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Unemployment Benefits under the Federal COVID-19 Relief Package

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Overview

As the COVID-19 pandemic has spread throughout the United States, it has led to mass shutdowns of businesses with many states being placed under shelter-in-place orders. This is leading to an unprecedented increase in unemployment, with initial unemployment claims hitting 3.3 million on the week of 3/21/20, which will likely increase in the coming weeks. To provide relief for these unemployed workers, the federal government is implementing an aid package which supplements state unemployment insurance benefits with an additional $600 per week in "Federal Pandemic Unemployment Compensation" through 7/31/2020.

This brief compares the unemployment benefits compensation through existing state systems and the new federal compensation to average weekly wages in each state. I find that maximum unemployment benefits would exceed 90% of average weekly wages in all states, with the ratio substantially higher in most states. In particular, maximum unemployment benefits would exceed:

- 130% of average wages in 6 states,
- 120% of average wages in 21 states, and
- 110% of average wages in 34 states.

Unemployment Insurance Benefits

Unemployment insurance (UI) are administered at the state-level, with a typical program providing 26 weeks of benefits, at a level determined as a fraction of previous weekly wages, up to a cap. The "replacement rate," the ratio of pre-unemployment wages which are provided by the unemployment insurance benefits, varies by worker across states. For example, in 2019: Q2 the average replacement rate across states was 45%, but ranged from 31% in Alaska to 56% in Hawaii.

In times of recession, the federal government has typically provided extended unemployment benefits, lengthening the duration of payments but not changing the levels, which kick in once state benefits are exhausted. As in past cases, the current federal relief package extends unemployment benefits to 39 weeks. New to this package is the additional benefit payments, providing an additional $600 per week through the end of July.

The historical average replacement rates by state are available from the Department of Labor, and are calculated as the weighted average of an unemployed claimant's weekly benefit amount divided by their full time equivalent normal weekly wage (this is "Replacement Ratio 1" from the Labor Department). Shown are the replacement rates in 2019:Q2. This replacement rate averages 45.0% across states. As lower wage workers have higher unemployment rates, the average weekly wage among unemployment claimants is typically below the average wage.

An alternative measure of replacement rates would take the maximum unemployment benefit by state compared to the average wage in the state. This measure gives an average replacement rate of 49.4%, which is higher as a reflection the fact that typical claimants do not receive the maximum benefit. To measure replacement rates under the federal expansion, I used this as a baseline and added the $600 per week. That is, I calculate the replacement rate under the expansion as the maximum benefit by state plus $600 divided by the state's average weekly wage (2019 annual average). This may better reflect the unemployment pool in the current situation, as unemployment has become widespread. The average replacement rate across states under this expansion now increases to 115.7%.

Figure 1 shows the measure of the replacement rate by state with the expanded benefits versus the state's average replacement rate. Here we see that the expanded benefits exceed 90% of average weekly wages in all states, with the ratio substantially higher in most states. In particular, as noted above, maximum unemployment benefits would exceed: 130% of average wages in 6 states, 120% of average wages in 21 states, and 110% of average wages in 34 states.

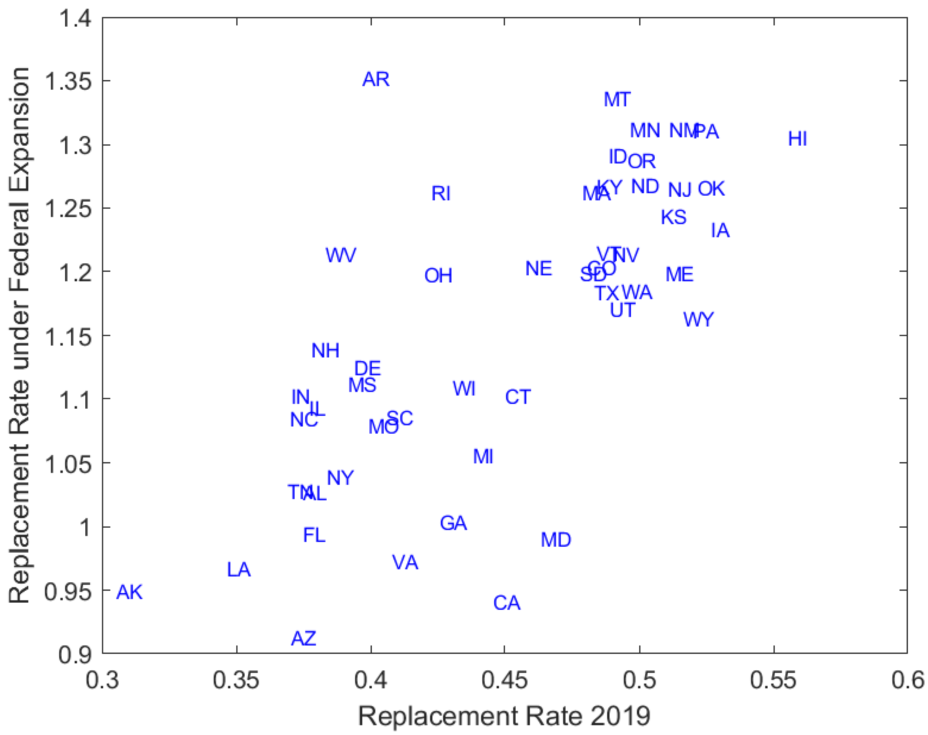

Figure 1: Replacement rates from unemployment insurance benefits in 2019 and under the new Federal Pandemic Unemployment Compensation.

Insurance and Incentives in Unemployment

In general, unemployment insurance programs try to balance insurance with incentives. That is, they seek to provide relief during unemployment spells while at the same time providing incentives for job search. Part of those incentives come through job search requirements, but providing replacement rates well below 100% also provides strong job search incentives. The magnitude of the disincentive effect of unemployment insurance is under some debate, and likely varies with the business cycle. For example, the same amount of search effort will be more likely to lead to a job offer in a tight labor market than in a recession.

Clearly the current situation with COVID-19 is very different from "normal times." Now unemployment has arisen due to the social distancing practices which first affected travel and service industries, and has grown due to government-ordered shutdowns. Many of these unemployment spells will likely be temporary, with workers rejoining their employers once the pandemic subsides and restrictions are removed. Further, while some employers (Amazon, Walmart, grocery stores) are looking to hire, many employers have put a hold on their hiring plans. Thus the disincentive effect of unemployment benefits right now is likely small and relief needs are large, which has prompted the federal response to increase unemployment benefits as well as many states waiving their job search requirements.

However, policymakers should be wary of implementing provisions during a crisis which will delay the economic recovery, as seems to have happened during the [Great Depression](#) and arguably the [2008 Recession](#) as well. While the Federal Pandemic Unemployment Compensation is time-limited, if the shutdowns associated with the pandemic are removed in the coming weeks, the unemployment benefits replacement rates well in excess of 100% may hamper the labor market recovery.

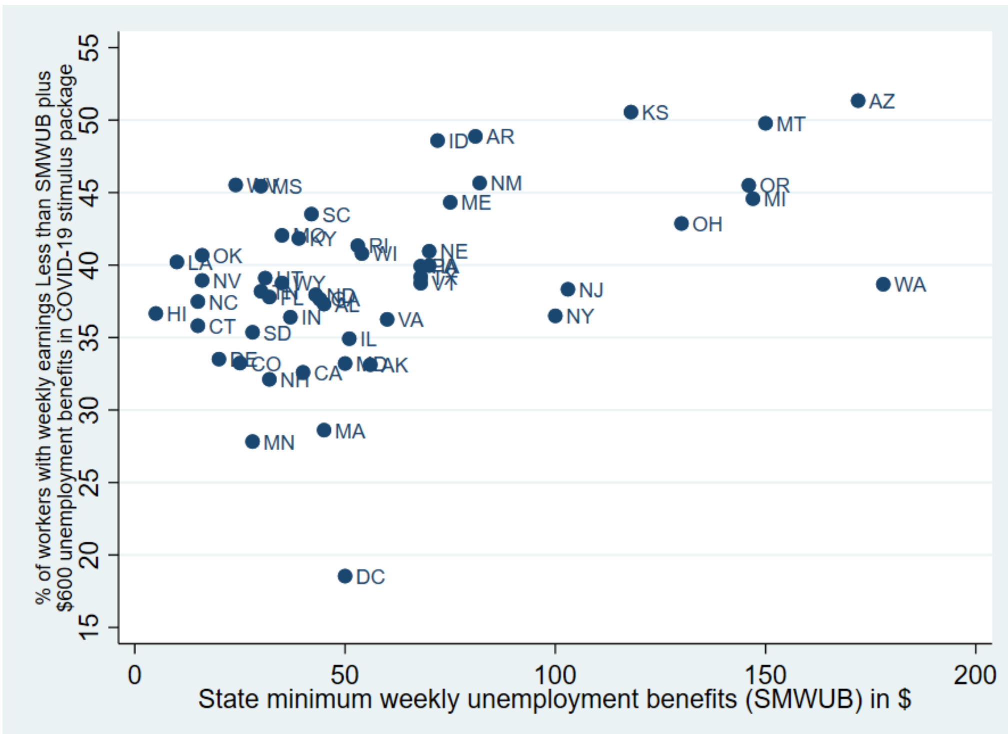

Figure 2: The share of workers in each state with weekly earnings lower than unemployment benefits under the existing state minimum benefit plus the Federal Pandemic Unemployment Compensation, versus the existing state minimum weekly unemployment benefit.

In addition, while the COVID-19 relief package includes other incentives for employers to retain workers on their payroll, the Federal Pandemic Unemployment Compensation may increase the incentive for employers to temporarily lay off workers, as in many cases the workers would temporarily receive higher pay from unemployment benefits.

In fact, as shown in Figure 2, 38% of workers in the US have weekly earnings less than the $600 unemployment benefits in the COVID-19 stimulus package plus the existing state minimum weekly unemployment benefits. Data on the horizontal axis is from the U.S. Department of Labor ([Table 3-5](#)). The vertical axis is calculated from the Current Population Survey in January and February 2020, accessed through [IPUMS](#). Thus a very large share of workers nationwide, and more than 50% in states like Arizona, Kansas and Montana, would earn more on unemployment than working under the federal benefits expansion.