THE HILL

Boost supply, not demand, during the pandemic

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COVID-19 is battering the U.S. economy, causing many businesses to cut back and close down. Policymakers are considering a huge $1 trillion stimulus package with an array of subsidies designed to boost consumption. Pundits often say things like "70 percent of the economy is consumption" and "America has a consumer-driven economy." That leads them to think that reviving growth rests on inducing people to spend.

Consumer spending is 70 percent of aggregate demand, but that is only one side of the economy. The other side is supply—the production of goods and services. The government can stimulate demand all it wants, but it won't move the needle on GDP if production is halted because of health fears. Instead, governments need to give producers certainty that it's doing everything it can to help people safely get back to work.

The first issue with a stimulus plan is that federal budget deficits already top 1 trillion dollars a year, and deficits will increase further even without such a package as the economy enters recession. Piling on more debt from a stimulus would risk triggering a financial crisis on top of the health care crisis. A fiscal stimulus won't help the economy, because the Keynesian notion that consumption is the driver of growth is false. President Obama pushed through an $800 billion stimulus after the financial crisis a decade ago and the U.S. suffered the slowest recovery since World War II.

The coronavirus is creating both a supply and a demand shock to the economy. The supply shock stems from disrupted supply chains and businesses closing down for safety reasons or due to government mandates. The demand shock stems from individuals cutting back on spending as their income declines and their fears rise. At the same time, businesses are deferring investments as revenues fall. So aggregate demand and supply are both shifting downward and reducing gross domestic product.

Policymakers are proposing to stimulate demand to re-inflate GDP. President Trump had proposed zeroing out the federal payroll tax, but now is leaning toward a $1,000 per-person stimulus check. This could start a bidding war for hand-outs because the "money for everyone" approach has bipartisan appeal.

However, a demand-side stimulus would accomplish little except moving the government closer to a debt crisis. It would have a hard time boosting GDP because the supply side of the economy is damaged by supply-chain bottlenecks and safety fears. A stimulus would give consumers more cash, but the economy will shrink nonetheless if restaurants, travel, and other goods and services are closed. Rather than raising output, much stimulus money would end up as personal savings or bid up prices for the products still available in a smaller economy.

What to do? Governments should help companies resume production safely. They should work to ensure availability of testing kits, sanitizers, gloves, masks and other equipment. South Korea is showing that widespread and rapid testing can empower the private sector with better information and reduced uncertainty.

There are plenty of regulations that the federal government, state governments, and local governments should reevaluate to give businesses operational flexibility. In particular, it's worth modifying regulations that make it more costly or more time-consuming to bring on new workers. Policies such as California's recently-enacted laws classifying gig economy workers as full-time employees, for example, hamper the kind of flexibility that workers need.

And as the pandemic unfolds, local government should do everything they can to preserve public health while looking for ways to allow businesses to safely reopen or resume operations. The more businesses that close, the more that supply chains for other businesses will be disrupted. The more workers who lose incomes, the more government handouts will be demanded that the country cannot afford.

To avoid a disastrous downward spiral, we need to employ every strategy to allow businesses to quickly retool for safety and resume operations. Closing businesses harms lower-income workers and brings about fear that shutdowns will be long-term, so it's critical that policymakers provide assurances that they have a plan in place that will eventually allow business as usual to pick up. News accounts indicate that businesses are doing just that. Companies are equipping workers with gloves and masks, taking worker temperatures, spacing out restaurant tables, reconfiguring factory work stations, sanitizing work areas, adjusting schedules, and allowing employees to work from home. Careful use of these practices could help speed up the process of getting people back to work once public health professionals give the all-clear.

Governments can also support production by reducing business costs. The U.S. Treasury is easing income tax payment deadlines, and local governments should do the same with property taxes. The government should also ease rules on the use of income tax losses to support business cashflow, while ensuring access to credit for cash-strapped firms.

But policymakers should refrain from imposing costly rules on businesses, such as mandates for paid sick leave, and from pursuing price-gouging cases, which undermine incentives for businesses to supply needed goods. These perhaps well-intentioned interventions don't work during regular times, and during a public health crisis they will likely have an even more destabilizing effect on markets for goods and services.

The federal government can expand the supply of critical health resources. It should repeal protocols that are undermining hospital flexibility in hard-hit areas and repeal restrictions on telemedicine and doctors practicing across state lines. Restrictions on virus testing have been a failure. Thankfully, the government has finally decided to allow companies to sell test kits directly to the public, which will empower the private-sector response.

Social distancing and some shutdowns are no-brainers. Schools should be closed because learning can move online, and visitors should be barred from places such as nursing homes. But proposals to shutter major industries, such as automobile manufacturing, are likely counterproductive overall. The economy would collapse with such closures, which would ruin many lives.

Treasury Secretary Steven Mnuchin said that a government stimulus is necessary because unemployment could reach 20 percent. But the way to prevent such a disaster is to help American businesses maintain production. Rather than Keynesian subsidies and top-down mandates, policymakers should support the private sector with medical supplies, widespread testing, and allowing flexible responses by businesses and hospitals.

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