

**Lessons for Automatic
Fiscal Stabilizers
from the Great
Recession and the
COVID Recession**

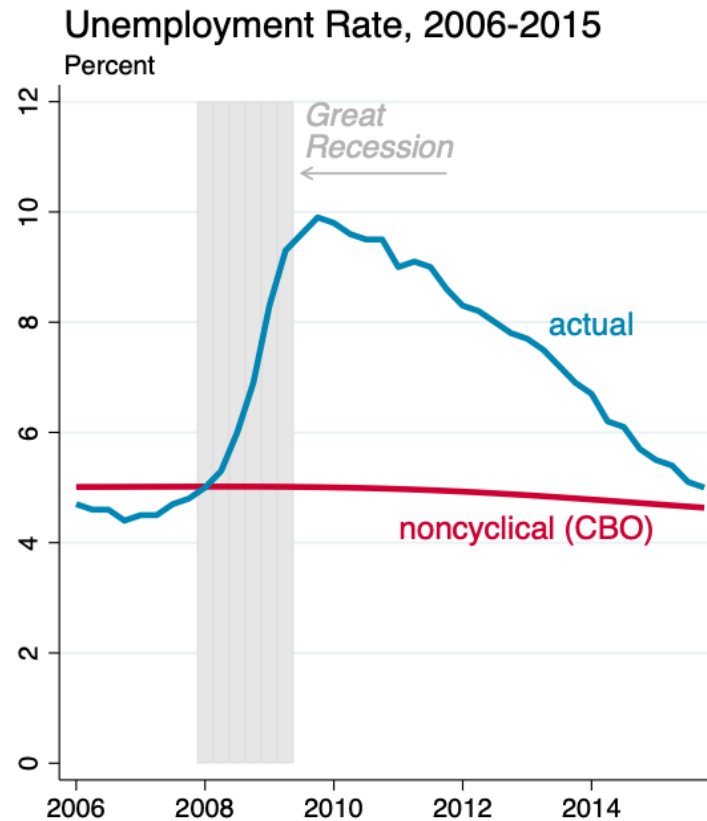
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40th Annual NBER Tax Policy and
the Economy Conference
September 18, 2025

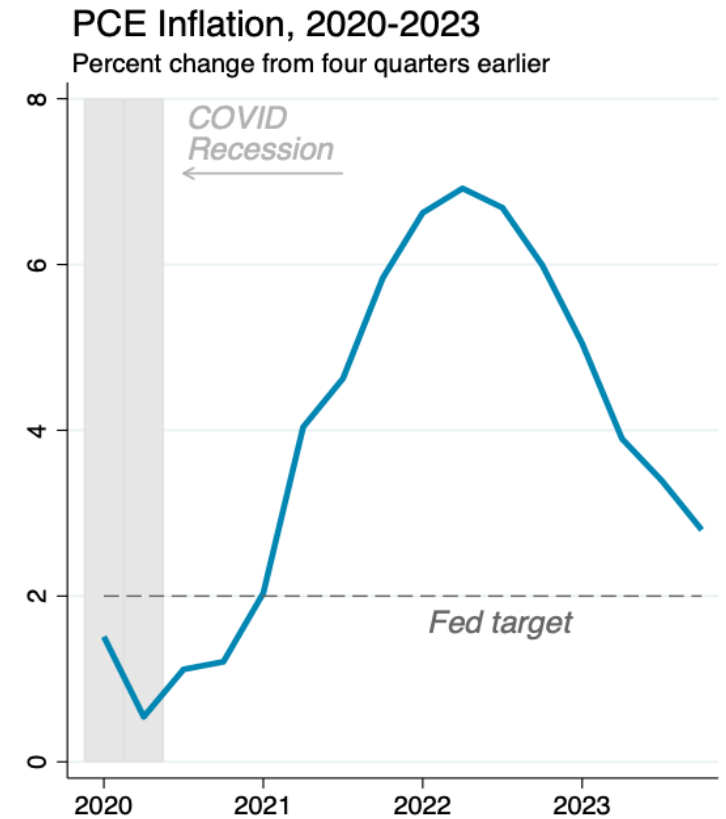
Fiscal and monetary policy responded forcefully to the Great Recession and the COVID recession

Policy actions sharply reduced the economic losses and human costs

But some outcomes beg the question of whether policy could have been better



Data source: Congressional Budget Office and Bureau of Labor Statistics (via FRED).



Data source: Bureau of Economic Analysis (via FRED).

Could expanded automatic fiscal stabilizers have improved outcomes during these periods?

We **simulate economic developments** during these periods

as if **discretionary fiscal actions had not been taken**, and

as if an **additional stabilizer**—tied to labor market conditions—had been in place

We **compare simulated outcomes to the realized outcomes**

Preview of findings

Great Recession: faster labor recovery

COVID Recession: less inflation

Fiscal costs: smaller cumulative deficits

Caveats—estimates are sensitive to assumptions; we test only one stabilizer design

Discretionary countercyclical fiscal policy

	Legislation	Spending Change	Revenue Change	Deficit Change	
GREAT RECESSION	Economic Stimulus Act of 2008 (2/13/08)	42	-82	124	
	American Recovery and Reinvestment Act (2/17/09)	663	-173	836	
	Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, certain provisions (12/17/10)	56	-136	192	
	Middle Class Tax Relief and Job Creation Act of 2012, certain provisions (2/22/12)	30	-93	123	
	TOTAL	791	-484	1275	← 10 percent of pre-crisis GDP
COVID RECESSION	Coronavirus Preparedness and Response Supplemental Appropriations Act, 2020 (3/6/20)	8	0	8	
	Families First Coronavirus Response Act (3/18/20)	97	-94	192	
	Coronavirus Aid, Relief, and Economic Security (CARES) Act (3/7/20)	1314	-408	1721	
	Paycheck Protection Program and Health Care Enhancement Act (4/24/20)	483	0	483	
	Consolidated Appropriations Act, 2021, Divisions M and N (12/27/20)	862	-5	868	
	American Rescue Plan Act of 2021 (3/11/21)	1803	-53	1856	
	TOTAL	4567	-560	5128	← 23 percent of pre-crisis GDP

Scale of existing automatic stabilizers

Great Recession:

FY 2009-2012: increased deficits by about \$1.1 trillion

FY 2013-2017: increased deficits by about \$700 billion

nearly as large
as
discretionary
stimulus

COVID:

FY 2020-2021: increased deficits by about \$450 billion

much smaller
than
discretionary
stimulus

Key design characteristics for potential new stabilizers

What **types of taxes and spending** should adjust?

Impact on demand, who is helped, administrative feasibility

What should be **the trigger** for adjustment?

Speed, starting and ending conditions, data availability

How much taxes and spending adjust?

Share of output gap to be closed

Methodology

New stabilizer: Direct payments to households



Triggers:

- ☒ Unemployment rate rises 0.5pp above 3-month lag
- ☐ Unemployment falls below 5 percent

Size: Proportional to unemployment gap \times GDP



Modeling approach: We calculate counterfactuals and dynamically simulate using rules of thumb for key economic relationships => more transparent compared with relying on a full model

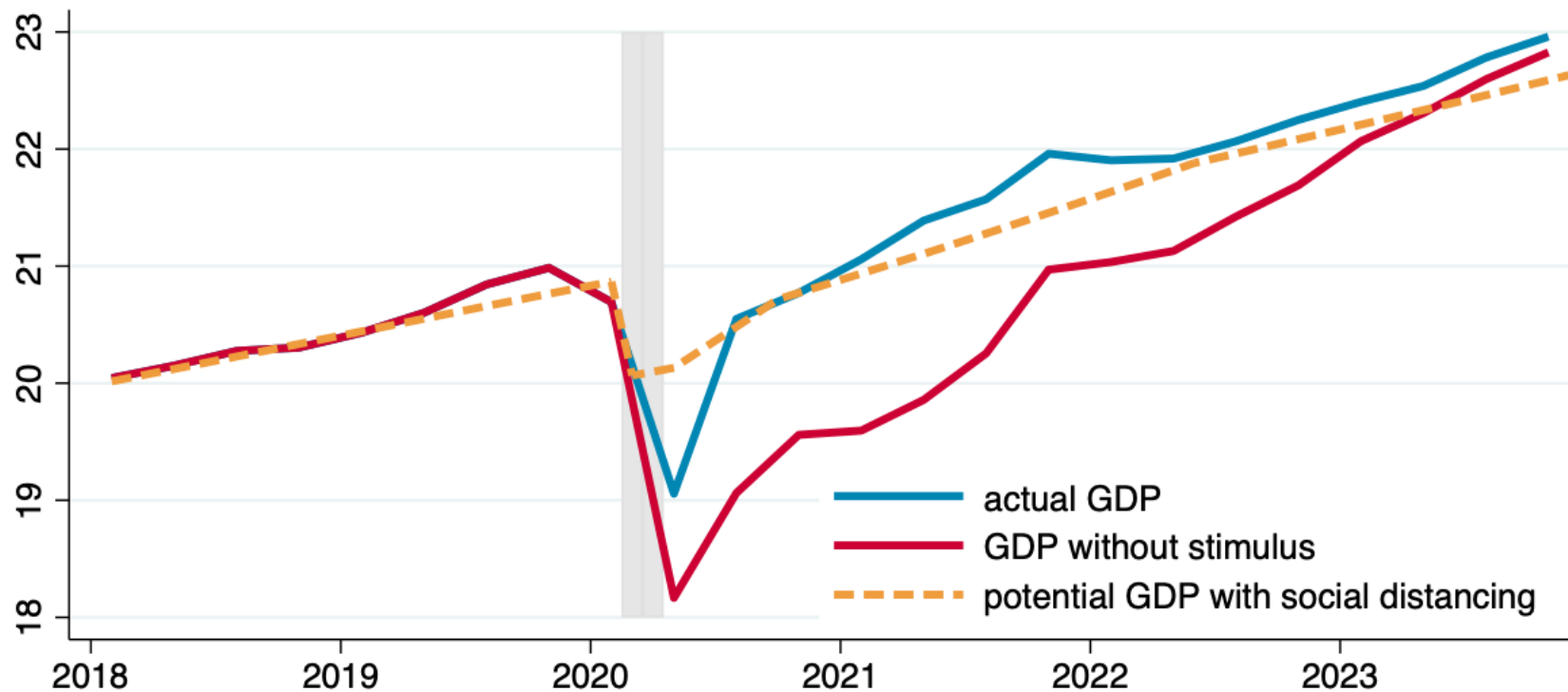
Key rules of thumb

Relationship	Rule of thumb	Source/Notes
Effects of fiscal stimulus on demand	Multipliers (following CBO)	Based on literature, adjusted for social distancing during COVID
Effects of demand on output, inflation	Nonlinear Phillips curve: flat below potential, 1-for-1 up to +1% above potential, 5-for-1 beyond	Captures inflation surge in 2021–22
Effects of output on unemployment	Okun's Law: 1% ↓ in output → +0.5 pp in unemployment rate	Standard empirical regularity
Pandemic potential output	Temporary 4% reduction , fading to zero by mid-2022	Captures social distancing impact

COVID era: stimulus lifted GDP above potential by 2021

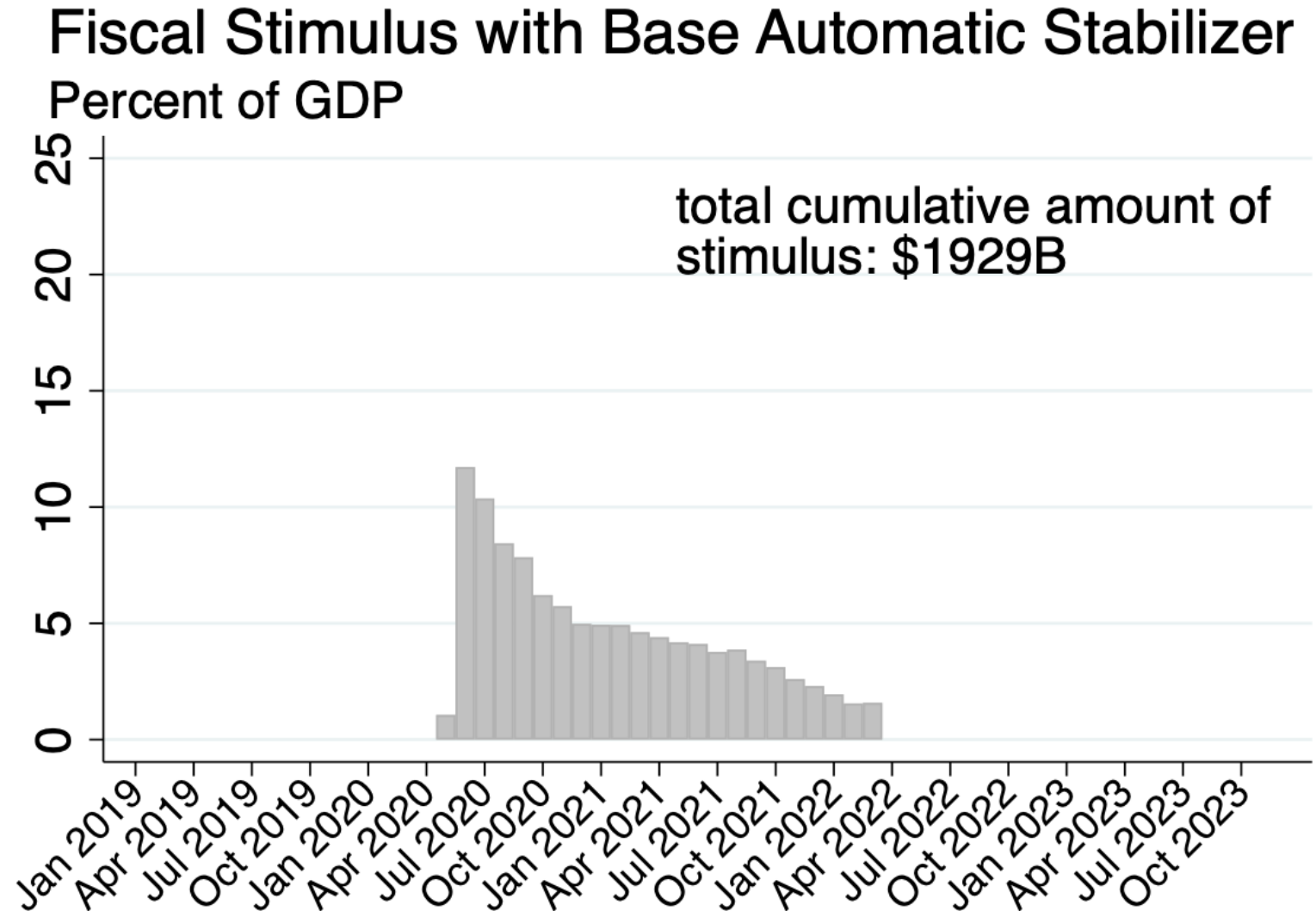
Real GDP

Trillions of 2017 dollars



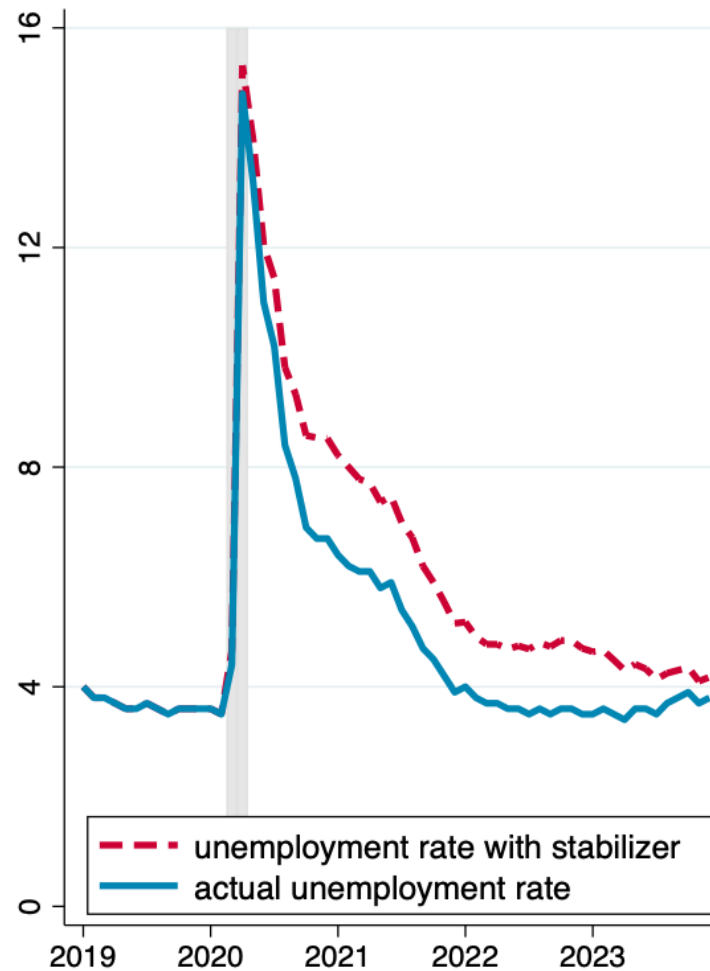
Data source: Bureau of Economic Analysis, Congressional Budget Office, and authors' calculations.
Shaded area corresponds to recession.

**COVID era:
Base stabilizer
would have
delivered smaller,
more gradual
support than
discretionary
actions**

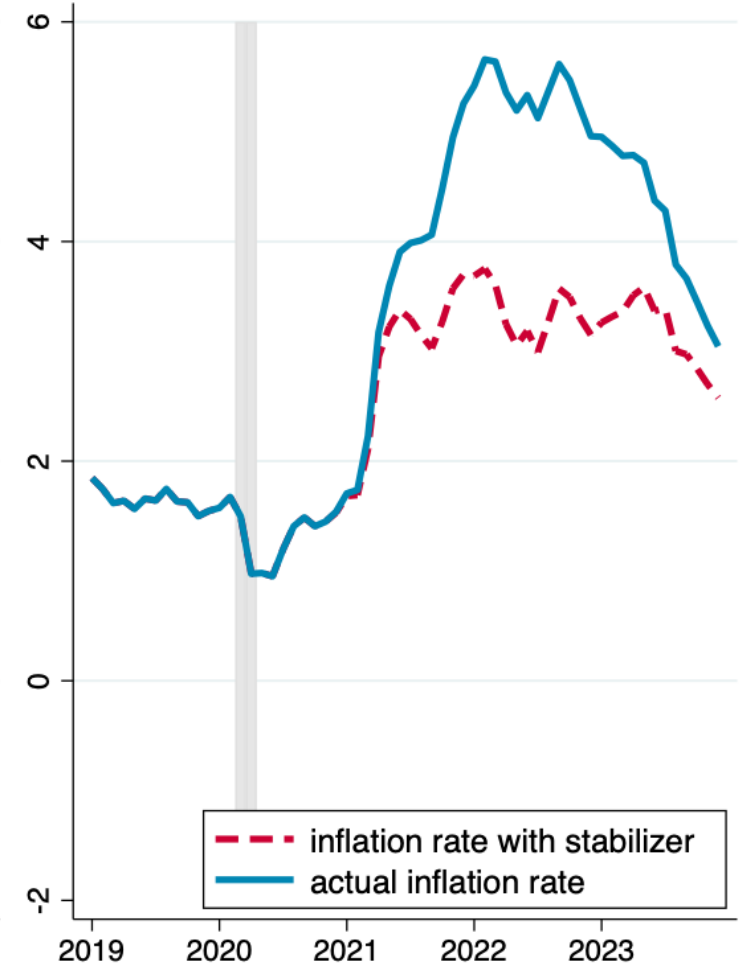


**COVID era:
Base
stabilizer
leads to
somewhat
slower jobs
recovery but
less inflation**

Unemployment Rate
Percent

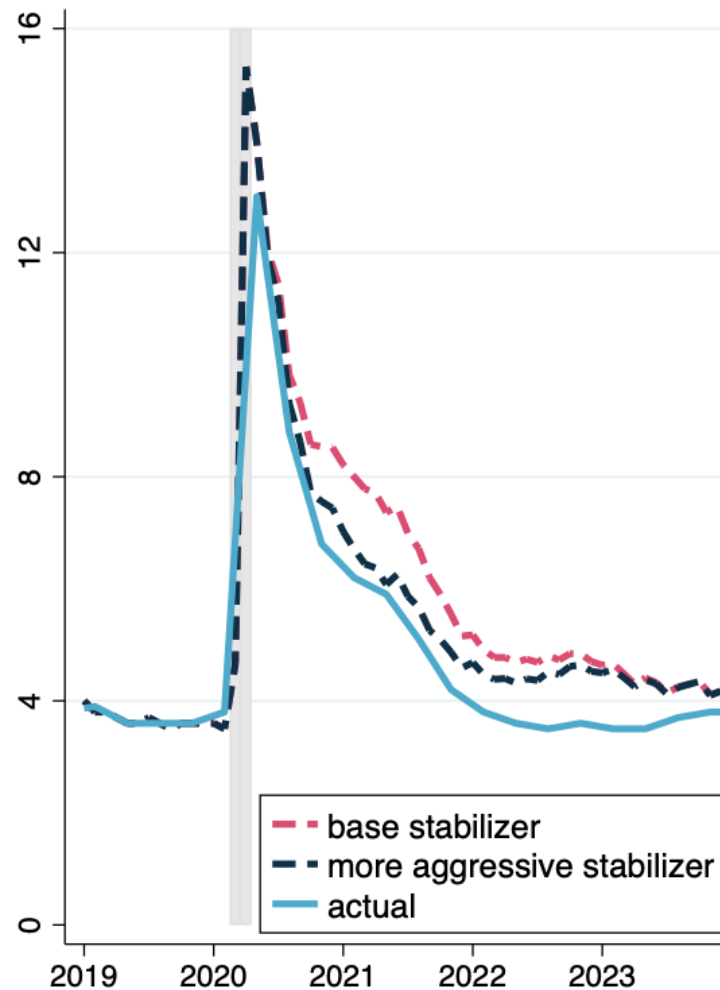


Core PCE Inflation Rate
12-month percent change

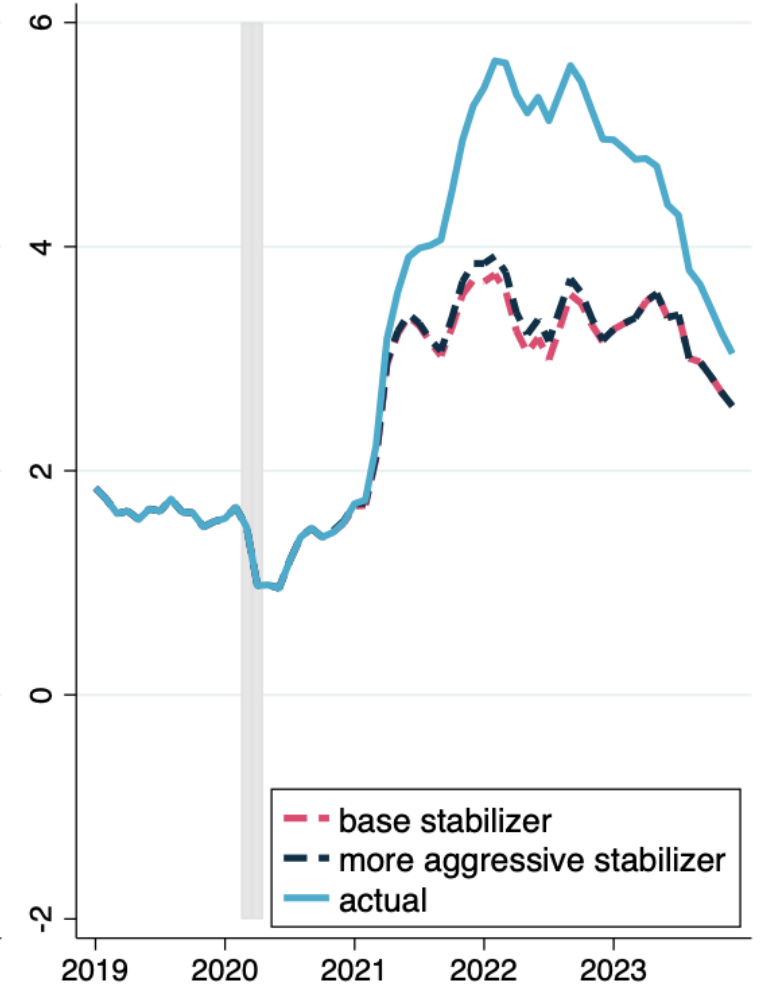


**COVID era:
More aggressive
stabilizer
(\$3.3T), delivers
nearly as strong
a recovery as
actual but with
less inflation**

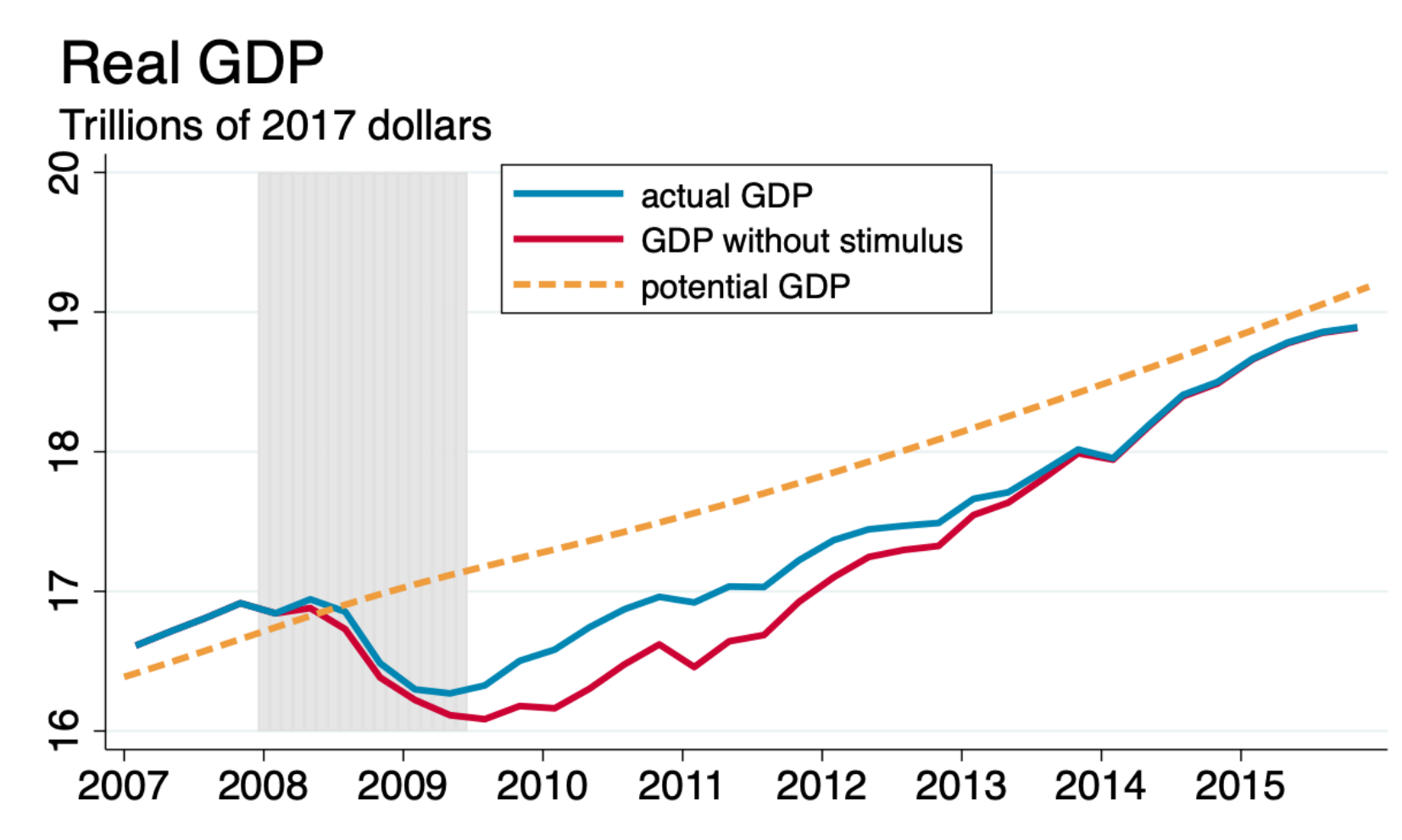
Unemployment Rate
Percent



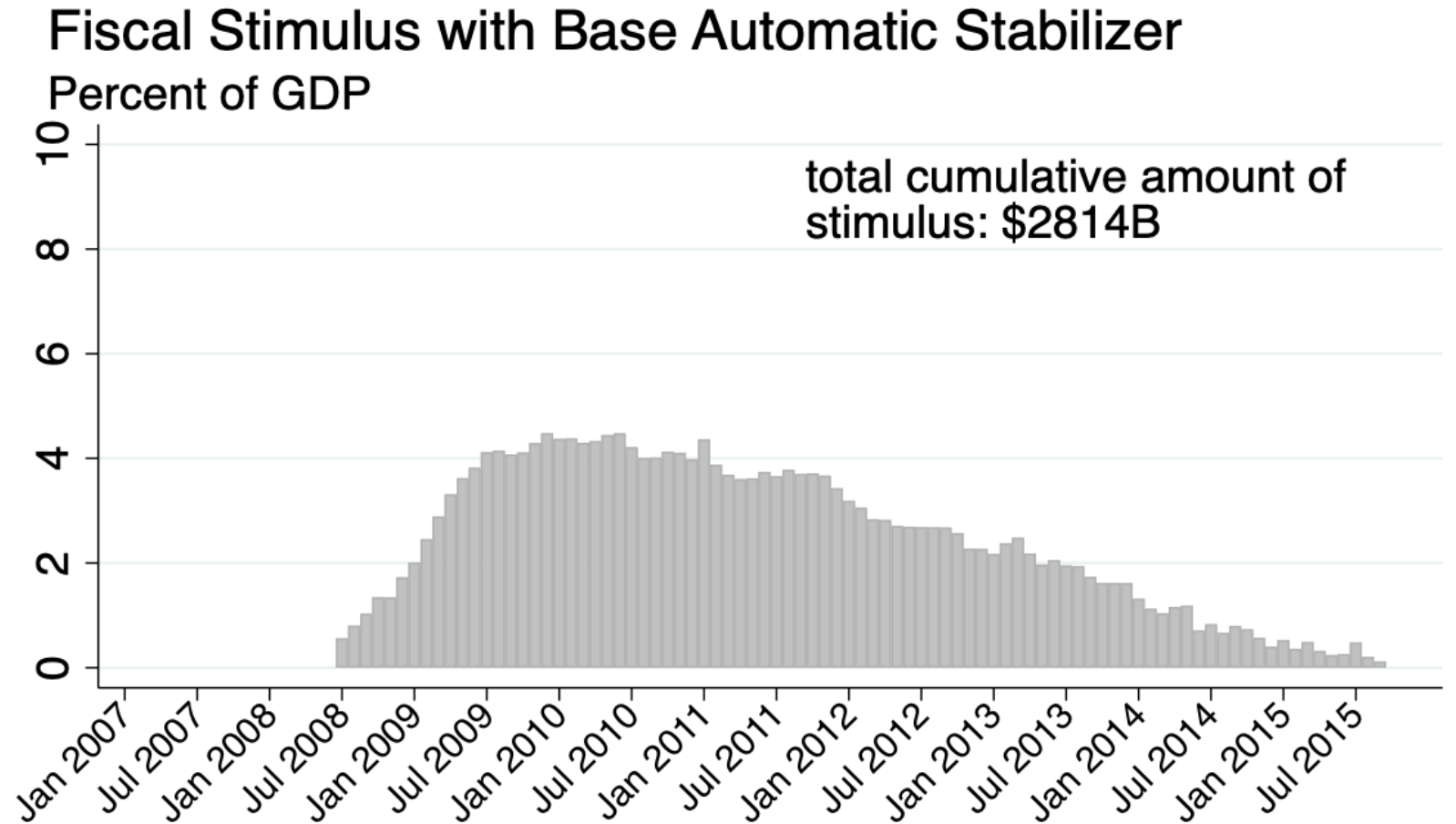
Core PCE Inflation Rate
12-month percent change



Great Recession era: Discretionary stimulus helped GDP recover, but output remained below potential for years.

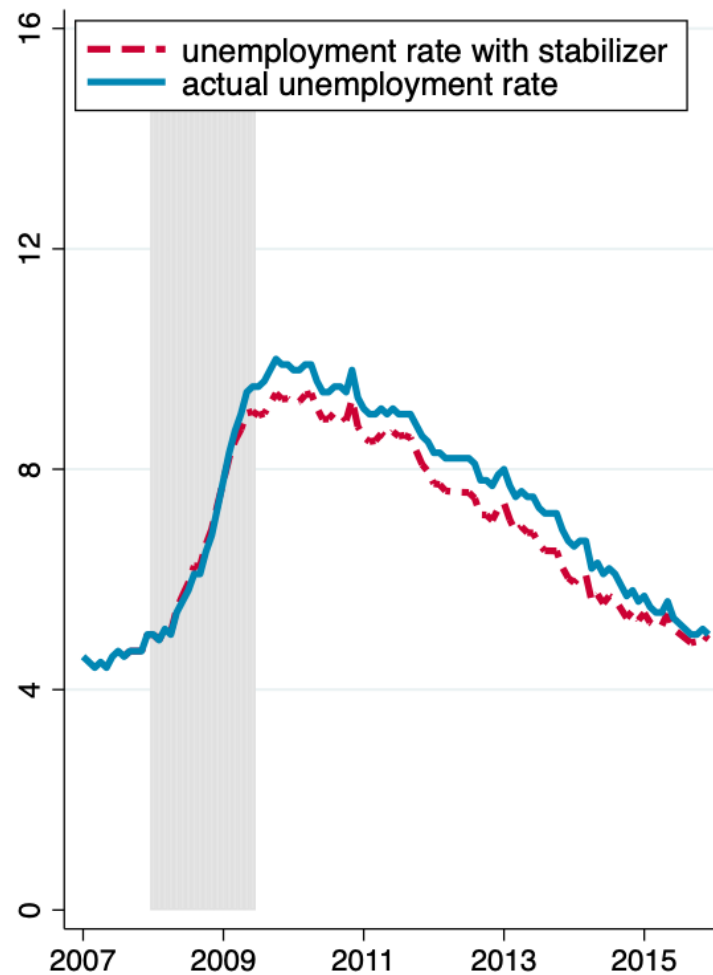


**Great
Recession era:
Base stabilizer
(\$2.8T of
stimulus) much
bigger and
more sustained
than enacted
policy**

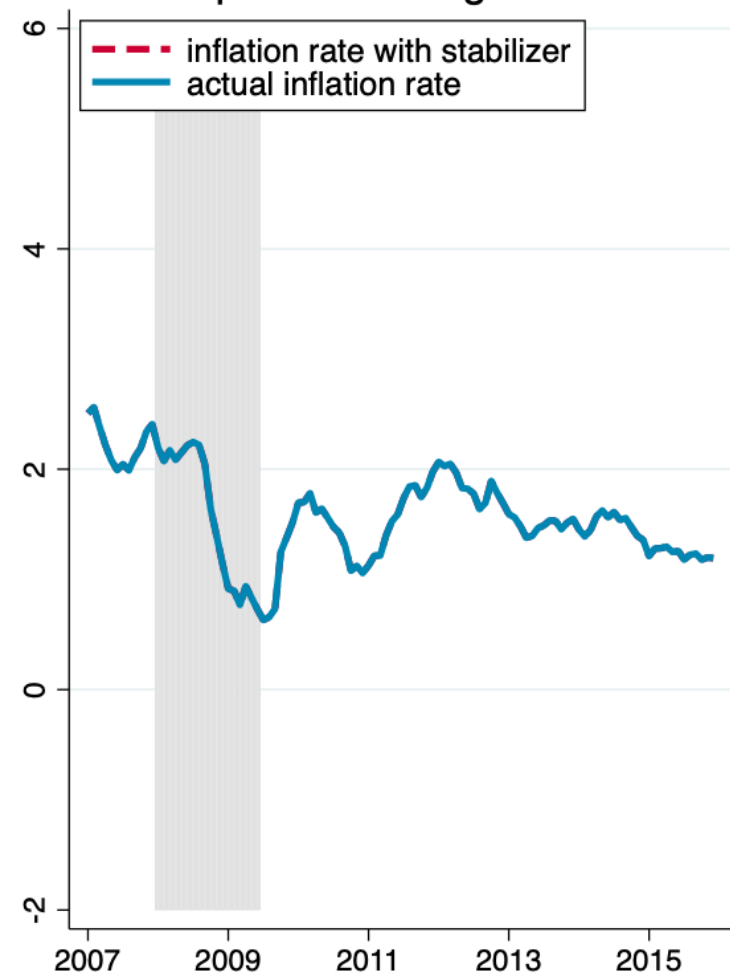


**Great
Recession era:
Base stabilizer
speeds up jobs
recovery
somewhat,
inflation
unchanged**

Unemployment Rate
Percent

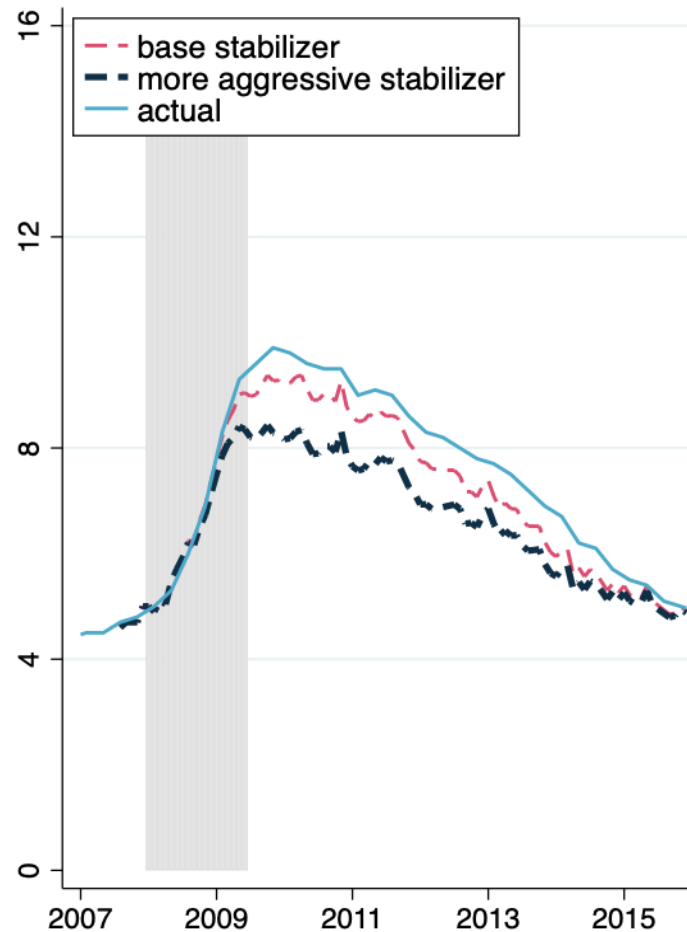


Core PCE Inflation Rate
12-month percent change

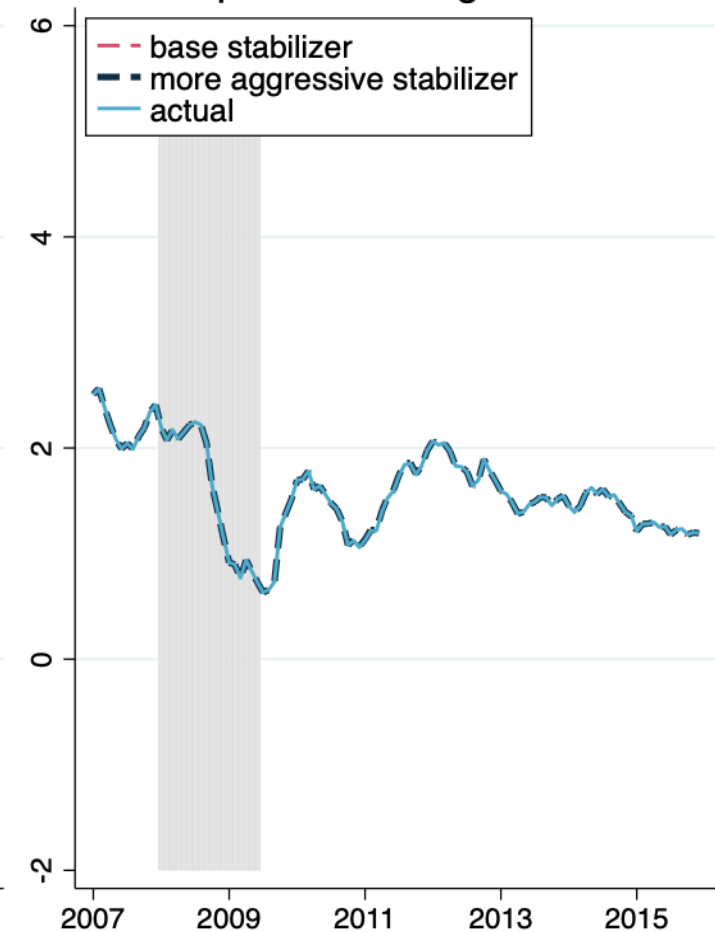


**Great
Recession era:
More
aggressive
stabilizer (\$4.4T
of stimulus)
leads to faster
jobs recovery,
inflation
unchanged**

Unemployment Rate
Percent



Core PCE Inflation Rate
12-month percent change

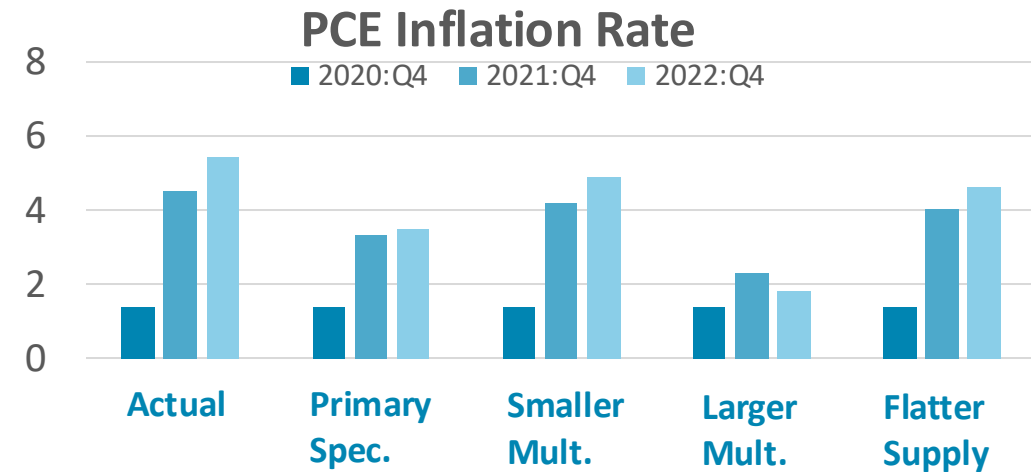
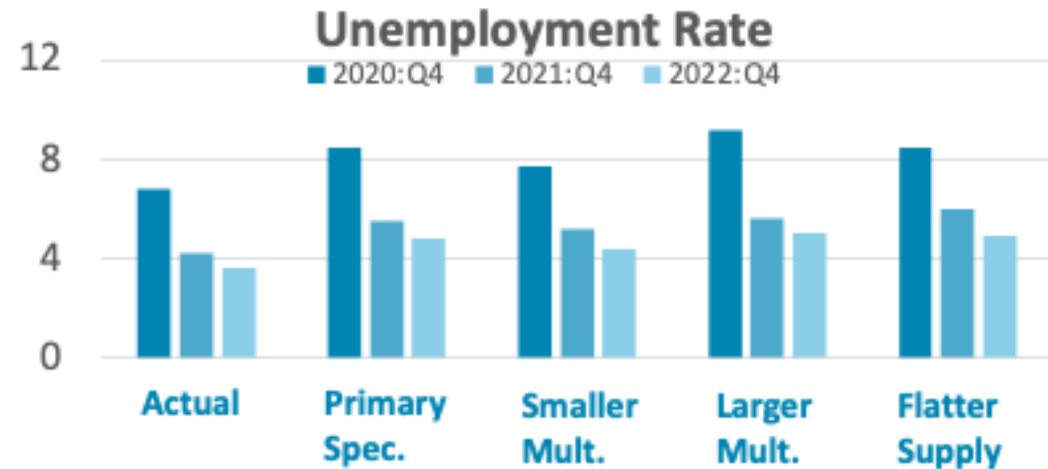


Sensitivity analysis for COVID Recession

Results vary with multipliers and supply curve slope

General story holds, with base automatic stabilizer

- much less costly than discretionary policies (\$1.7T to \$2.2T, compared with \$5.1T)
- leading to somewhat slower jobs recovery
- leading to lower inflation (materially so in some cases)



Summary

Simulations suggest an automatic stabilizer of the form we explore could have:

- Lowered unemployment faster after the Great Recession

- Held down inflation in the early 2020s

- Reduced federal borrowing overall—cumulative budgetary cost of \$4.7 trillion for the two recessions, about $\frac{1}{4}$ less than the cumulative \$6.4 trillion budgetary cost of the enacted discretionary actions

Caveats and directions for future research

Results sensitive to assumptions

Our stabilizer is not a substitute for crisis-specific measures (e.g., mortgage relief, public health)

Our stabilizer would not have responded as quickly to COVID's sudden onset as discretionary policy

Politicians may prefer to get “credit” for enacting discretionary policies

Scope to explore other types of stabilizers

Scope to explore other triggers, e.g., a fiscal “Taylor Rule”