sense to understand those experiencing poverty in broader terms. For our purposes, those who must rely on employment for income, and who now lack both, are better understood as part of the working-class. The narrower the definition of "the poor," the greater the associated stigma and the less government assistance is implied. Narrow definitions of need are especially out of step with the current economic morass.

More than a mere change in terminology is implied. The remedies for families in financial distress need to be as broad as the constituency in question and as great as the scope of the problem. You can't put out a forest fire with a water pistol. By June 2020, the number of workers claiming unemployment benefits had risen from about two million in the beginning of March to over 32 million. It remains at over 20 million at the start of December 2020. Heidi Shierholz notes that programs providing aid to 13 million of these workers will expire by the end of 2020.[5]

The catastrophic job losses in 2020 certainly command one's attention, but it should not obscure the longer-term, secular trend of increasing precarity: the tendency of employment to be less secure due to irregular work arrangements, reduced job security, and the absence of fringe benefits. At least one important cause has been the decline of trade unionism and the protections it provides.

The need for income support is manifest. The proper question is how best to do it.

Income Guarantees, American Style

The US public sector already provides a number of programs to guarantee their beneficiaries a minimum income. Some are classified as social insurance, while others are seen as part of the

5 Shierholz 2020.

safety net. The former reflects benefits that are earned, in light of the beneficiaries' prior contributions via the payroll tax. The latter are not, and are subject to stigma for that reason, notwithstanding the fact that every US resident pays some taxes. In fact, some immigrants' payroll taxes finance programs for which they are ineligible. Safety net benefits are restricted by means testing, under which assistance is targeted to those with low incomes and reduced for those with somewhat higher incomes or greater assets. Even so, gaps in the American system of income guarantees are notorious. The greatest has always been the absence of aid for able-bodied workers and their children who, for one reason or another, are not able to maintain employment or minimally decent levels of income.

A milestone in the dearth of assistance was reached in 1996, in the form of the Clinton Administration's misbegotten "welfare reform." The ultimate consequence was the virtual elimination of cash assistance formerly provided under Aid to Families with Dependent Children (AFDC), especially in southern states containing multitudes of low-income families. In recent years, state governments have also reduced the level and duration of unemployment benefits. Partially offsetting these cuts was a significant expansion of the Earned Income Tax Credit, limited to employed workers, carried through by the Clinton Administration.

At the same time, some safety net benefits of the "in-kind" type have endured or even blossomed in terms of spending levels. The two largest such programs are Medicaid and the Supplemental Nutrition Assistance Program (SNAP, formerly called food stamps). (In the case of payments to medical providers, spending increases do not necessarily equate to increased benefits for patients, considering the outsize inflation of health care costs.)

For their part, the "in-kind" programs have generally expanded in the recessions of 2007–2008 and 2020, but they are not enough. Notwithstanding the increased enrollment in SNAP, for instance, food insecurity has been exacerbated in the pandemic. There have been news reports of multitudes of families resorting to food banks. A great many families lacking health insurance coverage remained ineligible for Medicaid, though this gap was filled to some extent by Obama's Affordable Care Act.

In any case, families still need cash to pay for housing and other basic needs. The inability to meet some financial obligations, such as rent or medical bills, can cause families to tumble into deeper, more lasting financial distress.

A reduction in income, and consequently purchasing power, tends to push the economy down a negative spiral. Less spending causes greater job loss, and greater unemployment causes further spending reductions. Accordingly, income guarantees face the dual objectives of alleviating families' financial distress and stimulating the economy. The former objective depends on one's subjective view of what the income threshold is for avoiding distress. The latter is more of an analytical problem that macroeconomics seeks to answer what sort of aid generates the biggest "bang for the buck" in terms of the recovery of employment and the GDP.

In either case, aid is more justifiable the lower the recipient's income. Reduced income, if not the utter lack of income, usually commands more sympathy as a sign of distress. In economic models, lower income persons devote more of any assistance they receive to immediate expenditures, which is desirable for a more rapid economic recovery.

Cash Aid Now

The need for cash assistance has ballooned along with the recession. It could be argued that assuming the downturn is temporary, considering the promise of vaccines around the corner, the response should be as well. The fact remains, the downturn is not over. It would make more sense to keep aid flowing on automatic pilot until it can be shown to be no longer needed. At a minimum, that would argue for an extension of the measures in the CARES Act for direct payments to individuals and households, including continued expansion of unemployment benefits, paid sick leave, and cash payments to individuals and families with children. At the time of this writing, limited compromise measures have been enacted.

Another approach to providing financial relief to individuals and families that has grown in popularity is some kind of reduction, if not outright abolition, of different types of debt. Reduction or elimination of debt is tantamount to cash assistance, since it frees up cash otherwise committed to debt repayment. Reduction of debts owed to businesses, including landlords or medical care providers, is beyond the scope of this paper.

Student loans may be owed directly to the government, so reduction or abolition belongs in our context. Usually, this option is mentioned as a reform the Biden Administration could undertake that would not require the assent of the Congress. Debates over such a program dwell on the same questions noted above: who suffers the economic distress that justifies loan forgiveness, and what would be the economic impact?

There should be little doubt that most any sort of debt reduction would boost GDP. Under normal circumstances, that would be irrelevant in and of itself. Many different programs could boost GDP. The pertinent question would be which has the greatest stimulus effect.

As far as stimulus is concerned, a leading rationale for student debt reduction is that it could be done quickly by the next president, without the assent of Congress. That only speaks to the merits of the measure to a limited extent.

There are conflicting views on who needs loan forgiveness the most. Some of those who had paid off their loans would be resentful. So would some who were never able to afford college in the first place. Others with small loans who could not afford to attend schools with expensive tuitions might disapprove of the greater indulgence granted to those with loans incurred from attending elite institutions. To some degree, the greater a family's financial means, the more of a student loan is available. The bigger one's loan, the more abolition of the entirety of student debt would be beneficial. And finally, what about loans taken out in the future? We cannot hope to resolve such issues here, but it seems safe to say the determination of eligibility would be politically divisive.

More analytically tractable is the question of the distributional impact of alternative schemes. The most common criticism is that total loan forgiveness would be a kind of reverse redistribution. This view has been subject to criticism, which we will not try to dissect here.[6] Suffice to say that if indeed loan forgiveness is the only option available to the next president, at least in the short term for the sake of stimulus and relieving the financial burdens of some families, it is probably better than nothing.

Popular treatments of debt elimination usually gloss over the difficult analyses of this issue, preferring to dwell on the undeniable fact that many persons of limited means face

[6] Steinbaum 2020.

mandatory repayment obligations that oblige them to forego or postpone other decisions, such as saving for the future, having children, or purchasing a house.

From the standpoint of policy, the expenditure implied by debt relief might be better applied to alternative uses, assuming a cooperative US Senate, in keeping with the objective of fostering a less unequal distribution of wealth. Insofar as debt relief extends to families regardless of their income or wealth, its value as stimulus is undermined. The greater one's income, the less likely it is that a reduction in student debt will affect one's day-to-day spending habits.

Compared to the total abolition of debt, there is little doubt that less sweeping reforms would provide progressive relief. Tenable reforms include providing a cap on the amount of debt reduction provided to all borrowers, a more liberal schedule of required payments as a share of income (Lower payments for lower incomes are already permitted; they could be reduced further.), a reduction in the time period over which payments were required, or the ability to discharge such debts through bankruptcy.

A contrary view of priorities in the face of the current emergency is founded on the axiom of never letting a crisis go to waste. The current need for income support makes politically conceivable a permanent expansion – the inauguration of a universal guaranteed minimum income.

The UBI Mirage

In recent years, thanks in part to the 2020 presidential campaign of Andrew Yang, the idea of a Universal Basic Income (UBI) has become popular. Often the UBI is discussed as the only way to provide an income guarantee. At the same time, other ways of providing guarantees are misleadingly described as a UBI.

To be precise, a UBI is what used to be called a "demogrant." It was a controversial tenet in the presidential campaign of Senator George McGovern in 1972. Under a UBI, a broad section of the population would receive an unconditional cash payment on a regular basis. Yang campaigned for a benefit of $1,000 a month to all US citizens over 18.

The UBI is usually touted as politically uncontroversial ("everybody" gets it), favorable to work incentives (unlike welfare, the amount does not change with a recipient's income), and easy to pay for. Unfortunately, none of these claims are true. The basic concept suffers from fatal logical inconsistencies. A UBI would be neither universal nor basic. It would not necessarily be popular, and it is not without negative work incentives.

On the simplest level, a UBI that would truly be basic, in the sense of providing a minimally adequate income, would be improbably high in cost. There is more than a little room for disagreement that Yang's $12,000 a year, with nothing for children, would be adequate. That aside, in fiscal year 2020, federal outlays were $6.6 trillion. Advocates for a UBI estimated that Yang's UBI for adult citizens would cost in the neighborhood of $3 trillion. Either a huge segment of existing federal spending would have to be eliminated, or some combination of higher taxes and higher deficits would be required. Note that anything financed by a cut in some other type of spending is still financed by taxes or borrowing, just as the other spending was.

The likely need for higher taxes or deficits also exposes the fallacious idea that a cash benefit entailing extremely high budgetary outlays would be innocent of work disincentives. One way or another, the taxes used to finance such a UBI would carry some kind of work disincentive. We mention this not because we are worried about such disincentives – we aren't – but because this illusory feature of UBI is frequently invoked in its defense.

The universal feature of the UBI is thought to eliminate conflicts among groups, in contrast to means tested programs that are associated with net taxpayers (those whose federal taxes exceed their UBI benefit) and net benefit recipients. One way or another, the UBI is paid for with taxes. There is always a Peter who is enlisted to pay Paul. Moreover, we could expect ferocious arguments over the eligibility of immigrants, the mentally disabled, the homeless, and the incarcerated.

An alternative to the UBI is a negative income tax (NIT). It could be as broadly or narrowly targeted as desired. Basically, it consists of a cash benefit that decreases, the higher an eligible recipient's income.

SNAP is an example of an NIT for which the benefits provided are dedicated to purchases of food. It is beset with complicated rules and restrictions which would be best dispensed with.

The Earned Income Tax Credit works like an NIT, but it is restricted to those with labor earnings. Ideally, a new, unrestricted NIT would rescue those left stranded by the welfare reform of 1996, especially families with children without access to any other sort of income guarantee.

Some proposals for an income guarantee go by names such as a family allowance or a children's allowance. These are typically conceived of as universal and open-ended, with no benefit reduction for those with higher incomes. As we have seen previously, however, *any such program is really a buried NIT*. Given the specifics of such a program, once taxes are taken into account, it will be possible to highlight who is a net payer and who is a net beneficiary. Critics of such programs will not be reticent about pointing out such details.

Many in need lack eligibility for any existing income guarantees. Something additional is needed. An explicit NIT is a necessary objective. It could be called a family allowance, or even a UBI. The reality is that it will be financed with taxes, and the broader its eligibility, the more of it will have to be reclaimed with taxes. The greater the extent of money that makes a "round trip" (from government to beneficiary back to government), the greater the burden on tax administration and the greater the loss from tax avoidance or evasion. A less-than-universal NIT, in terms of eligibility, can be more generous and easier to implement.

There will be debates about how much coverage an income guarantee should provide, and for whom, but once the unrealism of the typical UBI proposals is set aside, it should be possible to design a plausible NIT that can fit inside the federal budget. Once again, the current crisis of mass income loss, sudden poverty, if you will, could spur the inauguration of a universal guaranteed minimum income.

Our Poor Relations: The States

State and local governments (SLGs) provide most public services in the US. The federal government's role is largely confined to mailing checks to individuals and health care providers and maintaining a defense and law enforcement establishment. Wags have described the federal government as a huge insurance company with an army.

As noted above, SLGs finances have been victimized by three shocks in 2020. One is the reduction in routine revenues, due to the recession and the decline in oil prices. Two is the added expenses incurred because of recessions, such as spending on Medicaid. And three is the added costs specifically due to the pandemic. The Dallas Federal Reserve estimated a proliferation of budget shortfalls in the neighborhood of 10 percent.[7]

SLGs aid in the pandemic relief legislation in 2020 was limited to the $150 billion fund under the CARES Act. The holes created in their budgets were much larger, and those shortfalls will persist into 2021, and thereafter.

Aside from carrying most of the responsibility for public service provision, SLGs also host the bulk of public fixed capital, chiefly roads, school buildings, and transit infrastructure. These roles incidentally imply a similarly dominant role in providing services and maintaining infrastructure associated with a Green New Deal. We return to this subject in Part II.

In recessions, state budget shortfalls tend to be "paid for" by lapses in the upkeep of fixed capital. SLG politicians prefer to postpone maintenance for the sake of maintaining employment and current services. Of course, what is not paid for now will require somewhat greater outlays later, since the depreciation of facilities doesn't take a time-out during recessions.

The decade prior to 2020 provides a dismal precedent for the current outlook. The Pew Trust found that by 2019, state governments had still not returned to the level of their tax collections, adjusted for inflation, prior to the great recession of 2007–2008.[8] Over roughly

7 Saving 2020.
8 Fehr 2019.

the same period (2010–2020), federal grants to SLGs for discretionary spending (excluding Medicaid, in particular) fell significantly.

A repeat of this scenario, described as a "lost decade" for the states, would drive SLGs into a deeper hole, leading to cuts in services and added failure to maintain capital facilities. Typically, austerity measures by state governments entail cuts in the support of local governments. The scope for new initiatives in the states, especially in the field of public health made necessary by the pandemic, would be dim, especially if must resign ourselves to the long-standing stagnation of federal aid to state and local governments.

On the spending side, Pew reported that the greatest victim of SLG spending cuts was aid to higher education. That meant students' families had to pay more out of pocket for fees and tuition to public colleges and universities, a trend relevant to the question of student debt relief discussed above.

For SLGs, 2019 was *before* the bottom dropped out of their finances. From March to August of 2020, a shortfall of more than eight percent of expected state government revenues was estimated. We could expect additional effects on local governments. For fiscal year 2021 (state government fiscal years usually run from July to June), Moody's Analytics estimated a shortfall between $153 and $203 billion from tax revenue declines and increases in Medicaid expenditures.[9]

How much do SLGs require? The Moody's estimate was premised on the pandemic subsiding by September 2020. The combined and estimated losses in fiscal years 20 and 21 are well above the $150 billion fund provided by the CARES Act. If we go by the yardstick suggested by the Dallas Fed, a 10 percent shortfall on spending in the amount of the 2018 level of $3.8 trillion, assuming some ordinary growth from 2018 to 2021, takes us to a need of about $400 billion. Bivens estimates a requirement of $500 billion annually through 2022.[10]

In keeping with the gambit of turning crisis into opportunity, the recession can also prompt policy makers to consider a revival of permanent federal fiscal assistance to state and local governments, formerly known as revenue sharing.

9 White, Crane, and Seltz 2020.
10 Bivens 2020.

There are two basic rationales for revenue sharing.

One is to offset long-term pressure on SLGs, including from the lost decade cited above, and a variety of longer-term factors.[11] Examples of these long-term pressures include the shift in retail purchases away from taxable goods bought at bricks and mortar stores to services and to online transactions. Another is the impact of the extraordinary growth of health care costs on Medicaid, the second-largest item in state government budgets.

The other rationale for revenue sharing is to fight recessions. Because SLGs are required to balance their budgets, they are obliged to enact fiscal policies that make recessions worse. In other words, they have to increase taxes and reduce spending to make up for the effects of downturns, which amounts to stimulus in reverse.

It remains for the federal government to forestall such contractionary effects on GDP by having a program that automatically allocates increased, timely assistance to states in the greatest economic difficulties. The Affordable Care Act included such a provision, but it was a temporary measure.

A formula grant program could provide ongoing fiscal assistance that increased in a timely fashion, according to individual states' economic circumstances and factors pertaining to their fiscal capacities and needs.[12] The overhead requirements for such a program on the federal end would be minimal, as was the case for the old revenue sharing program in the 1980s.

Conclusion

The pandemic imposes other demands on the federal government not discussed here. First and foremost, we need a plan to limit and beat back the spread of the virus until adequate vaccine distribution has been accomplished. Those suddenly lacking health insurance coverage will need safe harbor until more permanent solutions are established.

In this paper, we focus on cash assistance to families and to state and local governments.

11 Sawicky 1999.
12 Department of the Treasury 1985; GAO 2011.

Families relying on jobs and businesses that have been obliterated by the pandemic need income to tide them over. We have suggested this need is also a political opportunity to provide a more lasting program of guaranteed income.

State and local governments need aid to replace lost tax revenue, to defray added public service costs (particularly for the Medicaid program), and for pandemic-related expenses. Cutbacks in basic public services that we ordinarily take for granted, but that provide the essentials of a civilized life, would especially hurt those also most in need of cash assistance. The two really serve the same, broad constituency. Here as well, there is a political opportunity to institute a permanent program of fiscal assistance to avoid the dilemma of "waiting to fix the roof, until it is raining."

Both types of aid would play a crucial role in reviving the economy. As far as federal fiscal policy is concerned, there really is no more urgent pair of priorities. The first step in rebuilding is to avoid falling into a deeper hole.

In Part II, we discuss longer-term priorities in the field of public investment in the framework of a Green New Deal.

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