



## Washington Policy Research

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### THE SHIFTING FACTORS ON THE STIMULUS DEBATE

Fiscal and monetary policy have been key supports for both financial markets and the economy in the wake of COVID-19 hitting the US. With several key pieces of the CARES Act having ended in late summer (and with more set to expire at year-end), additional stimulus is needed to keep the economy afloat through the winter. Until now, however, the combination of vaccine success and a contentious lame duck Congressional session has led us to be fairly bearish on near-term stimulus prospects. That may have changed these past few days.

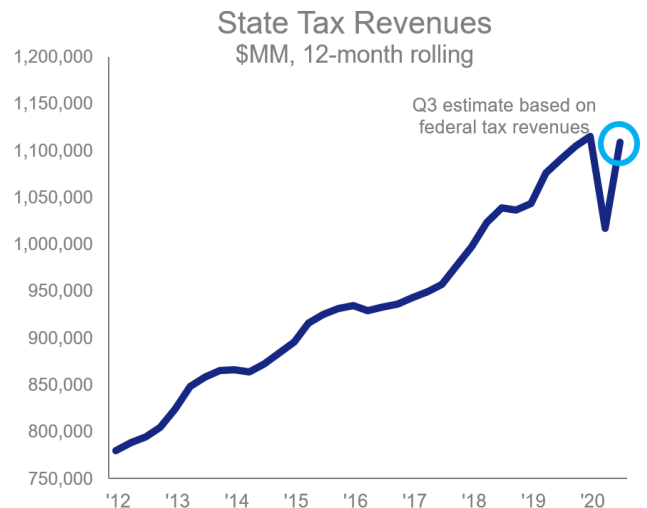
On Friday, President-elect Biden reportedly pressed House Speaker Pelosi and Senate Minority Leader Schumer to get a stimulus deal done soon, and importantly, to compromise on the size/scope of a package if necessary.

The reported success of both Pfizer and Moderna's vaccines has translated into Republicans believing just a small "bridge" of fiscal support is necessary to get the economy to the vaccine finish line. Though near-term economic weakness can be expected as the coronavirus spreads and lockdown restrictions ramp up, the medium-term outlook has improved drastically on the vaccine news. Health officials are now indicating the possibility that a huge portion of the country could be vaccinated by early next year. As such, the appetite for large-scale stimulus is falling and a "skinnier" package might have more success passing.

One source of compromise could be state and local budget aid. We've argued that the \$500 billion in aid being called for was disproportionate to the need of state governments. In fact, our analysis forecasts a V-shaped bounce in state tax revenues and suggests that a \$200 billion aid package to states would ensure a proper cushion.

One last kink in the stimulus debate: [control of the Senate is not yet determined](#). Since no candidate received 50% of the vote in the two Georgia Senate races on Election Day, both seats will be subject to runoff elections on January 5. If Democrats win both seats, that will bring the Democrats to 50 Senators (including Independents) and control of the chamber. Under that scenario, we would expect a much larger stimulus package (likely ~\$2 trillion). However, as of today, betting markets are assigning just a ~25% probability of that occurring.

Though the blowout success of multiple vaccine candidates provides a clean endgame for the coronavirus crisis, we believe that the high probability of near-term economic weakness necessitates additional fiscal stimulus—the only question is whether the political capital exists to get it done. We'll be watching these shifting sands closely over the coming weeks.



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