NEWSLETTER

THE RODNEY L. WHITE CENTER FOR FINANCIAL RESEARCH

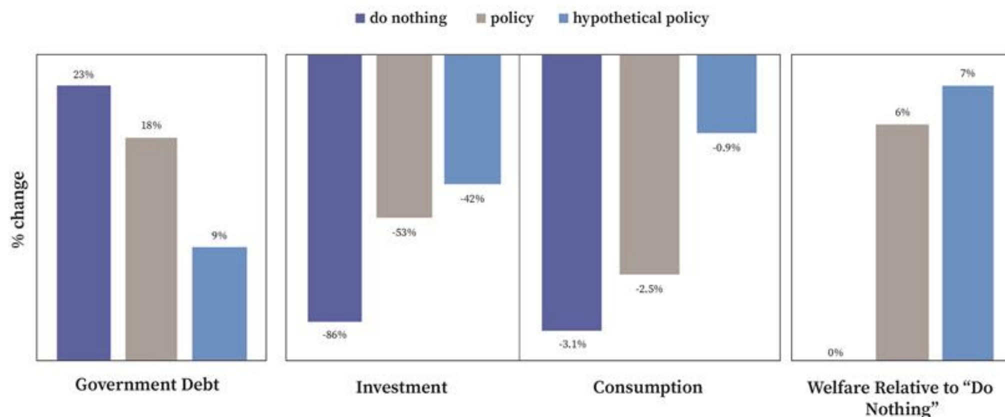
A Bite of Finance: The Latest from Wharton

COVID-19 Bailouts, Financing Education and Re-examining History

1. Can the COVID Bailouts Save the Economy?

By Vadim Elenev, Tim Landvoigt and Stijn van Nieuwerburgh

The authors estimate the likely impact of new lending programs designed to help firms survive the COVID-19 recession. They show that, while buying corporate debt is ineffective, the corporate loan programs helped prevent a much deeper economic crisis. The fiscal cost is high but doing nothing would cost more. However, a more targeted (hypothetical) policy designed to only help firms in critical need would cost significantly less and deliver substantively similar gains. The authors also predict that if pandemics are the new normal, we will have an economy with less debt, lower GDP and a smaller, but more robust, financial sector.



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2. The Impact of Social Insurance on Household Debt

By Gideon Bornstein and Sasha Indarte

Using data from recent Medicaid expansions, the authors argue that improved access to health insurance can have large welfare gains by enhancing financial resilience. They show Medicaid expansions led to a 2.2% increase in credit card debt, or around $20 billion. They estimate that expanding Medicaid to cover all non-elderly adults with no dependents would increase household credit card debt by 1.3%. Importantly, this comes from a higher willingness to lend by card issuers due to reductions in personal defaults.

Reduced household demand	
Fewer out of pocket expenses	-1.14%
Fewer options of default	-1.43%
Increased supply by issuers	
Improved credit risks	3.90%
Total Effect	**1.32%**

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3. Student Loans and Social Mobility

By Mehran Ebrahimian

Why do students from poor families invest so much less in college education than those from rich families? Using a novel nationally representative dataset on U.S. high-school and college students, the author finds that this lack of investment is largely due to factors such as differences in college preparedness and perceptions of the expected returns to education rather than a lack of access to financial resources. As a result, making public colleges tuition-free would disproportionally benefit wealthier students. Instead, to promote college access for lower-income students, the most cost-effective policy would be to expand federal needs-based grants.

Probability of college enrollment as function of income and key fundamentals

log (family income)	0.641***	0.498***	0.246***	0.297***
parents' education		√	√	√
SAT score, high-school GPA			√	√
Pell grant eligibility				√

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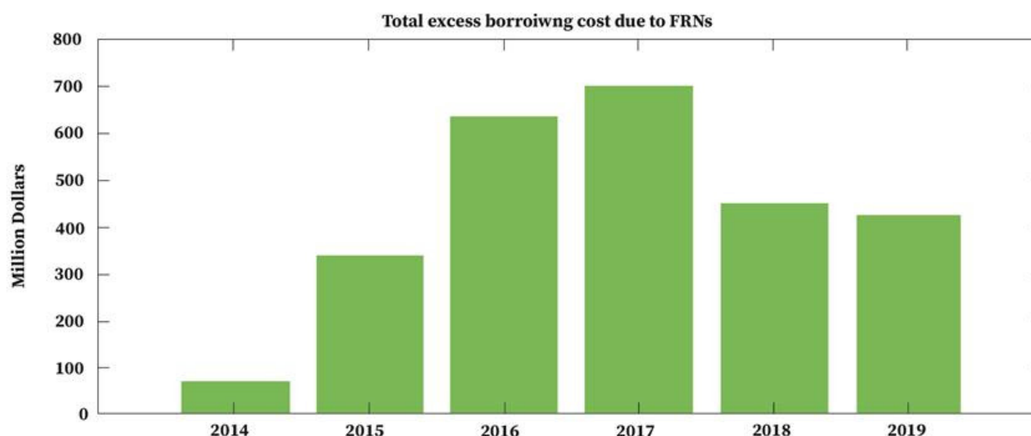
4. Should the U.S. Government Issue Floating Rate Notes?

By Jonathan S. Hartley and Urban Jermann

Since 2014, the U.S. Treasury began issuing floating-rate notes (FRNs) in addition to the standard fixed-rate Treasury. Issued at monthly auctions with a maturity of two years, their coupons are indexed to three-month T-bill rates. Using yield curves on auction dates, the authors calculate that borrowing via FRNs has been more expensive for the federal government than borrowing via comparable Treasury securities. The excess borrowing cost of FRNs amounts to between 5 and 39 bps, or several hundreds of millions of dollars per year. Nevertheless, they suggest usage of FRNs might be justified when outstanding short-term debt obligations expose the government to significant refinancing risk.



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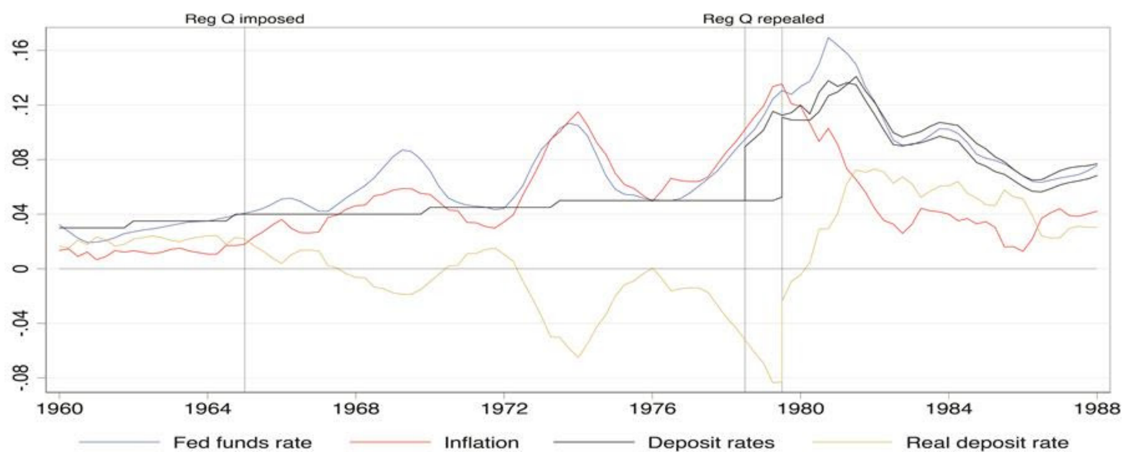
5. The Financial Origins of the Rise and Fall of American Inflation

By Itamar Drechsler, Alexi Savov and Philipp Schnabl

The rise in U.S. inflation during the '70s has traditionally been attributed to the Fed's failure to aggressively raise interest rates. In turn, Paul Volcker's hawkish stance is often credited with restoring Fed credibility and the subsequent decline in inflation. The authors challenge this conventional interpretation. Instead, they place the blame on Regulation Q, which imposed a hard ceiling on bank deposit rates, suppressed the returns to savings, and encouraged household spending. Regulation Q inhibited the pass-through of fed funds rate changes to deposit rates, stimulated deposit outflows, and decreased bank funding. This led to a credit crunch for firms, and thereby a drop in output and employment. When Regulation Q was finally repealed, deposit rates increased sharply and inflation started to decline. Although significant, the Volcker hikes came well after inflation started falling.



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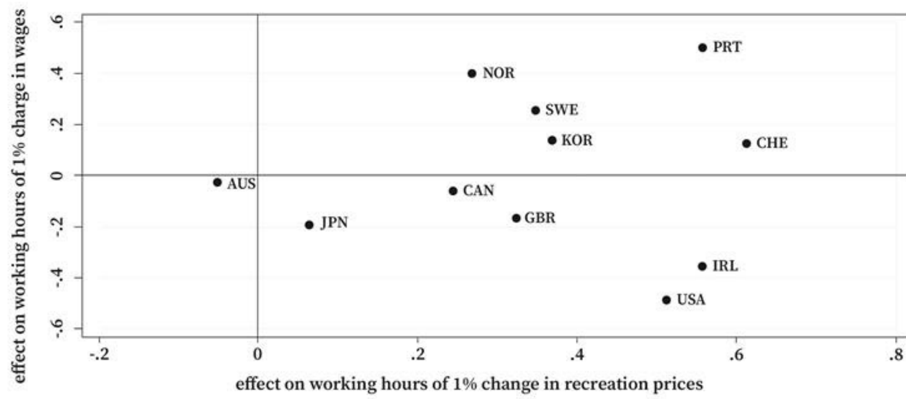
6. Cheap Thrills: the Price of Leisure and the Global Decline in Work Hours

By Alexandr Kopytov, Nikolai Roussanov and Mathieu Taschereau-Dumouchel

The authors show that, in many countries, the secular decline in average hours worked is largely attributed to the falling prices of leisure and recreation goods. By contrast, the impact of rising real wages is mixed. They argue that we can expect this decline to continue as new technologies are likely to make recreation even cheaper in the coming decades. Moreover, recreation goods of highly educated workers faced a steeper decline in prices than those of less-educated ones, explaining much of the rise in leisure inequality.



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