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Our Fiscal Policy Response to the COVID Crisis

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Abstract

"Although much of the national news media is rightly focused on things like social distancing, testing and vaccines, there is another important dimension to the 2020 coronavirus crisis that merits analysis—the use of massive amounts of debt to finance mitigation efforts."

Posting about financial stewardship amid the current pandemic from *In All Things* - an online journal for critical reflection on faith, culture, art, and every ordinary-yet-graced square inch of God's creation.

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Although much of the national news media is rightly focused on things like social distancing, testing and vaccines, there is another important dimension to the 2020 coronavirus crisis that merits analysis—the use of massive amounts of debt to finance mitigation efforts.

Deficit spending is reasonable on the surface, since debt can pull us through emergencies, and the Bible treats debt and its repayment as more-less normal parts of life (although clearly noting associated dangers). A Reformed Christian perspective, however, calls us to evaluate debt within the broader Biblical principle of stewardship. The wisdom of taking on debt, then, depends on whether the borrower's motives are appropriate, whether debt is necessary to accomplish a goal, whether the proceeds of debt are used wisely, and whether future burdens associated with debt are well understood and accompanied by a sensible plan for repaying it.

The current motivation for assuming debt—to save massive numbers of jobs and entire sectors of the economy—appears particularly justifiable, but we also need to be open to the possibility that we are really motivated mostly by fear, and that the debt is actually related to habits of self-indulgence and/or lack of self-discipline. The total federal debt is about 23 trillion at the date of this writing, or roughly $70,000 for each man, women and child in the country. The 2019 fiscal deficit was roughly a trillion dollars and estimates for the projected 2020 deficit now start at about $3 trillion. So, the accumulated federal debt by the end of fiscal 2020 will be almost three times what it was in 2007. In addition, our government has also promised to protect depositors if their financial institutions make mistakes, pensioners if their companies make mistakes, investors if their brokers make mistakes, and retirees when their government fails to put money aside for them. And now, they promise to protect all of us when planning weaknesses exacerbate viral outbreaks. Of course, none of these kinds of promises need paralyze an economy if the government was adequately funding them—but, unable to pay its current bills, few are discussing how to fund vague and distant promises.

Our government's financial assault on the virus has been astounding by historical standards. The first two-plus trillion dollars of spending came with the Corona Virus Aid, Relief, and Economic Security (CARES) Act. One piece of this legislation involved initiating hundreds of billions of dollars of 1% interest-rate "Paycheck Protection" loans to tens of millions of businesses with fewer than 500 employees, for up to two years, to allow them to maintain their payrolls. Congress tasked the Treasury with absorbing the losses on these loans if least 75% of the money was used to support payrolls. Then, several weeks later, Congress added another half trillion in paycheck protection, loans and health-care grants to the original allotment. The original bill also appropriated several-hundred billion dollars to cover the expected wave of unemployment claims, increasing normal payout levels by an additional $600/per week per person for four months, and extended these benefits to both furloughed employees and many, like Uber drivers, who are technically not employees, but independent contractors. In addition, Congress has offered targeted relief by waiving ordinary qualifiers for unemployment compensation (like earnings history requirements) by extending debt forbearance to groups like student loan recipients, and by offering direct aid to hard-hit-businesses like airlines. Finally, Congress authorized "Recovery Rebates" to bolster economic activity during the pandemic. Most individuals earning less than $75,000 will receive $1,200. Couples with joint earnings below $150,000 should receive $2,400, with an additional $500 per child.

Absent good planning, the current spending may be the best we can do to retain jobs and keep tax revenues from imploding. But, the wisdom of borrowing even for productive pursuits is constrained by the likelihood of repayment, which in turn depends on financing costs over the life of the loans. Currently, our central bank is holding interest rates down and people and institutions are willingly lending to our government to protect their savings, so the government is financing its debt at historically low interest rates. But, if rates return to a more normal level of, say 5%, a $25 trillion debt would require $1.25 trillion per year just for interest. Interest rates will surely go higher since the debt-to-GDP ratio will cause the debt to be downgraded by ratings agencies. Government borrowing also crowds out potential private borrowers and, consequently, economic growth. And, without near-miraculous growth, servicing this debt will require massive amounts of taxes and/or money-printing. Unfortunately, taxes exert a drag on the economy and excessive money creation greatly increases the likelihood of a return to the deadly stagflation of the late 1970s/early 80s.

Additionally, the percentage of debt owed to foreign entities continues to climb. If these investors exchange their dollar loans for yuan or yen, interest rates will rise yet again and the international value of the dollar will drop, further increasing fiscal deficits and lowering growth. A cheaper dollar, although helpful to exporting companies, makes the U.S. poorer relative to the rest of the world as it makes shopping and investing overseas more expensive and puts our companies and assets "on sale" to investors from other countries.

Historically, consumption spending has been increasing faster than investment spending in the U.S., which boosts current prosperity but impairs future prosperity. This stresses the financial markets to the point where they attempt to choke off excess consumption with credit contraction. But, government has been countering this with massive, debt-financed stimulus programs, undercutting the market's ability to correct imbalances, and replacing consumer and business spending /debt with government spending/debt. Prior to 2008, super-low interest rates led to massive consumer borrowing and a housing bubble. Starting in 2008, continued interest rate suppression coupled with new evidence that government was willing to bail out private companies led companies to pile on cheap debt and repurchase stock, encouraging a stock market bubble. Debt was never lowered, it just shifted it from one sector to another. Now the government is saddled with debt when the prospects for the economic growth needed to pay down that debt look more unlikely than ever, in part because debt-laden rescue programs prevent the rebalancing needed to achieve healthy savings and investment patterns.

Rescue packages can also be life and economy-altering at a microeconomic level. For example, augmenting our existing unemployment compensation program undercuts its work incentives. For many companies and employees in low-wage industries, $1,000 per week in unemployment compensation means both lower company costs and bigger checks for idled workers. The emergency package is also throwing money at employers who would have retained their employees without government money. Additionally, company owners are both uniquely qualified and richly rewarded for providing goods and services, and planning for the risks associated with doing this. Companies that don't frivolously pay out or spend all of their earnings, choosing instead to build up corporate "equity cushions" with their profits, and/or personal "equity cushions" with their compensation benefit during downturns for having done these things. Unfortunately, the bailout we are seeing is most critical for companies that did not exercise this kind of foresight or financial discipline. Finally, many families making well under $150,000 have emergency funds that can carry them months into the future. Why then offer the kind of government fallback that will encourage more citizens *to not* put money away for emergencies.

Oddly, as a Reformed Christian, I remain optimistic even during this downward fiscal spiral. Yes, we have managed to kick the debt can down the road one more time, and it is getting very close to a wall. Yes, it looks like we haven't yet learned the dangers of trying to make debt less burdensome by printing money, moving us ever closer to the kind of inflation and currency devaluation that plagues perpetually poor countries.
But, one recurring theme in creation-fall-redemption history is that God uses both troubled people and troubled times to both call people back to himself and to advance his kingdom. I believe the current crisis is reminding some very self-assured people of their limitations, while also laying bare the bankruptcy of radical individualism. It also reminds us what government can and cannot do well. My prayer is that it will lead to better planning for the next pandemic by simulating which programs capably target the needy without throwing billions at everyone, and that we will see immense advantages of incentivizing private and public savings, investment and stewardship over short-term stop-gap responses.