

He Said, He Said: Debating Two Possible Recoveries

By N. Gregory Mankiw

As an economist, I'm often asked during recessions to divine the path of the recovery that will follow. In the current Covid-19 downturn, I find myself of two minds on this question. I thought I would share them both.

THE PESSIMIST IN ME Economic downturns are often highly persistent. The National Bureau of Economic Research, the official arbiter of turning points in the business cycle in the United States, has not yet declared that the country is in a recession, but it surely is. Like others, this recession may leave scars on the economy for years to come.

THE OPTIMIST IN ME Yes, the economy is often slow to recover from downturns, including the Great Recession of 2008-9. But this recession is different. It is occurring not by accident but by design. Employment and production are falling because we want people to stay at home.

PESSIMIST It sure is different. Look at the most recent jobs report. The employment-population ratio fell by 1.1 percentage points, the largest one-month drop since the data began in 1948. And that record will be broken next month, when the economic carnage of the last few weeks appears in the data. This downturn will be the deepest since the Great Depression of the 1930s.

OPTIMIST But the employment report also offers a glimmer of hope. The number of job losers on temporary layoff increased by a whopping 1.05 million, while the number of permanent job losers increased by only 177,000. That breakdown differs from the pattern in previous recessions, and it bodes well for a quick recovery. Those on temporary layoff can easily return to work when the lockdown is over.

PESSIMIST What makes you so confident that this will actually happen?

OPTIMIST Think about beach communities. Every winter, local restaurants and retailers close down. Every summer, when tourists return, these businesses ramp up quickly. The same can happen nationwide once people can leave their homes.

PESSIMIST Yes, but those businesses plan for the winter downturn. This downturn was unexpected.

OPTIMIST Or think about the return of veterans after World War II. The domestic economy absorbed all those new workers with ease.

PESSIMIST But many women who entered the labor force during the war subsequently left when the war ended, opening up jobs for the returning men. Nothing like that will happen this time.

OPTIMIST But remember, many people are on temporary layoff. Their jobs are waiting for them.

PESSIMIST Temporary layoffs can turn into permanent job losses if stay-at-home orders continue much longer and businesses become insolvent.

OPTIMIST But we seem to be turning the corner on the pandemic. According to the Institute for Health Metrics and Evaluation, the daily number of coronavirus-related deaths in the United States may have peaked this past week, and we should soon be heading in the right direction. Daily deaths are projected to be close to zero by early summer.

PESSIMIST If the health situation is improving — and it may be early to say — the economic situation is not. Many people are still at home. When the draconian social distancing measures are relaxed so that normal economic life can resume, the health crisis could flare up again.

OPTIMIST With time, we'll find better ways to contain the spread of the virus than closing much of the economy. The key is widespread testing. If people were tested, say, every few weeks, regardless of whether they were symptomatic, the infected could be quarantined quickly, limiting the risk of contagion they pose to others.

PESSIMIST Tests for Covid-19 have been hard to get, and the wait for results has often been long, sometimes a week or more.

OPTIMIST The testing is improving. Some people can now get results in a matter of hours. The government will, however, need to invest much more in testing capacity for life to return to normal. We need tests to identify the currently infected as well as those who have recovered and have the antibodies, making them no longer vulnerable to the virus or a risk to others.

PESSIMIST Given the current dysfunction in Washington, counting on government seems like grasping at straws.

OPTIMIST The White House was caught flat-footed by the pandemic, and Congress is as divided as ever. But they still managed to pass an emergency fiscal package to meet the challenge. Most Americans got a tax credit, unemployment insurance was expanded, and small businesses were offered forgivable loans to help cover payroll and other expenses. And the law sensibly strengthened the Federal Reserve's ability to act as lender of last resort.

PESSIMIST The fiscal package poses some big problems. For some people, expanded unemployment insurance pays more than their jobs did, giving them little reason to return to work. Not enough money was appropriated for small businesses, leading to a scramble to be first in line for funds. And some small businesses that don't really need the money will enjoy unjustified windfalls from these forgivable loans.

OPTIMIST The legislation was not perfect, but you can't expect perfection in a crisis. It was a step in the right direction, and our elected leaders deserve a lot of credit for it. Some of the flaws can be fixed in future legislation.

PESSIMIST All that creates a lot of uncertainty, which is never good for the economy.

OPTIMIST True, but uncertainty is inevitable during a crisis.

PESSIMIST At least there's one thing we can agree on.