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Brookings economist and IRP affiliate Gary Burtless presented a lecture at IRP on November 19, 2009, on "Recession and Redistribution: The Economy, Public Policy, and the Poor." His talk, summarized in this issue of Fast Focus, represents one presentation in IRP's continuing series on the "Reorganization of Social Policy in a Recession," an interdisciplinary seminar series that brings distinguished researchers from other institutions to the UW–Madison campus to present their work on designing and evaluating public policies that support people in the current recession and on the net effects of those policies on vulnerable (especially poor) children and families. Support for the series is provided by the Office of the Assistant Secretary for Planning and Evaluation in the U.S. Department of Health and Human Services.

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The "Great Recession" and redistribution: Federal antipoverty policies

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Economists agree that the current recession ranks with the worst economic crises since World War II, and that it is taking a terrible toll on most Americans, but few analysts equate it with the Great Depression of the 1930s. The "Great Recession" would be more apt. Times are hard, but not dustbowl hard.[1]

How much is the federal government doing to mitigate the recession's effects, especially for the most vulnerable individuals and families? In this fiscal year, special Congressional actions will amount to more than 2 1/2 percent of U.S. output, and the extra spending and special tax cuts will almost certainly continue for a couple of more years. Do these efforts represent extraordinary departures for public policy? Yes and no. Some automatic responses to economic downturns are built into law; nonetheless, in the current crisis the Obama Administration and Congress have taken extraordinary discretionary steps—many of which are codified in the American Recovery and Reinvestment Act of 2009 (ARRA)—that represent firsts in the federal government's response. More actions are likely in the coming months.

The ARRA and the Worker, Homeownership, and Business Assistance Act of 2009, for example, extended unemployment insurance (UI) benefits to an unprecedented 22 months (the normal limit is 6 months). The ARRA also provided tax cuts to households and businesses and benefit increases to food stamp recipients. These kinds of actions represent standard responses to recessions. In a departure, spending on infrastructure, a common anti-recession approach to recovery in the past, has been negligible so far.

In addition to these traditional actions, the Obama Administration also has introduced several unprecedented policies to counteract the recession: provision of generous health insurance subsidies to pay a portion of the insurance-continuation premiums of laid-off workers and their families; massive grants to state governments to fund, for example, money for Medicaid and SCHIP, as well as emergency Temporary Assistance to Needy Families (TANF) cash assistance for the poorest families with children; and an extraordinary emphasis on protecting education and training spending in state budgets.

The economic situation

So, just how bad is it? The best indicator of the severity of the crisis is the unemployment rate, which, for workers aged 25 to 54 (who form the vast majority of the workforce) is now comparable to the worst rate of the post-war period. It is not yet higher, however, than the unemployment rate attained in the 1981–1982 recession. In fact, a comparison of the development of the unemployment rate in the 2008–2009 and the 1981–1982 recessions after the preceding period of economic expansion shows that the current recession started out slower than its predecessor, but then picked up momentum. As of the 22nd month after the recession's onset, the cumulative rise in unemployment is almost 2 1/2 percentage points higher now than it was in the 1981–1982 recession.

Examining the impact of the recession on American households' real per capita private income (i.e., wages, other employer fringe benefits such as pensions and health insurance, self-employment income from businesses and farms; interest and dividend payments; and income from rents) between December 2007 and September 2009 reveals a significant loss of private income. If the index of private income was set at 100 in December 2007, the last month of the decade's economic expansion, by September 2009, it had dropped to 91.5, a sizeable decline by any standard. Even workers who held onto their job in this recession have suffered substantial losses in household wealth, assuming they owned real estate, stocks, or bonds not guaranteed by the U.S. Treasury.

In response to the decline in private income and household wealth, private consumption has declined as well. The 2008–2009 fall in the percentage change in real consumption measured relative to consumption of 12 months earlier is the biggest in the post-war era since the Korean War. This compares to the last recession, in 2001, when consumption never fell below the previous year's level; and in 1990–1991, when it barely dipped to a negative level at all.

What does the United States do to protect against the downside of a recession, and how does this protection compare with that available in the rest of the world? Losing one's job—the worst downside of a recession—is one of the few effects that our safety net protects us against. There is no insurance against, for example, losing 50 percent of the value of your home or stock portfolio. Let's compare U.S. unemployment benefits to those provided by 21 other rich nations in the Organization for Economic Cooperation and Development (OECD). During the first 6 months after a layoff, U.S. unemployment benefits replace about 60 percent of the after-tax value of a worker's lost wages. We rank 14th among 22 OECD countries. Greece, Ireland, and Great Britain are among the seven nation's whose UI benefits are less generous than ours; Germany, France, Italy, and Canada are among the 13 nations providing higher benefits. Switzerland and Portugal are at the top of the heap, providing 78 percent and 80 percent, respectively, of after-tax value of worker's wages over the first 6 months after a layoff.

Although the United States ranks in the bottom third for the amount of UI benefits, it is competing with the United Kingdom for the very bottom of the list in a comparison of duration of UI benefits. In ordinary times, UI benefits in the United States are limited to just 6 months. At the moment, U.S. workers in states with high unemployment can receive up to 99 weeks (22.8 months) of unemployment benefits as a result of temporary federally funded programs. For workers suffering long-term unemployment, the result of somewhat lower-than-average weekly UI benefits and exceptionally brief duration of benefits amounts to fairly weak social protection. The OECD has calculated how much protection laid off workers receive if their joblessness lasts 5 years. Compared to 22 other rich OECD nations, the United States ranks 19th, ahead of only Italy and Greece, and well behind its other peers in regard to duration of UI benefits.

Figure 1 shows the percentage of the U.S. unemployed who have been jobless for 27 or more weeks between 1960 and August 2009, in successive recessions and successive economic booms. Clearly, the brief duration of benefits represents a problem for workers, especially those who remain unemployed for 6 months or more. The percentage of workers who have been unemployed longer than 6 months spikes late in every recession, and, over the years, that spike has gotten higher. By November 2009, more than 38 percent of the unemployed, a post-World-War-II record, had been jobless for 6 months or longer.

The changes in the economy have hurt younger men (under age 30) most, and especially the least educated, whose unemployment rate is at 25 percent—an all-time high.

Taken together, the spikes in long-term unemployment produce corresponding spikes in the percentage of UI claimants who run out of their regular benefits. In July 2008, we reached a new, 46-year record high UI exhaustion rate of 51 percent. Put another way, for the first time, more than half of the workers who file a first-time claim for UI benefits can expect to collect all 26 weeks of their standard benefits without finding a job.

Stimulus

Recent months have been exceptionally bad ones for American workers. What has the U.S. government done that is "special" for the unemployed in the current recession? In all recessions since the late 1950s the federal government has always stepped in to increase the potential duration of benefits, paying all extra costs to state UI systems. As we have seen, the federal government took the same step in this recession. In addition, it paid for an unusual weekly benefit hike (8 percent) and a first-time-ever subsidy of health-insurance-continuation premiums, covering 65 percent of the premium.

The government is helping the most disadvantaged by increasing monthly food stamp allotments, providing aid to

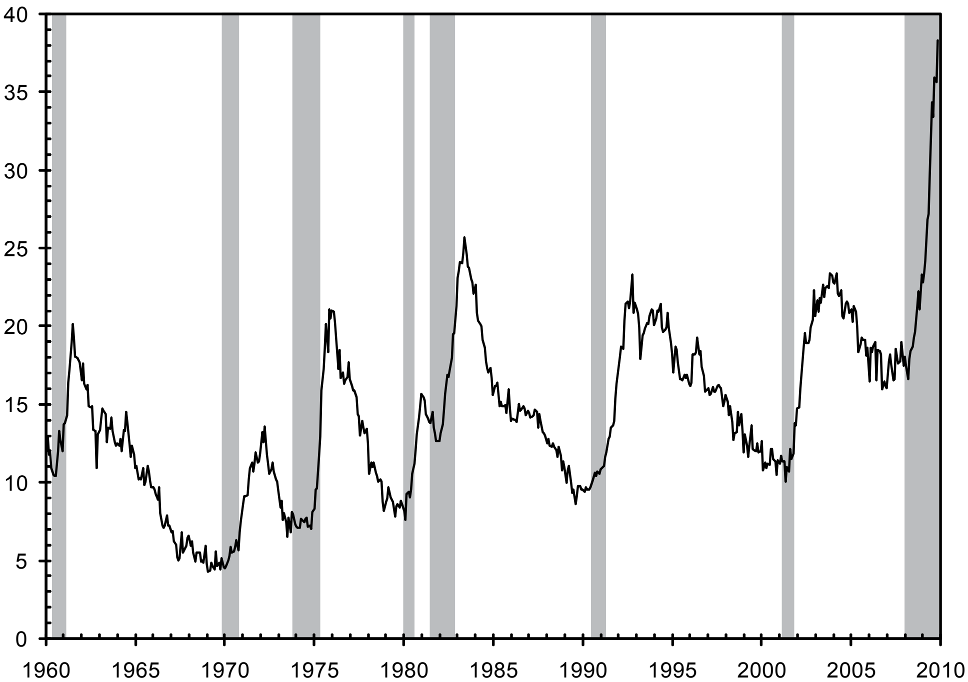

Figure 1. Percent of the unemployed who have been jobless for 27 or more weeks, 1960–November 2009.

Source: Author's tabulations of U.S. BLS data, downloaded December 8, 2009. Shaded areas indicate recession periods, from NBER.

states for social assistance to children, doubling the budget to train the unemployed and the hard-to-employ, and increasing the Earned Income Tax Credit—which economists John Karl Scholz, Robert Moffitt, and Benjamin Cowan identify as the nation's largest cash or near-cash antipoverty program—and the Child Tax Credit.[2] For those who are suffering but not desperate, the government is providing federal income tax cuts, special grants to Social Security and Veterans Affairs recipients, and Alternative Minimum Tax relief.

An analysis of the effect of government relief efforts so far reveals that personal taxes collected from households (including income tax, deductions for Social Security, Medicare, and unemployment insurance) plummeted in May 2008, because of the Bush Administration stimulus, and again in April 2009, in response to the falling economy, sharp income losses, and the Obama Administration stimulus package. Private income had fallen about 5 percent by summer 2009, and taxes fell about 20 percent.

The impact of the recession and stimulus package on government transfer payments has resulted in steady and large percentage increases in benefits, for example, in Supplemental Nutrition Assistance Program (SNAP or food stamps) and Social Security. In fact, Social Security has increased by about $25 billion more than population aging alone would have predicted, in large part as a safety net for older displaced workers. Meanwhile, unemployment insurance benefits have risen by a factor of four.

A comparison of loss in private incomes with increases in net government transfer payments since December 2007 reveals a drop of $572 billion in private incomes and an increase of $848 billion in net government transfers (at annual rates). Clearly, the huge swing in tax payments and transfer benefits has had a bigger impact on net household income than the drop in gross private incomes. Net *disposable* per capita household incomes were exactly the same in the second quarter as they were at the end of 2007, which was the peak of this decade's economic expansion. In the July through September quarter of 2009, real per capita disposable income was just 1.1 percent lower than it was at the end of the last expansion, even though real *private* per capita income declined a whopping 8.5 percent.

Figure 2 looks at the American Recovery and Reinvestment Act of 2009 stimulus spending through 2019, dividing expenditures into three categories: fiscal relief for state governments, direct income assistance and services, and investment in infrastructure and technology. Figure 3 looks at the timing of its effects from 2009–2015. The changes in spending levels over time are stark. In 2009–2010, the lion's share of spending is going to direct income assistance and services ($390 billion). Fiscal relief for state governments for schooling and Medicaid also starts out high in 2009–2010 ($129 billion), and then it will drop to $46 billion in 2011–2019. In the period from 2011 through 2019, expect a shift away from income assistance and services as well (down to $22 billion), and toward infrastructure and technology investment ($141 billion).

The timing of spending is such that the major effects are now just beginning to take hold in late 2009 and will peak in 2010 (Figure 3). Unless Congress enacts another stimulus package, spending will phase out rapidly after 2010.

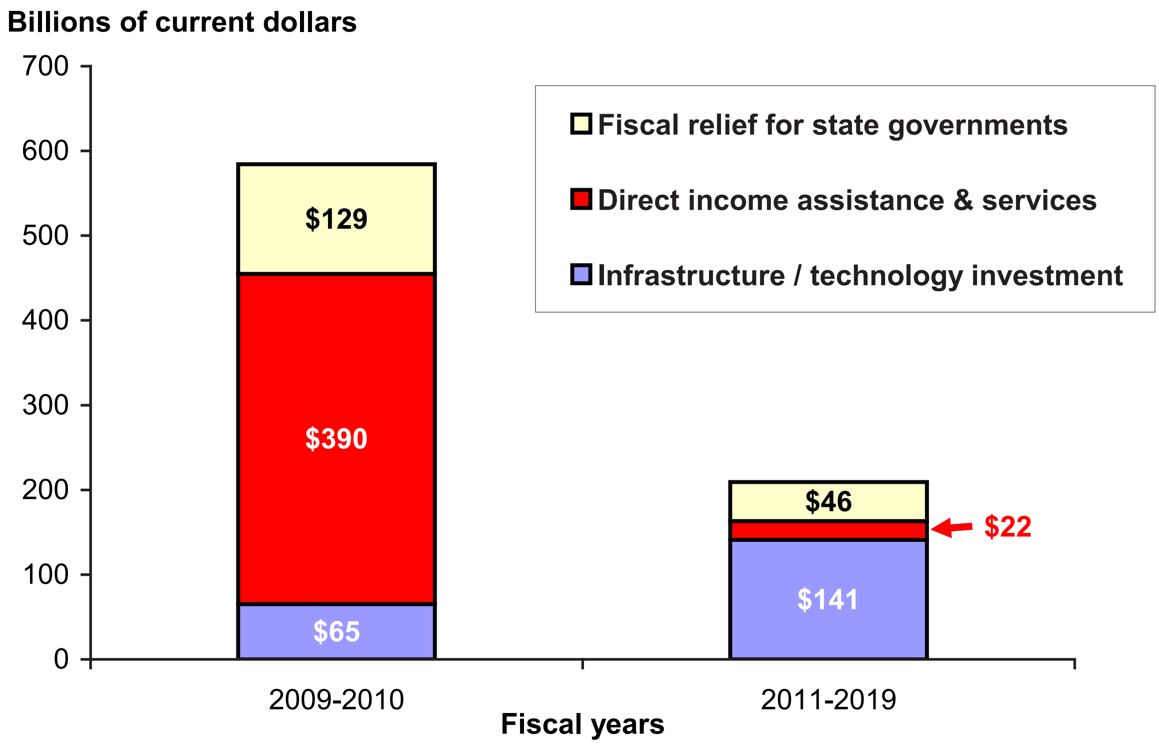

Figure 2. Expected Stimulus Spending under the American Recovery and Reinvestment Act of 2009, 2009–2019.

Source: Congressional Budget Office and Joint Committee on Taxation.

Many reporters and op-ed writers seem to think the best kind of anti-recession program puts shovels and hammers in workers' hands, gets them off the unemployment rolls, and produces a tangible public good—a smoother highway, a newer bridge, a refurbished school, a better insulated office or apartment. The current stimulus programs devote a relatively small percentage of outlays to such projects, especially in 2009 and 2010, when the recession is likely to be most severe. The ARRA and other federal stimulus spending on bricks and mortar projects is limited (see blue/bottom areas of Figures 2 and 3). Past experience with counter-cyclical infrastructure programs shows that if you spend the money quickly and without sufficient planning, you end up with projects of questionable value. It takes time to design, plan, and build high-quality infrastructure projects, and the bidding process takes time, as does finding qualified managers and a skilled workforce. If we expect this recession to last only a bit longer than the worst previous post-war recession, we don't have that kind of time.

Public infrastructure investment projects were much more successful in the Great Depression, when the bad times lasted for more than a decade. Many worthwhile projects were built through the Work Projects Administration (WPA), which was the largest New Deal agency. The WPA employed millions of people to carry out public works projects. Many communities still have a park, bridge, or school constructed by WPA workers. Indeed, many WPA structures are now considered national treasures and are protected as National Historic Landmarks. Public officials in the Great Depression had much more time to select, design, and build worthwhile projects than we have had in the typical post-war recession.

Despite the growth of aid to individuals, states, and localities in 2009 and 2010, by 2012 fiscal relief to state and local governments and direct income assistance to households will be largely phased out. This timing suggests that the major effects of the ARRA in increasing income assistance and state and local spending have already occurred or will occur in the next few months. If state budgets continue to deteriorate after 2010, another major dose of state and local fiscal relief may be needed.

Summary

Assessing the big picture of the Great Recession and the federal government's stimulus response, I applaud especially the Obama Administration's novel efforts. The expansion of unemployment insurance and the provision of a subsidy to cover the cost of health insurance continuation for workers who lose their insurance when they lose their jobs are worthwhile steps. I recommended both kinds of measures a couple of years before the recession began. When the severity of the likely recession became clear, I also urged the administration and Congress to consider programs to replace lost state and local funding for higher education. A deep recession is a good time for people aged 16 to 35 to invest in added education and in retraining. For many young adults, the biggest cost of going to school is the earnings they lose because they

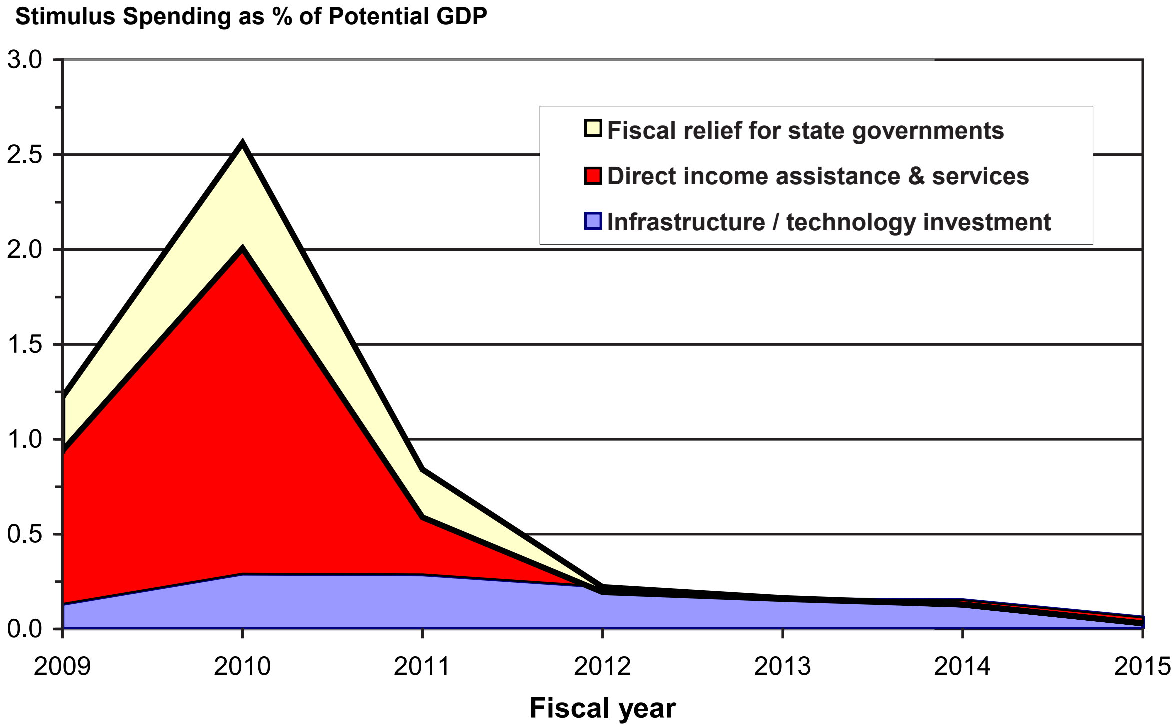

Figure 3. Expected Stimulus Spending under the American Recovery and Reinvestment Act of 2009, Fiscal Years 2009–2015.

Source: Congressional Budget Office and Joint Committee on Taxation.

are in a classroom rather than at work. When the unemployment rate tops 7 percent, this cost plummets for most laid-off workers. When jobs are almost impossible to find, an unemployed worker's "foregone earnings" while in school are essentially zero. Fortunately, the stimulus plan contains a highly unusual focus on protecting education and training funding. Also new is the large but time-limited federal aid to hard-pressed state governments. Even though this kind of fiscal relief is untested in a major recession, my guess is that it is a gamble with a high expected payoff.

A majority of respondents now tell pollsters they think the stimulus package has either made no difference to the economy or has actually made things worse. This assessment is wrong. Net household incomes and consumption are higher than they would have been without the stimulus, and essential state spending on benefits to the poor, health insurance, and education is higher than would have been the case without the federal aid. If Congress had rejected the Obama Administration's stimulus package the recovery would have begun later and joblessness would have increased faster. Even if the general public is unwilling to give the stimulus program even a gentleman's C, most economists, including me, think it deserves at least a B+.■

Sources for further reading

Research and commentary by Gary Burtless on the Brookings Institution Web site

Social Protection for the Economic Crisis: The U.S. Experience (July 15, 2009 [paper on which Burtless based his remarks])

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The Current Health of Financial Market Reform (September 14, 2009)

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Have the Stimulus Programs Failed? (August 04, 2009)

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Changing Poverty, Changing Policies, edited by Maria Cancian and Sheldon Danziger (September 2009, New York: Russell Sage Foundation)

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Stimulus for America's Community Colleges, Sara Goldrick-Rab and Alan Berube (February 3, 2009)

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[1]Burtless based his remarks in this brief on "Social Protection for the Economic Crisis: The U.S. Experience," available online at http://www.brookings.edu/papers/2009/0715_social_protection_burtless.aspx.

[2]See J. K. Scholz, R. Moffitt, and B. Cowan, "Trends in Income Support," (pp. 203–241) in *Changing Poverty, Changing Policies*, eds. M. Cancian and S. Danziger (New York: Russell Sage Foundation, September 2009).

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