The Brookings Institution
Recession Remedies Podcast

"How did expanded Unemployment Insurance affect the COVID-19 economy?"

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Episode Summary:

In response to the COVID-19 pandemic, the U.S. government implemented the largest expansion in federal unemployment insurance (UI) benefits in U.S. history. Did expanded UI reach those who needed help? Did it stimulate the economy? And did it disincentivize people from looking for work as the pandemic abated? Fiona Greig, managing director and co-president of the JPMorgan Chase Institute, and Pascal Noel, Neubauer Family Assistant Professor of Finance at the University of Chicago Booth School of Business, join host David Wessel to discuss lessons learned about unemployment insurance.

WESSEL: Welcome to the Recession Remedies podcast, exploring lessons learned from the economic policy response to the COVID-19 pandemic. I'm David Wessel.

In response to the pandemic, the U.S. government launched what's probably the largest expansion in history of federal unemployment insurance benefits, increasing the duration, the amount and the number of people eligible, at a cost to the federal government of roughly $700 billion. Did expanded unemployment insurance reach those who really needed help? Did it stimulate the economy? Did it discourage people from looking for work as the pandemic abated?

I'm going to put those questions today to Fiona Greig and Pascal Noel. Fiona's the managing director and co-president of the JPMorgan Chase Institute. And Pascal is the Neubauer Family Assistant Professor of Finance at the University of Chicago's Booth School of Business. They were among the authors of the chapter on unemployment insurance in our *Recession Remedies* book, which you can read for free at Brookings Dot Edu Forward Slash Recession Remedies.

Fiona, let me start with you. Unemployment insurance in the U.S. dates to the 1930s. It's a way to replace wages of people who lose their jobs. What were the most important changes that were made to UI during the COVID pandemic?

GREIG: That's a great question, I mean, normally in a recession, a typical thing we do is to extend the duration of UI benefits. What was new and dramatic this time was that we did two things: we increased the level of benefits. For many workers, actually, they were receiving more in unemployment insurance benefits than they had been earning prior to losing their job with the $600 supplement and the $300 supplements.

The second thing we did, though, is that we dramatically expanded eligibility. Through the Pandemic Unemployment Assistance Program, people who are unemployed, people who were self-employed, gig workers, people who were experiencing COVID themselves or caring for others, newly became eligible for unemployment insurance. And just to give you a sense of just how big these expansions were, as a share of labor income, never before had UI represented more than a couple percent. But during the pandemic, it represented 9 percent of labor income, which was four fold than ever before. And that pandemic unemployment assistance program actually accounted for about 40 percent of claims. So these were very big expansions in the unemployment insurance program.

WESSEL: Well if I added up all the wages paid in the economy, unemployment insurance represented at the peak 9 percent of that?

GREIG: That's right.

WESSEL: Right. Pascal, unemployment insurance has two benefits. One is to stimulate the economy in a recession by providing money for people to spend and getting the economy moving again. And the second is to help laid-off workers pay for rent and groceries, and so forth.

So let's start with the first. How good a job did unemployment insurance do in pulling us out of the very short but sharp recession caused by COVID-19, especially relative to the stimulus checks, the economic impact payments?

NOEL: So, what the evidence shows is that households who received these unemployment insurance payments spent a large fraction of these payments. And in fact, a larger fraction than households that received these economic impact payments that were, you know, the three rounds of the stimulus payments. About forty three cents of every dollar was spent from these unemployment insurance payments. And that really helped increase consumer spending and aggregate spending during the pandemic.

WESSEL: And, Fiona, what about the second goal, helping laid off workers? Did we reach the right people, and who got left out?

GREIG: Well, certainly the UI expansions ended up being very progressive support, by virtue of who lost their jobs—these were disproportionately low income workers—and of course those who received PUA were even disproportionately lower income. So, many people who received these supports were already the most financially vulnerable workers. And of course, this support hit them at a time when they had just lost their livelihood.

If we think about the level of benefits, of course with those flat $600 and then $300 supplements, those two were very progressive, right. A $600 supplement was much more meaningful for low wage worker than for high wage workers.

So, I think the big picture here is that we achieved much greater coverage with this expanded UI program during COVID than really ever before. We’ve seen recipiency rates—that is, the share of people who are unemployed receiving UI—in the range of 15, 25, 35 percent depending on the state. Well, during COVID, those numbers actually reached near 100 percent, which surprises people and raises other questions about overpayments, which we can also get to. But in terms of achieving the overall goal of providing support to people who had lost their income, this was very effective.

WESSEL: So, you referred to the $600 a week supplement that the federal government gave to on top of state unemployment benefits for a period of time. And then later it was a $300 a week supplement. And as you point out, $600 is a much bigger percentage increase for low wage workers than high wage workers. Why in God’s name did we do $600 or $300 instead of just increasing people’s benefits by some percentage amount?

GREIG: Well, because we couldn’t do it any other way. I think the right answer would have been to provide a proportional increase, right, to achieve this at some standard where we were trying to replace 100 percent of wages, let’s say. Well, in this case, because what we’re working with is actually 51 different UI systems, not one federal system, many states weren’t technologically able to assess benefit levels on an individual basis. And so we took an approach that was much coarser where we pegged the supplement to the average level of earnings for unemployed nationally, which meant that we actually provided a supplement initially of $600, which delivered actually replacement rates well over 100 percent for most workers. Then we subsequently dialed that back to $300, which I think was aimed at actually achieving a median replacement rate of one hundred percent.

WESSEL: I see, so, because the computer systems are so archaic in various states, and because we didn’t want anybody to get hurt, we ended up giving some people more money in unemployment than they would have made if they were working and indeed more money than some people were making who stayed on the job.

So, Pascal, that’s the kind of thing that leads some people to say that with such generous unemployment benefits, the government is actually discouraging people from taking jobs when they become available. So, what did we learn about that, or what have we learned so far about that, from our experience during the pandemic in the subsequent months?

NOEL: Absolutely. So, there’s been lots of prior estimates to try to understand the strength of the force that you describe. When you give people more generous benefits while they’re unemployed, they have less of an incentive to go and find work because their standard of living while they’re unemployed is good enough or better. And if you take those prior estimates and you say what should have happened if you paid people as large as we were paying during the pandemic, as you said more money on unemployment than they were earning at their prior wages, you would have expected a dramatic decrease in job finding, a dramatic decline in employment, which is not what we’ve actually seen.

So, we discuss a few pieces of research that we have done and others have done during the pandemic to try to tease out exactly how large this disincentive effect was during the pandemic in response to these very large supplements. And the broad conclusion from that research is that they were very small. So, these very generous supplements actually accounted for a very small amount of the aggregate employment fluctuations that occurred during the pandemic.

So, I’ll give you two ways to think about it. One way is that the disincentive effect was about five times smaller than you would have expected based on prior evidence. So, people were much less discouraged by very generous supplements than you would have expected based on prior on prior evidence. The second is to give you some numbers. So, the shortfall in employment in July 2020 was about 13 million jobs, fewer than what we had before the pandemic in February of 2020. And we calculate that that would have been about 12 million, twelve point one million, if not for the unemployment insurance supplement. And so that’s basically saying these very generous supplements that were really helping support people’s consumption during this time period was only reducing that gap by about 7 percent. So really, a small share of the aggregate employment declines were being caused by these very generous supplements.

WESSEL: Okay, so in other words, yes, some people are discouraged from looking for jobs because they can do pretty well on unemployment insurance, but there are fewer of them than you would have expected from all the research that economists have been doing for the last 30 or 40 years. So why do you think that is? Was it unique to the pandemic or were we just wrong before?

GREIG: I think we have a bunch of different candidate hypotheses. I’ll list a couple of them. One is initially there was low labor demand. Of course by 2021, labor demand was very high so that, we kind of rule that one out. A second issue was that households had accumulated quite a bit of extra cash, right, not just through UI, but through stimulus, through forbearance programs. And so maybe that gave families the feeling that they had more time, that they didn’t necessarily have to jump back into the labor force. A third issue was that, of course, we were in a pandemic, right? Families were experiencing concerns around the public health, environment, child care outages, or quarantine periods. And so all of these factors may be contributing to the hesitancy of the worker to return to work. And then finally there’s always the wonder whether there was publication bias in the historical literature, we don’t know.

I think we're testing some of these candidate explanations, but we don't have a smoking gun explanation. And that's for sure a question in our minds as we think about what are the lessons learned from the pandemic and whether this low work disincentive effect could carry through or would carry through to the next recession.

WESSEL: I see. So, your point is that there were so many other factors during the pandemic that unemployment insurance might have been an unusually small one, that was one point you made. And the second point when you referred to publication bias, you mean that maybe the economic journals tended to publish articles that found a big effect and they didn't publish the ones that showed no effect because no one's interested in no effect. And that may have biased our understanding of the system. Is that basically right?

GREIG: Yeah. I mean, we don't, we don't know. Open questions, David.

WESSEL: Okay, so, you talked a little bit about the 51 states. What changes do you think we should make to the system, to the way we organize the system, to the computers, before we had another recession, which could come sooner than I had hoped? Pascal, do you have views on that?

NOEL: There's a couple of buckets of changes. One core one is that we asked a lot of the state UI agencies during the during the pandemic. So we basically asked them to set up a whole way to pay people this federal $600 supplement on top of regular unemployment insurance payments. And we asked them to dramatically expand eligibility to a whole set of workers, as Fiona said, that accounted for like 40 percent of the people that were receiving unemployment insurance at certain points during the pandemic that never were eligible for this in the first place. And that was very, very difficult for the state UI agencies to actually implement. And as a result, a lot of workers had to wait a long time in order to actually receive these benefits, which was very difficult for them. They were being in the pandemic, they were losing their jobs, things were very difficult and it took a long time to actually get the money that they were eligible to receive as a result of these policies.

And so one thing that is really important that we can do going forward is try to plan ahead for these types of emergencies that might happen in the future. And that means setting up the technology systems so that the states are able to quickly pay supplements if Congress decides to provide these kind of supplements. And also set up a system such that we can actually expand eligibility when something like this might happen again. And that could mean keeping a version of this expanded eligibility policy in place even during normal times. So this Pandemic Unemployment Assistance Programs that expand eligibility to self-employed workers, to gig workers, who aren't eligible for regular unemployment insurance, have some program that is able to give assistance to these people so that when we have something like this that happens again, we're not having to scramble with 50 different state UI agencies to set this thing up to actually be able to pay people.

WESSEL: I see. So, it seems to me you're saying two things, both of which are important. One is we obviously need better administrative and IT systems at the states so that we have more flexibility. So, if we want to pay people only 100 percent of their wages instead of 120 percent, we can do that. And the second thing is that we made some important design changes to unemployment insurance. You mentioned that we made eligible people who are self-employed or the growing number of gig workers and all that. And if we want to be able to do that in the next recession, we should sort of organize that now before the crisis hits.

Finally, Fiona, let's say that another recession arrives, as one surely will someday, and you're called before Congress, and they said, we did lots of things during the COVID pandemic. One of them was expanded unemployment insurance. Should we do that again? And if so, what should we do the same or differently this time? What would you tell them?

GREIG: Well, I think what we have certainly learned from this pandemic is that this of all the things that we did, all the different types of support we offered people, UI, economic impact payments, PPP, support to state and local governments, the spending boost that came from UI was very high. So as a recession mitigation tool, as an economic stimulant, this was very effective. So, I think that gives grounds to thinking about UI as a first dollar of relief kind of frame.

Now does that mean that we should increase the level of benefits? Yes, possibly. I mean, our standard replacement rates of around 50 percent are very low by international standards. Might it make sense to bring that up to 60, 70, 80 percent in a next recession or in general? Probably. Should we also expand eligibility? I think, like Pascal said, probably yes. I mean, there are huge swaths of our labor force who would not have been protected but for those expansions. Now, they were protected through other means, right? We can take coarser instruments like economic impact payments, et cetera. But if we want to target the dollars in an efficient way to people who are experiencing income loss, UI does that very well.

And I should say that one of the big concerns around UI was not just that it might have deterred people from working, but we might have also experienced more fraud. And of course, when you have so many people receiving UI because so many people have lost their jobs, the sheer dollar value in absolute terms is going to increase. On a percentage basis, though, in normal times we see overpayments of around 10 percent. In the pandemic that went up, it went up to around 18, 19 percent, even including the PUA program. Is that an increase? Yes. But another way to frame it is that 82 percent of people rightly received UI, right, the right people who needed UI received it, and we did that in the context of having relaxed so many verification processes and third party verification and other administrative controls. And so perhaps one of the big surprises of this was the extraordinary levels of voluntary compliance in light of the ways in which we relaxed all of the controls around this program.

WESSEL: I think that's a really good point. So, I want to thank Pascal Noel from the University of Chicago Booth School of Business and Fiona Greig from the JPMorgan Chase Institute for this episode of the Recession Remedies podcast. And you can read their chapter and all the other chapters in our book at Brookings Dot Edu forward slash Recession Remedies.

Thank you for joining us.

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