HIGH SCHOOL EDITION
Journal of Student Research
Volume 12 Issue 3 (2023)

Economic Impact of Covid-19 in America

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ABSTRACT

This letter aims to provide a comprehensive analysis of the economic impact of the fiscal policies implemented by the U.S. government in response to the COVID-19 pandemic. It also aims to identify the key lessons for the U.S. government from its interventions and highlights the long-term implications of the policies implemented.

Introduction

The COVID-19 pandemic has resulted in an unprecedented economic downturn due to the rising unemployment rate and decreasing real wages and economic growth. In response to this crisis, the U.S. government implemented numerous fiscal policies to mitigate its effects on the economy and to support individuals, businesses, and families affected by the pandemic. This letter aims to analyze the impact of these fiscal policies on the U.S. economy during the COVID-19 pandemic. It focuses on key indicators such as economic growth, inflation, unemployment, and fiscal measures implemented by the government while specifically examining the effectiveness and sustainability of the policies implemented.

Before the COVID-19 pandemic, developed economies experienced lower economic growth than before the Global Financial Crisis (Layton & Makin, 2020). Hence, to mitigate the effects of the pandemic on the economy, the U.S. government implemented various fiscal policies, including stimulus packages and support for small businesses. However, the efficacy of these policies is being debated as some researchers argue that they do not address the problem in reality.

Literature Review

Due to the lower economic growth experienced by developed economies before the COVID-19 pandemic, the deficit of private investment in these economies slowed down the real wage growth (Layton & Makin, 2020). When the lockdown was implemented to prevent the spread of the COVID-19 virus, the International Monetary Fund (IMF) estimated a nearly 5% decrease in global growth, followed by a rebound the following year.

To deal with these recessionary outcomes, central banks worldwide and the U.S. Federal Reserve carried out quantitative easing by purchasing government bonds, with some banks even buying private-sector bonds. However, these purchases have many long-term implications, including the sudden inflation of asset prices and increased price inflation of goods and services due to increased economic activity. To address these issues, governments started implementing fiscal policies such as higher spending and lower taxes. However, this led to large fiscal deficits, such as the 2020 budget deficit spike. Furthermore, fiscal support was observed worldwide in methods such as additional welfare payments to individuals, grants to small businesses, payments to firms to retain staff, and other similar measures (Layton & Makin, 2020).

The U.S. government implemented several policies to mitigate the economic impact of the COVID-19 pandemic. However, policymakers were worried about potential business failures among small and medium-sized businesses. The decrease in fiscal support in 2021 could have resulted in liquidity problems for surviving but fragile firms.

Thus, during each lockdown, the economy experienced numerous shocks related to labor supply, productivity, and demand. After each lockdown, supply and productivity returned to the pre-COVID-19 levels, unlike sector-specific demands. Thus, policymakers had to consider the design and implementation of fiscal support policies to ensure that they are not only effective but sustainable in the long term (Garrincha's et al., 2021).

U.S. Core Policies During the COVID-19 Pandemic

In mid-March 2020, the U.S. government enacted the Coronavirus Aid, Relief, and Economy Security Act (CARES Act), a legislative measure with a monetary value of $2.3 trillion. This Act encompassed a one-time tax refund of $293 billion to individuals, extension of unemployment benefits, prevention of corporate bankruptcy through loans, and other forms of assistance. It allocated funds to state and local governments for assistance (IMF, 2020). The Paycheck Protection Program and Health Care Enhancement Act further increased the financial support provided to small businesses by offering additional resources and facilitating employee retention (IMF, 2020).

Furthermore, in 2021, the then U.S. president Donald Trump signed a COVID-19 relief and government funding bill, which included provisions such as improved unemployment benefits, including a weekly federal pay of $300 until March 14, 2021. In addition, individuals received stimulus payments of $600, besides increased funding for vaccines and education (IMF, 2020).

Economic Stance of the U.S. Government during the COVID-19 Pandemic

The U.S. government primarily relied on fiscal policy measures to address the effects of the COVID-19 pandemic on the economy. A fiscal policy involves government spending and taxation to influence the economy and is a suitable tool to alleviate the impact of the COVID-19 pandemic on families, individuals, and businesses. It allows for targeted intervention that supports specific groups that have been disproportionately affected by the pandemic.

In contrast, a monetary policy is used to primarily influence the market conditions and the cost of borrowing; thus, it exerts a less direct influence on the daily lives of individuals and businesses. Whereas the monetary policy plays an important role in stabilizing the economy, the fiscal policy provides direct assistance through methods such as direct cash payments, small business loans, unemployment benefits, and healthcare support.

To prioritize aid for those most in need, the U.S. government implemented the COVID Preparedness and Response Act and the Family's First Act. The former allowed the promotion of general population well-being, whereas the latter provided individuals with paid sick leave and extended absence in case of a COVID-19 diagnosis.

Hysteresis

The following three factors are the crucial indicators that provide insights into the state of a country's economy: the unemployment rate, inflation rate, and disposable personal income. The unemployment rate takes into account the individuals who are actively searching for work (Bondarenko, 2023). The inflation rate measures the price increases over time (Oner, 2019), and disposable personal income refers to the amount of income individuals have left to spend after tax deductions (Kenton, 2023). Economists and

policymakers use these three variables to assess the state of a country's economy and design appropriate policies.

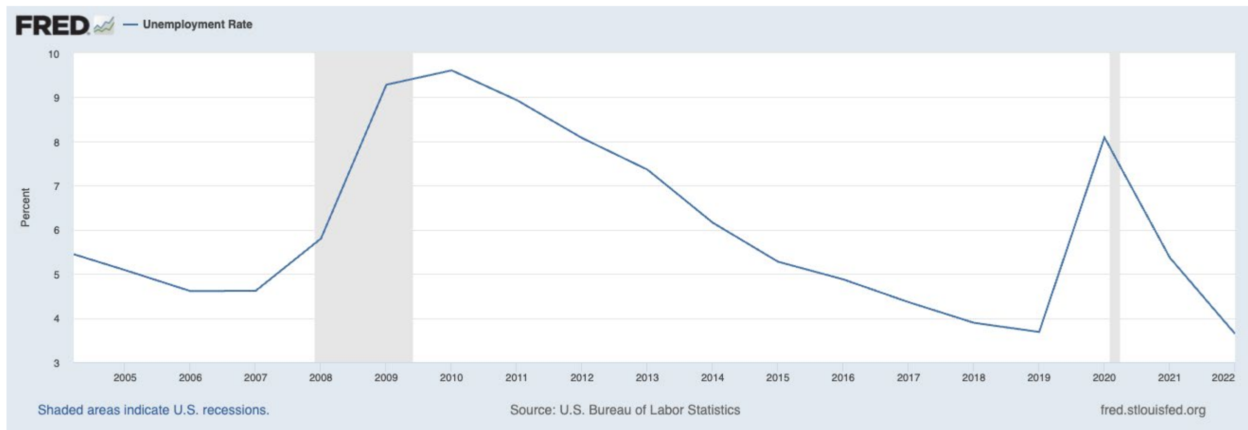

Figure 1: U.S. Bureau of Labor Statistics, Unemployment Rate [UNRATE], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/UNRATE, May 9, 2023.

The unemployment rate in the United States from early 2005 to 2022 is presented in Figure 1. As the COVID-19 pandemic peaked in March 2020 in the United States, a significant peak in unemployment occurred—the highest the country had witnessed since 2010. It can be inferred that this increase in unemployment was attributable to the infectious spread of the COVID-19 virus. To counter this sudden peak in unemployment, the U.S. government passed the CARES Act to aid the unemployed. The Paycheck Protection Act also supported individuals as it increased the financial support provided to small businesses, thus allowing them to retain their employees. These measures were important to combat the increasing unemployment rate and to prevent the resultant downward spiral of the U.S. economy as the GDP decreased.

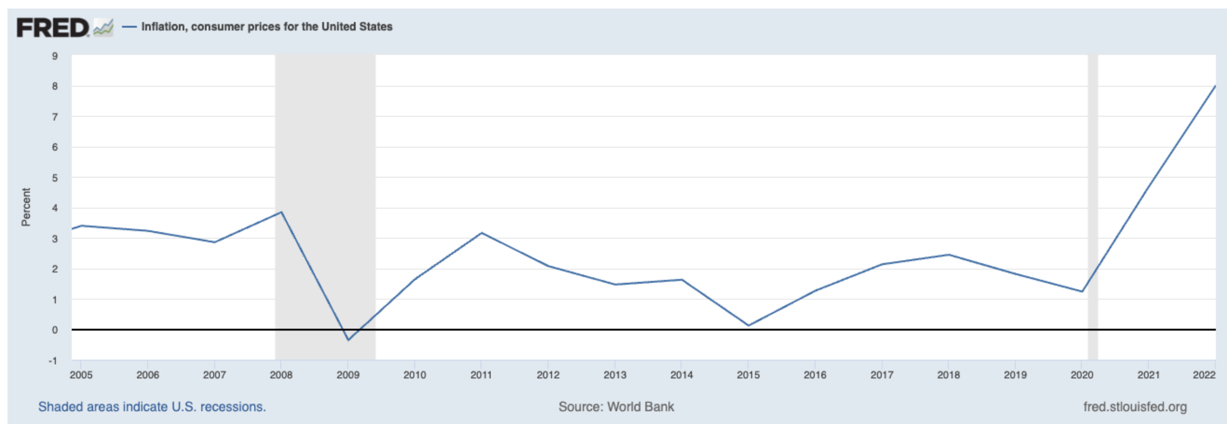

Figure 2: World Bank, Inflation, consumer prices for the United States, retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/FPCPITOTLZGUSA, May 9, 2023.

A graph of the inflation rate of the U.S. government as measured by the Consumer Price Index (CPI) is presented in Fig. 2. As mentioned elsewhere, the COVID-19 pandemic peaked in early 2020, and

a corresponding decrease in inflation during that period can be observed from the graph. Since inflation measured by the CPI shows the yearly change in the cost of specific goods and services, the decrease in their prices in 2020 reflects the overall economic downturn in the U.S. economy. The inflation increased as the government increased the money supply in the economy while enacting numerous fiscal measures to combat the disastrous effects due to the COVID-19 pandemic. As a result of the increase in money supply, the inflation rates started to increase. The sudden increase in inflation and the high unemployment rate resulted in stagflation, indicating an upcoming economic downturn in the U.S. economy.

Figure 3: U.S. Department of the Treasury. Fiscal Service, Federal Debt: Total Public Debt [GFDEBTN], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/GFDEBTN, May 14, 2023.

The annual total public debt in the U.S. is represented in Fig. 3, which shows that the U.S. debt experienced an instantaneous increase directly after COVID-19 entered the country. The fiscal measures taken to counteract the effects of the COVID-19 pandemic resulted in an increase in the public debt. The U.S. government increased spending through numerous acts such as the CARES, Paycheck Protection, and former President Trump's executive orders to support individuals in need. However, as it is increasingly difficult to service the high level of debt in an inflationary environment, a potential devaluation of the U.S. currency occurred.

Conclusion

In summary, the COVID-19 pandemic has had a detrimental effect on the U.S. economy as evidenced by the trends in inflation, disposable personal income, and unemployment illustrated in the graphs presented. The fiscal policies introduced by the U.S. government were effective in the short term as they increased the GDP and decreased the economic instability in the lives of most individuals. However, their long-term implications and policies that need to be designed to improve the economy further are difficult to predict. The U.S. government's decision to pass the CARES Act, Paycheck Protection Program and Health Care Enhancement Act, and the COVID relief bill was correct as these acts benefited both individuals and certain aspects of the economy.

However, the acts that provided stimulus checks to individuals to improve consumer spending and that provided tax forgiveness to small businesses and individuals increased the budget deficit, which could

have long-term adverse effects. Furthermore, the recent bank run in Silicon Valley alongside the increase in Federal Reserve's interest on the reserves to 5.15% has caused many to forecast a forced recession to remedy the lasting effects of COVID (Federal Reserve, 2023).

To mitigate these recent challenges, it is imperative to monitor the key economic indicators highlighted and implement the most effective policies that can promote long-term economic growth and stability. Though this will likely be a challenging process, the U.S.government must persevere to ensure that the economy recovers and thrives in the upcoming years.

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