Economic Roundtable Testimony

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The Beacon Hill Institute is pleased to offer its testimony to the roundtable called by the Executive Office of Administration and Finance and the Joint Ways and Means Committee.[1] We base our predictions on data from previous economic downturns.

BHI predicts that in 2020:

- **U.S. GDP will decline by 7.4 percent;**
- **Massachusetts GDP will decline by 7.2 percent;**
- **The Massachusetts unemployment rate will increase to 14.7 percent; and**
- **Massachusetts state tax revenues will decline by 20 percent.**

The coronavirus crisis will have a devastating impact on the economy. Businesses deemed non-essential have been ordered closed, leaving owners with no income to pay their employees or meet other business expenses. The unparalleled shutdown has rippled through the economy. Approximately 25 percent of the U.S. economy is offline.[2] Eight in 10 counties across the nation are under lockdown today. These counties represent 96 percent of all U.S. output.[3]

Markets have cratered due to the pandemic. The S&P 500 and Dow Jones indices are down over 25 percent from their previous highs. Markets recently improved slightly, resulting from the passage of a massive stimulus package. Markets must make substantial gains to recover the record-highs reached recently. In recent days the market has gone through stops and starts with no indication that investors can overcome market uncertainty and restore the market to a steady state. As health care models also remain uncertain as to the end of a lockdown, long-term equity markets are impossible to assess.

The labor market has already incurred significant losses and will show further losses as both consumer and business demand continues to fall. The restaurant, tourism, retail, and leisure industries have incurred the bulk of job losses thus far, as businesses have been shuttered or heavily limited in day-to-

[1] Prepared by the staff of the Beacon Hill Institute, including William F. Burke, Frank Conte and David G. Tuerck.
[2] Josh Mitchell, "State Shutdowns Have Taken at Least a Quarter of U.S. Economy Offline Eight in 10 U.S. counties are under lockdown orders, according to a study, and they represent nearly 96% of national output," Wall Street Journal, April 6, 2020. https://tinyurl.com/t2c5ekc.
[3] Ibid.

day operations. But employment in other sectors is sure to follow as construction sites close down, office parks empty, education goes offline and recreational outlets shutter.

As the April 3 Bureau of Labor Statistics payrolls report notes: "March data from the establishment and household surveys broadly reflect some of the early effects of the COVID-19 pandemic on the labor market....It is important to keep in mind that the March survey reference periods for both surveys predated many coronavirus-related business and school closures in the second half of the month."[4]

The report noted that the merchandise retail sector added 10,000 jobs. That number provides no solace as that front-line work is now high-risk. Even the predominant highly compensated high-growth health care sector is shedding jobs. Employment in health care and social assistance fell by 61,000 in March. Health care employment declined by 43,000, with job losses in offices of dentists, offices of physicians, and offices of other health care practitioners. Over the prior 12 months, health care employment had grown by 374,000. In March, according to the BLS, social assistance saw an employment decline of 19,000, reflecting a job loss in child day care services (-19,000). Over the prior 12 months, social assistance added 193,000 jobs.

The key professional and business services sector may prove to be at the forefront: In March, employment in this sector decreased by 52,000, with the decline concentrated in temporary help services (-50,000). To no one's surprise: employment also decreased in travel arrangement and reservation services (-7,000).

The ADP Research Institute, in its March national employment report, reported that nonfarm private sector employment fell by 27,000 jobs. ADP also reports job losses of 90,000 among small businesses and losses of 4,300 in US franchise employment.[5]

It is now widely expected that the pandemic will persist for a longer period of time than initially expected. This will only increase the burden on employers and could result in depression-level job losses. The implications across the board for the broader economy will be devastating.

Global supply chains face major disruptions and increased costs related with the pandemic. And if these problems worsen, consumers could see large shortages of essential goods and significant increases in prices.

Elsewhere in the economy, the residential and commercial real estate market will be burdened moving forward. Businesses that have been forced to close and people who have lost their jobs will be unable to pay their rent or mortgages, which could in turn lead to a collapse in the real estate market.

While the economy cannot functionally restart until the COVID-19 virus is properly contained, Congress has responded. The stimulus package signed into law by the President on March 27th is an imperfect, but necessary measure to help prevent economic collapse. The $2 trillion "stimulus" package is a step in the right direction in staving off incoming liquidity issues facing businesses large and small.

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[4] Bureau of Labor Statistics. Employment Situation Summary for March 2020, https://www.bls.gov/news.release/empsit.nr0.htm

[5] ADP National Employment Report: Private-sector employment decreased by 27,000 from February to March, on a seasonally adjusted basis." April 1, 2020. http://www.adpemploymentreport.com/2020/March/NER/docs/ADP-NATIONAL-EMPLOYMENT-REPORT-March2020-Final-Press-Release.pdf

Without revenue, businesses cannot pay expenses and thus, cannot pay their employees. Consumers already faced a severe lack of savings and now face the possibility of losing their livelihood due to the pandemic. The combination of these issues will prove devastating for the United States and Massachusetts economies in both the short and long term.

The U.S. Economy

As it currently stands, the global economy and U.S. economy face an inevitable deep recession. If the pandemic sustains for a long period of time, the state of the global and US economy could reach depression levels, with unprecedented job losses and shrinkage of GDP.

The Bureau of Economic Analysis will not release its first quarter GDP estimates until April 29. However, various institutions have released their forecast for US economic growth in the first quarter and for the rest of the year. Bank of America economists expect US real GDP to contract 10.4 percent for the year, with growth to return in the third quarter after significant contractions in both the first and second quarters.[6] Morgan Stanley economists expect US GDP to fall by 5.5 percent for the year.[7] Goldman Sachs expects GDP to fall by 6.4 percent.[8]

According to the IHS Markit U.S. Sector PMI, the U.S. private sector output declined significantly in 6 out of 7 industries (with the healthcare industry being the only exception).[9] According to the survey, the consumer services, technology, industrial, and financial industries saw record decreases resulting from business closures.

According to Bill Dunkelberg, Chief Economist of the National Federation of Independent Business, "The impact from the coronavirus will have a lasting effect on the small business economy. Labor shortages continued throughout the first half of March, but with the updated number of jobless claims, the small business labor situation has been altered. The severity and duration of the coronavirus outbreak and the mobility of regulations imposed will determine owners' ability to remain operational."[10]

Across the nation, state and local government revenue will face strains. Revenue for state and local governments will begin to fall due to mass closures of businesses around the country as the loss of jobs leads to massive short falls in personal income tax revenues. According to the Brookings Institute, state tax revenues fell by $120 billion from 2008 to 2009 due to the Great Recession. The revenue shortfalls for state and local governments could be even greater due to the pandemic. Spending will likely increase as more people file for unemployment and the number of people eligible for Medicaid increases. The strains on budgets will make it even more imperative that states receive assistance from the national government.

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[6] Mark DeCambre, "Brace for the 'deepest recession on record,' says BofA analysts, as jobless claims surge to 6.6 million," MarketWatch, April 4, 2020, https://www.marketwatch.com/story/brace-for-the-deepest-recession-on-record-says-bofa-analysts-as-jobless-claims-surge-to-66-million-2020-04-02

[7] Steve Goldstein, "Morgan Stanley forecasts 38% drop in second-quarter U.S. GDP," MarketWatch, April 3, 2020 https://www.marketwatch.com/story/morgan-stanley-forecasts-38-drop-in-second-quarter-us-gdp-2020-04-03

[8] Jeff Cox,"Goldman sees 15% jobless rate and 34% GDP decline, followed by the fastest recovery in history," MarketWatch, April 2, 2020, https://www.cnbc.com/2020/03/31/coronavirus-update-goldman-sees-15percent-jobless-rate-followed-by-record-rebound.html

[9] IHS MarkIt,"Rapid downturn in private sector activity led by consumer services in March," April 3, 2020. https://www.markiteconomics.com/Public/Home/PressRelease/c0cc472947fc4ee3b459aaf8209ea4c2

[10] National Federation of Independent Business, "Small Business Labor Market Remained Solid Until Virus Uproar in March," April 2, 2020 https://www.nfib.com/content/press-release/economy/small-business-labor-market-remained-solid-until-virus-uproar-in-march/

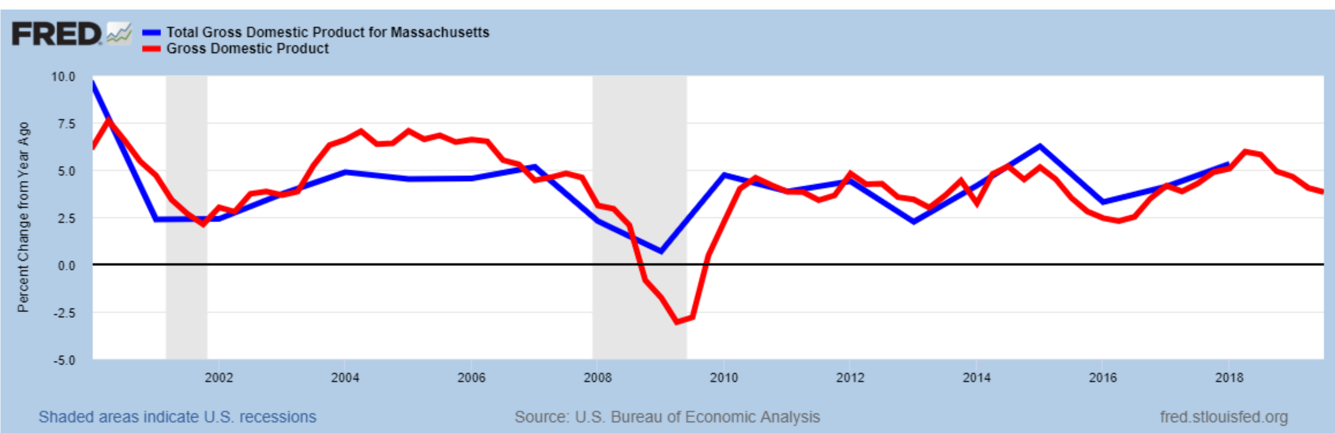
The Massachusetts Economy

Much of the latest data available for the Massachusetts economy predates the crisis. Nevertheless, it is clear that the Massachusetts economy will face a deep recession, possibly a depression, if the pandemic persists beyond May.

According to the March 28 Department of Labor Unemployment Insurance Weekly Claims report, workers in Massachusetts filed 181,062 unemployment claims.[11] In the previous week, unemployment claims in the state totaled 148,452. Massachusetts had the fifth highest insured unemployment rate in the country in the week ending March 14. Since then, 329,514 people have filed unemployment insurance claims in Massachusetts, representing 8.59 percent of the state's workforce.

The coming months will however see job losses continue to increase as businesses are strained from falling demand or are forced to close. According to a poll by Princeton Research Associates, nearly 90 percent of all Massachusetts residents expressed concern about their economic well-being.[12] This view was expressed in every region in the state. According to the Suffolk University Political Research Center, 53 percent of Massachusetts residents were concerned about their financial and employment situation as a result of the coronavirus crisis. The survey findings were also consistent for every region of the state.[13]

The Massachusetts economy typically outpaces the national economy in growth and generally performs better in an economic contraction. Over the past 20 years, the Massachusetts economy has outpaced the national economy in growth by an average of .2 percent per year. BHI believes that Massachusetts will continue to perform better than the rest of the country in the current economic crisis.



[11] U.S. Department of Labor, "Unemployment Insurance Weekly Claims Data - Report r539cy," April 6, 2020.
[12] Princeton Research Associates, March 16 poll, http://www.princetonresearchassociates.com/3_16_20_MassPOPS_State_by_Region.pdf,
[13] Suffolk University Political Research Center, Massachusetts Polling, March 28, 2020: MA Statewide Issues with The Boston Globe. https://www.suffolk.edu/-/media/suffolk/documents/academics/research-at-suffolk/suprc/polls/massachusetts2/2020/3-28-20-ma_marginals.pdf?la=en&hash=0BCF09C4A2768DE9CAB91CB4ADE3979F8D0F5489.

Estimates for GDP and Massachusetts Employment

The Institute took the average of the estimates from the economists of Bank of America, Morgan Stanley, and Goldman Sachs to get its estimate for a fall in US GDP of 7.4 percent in 2020. For Massachusetts, we predict, based on past experience, that GDP will contract by 7.2 percent on the year.

Massachusetts state tax revenues are set to face a significant strain as most revenue streams will fall significantly. We predict that state revenues will fall by 20 percent. During fiscal year 2002, Massachusetts state tax revenues fell by nearly 15 percent. During fiscal year 2009, revenues fell by nearly 13 percent (or by $2.579 billion). Over the same time period, US GDP fell 3.9 percent.

The Institute estimates that state tax revenues will fall by 20 percent if US GDP contracts by 7.4 percent this year.

Economists for the Bank of America are forecasting the national unemployment rate to jump to 15.6 percent on the year. Morgan Stanley economists have revised their unemployment forecast for the US to 15.7 percent on the year.[14] And Goldman Sachs economists have forecasted that the US unemployment rate will increase to 15 percent on the year."[15]

The Institute takes the average of the three estimates from Bank of America, Morgan Stanley, and Goldman Sachs to obtain our estimate of the national unemployment rate of 15.4 percent.[16] The Massachusetts unemployment rate has outperformed the national unemployment rate by an average of .7 percent over the past 20 years. Therefore we predict that the MA unemployment rate for the year will be 14.7 percent.

[14] Tommy Reggiori Wilkes and Sujata Rao, "U.S. economy to shrink at fastest rate since 1946, unemployment to top 15%: Morgan Stanley," Reuters, April 3, 2020. https://www.reuters.com/article/us-health-coronavirus-economy/u-s-economy-to-shrink-at-fastest-rate-since-1946-unemployment-to-top-15-morgan-stanley-idUSKBN21L0SC

[15] See Cox, April 2, 2020.

[16] See footnotes 6 and 8.

The Beacon Hill Institute for Public Policy Research focuses on federal, state and local economic policies as they affect citizens and businesses. The Institute conducts research and educational programs to provide timely, concise and readable analyses that help voters, policymakers and opinion leaders understand today's leading public policy issues.

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