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Keeping the Economy Going in COVID19 Lockdown – A Proposal for "Low Cost" Generalised Insurance of Business and Household Incomes

I have been musing on possible solutions to the economic impacts of pandemic from its early days. One week into New Zealand's COVID19 lockdown, and observing the global economic freefall taking place, I have landed on a solution I think is both increasingly necessary, and likely to be lower cost and more effective than existing measures, for seeing our economy through to the other side of the pandemic.

The problem I see is that the pandemic response is simultaneously collapsing many firms' ability to remain viable, and many households' ability to pay their bills. Job losses are merely a symptom of this, and wage subsidy schemes or one-off handouts are too limited (and expensive) a solution. This is not to argue for a trade-off between saving lives and saving the economy – I take it as given that some sort of extreme public health response is necessary, and want to focus instead on how to keep the economy going while it occurs.

What is needed is a scheme whereby both shareholders and employees share some burden/risk of the lockdown, but in a way they can manage in a reasonably low cost way. It is simply unrealistic to expect shareholders of firms facing lockdowns of unknown durations and frequencies to fully underwrite the incomes of employees (with or without the existing subsidy), especially given companies legislation liabilities on directors for trading while insolvent.

Yet, if those employees are not insured, then demand collapses, and businesses and the economy free-fall. Even healthy businesses (e.g. supermarkets) will face the pinch when households run out of money for food.

My initial thought involved generalised moratoria on fixed household and business expenditures like mortgages, leases and utilities, with government underwriting providers' losses to the extent they can't be recovered from customers in the future (e.g. through higher future mortgage payments). However, that would likely be expensive, and doesn't offer households enough income insurance for them to keep spending (e.g. on food) – if they have no income, then even moratoria won't help.

The solution came to me when thinking about what a utility company moratorium would amount to, which is the utility acting as the household's banker, by extending them a "utility overdraft". I think this would not be efficient (imagine all firms trying to set this up), and still not enough to adequately insure household incomes.

The alternative is a generalised loan scheme with the following features:

1. Government COMMITS to making interest-free loans available to all businesses, and to all households who don't already enjoy insured incomes (i.e. excluding superannuitants, beneficiaries, state employees – they can access WINZ's emergency loans as required in the normal way);

2. The loans are proportional to the businesses' and households' reported revenues in the most recent financial year, pro-rated to the length of any lockdown - proportionality is utterly key: a $585/week wage subsidy doesn't pay the mortgage for the many households who earn much more than this and who have leveraged themselves into lifestyles that amount of money won't sustain, and loans of this sort will be in proportion to both need and capacity to repay;

3. Government COMMITS IN ADVANCE to making further such loans as and when lockdowns are extended or reinstated;

4. Loans are repayable out of future income, by way of increased marginal tax rate for those who draw down the loans, recovered via IRD, and from estates of people who die before repaying - a bit like the student loan scheme (i.e. we have a lot of the necessary apparatus already in place);

5. Business loans are the liability of shareholders, not the firms themselves, so firms cannot voluntarily liquidate to avoid repaying them, nor can at-risk businesses think they can use the loans to gamble their way out of trouble - and firms don't make themselves insolvent by taking the loans on;

6. A condition of the business loans might be that businesses commit to paying [50%] of their employees' wages/salaries for the duration of any lockdown, with households able to top up any income shortfall through their own loans.

The commitment element of the above loans is a bit like Mario Draghi's famous "whatever it takes" speech – to avoid the economy (rather than just the banks, though surely they would follow the economy) falling into a free-fall.

Households need to know, whatever happens, they can still pay their bills on time. Yes it will cost them something in the future, in the form of slightly higher tax payments, but none of us gets out of this without pain. If they can keep paying their bills, then businesses relying on them doing so can "keep the party going", which in turn keeps employees partly insured, etc.

Offering shareholders a relatively low-cost means of keeping their firms in business lowers the risk of widespread liquidations. Yes, this will cost them in the future too, but they are not being asked to shoulder all the burden, as employees/households will too. Shareholders will still need to decide whether to fight on or to fold, but they can do so with greater confidence that there is a relatively low-cost way through (and their rivals will be facing the same pressures, so the competitive landscape needn't alter radically). But shareholders will not take on business loans unless they think their business has a shot at staying viable (since they carry the loans themselves).

Households might decide to take up the loans even if they don't need to. But that is probably the lesser risk to worry about at the moment. The scheme offers them income insurance if their employers can only (reasonably/realistically) offer them partial insurance. So, one way or another, households can "keep the party going".

What policymakers need to worry most about is household expenditures collapsing, since businesses will surely follow (and businesses collapsing also precipitates households not spending ...). And if households take on "student loans" they don't need, they will face higher future taxes and won't be able to shirk them.

Fiscally, government faces the cost of offering interest-free loans, but at current rates that is not so bad. And if the alternative is government underwriting large subsidies by borrowing against future generations, that is likely to be more costly and less inter-generationally equitable (the loans I propose are not slated to future generations). In any case, the real calculus for government is being able to take tax revenues from an economy that keeps ticking over, versus the lower revenues from an economy that tanks.

Like fighting COVID19 itself, solutions work best when implemented aggressively and early. This proposal is no different. Household and business incomes need insuring now if an irreversible decline in economic confidence is to be averted. I hope this proposal stimulates discussion and debate, and contributes to whatever solutions we ultimately land on.

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