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House of Representatives

Hearings of the Subcommittee on National Security, International Development, and Monetary Policy  
Paycheck Security: Economic Perspectives on Alternative Approaches to Protecting Workers' Pay During  
COVID-19

Sad to say, the US response to Covid-19 has been disappointing. We've done a much poorer job than other countries, both in maintaining the health of our people and that of our economy. And the two are related: There will not be a strong recovery until the pandemic is brought under control. There is now empirical evidence that it was more the fear of the virus that brought the economy down rather than the lockdown.

Congress responded to the pandemic with a massive amount of assistance. By all accounts, it succeeded in preventing much suffering that would otherwise have occurred. But in many ways, the programs were badly designed and badly implemented, with much of the money not going to where it was most needed, with the unemployment rate soaring far higher than elsewhere. This put strains on our unemployment insurance system, resulting in many of the unemployed not receiving money for weeks and weeks. The increase in unemployment is especially inopportune in the US, because so many depend on employer-provided health insurance. Losing health coverage in the midst of a pandemic is a calamity.

The program of assistance was predicated on there being a short shutdown; with enough love and care, and enough assistance, the nation, and the economy, would emerge in ten weeks or so, healthy and ready to get back to work. In short, it was predicated on a V-shaped recovery. Such beliefs appear now to be utter fantasy. With the pandemic continuing apace, no one thinks we will be back to normal by the end of this month.

The reality is that we need to plan for the pandemic to be around for an extended period of time. We could be lucky; we could discover effective therapeutics or vaccines, or the virus could mutate. But we shouldn't plan on it. Indeed, there is some evidence of a mutation making Covid-19 more contagious. It would be the height of irresponsibility not to plan for the pandemic being with us for an extended period of time. Even were we to get it better under control, with good testing, social distancing practices, and testing, it will continue to affect our economy. So too, the global slowdown that we are already in will affect us.

There are a few principles and priorities that should guide the next package of assistance. First, because we cannot have a healthy economy without a healthy population, health should be given priority. While some of the earlier programs did this, there are important lacunae. It was foolish, short-sighted, and unconscionable not to have ensured that everyone was provided with paid sick leave. We don't want

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people with the disease going to work and spreading the disease; but with so many Americans living paycheck to paycheck, it was inevitable that that would happen without paid sick leave. It was foolish, short-sighted and unconscionable for employers not to have provided face masks and protective gear to workers in exposed jobs; and if employers didn't do so voluntarily, OSHA should have required it. There are likely to be large increases in demand for Medicaid, and the states will be suffering large losses in tax revenue. With states having balanced-budget frameworks, only the Federal government can help them meet these needs.

Secondly, hysteresis effects are enormous: bankrupt firms don't become unbankrupt when the pandemic is over. Balance sheets of households and firms often take a long time to recover. That's why you did the right thing in responding quickly and massively. But all these investments in our future will be for naught if assistance is not continued so long as the pandemic and its economic aftermath persists.

There is a third powerful force that will depress the economy: precautionary behavior. As long as there is uncertainty, both about the course of the disease and the economy, there will be a reluctance to spend, either by firms or households. In previous downturns, like that of 2008, we provided assurances to workers that there would be extended UI so long as the unemployment rate remained elevated. We need to do that now. And we have to provide similar assurances to businesses. We need to provide income-contingent loans, where repayments and the duration of the loan automatically adjust to the circumstances of the economy and the firm, providing an automatic stabilizer to the economy.

Thus, there must be a commitment, in the famous words of Mario Draghi, "to do what it takes." But at the same time, we must spend our money well, which is why the design of the programs is so important.

As I wrote in my Roosevelt Institute Policy Brief in late April:

Even before the passage of the CARES Act, the alternative approach of *direct payments to employers to retain workers* seemed to some more likely to be more effective than the disparate programs included in that bill. The evidence over the last few weeks seems consistent with those expectations.

The evidence since then, both in the United States, which took an alternative course, and in those countries around the world that adopted programs similar to the H.R. 6918, the bipartisan Paycheck Recovery Act, strongly reinforces the conclusions I had reached at the time. I went on to describe the idea and explain its advantages.<sup>2</sup>

The federal government, both through the IRS and the Social Security Administration, has a direct link, in most cases electronically, with every employer in the US, so it should be easy to transfer money directly from the government to these employers based on employer retention. A paycheck guarantee program, such as the one proposed by Rep. Pramila Jayapal (D-WA), or the Paycheck Security Act, ... [as well as] Sens. Bernie Sanders (I-VT), Mark Warner (D-VA), Doug Jones (D-AL), and Richard Blumenthal (D-CT), give examples of what such a program

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<sup>2</sup> A *New York Times* article vividly describes the contrasting consequences of the alternative approaches. See Peter S. Goodman, Patricia Cohen and Rachel Chaundler, "European Workers Draw Paychecks. American Workers Scrounge for Food." July 3, 2020.

might look like. Provided that the employer retained employees, the government would make up for the shortfall in revenues experienced by any firm, based on a simple formula...

For example, a certain percent of the payroll for wages and salaries—possibly 100%—of up to, say, \$90,000—augmented by amounts representing “fringe benefits” and “overhead.”

...Several studies have estimated the costs of this kind of program, which obviously depend on the precise parameters. Variants range from \$115 billion to \$150 billion a month during the shutdown. Costs associated with partial shutdowns would be proportionally smaller.

These costs, however, are largely gross estimates, not net; the net costs are likely to be substantially smaller. The government would otherwise have to face additional costs in unemployment insurance and Medicaid. The program [could], moreover, replace the costly Paycheck Protection Program (PPP), which if the pandemic lasts much longer, could require a further injection of funds even beyond the “phase 3.5” monies authorized in late April.

Both the forecast that additional funding would be needed and that the PPP program would not be as effective as had been hoped have, unfortunately, been more than fully realized. I went on to argue that

The program might be made even more effective by providing supplementary support for training, so that workers who are not fully engaged in production could be more productive when the economy emerges from the pandemic. In the US, on-the-job training is far less common than in many other high wage-high productivity economies, such as Denmark (OECD 2018). This would not only be a more productive use of their time but would almost surely contribute to a more general sense of well-being.

This program represents a significant improvement over the existing PPP; it is simpler to administer, with more of the money going where it is needed, and considerably less costly and more effective.

Some will say, “Yes, we should have adopted the Paycheck Guarantee program. But that’s water over the dam. It’s now too late.” That argument might have had some validity if, as thought at the time these measures were adopted, the pandemic had been of short duration. But since then it has flared up, and there is a good chance it will be with us for a long time. As I’ve already said, we will need to maintain some kind of support, and this program is the best way forward. As I said then, and is so much clearer now:

....there is a compelling case for moving to a new program: Still more money will be required. ...More money will be spent, and it is important that it be spent well. The fixed costs of establishing a new program are small compared to the variable costs of running the existing program. The flaws in the PPP are inherent; there are no “easy fixes” that will enable it to do what it is supposed to—be an efficient, transparent way of getting money to those who most need it. It was not designed for transparency, so that Americans could know the most vulnerable were being protected.

It would be far easier to make a new program—along the lines of paycheck guarantee proposals—more transparent, with lower overheads and greater targeting of money where it's needed. Such a program would be more comprehensive and successful than the PPP in preserving links between employers and workers, which will prevent our unemployment and Medicaid systems from becoming overwhelmed and quicken our recovery.

I want to conclude with two more general comments. First, our assistance to the economy has to be far more comprehensive. There were some important sectors that did not receive the assistance that they needed. One sector is states and localities. I already referred to the severe budgetary constraints that they faced. These authorities are responsible for many of the services on which so many of our citizens depend, including education, health, and welfare. But cutbacks in spending will greatly weaken our economy, with large multiplier effects. It is austerity from below. In previous downturns we have seen the devastating macroeconomic effects. Already, layoffs of government workers are among the large sources of increasing unemployment. We will not have a robust recovery without adequate support for this vital sector of our economy. (One of the virtues of the Paycheck Recovery Act is that it allows states and localities to access grants.)

Secondly, our aspiration should not be a recovery in which sometime, say, in 2022 when we get back to where we were in late 2019, we simply pick up where we left off. Never has government played such a role in the economy—not even in the Great Depression or in the Great Recession. Citizens have the right to expect that the economy that emerges will be a better economy, serving the interests of all citizens. The pandemic has exposed the inequalities that were rife in our system. We need to move from an economy based on fossil fuels to one that allows us to live within our planetary boundaries. If we are to compete in the 21<sup>st</sup> century global economy, we must be more of a knowledge economy.

Yet one sector that has received far too little assistance and is likely to be ravaged by the pandemic is education and research, which by its very nature entails individuals working in close quarters with each other. It is this sector that has been the source of the country's comparative advantage; it is advances in science and technology that explain why our living standards are so much higher than they were 250 years ago. Yet this sector is being largely neglected.

In short, our spending must be cost-effective, timely, comprehensive, with a vision of the kind of economy that we want to emerge from the pandemic. When the country was first struck by the pandemic, Congress rose to the occasion by providing massive spending in the CARES Act. Congress now must rise to the occasion by a commitment to sustaining those efforts and redesigning our programs for the hard and potentially long struggle ahead. We need a program

with flexibility—that responds automatically to the changing dimensions of this pandemic and its economic consequences. We’ve already seen the consequences of the vicissitudes of the disease, with so many states and localities having to reverse re-opening.

We need a program along the design of the Paycheck Recovery Act of 2020.