Cutting off Additional Unemployment Benefits While Millions are Unemployed Would be a Human and Economic Catastrophe

Benefits to expire on July 31

In only 11 weeks, tens of millions of Americans have lost their jobs, as a pandemic and necessary public health closures drove the fastest implosion of the U.S. job market in history. The unemployment rate more than tripled in one month to 14.7 percent—the highest since the Great Depression. The U.S. Bureau of Labor Statistics has reported that the unemployment rate likely is closer to 20 percent after adjusting for potential misclassifications.[1]

Congress has responded forcefully. First, it passed the Families First Coronavirus Response Act, which provided $1 billion to help states quickly process state unemployment claims, interest-free federal loans to backstop state unemployment trust funds, and full federal financing of up to 20 additional weeks of unemployment benefits in high unemployment states. A few weeks later, Congress provided another 13 weeks of potential benefits and established special Pandemic Unemployment Assistance (PUA), which grants federal benefits to workers who don't qualify for state unemployment benefits, such as independent contractors.

The CARES Act also provided a $600 weekly federal benefit supplement, known as Federal Pandemic Unemployment Compensation (FPUC). FPUC helps ensure that laid off and furloughed workers do not have to choose between complying with public health measures and financial devastation. Congress chose a uniform flat dollar amount because the Administration advised that it was the only way to avoid multi-month delays caused by states' sorely outdated UI technology platforms. The supplement was set at $600 per week, so total unemployment benefits would replace 100 percent of wage income for the average worker.

Allowing FPUC to expire as scheduled on July 31st not only would damage the well-being of American families, but it also would strike a severe blow to businesses and the economy. Data from April show that FPUC alone offset roughly 30 percent of the loss in private-sector wages and salaries. Letting it expire would further weaken consumer demand and drive additional job losses; we roughly estimate that, based on previous recessions, FPUC is supporting as many 2.8 million jobs and reducing the unemployment rate by as much as 1.8 percent.

Concerns that FPUC is slowing the jobs recovery are misplaced given that most workers are ineligible for UI benefits if their employer recalls them. Moreover, the main obstacles to workers seeking employment again are their well-justified fear of contracting a deadly virus or bringing it home to a family member, lack of personal protective equipment, and the rapid disappearance of childcare options. Policymakers concerned about speeding the return to work should focus on building contact tracing and testing capacity as well as preserving child care infrastructure instead of cutting support from workers and their families in a public health and economic crisis.

Unemployment benefits have helped mitigate economic and psychological insecurity

Unemployment insurance benefits—including FPUC—have been essential for buffering millions of unemployed Americans from the economic hardship of job loss or furlough. Using data from the COVID Impact Survey, we find that 21 percent of unemployed workers between April 20th and May 10th had received benefits (an additional 20 percent had applied for benefits).[2] Among recently unemployed workers,[3] the fraction receiving unemployment benefits was 26 percent.

Recently unemployed workers receiving UI benefits fare better than those not receiving UI benefits on at least three different metrics—financial security, food security and mental health. It is important to note that there are differences between the two groups other than whether they receive UI that could drive the differences we see on these three metrics. Still, the idea that workers benefit from economic security programs like UI that help them to avoid sudden drops in income that can leave them in deep poverty is both commonsense and consistent with existing, careful research.[4]

In our analysis, we focus on recently unemployed workers—those who are on temporary layoff, have been furloughed, or have lost their job and searched for work since March. The differences are even larger when the comparison includes workers who lost their job and searched for work before March. All of the differences below are statistically significant.

- **Financial security:** Even with their benefits, 42 percent of recently unemployed workers receiving UI benefits could not cover an unexpected emergency expense of $400 without borrowing or selling an asset. But 69 percent of recently unemployed workers not receiving UI benefits would have to borrow or sell an asset to cover an unexpected $400 emergency.

- **Food security:** 23 percent of recently unemployed workers receiving UI benefits reported not having enough money to buy food in the previous week. By comparison, almost twice as many (43 percent) of recently unemployed workers not receiving UI benefits had that experience.

- **Mental health:** Recently unemployed workers receiving UI benefits reported, on average, feeling hopeless one day out of the previous seven. By comparison, recently unemployed workers not receiving UI benefits reported feeling hopeless 1.6 days out of the previous seven days.

These estimates are not causal but—given other evidence that preventing destitution is enormously important for workers' well-being—they suggest that UI benefits are providing critical support.

Regular unemployment benefits are meager in many states

Experts have long identified several elements of states' unemployment programs as overdue for reform such as eligibility criteria and outdated technology. One of the biggest shortcomings in many states is how little income regular unemployment benefits replace. Under the original design of the U.S. unemployment system, benefits are supposed to replace about half of a worker's wages and leading economists such as Raj Chetty of Harvard University have argued that they should cover more than half. [5] A bipartisan Advisory Council on Unemployment Compensation to the President and Congress recommended that UI should replace "at least 50 percent of lost earnings."[6]

However, they replaced less than 40 percent of workers' wages on average in 2019.[7][8] Importantly, there is considerable variation in average replacement rates across states. In no state does UI replace half of workers' wages on average and in just 13 states it replaced more than 45 percent of them. In 13 states, unemployment benefits replace less than one-third of workers' wages because the benefits are so minimal. In Florida, for example, the maximum benefit is just $275 per week – the equivalent of about $15,000 per year and below the poverty line for a family of two.

The FPUC helps make up for the meager level of wage replacement that regular UI benefits provide. Without it many unemployed individuals would be unable to pay rent, buy groceries, or purchase medicine if they were required to live on the meager benefits in many states' UI programs. Without FPUC, many workers will burn through their retirement savings, take on unsustainable amounts of debt, and rely on unconventional ways of buying necessities such as selling plasma.[9]

Expanded unemployment benefits have prevented a massive reduction in consumer spending

Enhanced unemployment benefits have also played a critical role in stabilizing the economy and preventing the collapse in demand for goods and services resulting from millions of Americans losing their jobs from being even more acute.

A recent analysis by the Brookings Institution's Hamilton Project found that UI spending increased by $45 billion in April, which offset roughly half the estimated loss in private wages and salaries in that month.[10] [11] This is confirmed by recent data from the U.S. Commerce Department showing that real disposable personal income actually *rose* 13.4 percent in April, but real personal income would have fallen 6.3 percent without transfers such as unemployment insurance and the stimulus payments.[12] This one-time spike will likely fall over subsequent months as the stimulus payments accounted for the bulk of it.

The FPUC in particular has played an essential role in propping up demand and preventing consumer spending from further cratering. The extra $600 in weekly benefits from FPUC accounts for $27 billion of the $45 billion increase (60 percent) in unemployment benefits in April compared to February. It thus offset roughly 30 percent of the decline in private wages and salaries alone.

A premature end to enhanced benefits could severely hurt consumer demand and deepen the recession

Millions of Americans living on less than half of their previous salaries is not only a major humanitarian catastrophe but could also worsen our current economic crisis. Businesses in communities across the country sell these workers goods and services, but income declines of 66 percent in some states would mean these workers buy significantly less. This will produce a downward spiral of falling demand as those businesses themselves begin to lay off workers.

Importantly, enhanced unemployment benefits are one of the most effective forms of stimulus since unemployed Americans will spend a large fraction of an additional dollar of income. Estimates from previous recessions of how much an additional dollar of unemployment benefits will boost GDP when the economy is weak range from $1.00 to $1.60.[13] Combined with the historical relationship between changes in GDP and changes in the unemployment rate,[14] we roughly estimate that FPUC is reducing the unemployment rate by 1.1-1.8 percentage points and protecting about 1.7-2.8 million jobs—jobs that could be destroyed if FPUC and the spending it supports are cut off. [15] These numbers are necessarily back-of-the-envelope and do not account for how the pandemic may affect consumption but provide some sense of how FPUC is supporting the economy.

The effects of this sudden disappearance of income and spending could have grave consequences and even turn our pandemic-turned-recession into a full-blown financial crisis by causing a wave of defaults and foreclosures. Goldman Sachs, for example, has written that it does not expect households to default on their debts in the short term as much as one would expect given the high unemployment rate because of the combination of expanded unemployment insurance benefits and direct payments from CARES. But it warns that "defaults could increase later in 2020 if UI benefits are not extended."[16]

The importance of unemployment insurance in preventing foreclosures is demonstrated by the results of one study finding that UI expansions from 2008 to 2013 prevented more than 1.3 million foreclosures, which is two-thirds more than the number of foreclosures prevented by the two largest foreclosure mitigation policies at the time (HAMP and HARP) combined. In fact, the federal government recouped one-sixth of the cost of the UI expansions from preventing losses to government-sponsored mortgage companies like Fannie Mae. [17]

Claims that unemployment benefits are too generous are misplaced

Some policymakers have expressed concern that FPUC may be hurting the economy more than helping, saying that the benefits could encourage workers to not return to work since some workers make more on unemployment than they did while working. These concerns largely are misplaced.

First, workers receiving unemployment benefits whose employers recall them to work full time are not eligible for unemployment benefits.[18] The replacement rate is not a factor since a worker cannot choose to retain her benefits if she refuses to return to work. The only exception is a narrow set of circumstances under the CARES Act specifically related to COVID-19 such as someone being diagnosed with COVID-19 or someone whose child's school is closed because of COVID-19. Any concern about FPUC preventing workers from working, therefore, must be limited to employers trying to hire *new* workers at relatively low wages and without other benefits to make the job attractive.

Second, the extra $600—like the complete wage replacement rate for the average worker it was intended to provide—is an essential backstop for public health measures that require workers to sacrifice jobs and freedom of movement to prevent community spread of COVID-19 and "flatten the curve" to prevent overtaxing hospital resources. The supplement helps keep them whole financially, preventing aggregate demand from going into free fall. With the virus still rampant in many communities, a significant share of unemployed workers cannot safely return to work whether or not unemployment benefits are available. One study estimates that 4 in 10 adults (almost 93 million people) are at risk of developing a serious illness from COVID-19 as a result of their age or underlying health status. Almost half of those adults (about 41 million people) are of prime working age, between the ages of 18 and 64.[19]

Finally, this concern typically ignores some of the other main reasons why workers may struggle to return to work even as public health measures are eased. The economy will likely remain significantly depressed for some time as entire sectors remain closed or have significantly lower demand for labor so even workers eager to go to work will not find jobs. Indeed, CBO is already predicting the unemployment rate (assuming expiration of FPUC) will be around 16 percent in the third quarter of 2020 (it peaked at 10 percent during the Great Recession).

Research normally finds only a modest effect of higher UI benefits on how long people stay unemployed[20] with most of the increased duration coming from allowing unemployed workers to take the time to find a job that is a good fit.[21] But those effects are *especially* modest when the economy is weak: one study found that the effect of unemployment benefits on how long someone remains unemployed are 40 percent smaller during a period of high unemployment since so many workers are applying for each job.[22]

Similarly, workers with children are not going to be able to work if schools remain closed or child care is unavailable. Almost 4.5 million child care slots are at risk of disappearing without sufficient federal support, which would directly prevent millions of Americans—especially women—from returning to work.[23] Indeed, the cross-national evidence suggests that policies that reduce the cost of child care are more effective at boosting labor-force participation than policies that reduce taxes on working. [24] Estimates show that the nation's child care infrastructure—essential to helping parents return to work—will need at least $10 billion a month given child care providers' loss in revenue.[25]

The risk of ending enhanced benefits too early is far greater than the cost of extending them

FPUC has been a remarkable policy success. It has helped reduce the suffering that requiring the unemployed to live on regular unemployment benefits would entail and helped plug the hole in aggregate demand that has resulted from millions of Americans losing their jobs. High unemployment rates are caused by the pandemic, the reduction in aggregate demand, and the child care crisis—not the FPUC.

Letting the FPUC expire at the end of July would be a colossal policy mistake, one that would cost our economy jobs, not fill them. FPUC is offsetting about 30 percent of the decline in private wages and salaries and is keeping as many as 2.8 million Americans employed, mostly by sustaining consumer spending. Workers are not eligible for benefits if they quit their job or refuse to go back to their job if after being recalled by their employer unless they face a specific COVID-19-related condition so it has likely had little, if any, effect on the unemployment rate so far. Letting it expire would do little to reduce unemployment and would, in fact, *increase* unemployment by sucking additional consumer spending out of the economy.

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[1] The April Jobs report states that millions more workers reported themselves to be "employed but absent from work" than in a typical April despite efforts by BLS to classify them as unemployed. If BLS reclassified the surge in workers who were "employed but absent from work" as unemployed, then the unemployment rate would have been almost five percentage points higher on a non-seasonally adjusted basis. https://www.bls.gov/news.release/empsit.nr0.htm

[2] COVID Impact Survey, https://www.covid-impact.org/project-overview

[3] We define workers as "unemployed" if they are laid off temporarily, furloughed, or consider themselves unemployed and looking for work. We define workers as "recently unemployed" if they are laid off temporarily, furloughed, or consider themselves as unemployed and looking for work since March. Workers need to have been unemployed for at least a week to be considered unemployed.

[4] Marianne Bitler and Hilary Hoynes, *The more things change, the more they stay the same? The safety net and poverty in the Great Recession, Journal of Labor Economics* 34 (2016): 403-S444; Matthew Ridley et al, "Poverty, Depression, and Anxiety: Causal Evidence and Mechanisms," National Bureau of Economic Research Working Paper No. 27157, May 2020; Lucie Schmidt, Lara Shore-Sheppard, and Tara Watson, "The Effect of Safety-Net Programs on Food Insecurity," *Journal of Human Resources*, 51 (3) (2016): 589-614; Molly Dahl, Thomas DeLeire, and Shannon Mok, "Food Insufficiency and Income Volatility in U.S. Households: The Effects of Imputed Earnings in the Survey of Income and Program Participation." Congressional Budget Office Working Paper 2012-07, 2012; National Academies of Sciences, Engineering, and Medicine, "A Roadmap to Reducing Child Poverty," National Academies Press, 2019, https://www.nap.edu/read/25246.

[5] Raj Chetty, "Moral hazard versus Liquidity and Optimal Unemployment Insurance," *Journal of Political Economy* 116(2): 173-234.

[6] Advisory Council on Unemployment Compensation, "Collected Findings and Recommendations: 1994-1996," https://oui.doleta.gov/dmstree/misc_papers/advisory/acuc/collected_findings/adv_council_94-96.pdf

[7] U.S. Department of Labor Employment and Training Administration, "UI Replacement Rates Report," https://oui.doleta.gov/unemploy/ui_replacement_rates.asp

[8] The U.S. Department of Labor provides two different methods for calculating replacement rates. "Replacement Ratio 1" is the weighted average of workers' weekly unemployment benefits divided by their weekly earnings assuming a 40 hour work-week. "Replacement Ratio 2" is the weighted average weekly benefits divided by the weighted average wage. Both ratios are useful with the former providing a better impression of the replacement a typical worker experiences and the latter providing a better impression of how well UI replaces lost wages for the economy. Replacement Ratio 2 is used in this report.

[9] Dylan Matthews, "Selling plasma to survive: how over a million American families live on $2 per day," *Vox*, September 2, 2015, https://www.vox.com/2015/9/2/9248801/extreme-poverty-2-dollars

[10] Ryan Nunn, Jana Parsons, and Jay Shambaugh, "Incomes Have Crashed. How Much Has Unemployment Insurance Helped?," The Hamilton Project, May 13, 2020, https://www.hamiltonproject.org/blog/incomes_have_crashed_how_much_has_unemployment_insurance_helped

[11] The COVID Impact Survey and Hamilton data are not directly comparable as they cover different periods and the share of lost income covered by the UI reported by the Hamilton Project is only private-sector wages and salaries while laid off government workers can receive UI as can private sector business owners/independent contractors who do not receive wages and salaries under the Pandemic Unemployment Assistance program.

[12] Table 5, U.S. Bureau of Economic Analysis, "Personal Income and Outlays: April 2020," May 29, 2020, https://www.bea.gov/sites/default/files/2020-05/pi0420_0.pdf

[13] Gabriel Chodrow-Reich and John Coglianese. "Unemployment Insurance and Macroeconomic Stabilization," *Recession Ready: Fiscal Policies to Stabilize the American Economy*, edited by Heather Boushey, Ryan Nunn, and Jay Shambaugh, Washington, D.C. Brookings Institution (2019): 153-179. Chodrow-Reich and Coglianese note that the fiscal multiplier for benefits for workers who have been unemployed for less than three months may be somewhat lower since they may have a lower marginal propensity to consume, but the bulk of UI claimants will surpass three months of unemployment over the next several weeks. Moreover, evidence that job losses are especially widespread among low-income households and the fact that UI benefits are available for the first time to especially marginalized workers through PUA may raise the short-term marginal propensity to consume of additional UI benefits.

[14] In their similar calculation of the effect of unemployment benefit changes on the unemployment rate, Chodrow-Reich and Coglianese assume that a 2.5 percent change in GDP reduces the unemployment rate by one percentage point (i.e. that the Okun's Law coefficient is 2.5).

[15] Estimates use CBO data indicating that FPUC will cost $176 billion and CBO data to roughly guess that the U.S. economy is $6.4 trillion from April 2020-July 2020 to assume that FPUC represents 2.7 percent of GDP while in place.

[16] https://twitter.com/Brendan_Duke/status/1266039452637552641

[17] Joanne W. Hsu, David A. Matsa, and Brian T. Melzer, "Unemployment Insurance as a Housing Market Stabilizer," The American Economic Review, 2018, 108(1): 49-81.

[18] Annelies Goger, Tracy Hadden Loh, and Nicole Bateman, "Debunking myths about COVID-19 relief's 'unemployment insurance on steroids'," The Brookings Institution, May 12, 2020, https://www.brookings.edu/research/debunking-myths-about-covid-19-reliefs-unemployment-insurance-on-steroids/

[19] Wyatt Koma et al, "How Many Adults Are at Risk of Serious Illness If Infected with Coronavirus? Updated Data," Kaiser Family Foundation, April 23, 2020, https://www.kff.org/coronavirus-covid-19/issue-brief/how-many-adults-are-at-risk-of-serious-illness-if-infected-with-coronavirus/

[20] Johannes F. Schmieder and Till M. von Wachter, "The Effects of Unemployment Insurance Benefits: New Evidence and Interpretation," Annual Review of Economics (8) (2016): 547–581.

[21] Chetty 2008

[22] Ioana Marinescu, "The General Equilibrium Impacts of Unemployment Insurance: Evidence from a Large Online Job board," *Journal of Public Economics* 171 (2019): 70-85.

[23] Steven Jessen-Howard and Simon Workman, "Coronavirus Pandemic Could Lead to Permanent Loss of Nearly 4.5 Million Child Care Slots," April 24, 2020, Washington, DC: Center for American Progress, https://www.americanprogress.org/issues/early-childhood/news/2020/04/24/483817/coronavirus-pandemic-lead-permanent-loss-nearly-4-5-million-child-care-slots/

[24] Henrik Jacobsen Kleven, "How Can Scandinavians Tax So Much?" Journal of Economic Perspectives, 28 (4) (2014): https://www.aeaweb.org/articles?id=10.1257/jep.28.4.77

[25] Rebecca Ulrich and Aaron Sojourner, "Child Care is Key to Our Economic Recovery," National Women's Law Center and Center for Law and Social Policy, April 2020,, https://nwlc-ciw49tixgw5lbab.stackpathdns.com/wp-content/uploads/2020/04/CCKeytoEconomicRecoveryNWLC.pdf