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2	Welfare and Spending Effects of Consumption Stimulus Policies	2
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18	Using a heterogeneous agent model calibrated to match spending dy-	18
19	namics over four years following an income shock (Fagereng et al.	19
20	(2021)), we assess the effectiveness of three fiscal stimulus policies im-	20
21	plemented during recent recessions. Unemployment insurance (UI)	21
22	—————	22
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1 extensions are the “bang for the buck” winner when the metric is ef-
2 fectiveness in boosting utility. Stimulus checks are second-best and
3 have two advantages (over UI): they arrive faster, and are scalable. A
4 temporary (two-year) cut in wage taxation is considerably less effec-
5 tive than the other policies and has negligible effects in the version of
6 our model without a multiplier.

7 KEYWORDS. fiscal policy, unemployment insurance extensions, pay-
8 roll tax cuts, HANK/heterogeneous agent models, marginal propen-
9 sity to consume, spending multipliers.

10 JEL CLASSIFICATION. E21, E62, H31.

12 1. INTRODUCTION

13 Fiscal policies that aim to boost consumer spending in recessions have been
14 tried in many countries in recent decades. The nature of such policies has varied
15 widely, perhaps because traditional macroeconomic models have not provided
16 plausible guidance about which ones are likely to be most effective—either in
17 reducing misery (a ‘welfare metric’) or in increasing output (a ‘GDP metric’).
18

19 But a new generation of macro models has shown that when microeconomic
20 heterogeneity across consumer circumstances (wealth; income; education) is
21 taken into account, the consequences of an income shock for consumer spend-
22 ing depend on a measurable object: the intertemporal marginal propensity to
23 consume (iMPC) introduced in [Auclert et al. \(2018\)](#). The iMPC extends the no-
24 tion of a marginal propensity to consume to account for the speed at which
25 households spend. Fortunately, new sources of microeconomic data, particu-
26 larly from Scandinavian national registries, have recently allowed the first high-
27 quality measurements of the iMPC ([Fagereng et al. \(2021\)](#)).
28

29 Even in models that can match a given measured iMPC pattern, the relative
30 merits of alternative policies depend profoundly both on the metric (welfare or
31 GDP) and on the quantitative structure of the rest of the model – for example,
32 whether multipliers exist and whether the degree of multiplication is different
under different economic conditions. Here, after constructing a microeconomi-

1 cally credible heterogeneous agent (HA) model, we examine that model's impli- 1
 2 cations for how effects of stimulus policies depend on the existence and timing 2
 3 of any "multipliers," which, following Krueger et al. (2016), we model in a clean 3
 4 and simple way, so that the interaction of the multiplier (if any) with the other 4
 5 elements of the model is reasonably easy to understand. This partial equilib- 5
 6 rium analysis allows us to transparently incorporate the possibility that multipli- 6
 7 ers may be larger in recessions. But we understand that a richer general equilib- 7
 8 rium framework could introduce transmission channels absent from the partial- 8
 9 equilibrium-plus-multiplier analysis, so we also analyze a standard HANK-and- 9
 10 SAM general equilibrium model modified to embed our households' consump- 10
 11 tion responses.¹ 11

12 By "microeconomically credible," we mean, at a minimum, a model that can 12
 13 match both the cross-sectional distribution of liquid wealth (following Kaplan 13
 14 and Violante (2014)'s definition of liquid wealth) and the entire pattern of the 14
 15 iMPC from Fagereng et al. (2021) (see Figure 1a for their data and our model's fit 15
 16 to it). 16

17 Standard HA models can match both the pattern of spending in years 1-4 (for 17
 18 a shock that arrives in year 0) and the initial distribution of liquid wealth.² But 18
 19 even a brief look at the figure convinces the eye that spending in the initial pe- 19
 20 riod when the shock arrives seems out of line with the smooth declining pattern 20
 21 in years 1-4. The eye is not wrong: HA models that match liquid assets and the 21
 22 spending pattern in years 1-4 seriously underpredict the amount of immediate 22
 23 spending that occurs on receipt of the income shock. 23

24 We call this initial extra spending the 'excess initial MPC.' Below, we describe 24
 25 a substantial and longstanding literature in which the pattern of an excess initial 25
 26 MPC has been documented, and a vigorous recent literature confirming the fact 26
 27 with different datasets and various theoretical explanations. 27

28

29 ¹The Econ-ARK (?) toolkit with which the partial equilibrium model was solved constructs the Jaco- 29
 30 bians necessary to connect a steady-state version of the model to the SSJ Toolkit. Our HANK-and-SAM 30
 31 model builds on Ravn and Sterk (2017, 2021). 31

32 ²For example, the model in Carroll et al. (2017). 32

1 If multipliers are operative only in recessions (or are more powerful in recessions), a model that fails to capture the excess initial MPC might generate the wrong answers for the effectiveness of the alternative fiscal policies. 1
2 2
3 3

4 The purpose of our paper is not to weigh in on which of the alternative models of an excess initial MPC is right. Instead we sought the simplest modeling device that would capture the empirical fact of an excess initial MPC and permit unambiguous welfare calculations. We accomplish this by adding to the standard model something we call “splurge” behavior, in which each household has a portion of income out of which they have a high MPC, and the remainder of their income is disposed of as in standard micro models with mildly impatient but time-consistent consumers. Because the available evidence finds high initial MPCs even among wealthy households, we assume that this splurge behavior is the same across households and independent of their liquid wealth holdings.³ 4
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14 Our resulting structural model could be used to evaluate a wide variety of consumption stimulus policies. We examine three that have been implemented in recent recessions in the United States (and elsewhere): an extension of unemployment insurance (UI) benefits, a means-tested stimulus check, and a payroll tax cut. 14
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19 Our first metric of policy effectiveness is “spending bang for the buck”: For a dollar of spending on a particular policy, how much multiplication is induced? 19
20 20
21 First, we calculate the policy-induced spending dynamics in an economy with no multiplier. We then follow Krueger et al. (2016)’s approach to modeling the aggregate demand externality, in which output depends mechanically on the level of consumption relative to steady state. But in our model, the aggregate demand externality is only switched on when the economy is experiencing a recession—there is no multiplication for spending that occurs after our simulated recession is over. 21
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30 ³Proponents of the theoretical models described in our literature review in section 1.1 may choose 30
31 to think of our splurge as a reduced form for a deeper explanation; we would not necessarily resist 31
32 such an interpretation. 32

1 Even without multiplication, a utility-based metric can justify countercyclical 1
 2 policy on welfare grounds because the larger idiosyncratic shocks to income that 2
 3 occur during a recession may justify a greater-than-normal degree of social insur- 3
 4 ance. Because our model's outcomes reflect the behavior of utility-maximizing 4
 5 consumers, we can calculate a measure of the effectiveness of alternative poli- 5
 6 cies: their effect on consumers' welfare. We call this "welfare bang for the buck." 6

7 The principal difference between the two metrics is that what matters for 7
 8 the degree of spending multiplication is how much of the policy-induced extra 8
 9 spending occurs during the recession (when the multiplier matters), while effec- 9
 10 tiveness in the utility metric also depends on who is doing the extra spending 10
 11 (because the recession hits some households much harder than others). 11

12 Because high-MPC consumers tend to have high marginal utility, a standard 12
 13 aggregated welfare function would favor redistribution to such consumers even 13
 14 in the absence of a recession. We are interested in the degree of *extra* motiva- 14
 15 tion for social insurance that is present in a recession, so we construct our social 15
 16 welfare metric specifically to measure only the *incremental* social welfare effect 16
 17 of alternative policies during recessions (beyond whatever redistributional logic 17
 18 might apply during expansions – see section 4.3). 18

19 When the multiplier is active, any reduction in aggregate consumption be- 19
 20 low its steady-state level directly reduces aggregate productivity and thus la- 20
 21 bor income. Hence, any policy stimulating consumption will also boost incomes 21
 22 through this aggregate demand multiplier channel. 22

23 Our results are intuitive. In the economy with no recession multiplier, the ben- 23
 24 efit of a sustained payroll tax cut is negligible.⁴ When a multiplier exists, the tax 24

25
 26 One reason there is any (welfare) benefit at all, even for people who have not experienced an 26
 27 unemployment spell, is that the heightened risk of unemployment during a recession increases the 27
 28 marginal value of current income because it helps them build extra precautionary reserves to buffer 28
 29 against the extra risk. A second benefit is that, for someone who becomes unemployed some time 29
 30 into the recession, the temporary tax reduction will have allowed them to accumulate a larger buffer 30
 31 to sustain them during unemployment. Finally, in a recession, there are more people who will have 31
 32 experienced a spell of unemployment, and the larger population of beneficiaries means that the con- 32
 sequences of the prior mechanism will be greater. But, quantitatively, all of these effects are small.

1 cut has more benefits, especially if the recession continues long enough that 1
2 most of the spending induced by the tax cut happens while the economy is still 2
3 in recession (and the multiplier still is in force). The typical recession, however, 3
4 ends long before our ‘sustained’ wage tax cut is reversed—and even longer be- 4
5 fore lower-MPC consumers have spent down most of their extra after-tax income. 5
6 Accordingly, even in an economy with a multiplier that is powerful during reces- 6
7 sions, much of the wage tax cut’s effect on consumption occurs when any multi- 7
8 plier that might have existed in a recession is no longer operative. 8

9 Even leaving aside any multiplier effects, the stimulus checks improve welfare 9
10 more than the wage tax cut, because at least a portion of such checks go to unem- 10
11 ployed people who have both high MPCs and high marginal utilities (while wage 11
12 tax cuts, by definition, go only to persons who are employed and earning wages). 12
13 The greatest “welfare bang for the buck” comes from the UI insurance extension, 13
14 because many of the recipients are in circumstances in which they have a much 14
15 higher marginal utility than they would have had in the absence of the recession, 15
16 whether or not the aggregate demand externality exists. 16

17 And, in contrast to the wage-tax cut, both the UI extension and the stimulus 17
18 checks concentrate most of the marginal increment to consumption at times 18
19 when the multiplier (if it exists) is still powerful. A disadvantage of the UI exten- 19
20 sion relative to the stimulus checks, in terms of “spending bang for the buck,” is 20
21 that it takes somewhat more time until the transfers reach the beneficiaries. The 21
22 stimulus checks are assumed to be distributed immediately in the same quarter 22
23 as the recession starts. Countering this disadvantage is the fact that the MPC of 23
24 UI recipients is higher than that of stimulus check recipients, and, furthermore, 24
25 the insurance nature of the UI payments reduces the precautionary saving mo- 25
26 tive. In the end, our model says that these two forces roughly balance each other, 26
27 so that the spending bang for the buck of the two policies is similar. In the wel- 27
28 fare metric, however, there is considerable marginal value to UI recipients even 28
29 if they receive some of the benefits after the recession is over (and no multiplier 29
30 exists). Hence, in the welfare metric, the relative value of UI benefits is increased 30
31 compared with the policy of sending stimulus checks. 31

32 32

1 We conclude that extended UI benefits should be the first weapon employed 1
 2 from this arsenal, as they have a greater welfare benefit than stimulus checks and 2
 3 a similar (multiplied) spending effect. But a disadvantage is that the total amount 3
 4 of stimulus that can be accomplished with the UI extension is constrained by the 4
 5 fact that only a limited number of people become unemployed. If more stimu- 5
 6 lation is called for than can be accomplished via the UI extension, checks have 6
 7 the advantage that their effects scale almost linearly in the size of the stimulus— 7
 8 see [Beraja and Zorzi \(2023\)](#) for a more detailed exposition of the relation between 8
 9 MPC and stimulus size. The wage tax cut is also, in principle, scalable, but its ef- 9
 10 fects are smaller because recipients have lower MPCs and marginal utility than 10
 11 check and UI recipients. In the real world, a tax cut is also likely the least flexi- 11
 12 ble of the three tools: UI benefits can be further extended, and multiple rounds 12
 13 of checks can be sent, but multiple rounds of changes in payroll tax rates would 13
 14 likely be administratively and politically more difficult. 14

15 One theme of our paper is that which policies are better or worse, and by how 15
 16 much, depends on both the quantitative details of the policies and the quantita- 16
 17 tive modeling of the economy. 17

18 But the tools we are using could be reasonably easily modified to evaluate a 18
 19 number of other policies. For example, in the COVID-19 recession in the US, not 19
 20 only was the duration of UI benefits extended, but those benefits were also sup- 20
 21 plemented by substantial extra payments to every UI recipient. We did not cali- 21
 22 brate the model to match this particular policy, but the framework could accom- 22
 23 modate such an analysis. 23

24 24

25 25

26 1.1 *Related literature* 26

27 27
 28 Our paper is part of the growing literature using structural heterogeneous agent 28
 29 models to examine effects of countercyclical fiscal policies. 29

30 Because the quantitative implications of HA models depend profoundly on 30
 31 getting certain microeconomic details right, we begin with a brief synopsis of 31
 32 what we view as the relevant takeaways from the micro literature. 32

1 1.1.1 *Microeconomic Evidence* For our purposes, the single most important 1
2 kind of micro evidence is on the iMPC; we explicitly target our partial equilibrium 2
3 model to match the microeconomic iMPC estimates of [Fagereng et al. \(2021\)](#), 3
4 whose evidence is the gold standard because their millions of datapoints allow 4
5 precise estimates over a long horizon (five years) and because their natural exper- 5
6 iment is almost ideal (a lottery win is a random shock by construction). Particu- 6
7 larly striking is their evidence on the excess initial MPC. Any worry that their Nor- 7
8wegian evidence might not apply in other countries is allayed by results in a new 8
9 paper by [Kotsogiannis and Sakellaris \(2024\)](#), who use data from a Greek lottery 9
10 and find that the induced extra monthly spending in the first three months after 10
11 the win is triple the induced extra spending in the remaining observed months. 11

12 There are, of course, many prominent papers dating all the way back to [Fried-](#) 12
13 [man \(1963\)](#) finding that the initial spending response to shocks is vastly greater 13
14 than implied by a representative agent model (in particular a steady stream of 14
15 state-of-the-art papers by Jonathan Parker and his collaborators). In much of that 15
16 literature there has been some evidence that the initial spending response was 16
17 out of line with the subsequent effects (see, e.g., [Parker et al. \(2013\)](#); [Broda and](#) 17
18 [Parker \(2014\)](#); [Johnson et al. \(2006\)](#)), but data limitations usually made it difficult 18
19 to sharply pin down the temporal pattern of spending (especially beyond the six 19
month horizon). 20

21 Another striking result in [Fagereng et al. \(2021\)](#) was that even households with 21
22 high liquid wealth exhibited high MPC's. [Boehm et al. \(2025\)](#), [Graham and Mc-](#) 22
23 [Dowall \(2024\)](#), [Crawley and Kuchler \(2023\)](#), and [Kueng \(2018\)](#) among others also 23
24 provide strong evidence of high MPCs for high-liquid-wealth households.⁵ 24
25 25

26 1.1.2 *Microeconomic Theories* A rapidly growing recent literature has used a va- 26
27 riety of data sources to reconfirm the high initial MPC, but with an eye to provid- 27
28 28

29 ⁵The “infrequent consumption good” model of [Melcangi and Sterk \(2024\)](#) has a similar flavor, but 29
30 is not about MPC's. It aims at accounting for high saving rates among high-income households dur- 30
31 ing normal times and high consumption during episodes where the infrequent consumption good 31
32 becomes available (such as high-end health care or education expenses). 32

¹ ing theoretical explanations. We sketch this literature because different theories ¹
² might have different implications for the spending consequences of a shock. ²

³ One possibility is that the burst of initial spending is rationalizable if the spend- ³
⁴ ing is on durables (Browning and Crossley, 2009). Mankiw (1982) showed that in ⁴
⁵ the frictionless case, spending on durable goods should be vastly more respon- ⁵
⁶ sive to an income shock than spending on nondurables. It seems plausible that ⁶
⁷ a model with a large number of goods that are durable at, say, the quarterly or ⁷
⁸ annual frequency could explain the ‘excess initial MPC’ as reflecting a rational ⁸
⁹ marginal propensity to eXpend (MPX).⁶ ⁹

¹⁰ Maxted et al. (2024) combine a simplified model of durables spending with ¹⁰
¹¹ the assumption common in behavioral economics that spending decisions are ¹¹
¹² influenced by “present bias” (people have time-inconsistent preferences). They ¹²
¹³ present a back-of-the-envelope calculation that yields a rough estimate that the ¹³
¹⁴ ratio of initial spending on durables to the spending that would occur if all spend- ¹⁴
¹⁵ ing were nondurable is roughly three to one (not far from the ratio estimated in ¹⁵
¹⁶ the Greek lottery episode studied by Kotsogiannis and Sakellaris (2024)). ¹⁶

¹⁷ Indarte et al. (2024) use high frequency bank account data to study spending ¹⁷
¹⁸ responses to the U.S. 2021 stimulus, and find substantial “excess MPC’s” especially ¹⁸
¹⁹ among low income households; like Maxted et al. (2024) they lean toward present ¹⁹
²⁰ bias as an explanation.⁷ ²⁰

²¹ The logic of Akerlof and Yellen (1985) and Cochrane (1989) suggests that the ²¹
²² utility consequences of ‘near-rational’ deviations from frictionless rational be- ²²
²³ havior is small. In that spirit, Boutros (2022) and Ilut and Valchev (2022) present ²³
²⁴ models with bounded rationality and costly re-optimization. Building on this ²⁴
²⁵

²⁶ ²⁶The NIPA accounts treat as ‘durable’ those goods whose expected lifetime is 3 years or more, but
²⁷ at the annual (or quarterly) frequency many more goods (and even services) are arguably durable – ²⁷
²⁸ for example, Blinder and Deaton (1985) mention clothes and shoes, and Hai et al. (2020) argue that ²⁸
²⁹ many services are durable at the annual frequency, which explains why people take vacations once a ²⁹
^{year.} ²⁹

³⁰ ³⁰A related theoretical insight is provided by Lian (2023), who shows that households anticipating
³¹ their own future consumption mistakes can rationally exhibit higher current MPCs; this is because ³¹
³² they know that any additional savings would be likely be disposed of suboptimally in the future. ³²

1 logic, [Andre et al. \(2025\)](#) argue that costs of reoptimization cause consumers to 1
2 resort to simple “quick-fix” consumption heuristics; for small shocks, most peo- 2
3 ple in their survey report that they anticipate that their MPC’s would be one or 3
4 zero. 4

5 The ‘splurge’ component of our consumption model is a simple modelling de- 5
6 vice that lets the model match the empirical evidence, regardless of what the right 6
7 deep explanation(s) may be. As we will show, the model with our splurge compo- 7
8 nent is consistent with all of what we described above as the key ‘takeaways’ from 8
9 the micro literature. 9

10
11 1.1.3 *Macroeconomic Models* Turning now to the macroeconomic setting, a 11
12 number of papers have addressed questions that are similar in spirit to ours. For 12
13 example, [McKay and Reis \(2016\)](#), [McKay and Reis \(2021\)](#), and [Phan \(2024\)](#) have 13
14 examined the role of automatic stabilizers in HA models. 14

15 But we follow much of the recent literature in treating recessions as ‘MIT 15
16 shocks’ – unanticipated events. And the policies we examine are discretionary, 16
17 which arguably makes sense as reflecting what occurs when the automatic stabi- 17
18 lizers have not automatically prevented a recession.⁸ 18

19 A relevant early contribution is by [Kaplan and Violante \(2014\)](#) who build a 19
20 model where agents save in both liquid and illiquid assets. Their model yields 20
21 a substantial consumption response to a stimulus payment, since MPCs are high 21
22 both for low-wealth households and for the many households (in their model) 22
23 with high net worth but little liquid assets (the “wealthy hand-to-mouth”). 23

24
25 ⁸In our model (and most others in the literature we are contributing to) consumers do not adjust 24
26 their labor supply in response to stimulus policies. This assumption is broadly consistent with the 25
27 empirical findings in [Ganong et al. \(2022\)](#) and [Chodorow-Reich and Karabarbounis \(2016\)](#). However, 26
28 the literature is conflicted on this subject; [Hagedorn et al. \(2017\)](#) and [Hagedorn et al. \(2019a\)](#) argue 27
29 that extensions of unemployment insurance affect both search decisions and vacancy creation lead- 28
30 ing to a rise in unemployment. [Kekre \(2022\)](#), on the other hand, evaluates the effect of extending 29
31 unemployment insurance in the period from 2008 to 2014, and finds that this extension raised ag- 30
32 gregate demand and implied a lower unemployment rate than without the policy. Finally, [Cohen and 31
Ganong \(2024\)](#) conduct a meta-analysis of the literature on how unemployment benefits impact un- 32
employment duration, and they find that the effects are modest.

¹ (Though the subsequent literature finding high MPC's even by wealthy house- ¹
² holds with ample liquidity casts doubt on this mechanism.) ²

³ [Bayer et al. \(2023\)](#) study discretionary fiscal policies implemented after a large ³
⁴ shock, in their case the COVID-19 pandemic. They find that targeted stimulus ⁴
⁵ through an increase in unemployment benefits has a much larger effect than ⁵
⁶ an untargeted policy. In contrast, we find that untargeted stimulus checks have ⁶
⁷ slightly larger spending effects than a targeted policy extending eligibility for ⁷
⁸ unemployment insurance. The difference derives from the fact that – in our ⁸
⁹ model as in the data – even middle- and high-liquid-wealth consumers have rela- ⁹
¹⁰ tively high MPCs, which means that much more of the stimulus checks get spent ¹⁰
¹¹ quickly. ¹¹

¹² [Carroll et al. \(2020b\)](#) also study the U.S. fiscal response to the COVID-19 pan- ¹²
¹³ demic, using a HA model similar in many respects to the one we study. They pre- ¹³
¹⁴ dicted⁹ the consumption response to the 2020 U.S. CARES Act that contained ¹⁴
¹⁵ both an extension of unemployment benefits and a stimulus check. They resolve ¹⁵
¹⁶ the tension between obtaining a realistic MPC and fitting the distribution of liq- ¹⁶
¹⁷ uid wealth by estimating the distribution of *ex-ante* heterogeneity in discount ¹⁷
¹⁸ factors that allows the model to match both kinds of data (discount heterogene- ¹⁸
¹⁹ ity is one of several competing mechanisms for resolving that tension discussed ¹⁹
²⁰ by [Kaplan and Violante \(2022\)](#)). But the model in that paper does not match the ²⁰
²¹ subsequently published evidence about the iMPC ([Fagereng et al. \(2021\)](#)); does ²¹
²² not incorporate a multiplier; and does not compare the *relative* effectiveness of ²²
²³ alternative stimulus policies. ²³

²⁴ Another related paper is [Broer et al. \(2025\)](#), who analyze the output response to ²⁴
²⁵ different fiscal policies in a HANK and SAM model similar to the one we present ²⁵
²⁶ in our robustness exercise. As we do in Section 5, they examine the policies in a ²⁶
²⁷ steady state rather than a recession. Unlike us, they do not calibrate their model ²⁷
²⁸ to match the wealth distribution and the iMPCs, and they do not evaluate the ²⁸
²⁹

³¹ “predicted” because the paper was published long before any data on the actual response were ³¹
³² available. ³²

1 policies using a welfare metric as we do in our baseline partial equilibrium set- 1
2 ting. 2

3 One criterion to rank policies is the extent to which induced spending is “mul- 3
4 tiplied,” and our paper therefore relates to the vast literature discussing the size 4
5 and timing of any multiplier. Our focus is on policies pursued in the Great Re- 5
6 cession, a period when monetary policy was essentially fixed at the zero lower 6
7 bound (ZLB). We therefore do not consider monetary policy responses to the 7
8 policies we evaluate in our primary analysis, and our work thus relates to pa- 8
9 pers such as [Christiano et al. \(2011\)](#) and [Eggertsson \(2011\)](#), who argue that fiscal 9
10 multipliers are higher in such circumstances. [Hagedorn et al. \(2019b\)](#) present an 10
11 HA model with both incomplete markets and nominal rigidities to evaluate the 11
12 size of the fiscal multiplier and also find that it is higher when monetary policy 12
13 is constrained. They focus on government spending instead of transfers and are 13
14 interested in the consequences of alternative options for financing that spend- 14
15 ing. [Broer et al. \(2023\)](#) also focus on fiscal multipliers for government spending 15
16 and show how they differ in representative agent and HA models with different 16
17 sources of nominal rigidities. Finally, [Ramey and Zubairy \(2018\)](#) find empirical 17
18 evidence that multipliers are higher when there is slack in the economy or the 18
19 ZLB binds. In any case, our concern in the versions of our model with multipliers 19
20 is to compare the *relative* size of any *differences* in multiplication across the poli- 20
21 cies we consider, which should thus be roughly scalable by the absolute size of 21
22 any multiplication effect, allowing a reader to scale our results by their preferred 22
23 estimate of the magnitude of recessionary multipliers. 23

24 Aside from the size of spending effects (whether multiplied or not), we are in- 24
25 terested in ranking policies in terms of their welfare consequences. Thus, the 25
26 paper relates to the recent literature on welfare comparisons in HA models. 26
27 Both [Bhandari et al. \(2021\)](#) and [Dávila and Schaab \(2022\)](#) introduce ways of de- 27
28 composing welfare effects. In the former case, these are aggregate efficiency, re- 28
29 distribution and insurance, while the latter further decomposes the insurance 29
30 part into intra- and intertemporal components. 30

31 One part of these decompositions is tricky: Under standard calibrations like the 31
32 ones we use, any change in redistribution tends to have powerful consequences 32

1 on welfare. We presume that there are real (but unmodeled) reasons that the 1
2 equilibrium degree of redistribution in normal (nonrecessionary) times is much 2
3 less than the model would call for. We therefore develop a welfare measure that 3
4 abstracts from any incentive for a planner to increase redistribution in the steady 4
5 state (or “normal” times). 5

6 6

7 1.2 *Organization* 7

8 The paper is organized as follows. Section 2 presents our baseline partial equi- 8
9 librium model of households’ consumption and saving problem as well as how 9
10 we model a recession and the potential response in terms of three different con- 10
11 sumption stimulus policies. Section 3 describes the steps we take to parameterize 11
12 the model and discusses the implications for some moments that we do not tar- 12
13 get. In section 4 we compare the three policies implemented in a recession both 13
14 in terms of their multipliers and in terms of a welfare measure that we introduce. 14
15 Section 5 presents a general equilibrium HANK and SAM model where we com- 15
16 pare the multipliers of the same three policies to the partial equilibrium results. 16
17 Section 6 concludes. Finally, the appendix provides more details of the HANK and 17
18 SAM model discussed in Section 5, while an online appendix shows results from 18
19 a version of the model without splurge consumption. 19

20 20

21 2. MODEL 21

22 Consumers differ by their level of education and, within education group, by sub- 22
23 jective discount factors (calibrated to match the within-group distribution of liq- 23
24 uid wealth). We first describe each kind of consumer’s problem, given an income 24
25 process with permanent and transitory shocks calibrated to their type, as well as 25
26 type-specific shocks to employment. The next step describes the arrival of a re- 26
27 cession and the policies we study as potential fiscal policy responses. The last sec- 27
28 tion discusses an extension incorporating aggregate demand effects that induce 28
29 feedback from aggregate consumption to income and (via the marginal propen- 29
30 sity to consume) back to consumption, amplifying the effect of a recession when 30
31 it occurs. 31

32 32

1 A consumer i has education $e(i)$ and a subjective discount factor β_i . The con- 1
 2 sumer faces a stochastic income stream, $y_{i,t}$, and chooses to consume a fraction 2
 3 of that income when it arrives—the ‘splurge’, described in the introduction.¹⁰ 3
 4 With what is left over, the consumer chooses to optimize consumption without 4
 5 regard to the fraction that was already spent. Therefore, consumption each pe- 5
 6 riod for consumer i can be written as in (1): 6

$$7 \quad c_{i,t} = c_{sp,i,t} + c_{opt,i,t}, \quad (1) \quad 7 \\ 8 \quad 8 \\ 9 \quad 9$$

10 where $c_{i,t}$ is total consumption, $c_{sp,i,t}$ is the splurge consumption, and $c_{opt,i,t}$ 10
 11 is the consumer’s optimal choice of consumption after splurging. Splurge con- 11
 12 sumption is simply a fraction of income, as shown in (2): 12

$$13 \quad c_{sp,i,t} = \varsigma y_{i,t}, \quad (2) \quad 13 \\ 14 \quad 14$$

15 while the optimized portion of consumption is chosen to maximize the perpetual- 15
 16 youth lifetime expected-utility-maximizing consumption, where D is the death 16
 17 probability: 17

$$18 \quad \sum_{t=0}^{\infty} \beta_i^t (1 - D)^t \mathbb{E}_0 u(c_{opt,i,t}), \quad (3) \quad 18 \\ 19 \quad 19 \\ 20 \quad 20$$

21 We use a standard CRRA (constant relative risk aversion) utility function, so 21
 22 $u(c) = c^{1-\gamma}/(1-\gamma)$ for $\gamma \neq 1$ and $u(c) = \log(c)$ for $\gamma = 1$, where γ is the coefficient 22
 23 of relative risk aversion. The optimization is subject to the budget constraint (4), 23
 24 given existing market resources $m_{i,t}$ and income state, and a no-borrowing con- 24
 25 straint: 25

$$26 \quad a_{i,t} = m_{i,t} - c_{i,t}, \quad 26 \\ 27 \quad m_{i,t+1} = Ra_{i,t} + y_{i,t+1}, \quad (4) \quad 27 \\ 28 \quad 28 \\ 29 \quad a_{i,t} \geq 0, \quad 29$$

30 ¹⁰One attractive feature of the splurge assumption is that it is also consistent with evidence 30
 31 from Ganong and Noel (2019), that spending drops sharply following the large and predictable drop 31
 32 in income after the exhaustion of unemployment benefits; see Section 3.3.4. 32

1 where R is the gross interest factor for accumulated assets $a_{i,t}$, and $y_{i,t+1}$ is deter-
 2 mined by (6).

3

4 2.1 *The income process* 4

5 Consumers face a stochastic income process with permanent and transitory
 6 shocks to income, along with unemployment shocks. In normal times, con-
 7 sumers who become unemployed receive unemployment benefits for two quar-
 8 ters. Permanent income evolves according to (5):

9

$$10 \quad p_{i,t+1} = \psi_{i,t+1} \Gamma_{e(i)} p_{i,t}, \quad (5) \quad 10$$

11 where $\psi_{i,t+1}$ is the shock to permanent income and $\Gamma_{e(i)}$ is the average growth
 12 rate of income for the consumer's education group $e(i)$.¹¹ The realized growth
 13 rate of permanent income for consumer i is thus $\hat{\Gamma}_{i,t+1} = \psi_{i,t+1} \Gamma_{e(i)}$. The shock to
 14 permanent income is normally distributed with variance σ_ψ^2 .

15 The actual income a consumer receives, given the permanent income from (5),
 16 will be subject to the individual's employment status as well as transitory shocks,
 17 $\xi_{i,t}$, as shown in (6):

$$19 \quad y_{i,t} = \begin{cases} \xi_{i,t} p_{i,t}, & \text{if employed} \\ 20 \quad \rho_b p_{i,t}, & \text{if unemployed with benefits} \\ 21 \quad \rho_{nb} p_{i,t}, & \text{if unemployed without benefits} \end{cases} \quad (6) \quad 20$$

22 where $\xi_{i,t}$ is normally distributed with variance σ_ξ^2 , and ρ_b and ρ_{nb} are the replace-
 23 ment rates for an unemployed consumer who is or is not eligible for unemploy-
 24 ment benefits, respectively.

25 A Markov transition matrix Π generates the unemployment dynamics where
 26 the number of states is given by 2 plus the number of periods that unemploy-

27 ¹¹We model the rate of growth for permanent income for each education group and keep this rate
 28 unchanged during periods of unemployment. There is evidence, e.g. in [Davis and Wachter \(2011\)](#),
 29 that unemployment, especially in a recession, leads to permanent income loss. This finding could be
 30 added to the model—see [Carroll et al. \(2020b\)](#) for an example—but is not material to the evaluation
 31 of stimulus payments here so we have chosen to keep the model simple.

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ment benefits last. An employed consumer can continue being employed or move to being unemployed with benefits.¹² The first row of Π is thus given by $[1 - \pi_{eu}^{e(i)}, \pi_{eu}^{e(i)}, 0]$, where $\pi_{eu}^{e(i)}$ indicates the probability of becoming unemployed from an employed state and 0 is a vector of zeros of the appropriate length. Note that we allow this probability to depend on the education group of consumer i and will calibrate this parameter to match the average unemployment rate for each education group. Upon becoming unemployed, all consumers face a probability π_{ue} of transitioning back into employment and a probability $1 - \pi_{ue}$ of remaining unemployed with one less period of remaining benefits. After transitioning into the unemployment state where the consumer is no longer eligible for benefits, the consumer will remain in this state until becoming employed again. The probability of becoming employed is thus the same for each of the unemployment states and education groups.

2.2 Recessions and policies

We model the arrival of a recession, and the government policy response to it, as an unpredictable event—an MIT shock. We have four types of shocks: one representing a recession and one for each of the three different policy responses we consider. The policy responses are usually modeled as in addition to the recession, but we also consider a counterfactual in which the policy response occurs without a recession in order to understand the welfare effects of the policy.

2.2.0.1 Recession. At the onset of a recession, several changes occur. First, the unemployment rate for each education group doubles: Those who would have been unemployed in the absence of a recession are still unemployed, and an additional number of consumers move from employment to unemployment. Second, conditional on the recession continuing, the employment transition matrix is adjusted so that unemployment remains at the new high level and the expected length of time for an unemployment spell increases. In our baseline calibration, discussed in detail in section 3.3.1, we set the expected length of an unemployment spell to one and a half quarters in normal times, and this length increases to

¹²That is, as long as we assume that there is at least one period of unemployment benefits.

1 four quarters in a recession. Third, the end of the recession occurs as a Bernoulli 1
2 process calibrated for an average length of recession of six quarters. Finally, at the 2
3 end of a recession, the employment transition matrix switches back to its origi- 3
4 nal probabilities, and, as a result, the unemployment rate trends down over time, 4
5 back to its steady-state level. The details of how certain model parameters change 5
6 in a recession are presented in section 3.3.2. 6

7 7
8 2.2.0.2 *Policies.* The policies we consider in response to a recession are inspired 8
9 by the Economic Stimulus Act of 2008 and the Tax Relief, Unemployment Insur- 9
10 ance Reauthorization, and Job Creation Act of 2010. The former included means 10
11 tested stimulus checks in the form of tax rebates, and the latter included both an 11
12 extension of unemployment benefits and a tax cut. Based on these examples we 12
13 therefore consider the following stimulus policies in our framework: 13

14 14
15 2.2.0.3 *1. Stimulus check.* In this policy response, the government sends money 15
16 to every consumer that directly increases the household's market resources. The 16
17 checks are means-tested depending on permanent income. A check for \$1,200 17
18 is sent to every household with permanent income less than \$100,000, and this 18
19 amount is then linearly reduced to zero for households with a permanent income 19
20 greater than \$150,000. Similar policies were implemented in the U.S. in 2001, 20
21 2008, and during the pandemic. 21

22 22
23 2.2.0.4 *2. Extended unemployment benefits.* In this policy response, unemploy- 23
24 ment benefits are extended from two quarters to four quarters. That is, those who 24
25 become unemployed at the start of the recession, or who were already unem- 25
26 ployed, will receive unemployment benefits for up to four quarters (including 26
27 quarters leading up to the recession). Those who become unemployed one quar- 27
28 ter into the recession will receive up to three quarters of unemployment benefits. 28
29 These extended unemployment benefits will occur regardless of whether the re- 29
30 cession ends, and no further extensions are granted if the recession continues. 30
31 This policy reflects temporary changes made to unemployment benefits in the 31
32 U.S. following the great recession. 32

3. Payroll tax cut. In this policy response, employee-side payroll taxes are reduced for a period of eight quarters.¹³ During this period, which continues irrespective of whether the recession continues or ends, employed consumers' income is increased by 2 percent. The income of the unemployed is unchanged by this policy. Households also believe there is a 50-50 chance that the tax cut will be extended by another two years if the recession has not ended when the first tax cut expires.¹⁴ The payroll tax cut introduced in the U.S. in 2010 was itself an extension of previously implemented cuts and had a two-year horizon.

10
11 2.2.0.6 *Financing the policies.* Some work in the HA macro literature has shown 11
12 that if taxes are raised immediately to offset any fiscal stimulus, results can be 12
13 very different than they would be if, as occurs in reality, recessionary policies are 13
14 debt financed. However, typical fiscal rules assume that any increase in debt gets 14
15 financed over a long interval. Accordingly, almost all of the effects of any partic- 15
16 ular fiscal rule will be similar for each of our policies so long as the great majority 16
17 of the debt is repaid after the short recessionary period that is our main focus. 17

To keep our analysis as simple as possible, we do not model the debt repayment. Any of a variety of fiscal rules could be imposed for the period following our short period of interest, but we did not want to choose any particular fiscal rule in order to avoid making a choice that has little consequence for our key question. Advocates of alternative fiscal rules likely already have intuitions about how such rules' economic consequences differ, but those consequences—under our partial equilibrium analysis—will be similar for all three policies we consider. Alternative choices of fiscal rules will therefore not affect the ranking of policies that is our principal concern.¹⁵

²⁷ _____
²⁸ ¹³Although payroll taxes are paid by both the employer and the employee, the payroll tax cuts in
²⁹ the U.S. have been applied only the employee side. ²⁹

³⁰ ¹⁴The belief that the payroll tax cut may be extended makes little difference to the results.

³¹ In our general equilibrium analysis in section 5, we apply a fiscal rule that assumes debt is slowly paid back over time. 31

³² 32

2.3 Aggregate demand effects

² Our baseline model is a partial equilibrium model that does not include any
³ feedback from aggregate consumption to income. In an extension to the model,
⁴ we add aggregate demand effects during the recession. The motivation for this
⁵ specification comes from the idea that spending in an economy with substantial
⁶ slack and in which the central bank is unable to prevent a recession will result
⁷ in higher utilization rates and greater output. By contrast, government spending
⁸ in an economy running at potential with an active monetary policy will not suc-
⁹ ceed in increasing output. The recent inflation experience of the U.S. provides
¹⁰ some evidence that output responds highly non-linearly to aggregate demand.
¹¹ This idea is explored in a recent revival of research into non-linear Phillips curves,
¹² such as [Benigno and Eggertsson \(2023\)](#) and [Blanco et al. \(2024\)](#).

¹³ With this extension, any changes in consumption away from the steady-state
¹⁴ consumption level feed back into labor income. Aggregate demand effects are
¹⁵ evaluated as in (7):

$$AD(C_t) = \begin{cases} \left(C_t / \tilde{C} \right)^{\kappa}, & \text{if in a recession} \\ 1, & \text{otherwise,} \end{cases} \quad (7)$$

where \tilde{C} is the level of consumption in the steady state. Idiosyncratic income in the aggregate demand extension is multiplied by the aggregate demand function from (7), as shown in (8):

$$\mathbf{y}_{AD,i,t} = AD(C_t)\mathbf{y}_{i,t}, \quad (8)$$

The series $v_{AD, it}$ from (8) is then used for each consumer's budget constraint (4).

3. PARAMETERIZING THE MODEL

28 This section describes how we set the model's parameters. First, we estimate the
29 extent to which consumers 'splurge' when receiving an income shock. Given the
30 lack of empirical evidence on the marginal propensity to consume over time for
31 the US, we instead use Norwegian data to estimate the splurge. Specifically, we
32 calibrate our model to the Norwegian economy and match evidence from Nor-

1 way on the profile of the marginal propensity to spend over time and across dif- 1
2 ferent wealth levels, as provided by Fagereng et al. (2021).¹⁶ 2

3 Second, we set up the full model on U.S. data, taking the splurge factor as given 3
4 from the Norwegian estimation. In the full model, agents differ according to their 4
5 level of education and their subjective discount factors. A subset of the param- 5
6 eters in the model are calibrated equally for all types, and some parameters are 6
7 calibrated to be specific to each education group. Finally, a distribution of subjec- 7
8 tive discount factors is estimated separately for each education group to match 8
9 features of each within-group liquid wealth distribution. 9

10 10

11 3.1 *Estimation of the splurge factor* 11

12 The splurge allows us to capture the shorter- and longer-term response of con- 12
13 sumption to income shocks, especially for consumers with significant liquid 13
14 wealth. The main aim of this paper, however, is to rank consumption stimulus 14
15 policies, not to provide a microfoundation for the splurging behavior. We view the 15
16 splurge factor as a model device that enables us to rank the policies in a model 16
17 that is consistent with the best available micro-evidence of spending patterns 17
18 over time after a transitory income shock. In Appendix B we provide results from 18
19 our model without a splurge factor. There we show that such a model provides 19
20 a worse fit to the moments in the data that we are interested in, but not dra- 20
21 matically so, and that our conclusions regarding the ranking of the policies are 21
22 not affected. However, in our view, this version of the model requires households 22
23 with unreasonably low discount factors. 23

24 The specific exercise we carry out in this section, is to show that our model 24
25 can account well for the results of Fagereng et al. (2021), who study the effect of 25
26 lottery winnings in Norway on consumption using millions of records from the 26
27 Norwegian population registry. We calibrate our model to reflect the Norwegian 27
28 economy and, using their results, estimate the splurge factor, as well as the distri- 28
29 bution of discount factors in the population, to match two empirical moments. 29
30

31 ¹⁶Appendix B discusses an alternative calibration method, which solely relies on US data. The main 31
32 results derived in that calibration are in line with those discussed in the main text. 32

1 First, we take from Fagereng et al. (2021) the marginal propensity to consume 1
 2 out of a one-period income shock. We target not only the initial (aggregate) re- 2
 3 sponse of consumption to the income shock, but also the subsequent effect on 3
 4 consumption in years one through four after the shock. We also target the initial 4
 5 consumption response in the cross-section, i.e. across the quartiles of the liquid 5
 6 wealth distribution, for which empirical estimates are also provided. The shares 6
 7 of lottery winnings expended at different time horizons, as found in Fagereng 7
 8 et al. (2021), are plotted in figure 1a. Table 1 (second row) shows the initial con- 8
 9 sumption response across liquid wealth quartiles. 9

10 Second, we match the steady-state distribution of liquid wealth in the model to 10
 11 its empirical counterpart. Because of the lack of data on the liquid wealth distri- 11
 12 bution in Norway, we use the corresponding data from the United States, assum- 12
 13 ing that liquid wealth inequality is comparable across these countries.¹⁷ Specifi- 13
 14 cally, we impose as targets the cumulative liquid wealth shares for the entire pop- 14
 15 ulation at the 20th, 40th, 60th, and 80th income percentiles, which, in data from 15
 16 the Survey of Consumer Finances (SCF) in 2004 (Board of Governors of the Fed- 16
 17 eral Reserve System, 2004) (see section 3.2 for further details), equal 0.03 percent, 17
 18 0.35 percent, 1.84 percent, and 7.42 percent, respectively. Hence, 92.6 percent of 18
 19 the total liquid wealth is held by the top income quintile. We also target the mean 19
 20 liquid wealth to income ratio of 6.60. The data are plotted in figure 1b. 20

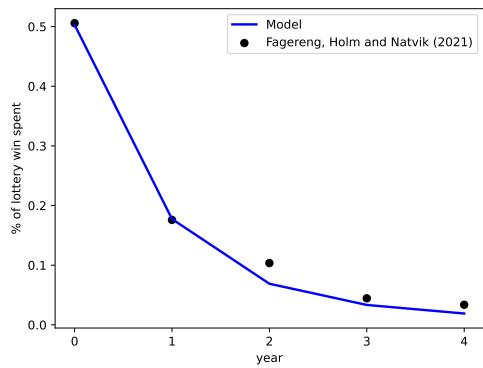
21 21
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30 ¹⁷Data from the Norwegian tax registry contains information on liquid assets, but not liquid debt. 30
 31 Only total debt is reported – which is mainly mortgage debt. Therefore, we cannot construct liquid 31
 32 wealth as Kaplan and Violante (2014) can for the U.S. 32

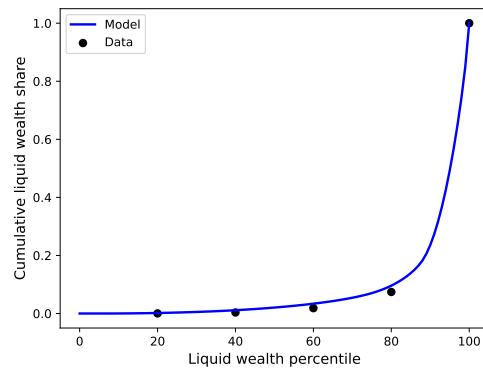
1 TABLE 1. MPC's across wealth quartiles and in total

2 Targeting K/Y and avg MPC by quartile

	MPC					
	1st WQ	2nd WQ	3rd WQ	4th WQ	Agg	K/Y
Model	0.27	0.48	0.60	0.66	0.50	6.58
Data	0.39	0.39	0.55	0.66	0.51	6.60

8 FIGURE 1. Model fit to spending behavior and wealth distribution
9

18 (a) Spending dynamics after lottery win



18 (b) Liquid wealth distribution

20 **Note:** This figure demonstrates the calibration of the splurge factor (Section 3.1). Panel (a) shows
21 the model's fit to the dynamic consumption response following lottery wins in Norway, as estimated
22 by Fagereng et al. (2021) using millions of population registry records. The splurge factor of $\varsigma = 0.249$
23 allows the model to match both the high initial MPC and the gradual spending over subsequent years.
24 Panel (b) shows the model's fit to the U.S. liquid wealth distribution from the 2004 SCF, with 92.6% of
25 liquid wealth held by the top income quintile. See Section 3.2 for the liquid wealth definition following
Kaplan and Violante (2014).

26 For this estimation exercise, the remaining model parameters are calibrated
27 to reflect the Norwegian economy. Specifically, we set the real interest rate to 2
28 percent annually and the unemployment rate to 4.4 percent, in line with Aurs-
29 land et al. (2020). The quarterly probability to survive is calibrated to $1 - 1/160$,
reflecting an expected working life of 40 years. Aggregate productivity growth is
set to 1 percent annually, following Kravik and Mimir (2019). The unemployment
net replacement rate is calibrated to 60 percent, following OECD (2020). Finally,

¹ we set the real interest rate on liquid debt to 13.6 percent, following data from the ¹
² Norwegian debt registry [Gjeldsregistret \(2022\)](#).¹⁸ ²

³ Estimates of the standard deviations of the permanent and transitory shocks ³
⁴ are taken from [Crawley et al. \(2024\)](#), who estimate an income process on admin- ⁴
⁵ istrative data for Norwegian males from 1971 to 2014. The estimated annual vari- ⁵
⁶ ances for the permanent and transitory shocks are 0.004 and 0.033, respectively.¹⁹ ⁶
⁷ As in [Carroll et al. \(2020a\)](#), these are converted to quarterly values by multiplying ⁷
⁸ the permanent and transitory shock variances by 1/4 and 4, respectively. Thus, ⁸
⁹ we obtain quarterly standard deviations of $\sigma_\psi = 0.0316$ and $\sigma_\xi = 0.363$. ⁹

¹⁰ Using the calibrated model, we simulated unexpected lottery winnings and ¹⁰
¹¹ calculate the share of the lottery spent in each year. Specifically, each simulated ¹¹
¹² agent receives a lottery win in a random quarter of the first year of the simula- ¹²
¹³ tion. The size of the lottery win is itself random and spans the range of lottery ¹³
¹⁴ sizes found in [Fagereng et al. \(2021\)](#). The estimation procedure minimizes the ¹⁴
¹⁵ distance between the target and model moments by selecting the splurge factor ¹⁵
¹⁶ and the distribution of discount factors in the population, where the latter are ¹⁶
¹⁷ assumed to be uniformly distributed in the range $[\beta - \nabla, \beta + \nabla]$. We approximate ¹⁷
¹⁸ the uniform distribution of discount factors with a discrete approximation and ¹⁸
¹⁹ let the population consist of seven different types. ¹⁹

²⁰ The estimation yields a splurge factor of 0.246 and a distribution of discount ²⁰
²¹ factors described by $\beta = 0.968$ and $\nabla = 0.0578$. Given these estimated parameters ²¹
²² and the remaining calibrated ones, the model is able to replicate the time path of ²²
²³ consumption in response to a lottery win from [Fagereng et al. \(2021\)](#) and the tar- ²³
²⁴ geted distribution of liquid wealth well, see Figure 1. Also, the targeted moments ²⁴
²⁵

²⁶¹⁸Specifically, we determine the average volume-weighted interest rate on liquid debt, which con- ²⁶
²⁷sists of consumer loans, credit and payment card debt and all other unsecured debt. We use data from ²⁷
²⁸December 2019. Note that although these data let us pin down aggregate quantities, they do not solve ²⁸
²⁹the issue referred to in footnote 17, since we cannot link them to the tax registry at the individual ²⁹
³⁰level. We set the borrowing limit on liquid debt to zero.

³⁰¹⁹As shown in [Crawley et al. \(2024\)](#), an income process of the form that we use here is more accu- ³⁰
³¹rately estimated using moments in levels not differences. Hence, we take the numbers from column ³¹
³²3 of Panel C in their table 4. ³²

1 discussed in Table 1 are captured well. In particular, the model is able to account 1
2 for the empirical fact, in the first column, that the MPC for high-wealth agents is 2
3 far above the near-zero value predicted by a model without a splurge. 3

4 4

5 5

6 *3.2 Data on permanent income, liquid wealth, and education* 6

7 7

8 Before we move on to the parameterization of the full model, we describe in detail 8
9 the data that we use to get measures of permanent income, liquid wealth, and the 9
10 division of households into educational groups in the United States. We use data 10
11 on the distribution of liquid wealth from the 2004 wave of the SCF ([Board of Gov-](#) 11
[ernors of the Federal Reserve System, 2004](#)). We restrict our attention to house- 12
holds where the head is of working age, which we define to be in the range from 13
14 25 to 62. The SCF-variable “normal annual income” is our measure of the house- 14
15 hold’s permanent income, and, to exclude outliers, we drop the observations that 15
16 make up the bottom 5 percent of the distribution of this variable. The smallest 16
17 value of permanent income for households in our sample is thus \$16,708. 17

18 Liquid wealth is defined as in [Kaplan and Violante \(2014\)](#) and consists of cash, 18
19 money market, checking, savings, and call accounts; directly held mutual funds; 19
20 and stocks and bonds. We subtract off liquid debt, which is the revolving debt on 20
21 credit card balances. Note that the SCF does not contain information on cash 21
22 holdings, so these are imputed with the procedure described in Appendix B.1 22
23 of [Kaplan and Violante \(2014\)](#), which also describes the credit card balances that 23
24 are considered part of liquid debt. We drop any households that have negative 24
25 liquid wealth. 25

26 Households are classified into three educational groups. The first group, 26
27 “Dropout,” applies to households where the head of household has not obtained 27
28 a high school diploma; the second group, “Highschool,” includes heads of house- 28
29 holds who have a high school diploma and those who, in addition, have some 29
30 years of college education without obtaining a bachelor’s degree; and the third 30
31 group, “College,” consists of heads of households who have obtained a bachelor’s 31
32 degree or higher. With this classification of the education groups, the Dropout 32

¹ group makes up 9.3 percent of the population, the Highschool group 52.7 per-
² cent, and the College group 38.0 percent.

³ With our sample selection criteria, we are left with a sample representing about
⁴ 61.3 million U.S. households.

⁵ 3.3 *Parameters in the full model* ⁶

⁷ With households classified into the three education groups using the SCF data,
⁸ we proceed to set the parameters of the model as follows. First, we calibrate a
⁹ set of parameters that apply to all types of households in the model. Second, we
¹⁰ calibrate another set of parameters that are specific to each education group to
¹¹ capture broad differences across these groups. Finally, given the calibrated pa-
¹² rameters we estimate discount factor distributions for each education group that
¹³ allow us to match the distribution of liquid wealth in each group.

¹⁴ The model is a simplified model for households in that we do not take into ac-
¹⁵ count heterogeneity across household size or composition. The households are
¹⁶ ex-ante heterogeneous in their subjective discount factors as well as their level of
¹⁷ education. We classify the education level of the household based on the educa-
¹⁸ tion of the head of the household, and we typically think of individual character-
¹⁹ istics as applying to that person.

²⁰ A period in the model is one quarter. This choice makes it realistic to consider
²¹ stimulus policies that are implemented in the same period as a recession starts.
²²

²³ 3.3.1 *Calibrated parameters — Normal times* Table 2 presents our calibration
²⁴ of the model parameters in normal times. Panel A lists parameters that are cali-
²⁵ brated equally across all types in the model, and Panel B lists parameters in the
²⁶ model that are education specific. In the next subsection we present how certain
²⁷ model parameters change when the economy enters a recession.

²⁸ **Preferences, survival and interest rates.** All households are assumed to have a
²⁹ coefficient of relative risk aversion equal to $\gamma = 2$. We also assume that all house-
³⁰ holds have the same propensity to splurge out of transitory income gains and set
³¹ $\varsigma = 0.246$, the value estimated in section 3.1. However, each education group is di-
³² vided into types that differ in their subjective discount factors. The distributions

1 of discount factors for each education group are estimated to fit the distribution 1
2 of liquid wealth within that group, and this estimation is described in detail in 2
3 section 3.3.3. Regardless of type, households face a constant survival probability 3
4 each quarter. This probability is set to $1 - 1/160$, reflecting an expected working 4
5 life of 40 years. The real interest rate on households' savings is set to 1 percent per 5
6 quarter. 6

7 **Labor market risk while employed.** When consumers are born, they receive an 7
8 initial level of permanent income. This initial value is drawn from a log-normal 8
9 distribution that depends on the education level the household is born with. For 9
10 each education group, the parameters of the distribution are determined by the 10
11 mean and standard deviation of log-permanent income for households in that 11
12 group where the head of the household is of age 25 in the SCF 2004. For the 12
13 Dropout group, the mean initial value of quarterly permanent income is \$6,200; 13
14 for the Highschool group, it is \$11,100; and for the College group, it is \$14,500. 14
15 The standard deviations of the log-normal distributions for each group are, re- 15
16 spectively, 0.32, 0.42, and 0.53. 16

17 While households remain employed, their income is subject to both perma- 17
18 nent and transitory idiosyncratic shocks. These shocks are distributed equally 18
19 for the three education groups. The standard deviations of these shocks are taken 19
20 from Carroll et al. (2020a), who set the standard deviations of the transitory and 20
21 permanent shocks to $\sigma_\xi = 0.346$ and $\sigma_\psi = 0.0548$, respectively. 21

22 Permanent income also grows, on average, with a growth factor $\Gamma_{e(i)}$ that de- 22
23 pends on the level of education. These average growth rates are based on num- 23
24 bers from Carroll et al. (2020b), who construct age-dependent expected perma- 24
25 nent income growth factors using numbers from Cagetti (2003) and fit the age- 25
26 dependent numbers to their life-cycle model. We construct the quarterly growth 26
27 rates of permanent income in our perpetual-youth model by taking the average 27
28 of the age-dependent growth rates during a household's working life. The aver- 28
29 age gross quarterly growth rates that we obtain for the three education groups 29
30 are then $\Gamma_d = 1.0036$, $\Gamma_h = 1.0045$, and $\Gamma_c = 1.0049$. 30

31 31

32 32

1 TABLE 2. Calibrated Model Parameters — Normal times
 2 Panel A: Parameters that apply to all types

3 Parameter	Notation	Value
Risk aversion	γ	2.0
Splurge	ς	0.25
Survival probability, quarterly	$1 - D$	0.994
Risk free interest rate, quarterly (gross)	R	1.01
Standard deviation of transitory shock	σ_ξ	0.346
Standard deviation of permanent shock	σ_ψ	0.0548
Unemp. benefits replacement rate (share of PI)	ρ_b	0.7
Unemp. income w/o benefits (share of PI)	ρ_{nb}	0.5
Avg. dur. of unemp. benefits in normal times (quarters)		2
Avg. dur. of unemp. spell in normal times (quarters)		1.5
Prob. of leaving unemp.	π_{ue}	0.667
Consumption elasticity of aggregate demand effect	κ	0.3

15 Shows parameters calibrated the same for all types.

17 Panel B: Parameters calibrated for each education group

19	Dropout	Highschool	College	18
Percent of population	9.3	52.7	38.0	20
Avg. quarterly PI of “newborn” agent (\$1000)	6.2	11.1	14.5	21
Std. dev. of log(PI) of “newborn” agent	0.32	0.42	0.53	22
Avg. quarterly gross growth factor for PI (Γ_e)	1.0036	1.0045	1.0049	23
Unemp. rate in normal times (percent)	8.5	4.4	2.7	23
Prob. of entering unemp. (π_{eu}^e , percent)	6.2	3.1	1.8	24

25 Shows parameters calibrated for each education group. (“PI” is permanent income).

27
 28 **Unemployment.** Consumers also face the risk of becoming unemployed and
 29 will then have access to unemployment benefits for a certain period. The param-
 30 eters describing the unemployment benefits in normal times are based on the
 31 work of [Rothstein and Valletta \(2017\)](#), who study the effects on household in-
 32 come of unemployment and of running out of eligibility for benefits. The unem-

1 ployment benefits replacement rate is thus set to $\rho_b = 0.7$ for all households, and 1
2 when benefits run out, the unemployment replacement rate without any benefits 2
3 is set to $\rho_{nb} = 0.5$. These replacement rates are set as a share of the households' 3
4 permanent income and are based on the initial drop in income upon entering an 4
5 unemployment spell, presented in figure 3 in [Rothstein and Valletta \(2017\)](#).²⁰ 5

6 The duration of unemployment benefits in normal times is set to two quarters, 6
7 so that our Markov transition matrix Π has four states. This length of time corre- 7
8 sponds to the mean duration of unemployment benefits across U.S. states from 8
9 2004 to mid-2008 of 26 weeks, reported by [Rothstein and Valletta \(2017\)](#). 9

10 The probability of transitioning out of unemployment is set to match the aver- 10
11 age duration of an unemployment spell in normal times. In data from the Bureau 11
12 of Labor Statistics, this average duration was 19.6 weeks or 1.5 quarters in 2004. 12
13 We do not have data on education-specific duration rates, however, so we set the 13
14 average duration of unemployment to 1.5 quarters for all households. This im- 14
15 plies that the transition probability from unemployment to employment is set to 15
16 $\pi_{ue} = 2/3$. 16

17 The Bureau of Labor Statistics provide data on unemployment rates for differ- 17
18 ent education groups, and we match the average rate in each group in 2004 by 18
19 setting an education-specific probability of transitioning from employment into 19
20 unemployment. Note that this calibration strategy is consistent with the results 20
21 in [Mincer \(1991\)](#) who finds that the main difference between education groups 21
22 is in the incidence of unemployment, and not its duration.²¹ More recent work 22
23 by [Elsby and Hobijn \(2010\)](#) includes data up to 2009 and echoes [Mincer's](#) results. 23

24 ²⁰See the lines for their UI exhaustee sample including and excluding UI income. [Rothstein and](#) 24
25 [Valletta \(2017\)](#) also point out that “UI benefits replace about 40 percent of the lost earnings on aver- 25
26 age” (page 894). For a household with two income earners with equal income, these findings would 26
27 mean that income drops to 70 percent when one earner becomes unemployed and to 50 percent 27
28 when benefits run out. In this paper we ignore several of the channels studied by [Rothstein and Val- 28
29 letta \(2017\)](#) such as within household insurance and other social programs that can provide income 29
even after UI benefits have run out.

30 ²¹[Mincer \(1991\)](#) states that “the reduction of the incidence of unemployment [at higher education

31 levels] is found to be far more important than the reduced duration of unemployment in creating the

32 educational differentials in unemployment rates” (page 1).

1 The average unemployment rate in 2004 was 8.5 percent for the Dropout group,
 2 4.4 percent for the Highschool group, and 2.7 percent for the College group. These
 3 values imply that the probabilities of transitioning into unemployment in nor-
 4 mal times are $\pi_{eu}^d = 6.2$ percent, $\pi_{eu}^h = 3.1$ percent, and $\pi_{eu}^c = 1.8$ percent, respec-
 5 tively.²²

6 Finally, the strength of the aggregate demand effect in recessions is determined
 7 by the consumption elasticity of productivity. We follow Krueger et al. (2016) and
 8 set this to $\kappa = 0.3$.

9
 10 3.3.2 *Calibrated parameters — Recession* Table 3 shows the model parameters
 11 that change when a recession hits. Panel A shows the change in two parameters
 12 that apply to all types, and Panel B shows changes in some parameters that differ
 13 across education groups. For completeness, panel C summarizes the remaining
 14 parameters describing how we model a recession and the three policies we con-
 15 sider as potential responses to a recession.

16 The two immediate changes that occur at the outset of a recession is that the
 17 unemployment rate doubles for all education groups, and the expected duration
 18 of an unemployment spell increases from 1.5 to 4 quarters. The duration of un-
 19 employment is the same across the three education groups, and this implies that
 20 the probability of leaving unemployment is set to $\pi_{ue} = 0.25$ in a recession.

21 The increase in the expected duration of unemployment combined with the
 22 doubling of the education-specific unemployment rates pin down new values
 23 for the probabilities of transitioning from employment to unemployment dur-
 24 ing the recession. Due to the large increase in the unemployment duration, the
 25 values that we obtain end up being slightly smaller than those transition proba-
 26 bilities in normal times. The probability π_{eu} in a recession is set to 5.1 percent for

27 ²²Also note that the probability of transitioning from employment to unemployment is the proba-
 28 bility of a job separation times the conditional probability of unemployment given a job separation.
 29 Mincer (1991) reports that both of these are lower for higher education levels. For our calibration, this
 30 means that a higher job finding rate *within* the quarter of the job separation for more educated work-
 31 ers translates into a lower probability of transitioning from employment to unemployment during a
 32 quarter. In that sense, our calibration is consistent with short-term job-finding rates being higher for
 33 more educated workers.

1 the Dropout group, 2.4 percent for the Highschool group, and 1.4 for the College 1
2 group. 2

3 Our calibration of the transition probabilities between employment and un- 3
4 employment during a recession are thus broadly in line with the results of Elsby 4
5 and Hobijn (2010). They find that unemployment duration does not vary much 5
6 between education groups and that the flow from unemployment to employment 6
7 drops sharply for all groups in a recession. The flow into unemployment is more 7
8 stable, but they find that it tends to increase a little bit in recessions.²³ This differs 8
9 from the small decrease in the transition probabilities from employment into un- 9
employment that our calibration strategy implies, which follows from our choice 10
10 of targeting a doubling of the unemployment rate for each group rather than an 11
11 even larger increase. 12

13 3.3.3 *Estimating the discount factor distributions* Discount factor distributions 13
14 are estimated separately for each education group to match the distribution of 14
15 liquid wealth for households in that group. To do so, we let each education group 15
16 consist of types that differ in their subjective discount factor, β . The discount fac- 16
17 tors within each group $e \in \{d, h, c\}$ are assumed to be uniformly distributed in the 17
18 range $[\beta_e - \nabla_e, \beta_e + \nabla_e]$. The parameters β_e and ∇_e are chosen for each group sep- 18
19 arately to match the median liquid-wealth-to-permanent-income ratio and the 19
20 20th, 40th, 60th, and 80th percentile points of the Lorenz curve for liquid wealth 20
21 for that group. We approximate the uniform distribution of discount factors with 21
22 a discrete approximation and let each education group consist of seven different 22
23 types. 23

24 Panel A of table 4 shows the estimated values of (β_e, ∇_e) for each education 24
25 group. The panel also shows the minimum and maximum values of the dis- 25
26 count factors we actually use in the model when we use a discrete approximation 26
27 with seven values to approximate the uniform distribution of discount factors. 27
28 Panel B of table 4 shows that with these estimated distributions, we can exactly 28
29 match the median liquid-wealth-to-permanent-income ratios for each educa- 29
30 tion group. Figure 2 shows that with the estimated distributions, the model quite 30
31

32 ²³See the bottom row of Figure 8 in Elsby and Hobijn (2010) for these results. 32

1 TABLE 3. Calibrated Model Parameters — Recession
 2 Panel A: Parameters that apply to all types

3 Parameter	4 Notation	5 Value
4 Avg. duration of unemp. spell in a recession (quarters)		4
5 Prob. of leaving unemployment in a recession	π_{ue}	0.25
8 Panel B: Parameters calibrated for each education group		
10		
11 Unemp. rate at the start of a recession (percent)	17.0	8.8
12 Prob. of entering unemployment (π_{eu}^e , percent)	5.1	2.4
14 Panel C: Parameters describing policy experiments		
16 Parameter		16 Value
17 Average length of recession		17 6 quarters
18 Size of stimulus check		18 \$1,200
19 PI threshold for reducing check size		19 \$100,000
20 PI threshold for not receiving check		20 \$150,000
21 Extended unemployment benefits		21 4 quarters
22 Length of payroll tax cut		21 8 quarters
23 Income increase from payroll tax cut		22 2 percent
24 Belief (probability) that tax cut is extended		23 50 percent
24 Note: "PI" refers to Permanent Income		
26		
27		
28		
29		
30		
31 closely matches the distribution of liquid wealth within each education group as		
32 well as for the population as a whole. Thus, our model does not suffer from the		

1 TABLE 4. Estimated discount factor distributions and estimation targets 1

2 Panel A: Estimated discount factor distributions 2

	Dropout	Highschool	College
(β_e, ∇_e)	(0.719, 0.318)	(0.929, 0.072)	(0.983, 0.014)
(Min, max) in approximation	(0.447, 0.991)	(0.868, 0.991)	(0.971, 0.995)

7 Panel B: Estimation targets 7

	Dropout	Highschool	College
Median LW/ quarterly PI (data, percent)	4.64	30.2	112.8
Median LW/ quarterly PI (model, percent)	4.64	32.00	112.81

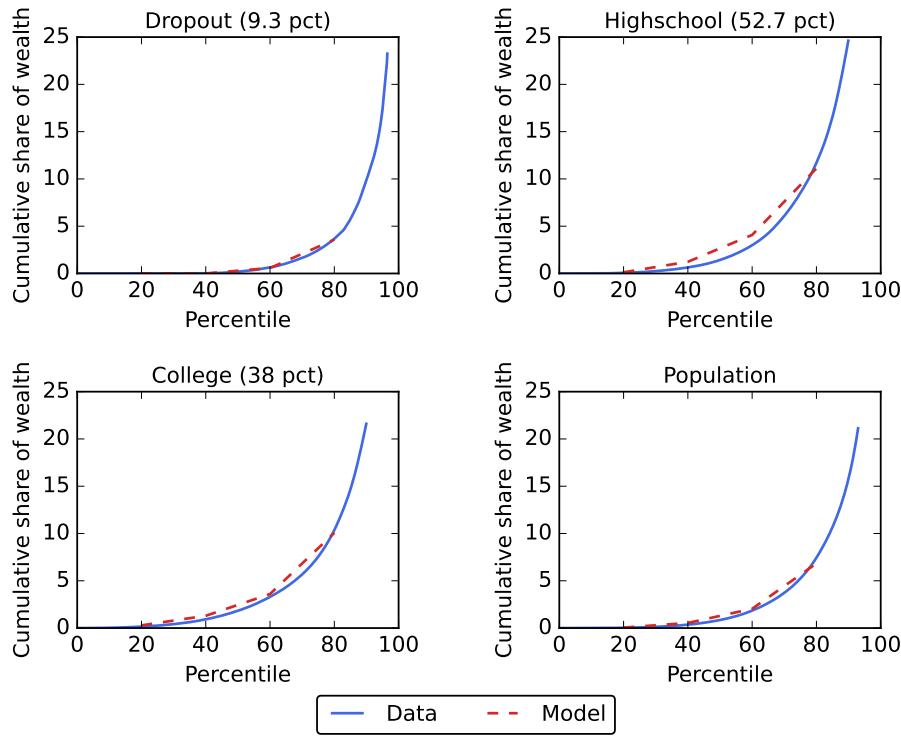
12 Note: Panel (A) shows the estimated parameters of the discount distributions for each education
 13 group. It also shows the minimum and maximum values we use in our discrete approximation to
 14 the uniform distribution of discount factors for each group. Panel (B) shows the weighted median
 15 ratio of liquid wealth to permanent income from the 2004 SCF and in the model. In the annual data
 16 from the SCF, the annual PI is divided by 4 to obtain a quarterly number.

17 “missing middle” problem, identified in [Kaplan and Violante \(2022\)](#), in which the
 18 middle of the wealth distribution has too little wealth.²⁴ 17
 19

20 Note that several of the types in the Dropout group are estimated to have quite
 21 low discount factors (they are very impatient). In this way, the model fits the
 22 feature of the data for the Dropout group that the bottom quintiles accumulate
 23 hardly any liquid wealth. Such low estimates for discount factors are in line with
 24 those obtained in the literature on payday lending.²⁵ 24

25 ²⁴One technical point to note about our estimation, is that we impose the constraint that the
 26 Growth Impatience Condition (GIC), discussed in [Carroll \(2022\)](#), is never violated. (The GIC is re-
 27 quired to prevent the ratio of total wealth to total income of any group from approaching infinity. It
 28 does this by making sure that the growth of wealth of the group is less than or equal to the growth
 29 of income.) The constraint is imposed by calculating an upper bound for the discount factors β^{GIC}
 30 where the GIC holds with equality. The estimation procedure ensures that no type ends up with a
 discount factor higher than this upper bound.

31 ²⁵See, for example, [Skiba and Tobacman \(2008\)](#), who estimate two-week discount rates of 21 per-
 32 cent, and [Allcott et al. \(2021\)](#), who estimate an initial period discount factor between 0.74 and 0.83 in 31
 32

1 FIGURE 2. Wealth distribution fit by education group
2

18 **Note:** This figure validates the discount factor estimation methodology (Section 3.3.3). Separate dis-
 19 count factor distributions $\beta_e \pm \nabla_e$ are estimated for each education group to match the median
 20 liquid-wealth-to-permanent-income ratio and the 20th, 40th, 60th, and 80th percentile points of the
 21 Lorenz curve for liquid wealth. The model successfully avoids the “missing middle” problem identi-
 22 fied by Kaplan and Violante (2022), where insufficient wealth accumulation occurs in the middle of
 23 the distribution. The “Population” panel demonstrates that pooling the three calibrated education
 24 groups produces a realistic aggregate liquid wealth distribution.

25 **3.3.4 Implications for non-targeted moments** Before we move on to compare
 26 different consumption stimulus policies in the calibrated model, we also report
 27 implications of the model for some non-targeted moments. Panel A of table 5
 28 shows the wealth distribution across the three education groups in the data and

29 a model where a period is eight weeks long. Both of these papers use quasi-hyperbolic preferences, so
 30 the estimates are not directly comparable with parameters in our model. Nevertheless, they support
 31 the point that high discount rates are necessary to model the part of the population that takes out
 32 payday loans at very high interest rates.

1 in the model. The model matches these shares quite closely, which may not be 1
2 surprising given that we calibrate the size of each group and we manage to fit the 2
3 wealth distribution within each group separately. The panel also reports the aver- 3
4 age marginal propensity to consume for the different groups. To be comparable 4
5 to numbers reported in Fagereng et al. (2021), these are calculated as the average 5
6 MPC in the year of a lottery win. Lottery wins occur in a random quarter of the 6
7 year that differs across individuals. The MPC for an individual depends on the 7
8 spending pattern after the win, and these are averaged across individuals within 8
9 each education group. 9

10 Panel B of table 5 shows similar numbers to Panel A, sorted by quartiles of 10
11 the liquid wealth distribution instead of education groups. Our model yields a 11
12 slightly more concentrated liquid wealth distribution than in the data. However, 12
13 it does produce a fairly high MPC even for households in the highest quartile of 13
14 the liquid wealth distribution. This is consistent with the results found in the Nor- 14
15wegian data by Fagereng et al. (2021), but also with recent results in Graham and 15
16 McDowell (2024). In an administrative dataset from a large US financial institu- 16
17 tion, they find that the spending response to an income receipt is large across the 17
18 distribution of liquid asset holdings. In our model, we obtain this result due to 18
19 the inclusion of the splurge factor. As shown in Appendix B, the model is not able 19
20 to generate a high MPC for the highest wealth quartile without splurge consump- 20
21 tion. 21

22 Finally, we consider the implications of our model for two different patterns of 22
23 spending over time. The first pattern is the dynamics of spending after a lottery 23
24 win from Fagereng et al.. This pattern was used in the estimation of the splurge 24
25 factor in section 3.1, but was not targeted when estimating the discount factor 25
26 distributions for each education group in section 3.3.3. Figure 3a shows that the 26
27 model that is estimated taking the value of the splurge as given, results in a dis- 27
28 tribution of spending over time that is very similar to the one found in the Nor- 28
29wegian data. 29

30 The second pattern concerns the dynamics of income and spending for house- 30
31 holds that become unemployed and remain unemployed long enough for unem- 31
32 ployment benefits to expire. Figure 3b shows the pattern of income and spend- 32

1 TABLE 5. Model fit with respect to non-targeted moments
23 Panel A: Non-targeted moments by education group
4

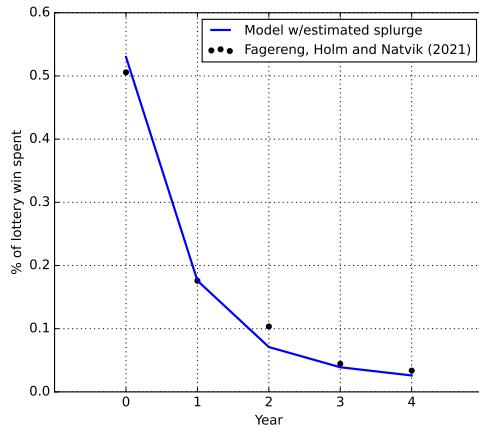
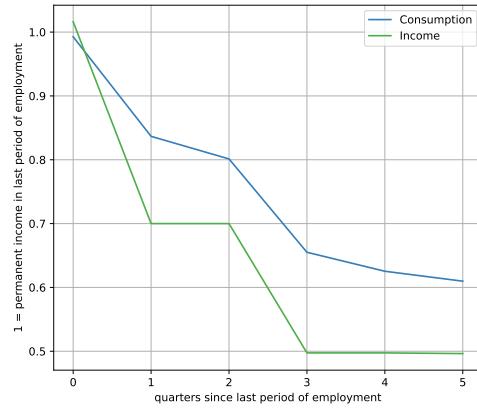
	Dropout	Highschool	College	Population
Percent of liquid wealth (data)	0.8	17.9	81.2	100
Percent of liquid wealth (model)	1.2	17.5	81.3	100
Avg. lottery-win-year MPC	0.78	0.59	0.38	0.53

8 Panel B: Non-targeted moments by wealth quartile
9

	WQ 4	WQ 3	WQ 2	WQ 1
Percent of liquid wealth (data)	0.14	1.60	8.51	89.76
Percent of liquid wealth (model)	0.12	1.01	3.90	94.96
Avg. lottery-win-year MPC	0.32	0.47	0.60	0.73

14 **Note:** Percent of liquid wealth held by each group in the 2004 SCF and in the model, and average
 15 MPCs after a lottery win for each group. MPCs are calculated for each individual for the year of a
 16 lottery win, taking into account that the win takes place in a random quarter of the year that differs
 17 across individuals.

18
19
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21
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28
29 ing for such households. [Ganong and Noel \(2019\)](#) report the empirical result that
 30 nondurable spending drops by 12 percent the month when benefits expire. Our
 31 quarterly model is broadly consistent with this as the drop in spending the quar-
 32 ter after the expiry of UI benefits is 18 percent.
32

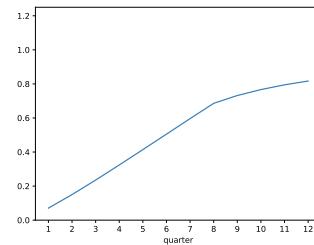
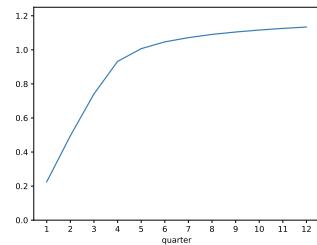
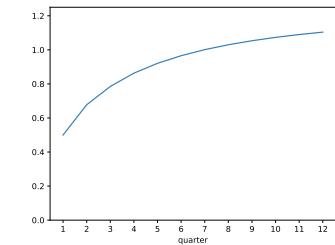
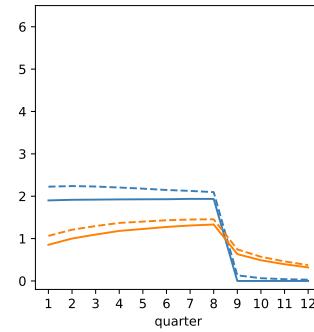
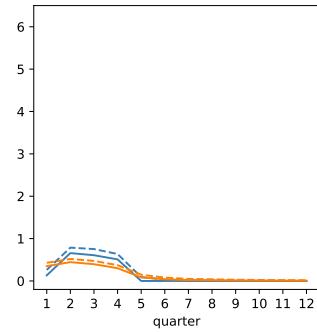
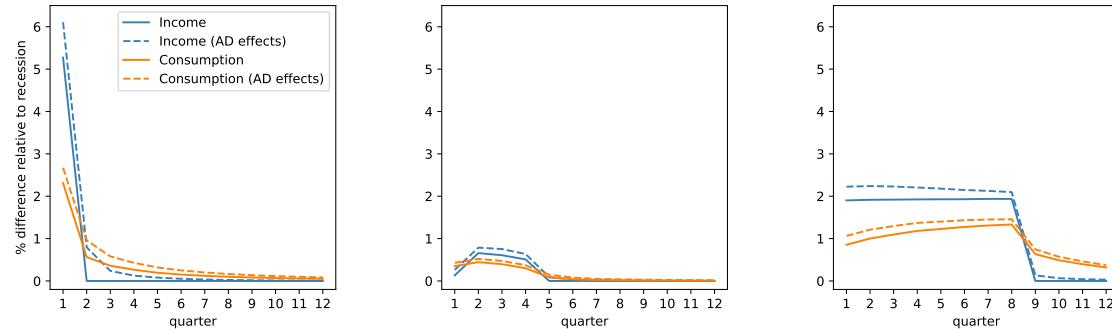
1 FIGURE 3. Model validation for non-targeted spending patterns
211 (a) Dynamic spending after lottery win
1213 (b) Spending upon UI benefit expiry
14

15 **Note:** This figure demonstrates model performance on non-targeted validation moments (Section
16 3.3.4). Subfigure (a) shows the model's dynamic consumption response compared to Fagereng
17 et al. (2021) estimates using the discount factor distributions estimated separately for each education
18 group. Subfigure (b) validates the model against Ganong and Noel (2019), who find that nondurable
19 spending drops by 12% the month when UI benefits expire; our quarterly model predicts an 18% drop
the quarter after benefit expiry, demonstrating broad consistency with this empirical pattern.

21 **4. COMPARING FISCAL STIMULUS POLICIES**
22

23 In this section, we present our results where we compare three policies to provide
24 fiscal stimulus in our calibrated model. The policies we compare are a means-
25 tested stimulus check, an extension of unemployment benefits, and a payroll tax
26 cut. Each policy is implemented at the start of a recession, and we compare re-
27 sults both with and without aggregate demand effects being active during the re-
28 cession. First, we present impulse responses of aggregate income and consump-
29 tion after the implementation of each policy. Then we compare the policies in
30 terms of their cumulative multipliers and in terms of their effect on a welfare
31 measure that we introduce. Finally, based on these comparisons, we can rank the
32 three policies.

1	4.1 Impulse responses	1
2		2
3		3
4	The impulse responses that we present for each stimulus policy are constructed	4
5	as follows:	5
6	• A recession hits in quarter one.	6
7	• We compute the subsequent path for the economy without any policy intro-	7
8	duced in response to the recession.	8
9	• We also compute the subsequent path for the economy with a given policy	9
10	introduced at the onset of the recession in quarter one.	10
11	• The impulse responses we present are then the <i>difference</i> between these two	11
12	paths for the economy and show the effect of a policy relative to a case where	12
13	no policy was implemented.	13
14	• The solid lines show these impulse responses for an economy where the ag-	14
15	gregate demand effects described in section 2.3 are not active, and the dashed	15
16	lines show impulse responses for an economy where the aggregate demand	16
17	effects are active during the recession.	17
18	• Red lines refer to aggregate labor and transfer income, and blue lines refer to	18
19	consumption.	19
20		20
21	All graphs show the average response of income and consumption (averaged	21
22	over recessions of different lengths). Specifically, we simulate recessions lasting	22
23	from only one quarter up to 20 quarters. We then take the sum of the results	23
24	across all recession lengths weighted by the probability of this recession length	24
25	occurring (given our assumption of an average recession length of six quarters).	25
26		26
27		27
28		28
29		29
30		30
31	4.1.1 Stimulus check Figure 4a shows the impulse response of income and con-	31
32	sumption when stimulus checks are issued in the first quarter of a recession.	32

1 FIGURE 4. Policy effectiveness during recessions with aggregate demand effects
2

Note: This figure compares policy effectiveness during recessions (Section 2.2). Recession periods are characterized by higher unemployment rates and increased economic uncertainty. The model demonstrates that UI extensions become particularly effective during recessions due to better targeting of high-MPC households. Stimulus checks maintain effectiveness but with diminished relative performance compared to UI extensions. Payroll tax cuts show the least effectiveness across all economic conditions, confirming the robustness of the main policy rankings.

In the model without a multiplier, the stimulus checks account for 5 percent of the first quarter's income. In the following quarters, there are no further stimulus payments, and income remains the same as it would have been without the stimulus check policy. Consumption is about 2.5 percent higher in the first quarter, which includes the splurge response to the stimulus check. Consumption then drops to less than 1 percent above the counterfactual, and the remainder of the stimulus check money is then spent over the next few years. In the model with

1 aggregate demand effects, income in the first quarter is 6 percent higher than the 1
 2 counterfactual, as the extra spending feeds into higher incomes. Consumption 2
 3 in this model jumps to a higher level than without aggregate demand effects and 3
 4 comes down more slowly as the feedback effects from consumption to income 4
 5 dampen the speed with which income—and hence the splurge—return to zero. 5
 6 After a couple of years, when the recession is most likely over and aggregate de- 6
 7 mand effects are no longer in place, income is close to where it would be without 7
 8 the stimulus check policy, although consumption remains somewhat elevated. 8

9 4.1.2 *UI extension* The impulse responses in Figure 4b show the response to a 9
 10 policy that extends unemployment benefits from 6 months to 12 months for a 10
 11 period of a year. In the model without aggregate demand effects, the path for in- 11
 12 come now depends on the number of consumers who receive the extended un- 12
 13 employment benefits. These consumers are those who have been unemployed 13
 14 for between 6 and 12 months. In the first quarter of the recession, the newly 14
 15 unemployed receive unemployment benefits regardless of whether they are ex- 15
 16 tended or not. Therefore, it is in the second and third quarters, when the effects 16
 17 of the recession on long-term unemployment start to materialize, that the ex- 17
 18 tended UI payments ramp up, amounting to an aggregate increase in quarterly 18
 19 income by 0.7 percent. By the fifth quarter, the policy is no longer in effect, and 19
 20 income from extended unemployment goes to zero. Consumption in the first 20
 21 quarter jumps by more than income (by 0.3 percent), prompted by both the in- 21
 22 crease in expected income and the reduced need for precautionary saving given 22
 23 the extended insurance. In the model without aggregate demand effects, con- 23
 24 sumption is only a little above the counterfactual by the time the policy is over. 24
 25 In the model with aggregate demand effects, there is an extra boost to income 25
 26 of about the same size in the first and second quarters. As this extra aggregate 26
 27 demand induced income goes to employed consumers, more of it is saved, and 27
 28 consumption remains elevated several quarters beyond the end of the policy. 28

29 4.1.3 *Payroll tax cut* The final impulse response graph, Figure 4c, shows the im- 29
 30 pulse response for a payroll tax cut that persists for two years (eight quarters). In 30
 31 the model without aggregate demand effects, income rises by close to 2 percent 31
 32

1 as the take-home pay for employed consumers goes up. After the two-year pe- 1
 2 riod, income drops back to where it would have been without the payroll tax cut. 2
 3 Consumption jumps close to 1 percent in response to the tax cut. Over the pe- 3
 4 riod in which the tax cut is in effect, consumption rises somewhat as the stock 4
 5 of precautionary savings goes up. Following the drop in income, consumption 5
 6 drops sharply because of the splurge and then decreases over time as consumers 6
 7 spend out the savings they built up over the period the tax cut was in effect. In the 7
 8 model with aggregate demand effects, income rises by about 2.3 percent above 8
 9 the counterfactual and then declines steadily as the probability that the recession 9
 10 remains active—and hence the aggregate demand effects in place—goes down 10
 11 over time. Following the end of the policy, the savings stock in the model with ag- 11
 12 gregate demand effects is high, and consumption remains significantly elevated 12
 13 through the period shown. 13

14

15 4.2 Multipliers

16 In this section, we compare the fiscal multipliers across the three stimulus poli- 16
 17 cies. Specifically, we employ the cumulative multiplier, which captures the ratio 17
 18 between the net present value (NPV) of stimulated consumption up to horizon t 18
 19 and the full-horizon NPV of the cost of the policy. We thus define the cumulative 19
 20 multiplier up to horizon t as 20
 21

$$22 M(t) = \frac{NPV(t, \Delta C)}{NPV(\infty, \Delta G)}, \quad (9)$$

23 where ΔC is the additional aggregate consumption spending up to time t in the 23
 24 policy scenario relative to the baseline and ΔG is the total government expen- 24
 25 diture caused by the policy. The NPV of a variable X_t is given by $NPV(t, X) = 25$
 26 $\sum_{s=0}^t \left(\prod_{i=1}^s \frac{1}{R_i} \right) X_s$. 26
 27

28 The multiplier hence captures the amount of induced consumption at differ- 28
 29 ent horizons relative to the total (i.e. full-horizon) cost of the policies.²⁶ 29
 30

31 ²⁶In the case that there is no aggregate demand effect, these multipliers converge to 1 as t goes to 31
 32 infinity. 32

1 The second row in Figure 4 plots the cumulative multipliers at different hori- 1
 2 zons, and table 6 shows the 10y-horizon multiplier for each policy. The stimulus 2
 3 check, which is paid out in quarter one, exhibits the largest multiplier on impact. 3
 4 About 50 percent of the total policy expenditure is immediately spent by con- 4
 5 sumers. After two years, and because of the aggregate demand effects, consump- 5
 6 tion has increased cumulatively by more than the cost of the stimulus check. Over 6
 7 time, the policy reaches a total multiplier of 1.234. Without AD effects the policy 7
 8 only generates a multiplier of 0.879. The last two rows in table 6 show the ex- 8
 9 pected share of the policy expenditures and stimulated consumption that occurs 9
 10 during a recession. For the stimulus check all of the policy expenditures occur 10
 11 in the first quarter and thus with certainty during the recession. However, since 11
 12 induced consumption also takes place during later periods at which time the re- 12
 13 cession may have already ended, the share of stimulated consumption during the 13
 14 recession is lower at 74.2 percent. 14

15 Since spending for the UI policy is spread out over four quarters (and peaks 15
 16 in quarters two to three), the multiplier in the first quarter is considerably lower 16
 17 than in the case of the stimulus check. However, the UI extension policy is tar- 17
 18 geted in the sense that it provides additional income only to those consumers 18
 19 who have large MPCs, because of unemployment. Also, over the medium-term 19
 20 UI extension expenditures are more likely to induce consumption spending dur- 20
 21 ing the recession compared to the check stimulus, see the last row in table 6. This 21
 22 is because UI extension expenditures affect agents who spend the additional in- 22
 23 come relatively quickly once it reaches them. Therefore, the cumulative muliti- 23
 24 plier of the UI extension exceeds that of the stimulus check after about one year. 24

25 The payroll tax cut has the lowest multiplier irrespective of the considered hori- 25
 26 zon. A multiplier of close to 1 is reached only after 10 years with AD effects. These 26
 27 relatively small numbers reflect that policy spending lasts for a long time and is 27
 28 thus more likely to occur after the recession has ended. Moreover, only employed 28
 29 consumers, often with relatively low MPCs, benefit directly from the payroll tax 29
 30 cut. Therefore, the policy is poorly targeted if the goal is to provide short-term 30
 31 stimulus. 31

32 32

1 TABLE 6. Comparing fiscal stimulus policy effectiveness
2

		Stimulus check	UI extension	Tax cut	
3	10y-horizon Multiplier (no AD effect)	0.878	0.906	0.846	3
4	10y-horizon Multiplier (AD effect)	1.228	1.209	0.975	4
5	10y-horizon (1st round AD effect only)	1.153	1.147	0.949	5
6	Share of policy expenditure during recession	100.0%	79.6%	57.8 %	6
7	Share of policy cons. stimulus during recession	73.6%	81.1%	41.8 %	7

8 Note: Policies are implemented during a recession with or without the aggregate demand effect active.
 9 Multipliers show cumulative consumption response over 10 years relative to total policy cost. Share
 10 percentages indicate the proportion of policy expenditure and induced consumption stimulus occur-
 11 ring during the recession period. The row “1st round AD effect only” captures the direct consump-
 12 tion impact of the policies and the additional boost to consumption resulting from the aggregate demand
 13 effects materializing on aggregate demand effects acting on indirectly stimulated consumption.

14
 15
 16
 17
 18 Table 6 contains an additional (middle) row with results for an economy where
 19 we only consider a “first-round” aggregate demand effect. To understand these
 20 values note that the policies initially increase the income of consumers directly,
 21 which leads to a boost in consumption. As a consequence, this boost triggers an
 22 aggregate demand effect which increases the income of everyone and in turn
 23 leads to an additional boost to consumption. We refer to the sum of this initial
 24 and the indirect boost to consumption as the first-round AD effect. However, the
 25 AD effect continues as the indirect boost to consumption triggers another round
 26 of income increases which further boost consumption and so on. One might ar-
 27 gue that these higher-order rounds of the AD effect are not likely to be anticipated
 28 by consumers. Since higher-order consumption boosts only materialize if con-
 29 sumers anticipate them and act accordingly, the overall increase in consumption
 30 might turn out to be smaller than suggested by the full AD effect. As shown in the
 31 middle row of the table, the multipliers are smaller when excluding higher-order
 32 rounds. Nevertheless, the ranking of the policies remains unchanged.

4.3 Welfare

In this section, we look at the welfare implications of each stimulus policy. To do so, we need a way to aggregate welfare in our model with individual utility functions. In our model, some households consume much less than other households, and a social planner with equal weights on each household could substantially increase welfare through redistribution across households even in normal times. We are interested in the benefit of carrying out fiscal policies in a recession, so we do not want our results to reflect the benefits of redistribution inherent in our model in normal times.

Our welfare measure weights the felicity of a household at time t by the inverse of the marginal utility of the same household in a counterfactual simulation in which neither the recession occurred nor the fiscal policy was implemented, discounted by the real interest rate.²⁷ This weighting scheme means that in normal times the marginal benefit or cost to a social planner of moving a dollar of consumption from one household at one time period to another household at the same or a different time period is zero. Hence, in normal times, any redistributive policy has zero marginal benefit. However, in a recession when the average marginal utility is higher than in normal times, there can be welfare benefits to government borrowing to allow households to consume more during the recession.

As with all social welfare measures, ours is not without ethical issues. We have chosen our welfare measure over one with equal weights because an equal-weights measure would be increasing with the size of any redistributive policy.²⁸ However, similar to Negishi weights, our welfare measure gives greater weight to

²⁷Discounting at the real interest rate accounts for the fact that a redistributive policy over time will require borrowing or lending at the real interest rate. The preference discount factors of households would appear in both the numerator and the denominator—the utility and marginal utility—and therefore cancel and do not play a role in our welfare measure.

²⁸Using a version of an equal-weights measure results in an even greater welfare benefit to extended unemployment insurance—see the previously distributed draft of this paper, Carroll et al. (2023). However, because the size of the extended unemployment benefits policy is much larger in a recession compared to normal times, while the size of the other two policies does not change signif-

1 households that are well off.²⁹ Furthermore, our welfare measure distinguishes 1
 2 between households that would have suffered unemployment in normal times 2
 3 and households that are made unemployed as a result of the recession—giving 3
 4 the latter a higher weight in the social welfare function. 4

5 Let $c_{it,normal}$ be the consumption—inclusive of the splurge—of household i 5
 6 at time t in the baseline simulation with no recession and no fiscal policy. The 6
 7 (undiscounted) marginal utility of an extra unit of consumption for this house- 7
 8 hold in this time period is $u'(c_{it,normal})$. 8

9 Let $c_{it,policy,Rec,AD}$ be the consumption of the same household under the fis- 9
 10 cal policy, $policy$, possibly a recession, $Rec \in \{0, 1\}$, and in an economy with or 10
 11 without aggregate demand effects, $AD \in \{0, 1\}$.³⁰ 11

12 We also denote the net present value of the government expenditures of the 12
 13 policy as $NPV(policy, Rec, AD)$. With this notation, we can now define the wel- 13
 14 fare bang for the buck of a policy as: 14

$$15 \\ 16 \quad \mathcal{W}(policy, Rec, AD) = \frac{\sum_{i=1}^N \sum_{t=0}^{\infty} \frac{1}{R^t} \frac{u(c_{it,policy,Rec,AD}) - u(c_{it,none,Rec,AD})}{u'(c_{it,normal})}}{NPV(policy, Rec, AD)}. \quad (10) \\ 17 \\ 18 \\ 19$$

20 In normal times, this welfare measure will be exactly equal to one for any 20
 21 small-scale fiscal expansion. To see this, note that the numerator, $u(c_{it,policy,0,0}) -$ 21
 22 $u(c_{it,none,0,0})$, is equal to the change in consumption multiplied by the marginal 22

23 significantly in a recession, this equal-weights measure almost mechanically favored the extended unem- 23
 24 ployment benefits policy. 24

25 Negishi weights have been used in the climate literature as a way to separate the welfare benefits 25
 26 of climate mitigation policies from broader questions about global income redistribution. Our prob- 26
 27 lem of separating the welfare benefits of recession mitigation policies from income redistribution in 27
 28 normal times is similar, but complicated by our incomplete markets setup. With complete markets, 28
 29 under which there is no potential benefit to redistributing consumption across time for any individ- 29
 30 ual household, our measure is identical to Negishi weights. 30

31 In the simulations, household i experiences the same permanent and transitory shock sequence, 30
 32 but in the recession simulation some households experience unemployment during periods in which 31
 32 the same household is employed in the baseline simulation. 32

1 TABLE 7. Welfare effectiveness: policy “bang for the buck” comparison
2

	Stimulus check	UI extension	Tax cut
$\mathcal{W}(\text{policy}, \text{Rec} = 0, \text{AD} = 0)$	0.96	0.85	0.99
$\mathcal{W}(\text{policy}, \text{Rec} = 1, \text{AD} = 0)$	1.00	1.82	0.98
$\mathcal{W}(\text{policy}, \text{Rec} = 1, \text{AD} = 1)$	1.35	2.13	1.11

6 Note: Welfare “bang for the buck” measures for each policy as defined by equation (10). Values near
 7 1.0 in normal times ($\text{Rec}=0$) are expected by definition for marginal policies. In recession scenarios,
 8 UI extension emerges as the clear winner with dramatically higher welfare effectiveness (1.83 without
 9 aggregate demand effects, 2.15 with), reflecting its superior targeting to high-MPC, high-marginal-
 10 utility households. $\text{Rec}=0$ indicates normal times, $\text{Rec}=1$ indicates recession. $\text{AD}=0$ and $\text{AD}=1$ indi-
 11 cate whether aggregate demand effects are inactive or active, respectively.

12 utility in normal times. As the total change in consumption is equal to the net
 13 present value of the policy, which we divide by, the total welfare measure is equal
 14 to one. Note that for large increases in consumption, this measure may be less
 15 than one because the utility function is concave.

17 Table 7 shows the welfare measure for each policy as defined by equation (10).
 18 The top row of the table shows the welfare measure for implementing each policy
 19 in normal times. For marginal policies, this is equal to one by definition. Indeed,
 20 the value for both the stimulus check and the tax cut policy is very close to one.
 21 However, the welfare measure for the extended unemployment policy in normal
 22 times is noticeably less than one. This is because, although this policy is smaller
 23 in absolute size than the other policies, its consumption effects are concentrated
 24 on a small number of households that remain unemployed long enough to re-
 25 ceive the extended benefits. For these households, the effect on consumption is
 26 large enough such that the non linearity of the consumption function leads to
 27 smaller welfare benefit than the marginal utility of consumption would other-
 28 wise imply.

29 The second row of table 7 shows the welfare benefit of each policy in a reces-
 30 sion without any aggregate demand effects. Again, the stimulus check and tax
 31 cut policies have measures that are close to one—pulling forward consumption
 32 has little welfare benefit for the average household because the average marginal

1 utility of consumption is only a little higher than in normal times. By contrast, 1
2 the policy sees benefits of 1.8 dollars for every dollar spent on extended UI ben- 2
3 efits during a recession. This is because many of the households who are unem- 3
4 ployed for many quarters in the recession would have never been unemployed, 4
5 or quickly reemployed, in normal times and hence their marginal utility of con- 5
6 sumption is much higher in the recession than in normal times. 6

7 The third row of the table shows the welfare measure for each policy in a reces- 7
8 sion in the version of the model with aggregate demand effects during the reces- 8
9 sion. The payroll tax cut now has a noticeable benefit, as some of the tax cut gets 9
10 spent during the recession, resulting in higher incomes for all consumers. How- 10
11 ever, the tax cut is received over a period of two years, and much of the relief may 11
12 be after the recession—and hence the aggregate demand effect—is over. Further- 12
13 more, because the payroll tax cut goes only to employed consumers who have 13
14 lower MPCs than the unemployed, the spending out of this stimulus will be fur- 14
15 ther delayed, possibly beyond the period of the recession. By contrast, the stimu- 15
16 lus check is received in the first period of the recession and goes to both employed 16
17 and unemployed consumers. The earlier arrival and higher MPCs of the stimulus 17
18 check recipients mean more of the stimulus is spent during the recession, lead- 18
19 ing to greater aggregate demand effects, higher income, and higher welfare. The 19
20 extended UI arrives, on average, slightly later than the stimulus check. However, 20
21 the recipients, who have been unemployed for at least six months, spend most of 21
22 the extra benefits within 1-2 quarters, resulting in substantial aggregate demand 22
23 effects during the recession. In contrast to the payroll tax cut, extended UI has 23
24 the benefit of automatically reducing if the recession ends early, making fewer 24
25 consumers eligible for the benefit. 25

26 26

27 4.4 Comparing the policies 27

28 The results presented in sections 4.2 and 4.3 indicate that the extension of un- 29
employment benefits is the clear “bang for the buck” winner. The extended UI 30
payments are well targeted to consumers with high MPCs and high marginal 31
utility, giving rise to large multipliers and welfare improvements. The stimulus 32

1 checks come in slightly higher when measured by their short-term multiplier ef- 1
 2 fect but are a distant second when measured by their welfare effects. The stim- 2
 3 ulus checks have large initial multipliers because the money gets to consumers 3
 4 at the beginning of the recession and therefore induce aggregate demand effects 4
 5 more quickly. However, the checks are not well targeted to high-MPC consumers, 5
 6 so even though the funds arrive early in the recession, they are spent out more 6
 7 slowly than the extended unemployment benefits.³¹ Furthermore, the average 7
 8 recipient of a stimulus check has a much lower marginal utility than consumers 8
 9 receiving unemployment benefits, so the welfare benefits of this policy are sub- 9
 10 stantially muted relative to UI extensions. 10

11 The payroll tax cut policy does poorly by both measures: It has a low overall 11
 12 multiplier and negligible welfare benefits. The reasons are that the funds are slow 12
 13 to arrive, so the subsequent spending often occurs after the end of the recession, 13
 14 and that the payments are particularly badly targeted—they go only to employed 14
 15 consumers. 15

16 While it is clear from the analysis that the extended unemployment benefits 16
 17 should be the first tool to use, a disadvantage of them is that they are limited 17
 18 in their size. If a larger fiscal stimulus is deemed appropriate, stimulus checks 18
 19 provide an alternative option that will stimulate spending during the recession 19
 20 even if the welfare benefits are lower than the UI extension. 20

21 21

22 4.5 *Results in a model without the splurge* 22

23 We introduce the splurge in our model with the aim of matching empirical evi- 23
 24 dence on the dynamics of spending in response to transitory income shocks. The 24
 25 splurge acts as a stand-in for competing theories for why agents may spend more 25
 26 out of those shocks than suggested by a simple model in which forward-looking 26
 27 agents solely maximize utility. However, it is natural to consider to what extent 27
 28 the splurge is in fact necessary to match the empirical patterns and the impli- 28
 29 29

30 ³¹Theoretically, stimulus checks could be targeted to the highest-MPC households which, for small- 30
 31 sized policies, would mean households with an MPC of one. However, data limitations and other 31
 32 practicalities make means-testing stimulus checks by income the extent of targeting in practice. 32

1 cations for our results ranking the different policies. To assess this we reestimate 1
2 the model without the splurge and recompute all our results regarding the rela- 2
3 tive effectiveness of the policies in this version of the model. 3

4 The details of this exercise are in Appendix B. There we discuss how the es- 4
5 timation of the Norwegian model in section 3.1 is affected if we do not include 5
6 splurge consumption, and the estimation of the discount factor distributions for 6
7 each education group in the US economy without taking the splurge as given. The 7
8 general result is that the we can match the liquid wealth distributions that we tar- 8
9 get also in models that do not include a splurge. The models do so by estimating 9
10 wider distributions of discount factors than we found in section 3.1 and 3.3.3. 10

11 Without the splurge the models do struggle to exactly match the dynamics of 11
12 spending after a temporary income shock, however. In particular, for the esti- 12
13 mation of the Norwegian model, we can compare the model's implications for 13
14 MPCs for different wealth quartiles to empirical estimates. Without the splurge, 14
15 the model leads to an MPC for the top wealth quartile that is far lower than in the 15
16 data. In the US model this MPC is also markedly lower compared to the model 16
17 with splurge consumption, but for the US we do not have an empirical estimate 17
18 to compare to. 18

19 To evaluate the impact of splurge consumption on our ranking of the policies, 19
20 we simulate the three fiscal policies in the reestimated model without the splurge. 20
21 There are only minor shifts in the multipliers of the policies, but the lower average 21
22 MPCs reduces multipliers for the check and tax cut policy relative to the model 22
23 with the splurge. In contrast, the UI extension becomes slightly more effective in 23
24 stimulating consumption as the wider distribution of discount factors implies a 24
25 larger share of the population that hits the borrowing constraint upon expiry of 25
26 UI benefits. Hence, the extension of UI benefits affects agents more strongly in 26
27 the model without the splurge. 27

28 More importantly for the main conclusion of our paper, table 8 compares the 28
29 welfare implications of the policies in the two models. Generally, the welfare met- 29
30 ric varies only marginally across the models. When aggregate demand effects are 30
31 active, we see slightly larger differences in the welfare evaluation, with the check 31
32 policy losing ground against the UI extension. This is because the welfare im-

1 TABLE 8. Welfare for policies both out of and in a recession, with/without AD effects 1

		Stimulus check	UI extension	Tax cut
3	$\mathcal{W}(\text{policy}, Rec = 0, AD = 0)$	0.97(0.96)	0.84(0.85)	0.99(0.99)
4	$\mathcal{W}(\text{policy}, Rec = 1, AD = 0)$	1.00(1.00)	1.80(1.82)	0.97(0.98)
5	$\mathcal{W}(\text{policy}, Rec = 1, AD = 1)$	1.27(1.35)	2.12(2.13)	1.09(1.11)

6 Note: The values outside of the brackets capture the welfare in the model without the splurge, while
 7 those inside the brackets are welfare with the splurge. $Rec=0$ indicates normal times, $Rec=1$ indicates
 8 recession. $AD=0/1$ indicates aggregate demand effects inactive/active.

9
 10 pact of the check in the model with the splurge is contingent on the checks be- 10
 11 ing spent quickly due to a high average MPC and thus generating strong aggre- 11
 12 gate demand effects while the recession is still ongoing. In the absence of the 12
 13 splurge only liquidity-constrained agents spend the check money quickly, such 13
 14 that recession-induced aggregate demand effects are smaller. 14

15 Overall, we can conclude that the ranking of the policies remains unaffected by 15
 16 the splurge. The splurge is thus helpful in matching available empirical evidence, 16
 17 but does not affect the assessment of the effectiveness of the considered policies. 17

19 5. ROBUSTNESS IN A HANK AND SAM MODEL 19

20
 21 The main results of this paper are presented in a partial equilibrium setup with 21
 22 aggregate demand effects that do not arise from general equilibrium effects. We 22
 23 think there are many advantages to studying the welfare and multiplier effects in 23
 24 this setting without embedding the model in general equilibrium. First, general 24
 25 equilibrium models often struggle to adequately capture the feedback mecha- 25
 26 nisms between consumption and income, particularly the asymmetric nature of 26
 27 these relationships during recessionary versus expansionary periods. Addition- 27
 28 ally, a complete general equilibrium treatment would necessitate the analysis 28
 29 of numerous complex channels including investment dynamics, firm ownership 29
 30 structures and dividend distribution policies, inventory management, and inter- 30
 31 national trade flows—elements that, while important in their own right, would 31
 32 potentially obscure the core mechanisms we aim to investigate. 32

1 Despite the advantages of our partial equilibrium approach, here we comple- 1
2 ment our analysis with a general equilibrium HANK and SAM model, as standard 2
3 as possible, that is able to capture supply-side effects that are absent from the 3
4 partial equilibrium model. In particular, fiscal policies can generate labor market 4
5 responses that our partial equilibrium analysis does not address. These supply- 5
6 side channels can affect both the welfare implications and the fiscal multipliers of 6
7 different policy interventions. Furthermore, standard to the HANK and SAM lit- 7
erature, the general equilibrium model generates a self-reinforcing precau- 8
9 tionary saving channel that amplifies business cycles. During a recession, height- 9
10 ened unemployment risk prompts households to increase savings and reduce 10
11 consumption which in turn weakens both aggregate and labor demand. The re- 11
12 sulting decline in labor demand further raises unemployment risk, reinforcing 12
13 precautionary savings. 13

14 We embed the consumption choices of our households—with heterogene- 14
15 ity over education type and discount factors—in a New Keynesian model with 15
16 search and matching frictions that closely follows [Du \(2024\)](#), which, in turn, is in 16
17 spirit of the seminal work of [Ravn and Sterk \(2017, 2021\)](#). Aside from the house- 17
18 hold block of the model, the framework is standard and follows from the HANK 18
19 and SAM literature. The model features nominal price rigidities à la Rotemberg, a 19
20 monetary authority that sets the nominal interest rate following a standard Taylor 20
21 rule that responds to inflation, and a fiscal authority that taxes labor income and 21
22 borrows debt from households to fund unemployment insurance and interest on 22
23 past debt. As in [Gornemann et al. \(2021\)](#), [Bardoczy \(2024\)](#), and [Graves \(2024\)](#), 23
24 households randomly search for jobs and match with a labor agency that sells la- 24
25 bor to intermediate good producers. Complete details of the model are provided 25
26 in appendix A. 26

27 The general equilibrium structure generates fiscal multipliers through an 27
28 intertemporal Keynesian cross mechanism, which becomes particularly pro- 28
29 nounced when monetary policy is passive. Moreover, the search and matching 29
30 framework allows the employment rate to respond to policy interventions, al- 30
31 lowing us to capture both demand and supply effects of fiscal policies. 31

32 32

1 Our approach in this section relies on linearizing the macro dynamics of the 1
 2 model and employs the Sequence Space Jacobian methods developed by Auclert 2
 3 et al. (2021). This linearization imposes certain constraints on our analysis. No- 3
 4 tably, we cannot evaluate the effects of different policies starting from a deep re- 4
 5 cessionary state, as we do in our main results.³² This limitation prevents us from 5
 6 conducting welfare comparisons between recessionary periods and the steady 6
 7 state. Additionally, the Keynesian cross mechanism embedded in the model ex- 7
 8 hibits uniform behavior regardless of the degree of economic slack—a feature 8
 9 that stands in contrast to the state-dependent multipliers we apply in our partial 9
 10 equilibrium analysis.³³ 10

11 The consumption response in this general equilibrium model to each of the 11
 12 three policies is shown in the top row of Figure 5. For each of the three fiscal poli- 12
 13 cies, we have shown the consumption response under three different monetary 13
 14 policy rules: 1) an active Taylor rule with a coefficient of 1.5 on inflation; 2) a fixed 14
 15 nominal rate (simulating an effective lower bound); and 3) a fixed real rate (clos- 15
 16 est in spirit to our partial equilibrium analysis). 16

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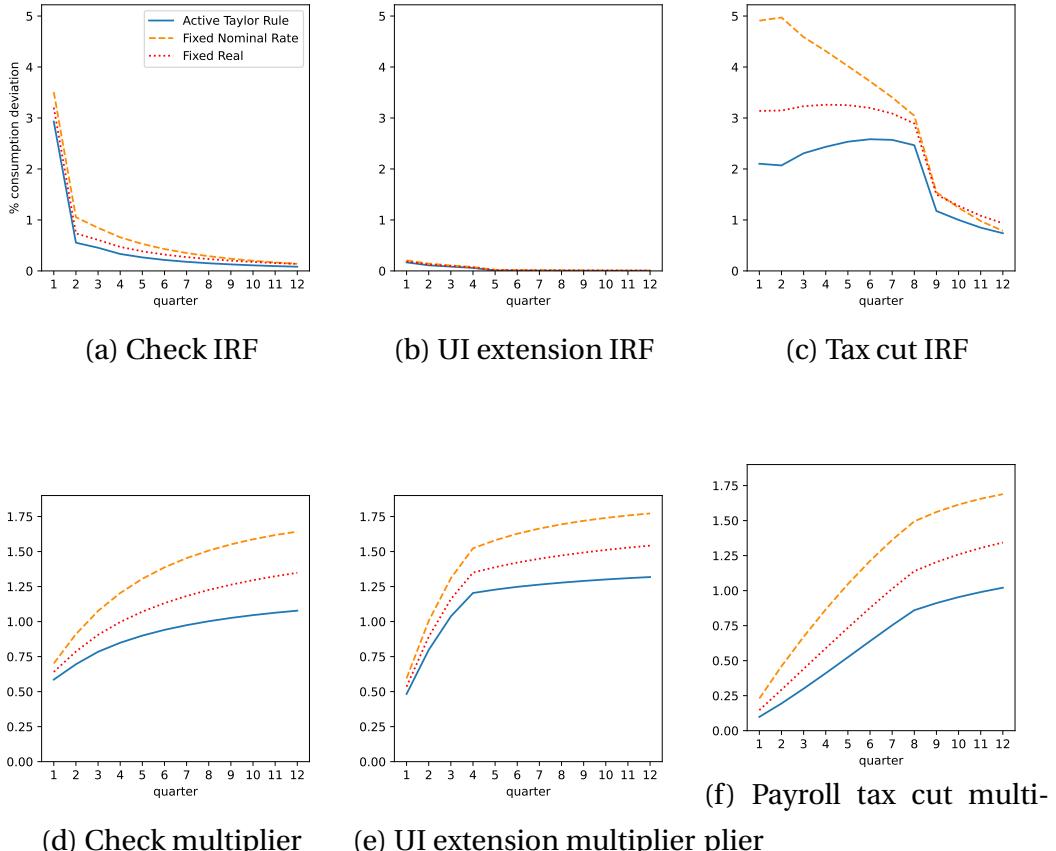
25 25

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27 27

28 ³²One approach to overcome this limitation, which could be used in future work, is described 28
 29 in Boppart et al. (2018). 29

30 ³³We note two additional technical limitations of our general equilibrium implementation. First, 30
 31 stimulus payments in the model are specified as proportional to permanent income, rather than as 31
 32 means-tested fixed dollar amounts as implemented in practice and in our partial equilibrium frame- 32
 work. Second, splurge behavior only occurs out of equilibrium.

1 FIGURE 5. General equilibrium policy comparison in HANK-SAM model
2

Note: This figure presents general equilibrium results from the HANK-SAM model (Section 5). Subfigures (a)-(c) show consumption impulse responses under three monetary policy rules: active Taylor rule, fixed nominal rate (ZLB), and fixed real rate. Subfigures (d)-(f) show corresponding cumulative multipliers over time. The general equilibrium framework generates multipliers through an intertemporal Keynesian cross mechanism, particularly pronounced when monetary policy is passive. Results validate the partial equilibrium findings that UI extensions achieve the highest multipliers across all policy environments.

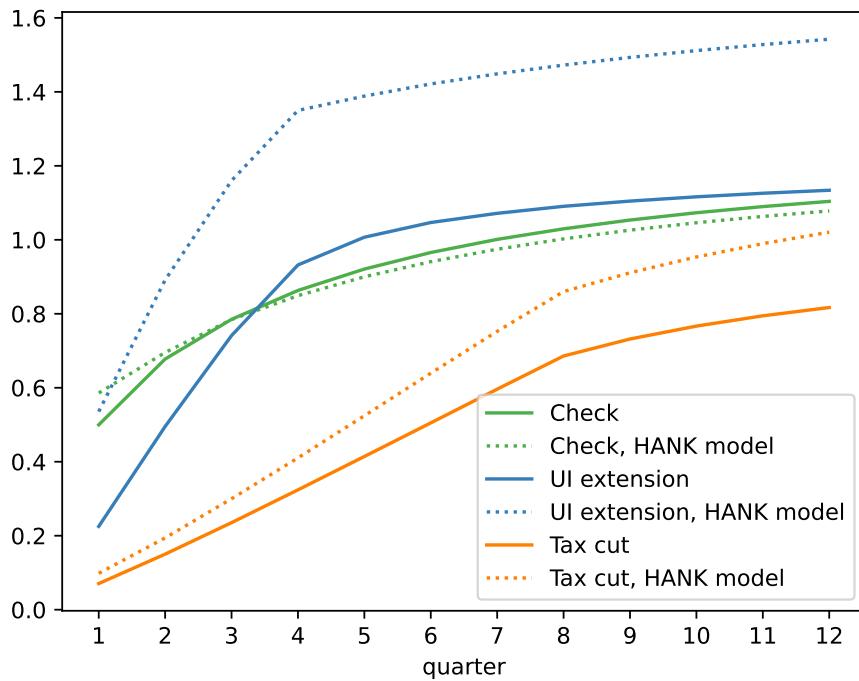
Overall, the IRFs from this model are similar to those from the partial equilibrium analysis, especially under the fixed real-rate rule. Note that the magnitude of the consumption response to the UI extension is lower than in our main analysis—a consequence of lower long-term unemployment in this HANK exer-

1 cise of deviating from the steady state.³⁴ Furthermore, although we are unable 1
 2 to repeat our welfare analysis under a recession in this model, the distributional 2
 3 effects of the policies are similar. Most importantly, the mechanism leading to far 3
 4 greater welfare benefits for the UI extension, namely that the newly unemployed 4
 5 have high marginal utility, are robust to the supply-side effects of a general equi- 5
 6 librium HANK and SAM model. 6

7 The bottom row of Figure 5 shows the corresponding cumulative multipliers 7
 8 for each policy and monetary policy rule. Figure 6 compares these consump- 8
 9 tion multipliers over different horizons under a fixed real rate rule to those in 9
 10 our baseline partial equilibrium model. The multipliers are bigger in the HANK 10
 11 and SAM model. Nevertheless, in both models, the relative ranking of the con- 11
 12 sumption multipliers over time horizons are similar, with the effect of the tax cut 12
 13 substantially smaller than the stimulus check or UI extension policies, despite 13
 14 the inclusion of supply-side effects in this HANK model. However, in contrast to 14
 15 the partial equilibrium model, towards the end of the period shown the tax cut 15
 16 consumption multiplier is near that of the stimulus check. This is because the 16
 17 aggregate demand effects in our partial equilibrium model do not continue be- 17
 18 yond the recession, dampening the benefits of the tax cut policy—in which much 18
 19 of the extra spending occurs after the recession is over—relative to the stimulus 19
 20 check and extended UI policies. 20

21 As discussed in the literature review, Broer et al. (2025) also compute fiscal 21
 22 multipliers for commonly implemented stimulus policies in a HANK and SAM 22
 23 framework. A key distinction is that our model exhibits more spending out of 23
 24 income shocks in the quarters following the quarter of the shock. As shown 24
 25 in Auclert et al. (2018), accounting for the path of iMPCs beyond the first quar- 25
 26 ter significantly amplifies cumulative fiscal multipliers. By capturing this per- 26
 27 27

28
 29 ³⁴By contrast, our main analysis considers deviations from a recessionary scenario. Note that the 29
 30 dynamics of the UI extension IRF are also somewhat faster acting. This is because, under the recession 30
 31 that we study in the partial equilibrium analysis, the large mass of newly-unemployed households do 31
 32 not start receiving extended UI for six months. 32

1 FIGURE 6. Multiplier comparison: partial equilibrium vs. HANK model
2
3

18 Note: This figure compares consumption multipliers across model frameworks (Section 5). The com-
 19 parison shows multipliers over different time horizons under a fixed real rate rule between the base-
 20 line partial equilibrium model (with state-dependent multipliers during recessions) and the general
 21 equilibrium HANK-SAM model (with uniform Keynesian cross mechanism). Both models show the
 22 tax cut policy substantially underperforming relative to stimulus checks and UI extensions, validat-
 23 ing the robustness of policy rankings across modeling approaches. The HANK model produces larger
 24 overall multipliers due to general equilibrium effects.

25 sistence—consistent with microeconomic evidence—our model produces larger
 26 multipliers for the untargeted stimulus check than those in Broer et al. (2025).

27 6. CONCLUSION

28 For many years leading up to the Great Recession, a widely held view among
 29 macroeconomists was that countercyclical policy should be left to central banks,
 30 because fiscal policy responses were unpredictable in their timing, their content,
 31 and their effects. Nevertheless, even during this period, fiscal policy responses to

1 recessions were repeatedly tried, perhaps because the macroeconomists' advice 1
2 to fiscal policymakers — “don't just do something; stand there” — is not politically 2
3 tenable. 3

4 This paper demonstrates that macroeconomic modeling has finally advanced 4
5 to the point where we can make reasonably credible assessments of the effects 5
6 of alternative policies like those that have been tried. The key developments 6
7 have been both (1) the advent of national registry datasets that can measure cru- 7
8 cial microeconomic phenomena, and (2) the creation of tools of heterogeneous 8
9 agent macroeconomic modeling that can match those micro facts and glean their 9
10 macroeconomic implications. 10

11 We examine three fiscal policy experiments that have actually been imple- 11
12 mented in the past: an extension of UI benefits, a stimulus check, and a time- 12
13 limited tax cut on labor income. Our model suggests that the extension of UI 13
14 benefits is a clear “bang for the buck” winner. While the stimulus check arrives 14
15 faster and generates multiplier effects more quickly, it is less well targeted to high- 15
16 MPC households than an extension of UI benefits. By contrast, the welfare gains 16
17 from extended UI benefits are significantly greater than those from a stimulus 17
18 check. The chief drawback of the UI extension is that its size is limited by the fact 18
19 that a relatively small share of the population are unemployed at any given time. 19
20 In contrast, stimulus checks are easily scalable while exhibiting only slightly less 20
21 recession-period stimulus (in a typical recession). However, since some of the 21
22 stimulus checks flow to well-off consumers, such checks do worse than UI ex- 22
23 tensions when we evaluate welfare consequences. Finally, the payroll tax cut is 23
24 the least effective in terms of both the multiplier and welfare effect, since it tar- 24
25 gets only employed consumers and, for a typical recession, more of its payouts 25
26 are likely to occur after the recessionary period (when multipliers may exist) has 26
27 ended. 27

28 The tools we are using could be easily modified to evaluate a number of other 28
29 policies. For example, in the COVID-driven recession, not only was the duration 29
30 of UI benefits extended, but those benefits were also supplemented by substan- 30
31 tial payments to all UI recipients. We did not calibrate the model to match this 31
32 particular policy, but the framework could easily accommodate such an analysis. 32

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64 APPENDICES

1 APPENDICES

2 APPENDIX A: DETAILS OF THE HANK AND SAM MODEL
3

4 A.1 *Households*

5 The household block follows closely to the main text with a few exceptions.
6 First, the splurge only occurs out of equilibrium—that is, the steady state of the
7 model is calculated without the splurge behavior. Second, the level of perma-
8 nent income of all newborns is equal to one. Furthermore, all households face the
9 same employment to unemployment and unemployment to employment prob-
10 abilities. The probabilities are calibrated to the transition probabilities of high
11 school graduates from the main text. Lastly, following the notation of Auclert et al.
12 (2020), r_t^a will denote the economy wide ex-ante real interest rate.
13

14

15 A.2 *Goods Market*

16

A continuum of monopolistically competitive intermediate goods producers, in-
dexed by $j \in [0, 1]$, produces intermediate goods Y_{jt} , which are sold to a final
goods producer at price P_{jt} . Each period, these producers fully consume their
profits.

20

21

22 A.3 *Final Goods Producer*

23

A perfectly competitive final goods producer purchases intermediate goods Y_{jt}
from intermediate good producer j at price P_{jt} and produces the final good Y_t
using a CES production function:

27

28

29 30
$$Y_t = \left(\int_0^1 Y_{jt}^{\frac{\epsilon_p - 1}{\epsilon_p}} dj \right)^{\frac{\epsilon_p}{\epsilon_p - 1}},$$

31

where ϵ_p is the elasticity of substitution.

Given P_{jt} , the price of intermediate good j , the final goods producer maximizes profits by solving:²

$$\max_{Y_{jt}} P_t \left(\int_0^1 Y_{jt}^{\frac{\epsilon_p - 1}{\epsilon_p}} dj \right)^{\frac{\epsilon_p}{\epsilon_p - 1}} - \int_0^1 P_{jt} Y_{jt} dj.$$

The first order condition leads to demand for good j given by

$$Y_{jt} = \left(\frac{P_{jt}}{P_t} \right)^{-\epsilon_p} Y_t,$$

and the price index

$$P_t = \left(\int_0^1 P_{jt}^{1-\epsilon_p} dj \right)^{\frac{1}{1-\epsilon_p}}.$$

A.4 *Intermediate Goods Producers*

Intermediate goods producers produce according to a production function linear in labor L_t :

$$Y_{jt} = Z L_{jt},$$

where Z is total factor productivity.

Each intermediate goods producer hires labor L_t from a labor agency at cost h_t . Given this labor cost, each producer sets P_{jt} to maximize profits while facing price stickiness à la [Rotemberg \(1982\)](#). In HANK models with sticky prices, profits tend to be countercyclical, and when households have high MPCs, this can generate countercyclical consumption responses to dividends. To simplify, we assume that intermediate goods producers fully consume their profits rather than distributing them to households, thereby abstracting from consumption responses to firm profits. Each producer maximizes profits by solving:

$$J_t(P_{jt}) = \max_{\{P_{jt}\}} \left\{ \frac{P_{jt} Y_{jt}}{P_t} - h_t L_{jt} - \frac{\varphi}{2} \left(\frac{P_{jt} - P_{jt-1}}{P_{jt-1}} \right)^2 Y_t + J_{t+1}(P_{jt+1}) \right\},$$

where φ determines the cost of adjusting the price and, hence, the degree of price stickiness.

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The problem can be rewritten as the standard New Keynesian maximization problem:²

$$\max_{\{P_{jt}\}} \mathbb{E}_t \left[\sum_{s=0}^{\infty} M_{t+s}^A \left(\left(\frac{P_{jt+s}}{P_{t+s}} - MC_{t+s} \right) Y_{jt+s} - \frac{\varphi}{2} \left(\frac{P_{jt+s}}{P_{jt+s-1}} - 1 \right)^2 Y_{t+s} \right) \right],$$

where $MC_t = \frac{h_t}{Z}$.⁶

Given that all firms face the same adjustment costs, there exists a symmetric equilibrium where all firms choose the same price with $P_{jt} = P_t$ and $Y_{jt} = Y_t$.⁷

The resulting Phillips Curve is⁹

$$\epsilon_p MC_t \stackrel{11}{=} \epsilon_p - 1 + \varphi(\Pi_t - 1)\Pi_t - M_{t+1}\varphi(\Pi_{t+1} - 1)\Pi_{t+1} \frac{Y_{t+1}}{Y_t}$$

where $\Pi_t = \frac{P_t}{P_{t+1}}$.¹³

¹⁴

¹⁵

A.5 *Labor market*

¹⁶

A risk-neutral labor agency supplies labor N_t to intermediate goods producers at cost h_t by hiring households at wage w_t . To hire workers, the agency posts vacancies v_t , which are filled with probability ϕ_t . Household job search is random. Following Bardoczy (2024), we assume the labor agency cannot observe individual household productivity. Instead, it only observes the average productivity of all employed workers, which is normalized to one.

Labor agency. The labor agency determines how many vacancies to post and how much labor to sell by solving the following problem:

$$J_t(N_{t+1}) = \max_{N_t, v_t} \left\{ (h_t - w_t)N_t - \kappa v_t + \mathbb{E}_t \left[\frac{J_{t+1}(N_t)}{1 + r_t^a} \right] \right\},$$

²⁷

subject to

²⁸

²⁹

³⁰

$$N_t = (1 - \omega)N_{t-1} + \phi_t v_t.$$

The parameters κ and ω are, respectively, the cost of posting a vacancy, and the job separation rate.³²

The resulting job creation curve is:

$$\frac{2}{3} \frac{\kappa}{\phi_t} = (h_t - w_t) + (1 - \omega) E_t \left[\frac{\kappa}{(1 + r_t^a) \phi_{t+1}} \right].$$

Matching. The matching process between households and the labor agency follows a Cobb-Douglas matching function:

$$\frac{7}{8} m_t = \chi e_t^\alpha v_t^{1-\alpha},$$

where m_t is the mass of matches, e_t is the mass of job searchers, α is the matching function elasticity, and χ is a matching efficiency parameter.

The vacancy filling probability ϕ_t and the job finding probability η_t evolve as follows:

$$\frac{13}{14} \eta_t = \chi \Theta_{it}^{1-\alpha}$$

$$\frac{15}{16} \phi_t = \chi \Theta_t^{-\alpha}$$

where $\Theta_t = \frac{v_t}{e_t}$ is labor market tightness.

Wage Determination. Following Gornemann et al. (2021) and Blanchard and Galí (2010), we assume the real wage evolves according to the following rule:

$$\log \frac{w_t}{w_{ss}} = \phi_w \log \left(\frac{w_{t-1}}{w_{ss}} \right) + (1 - \phi_w) \log \left(\frac{N_t}{N_{ss}} \right),$$

where ϕ_w dictates the extent of real wage rigidity.

25 26 A.6 *Fiscal Policy*

27 The government issues long term bonds B_t at price q_t^b in period t that pays δ^s in
28 period $t+s+1$ for $s \in \{0, 1, 2, \dots\}$.

29 The bond price satisfies the no arbitrage condition:

$$\frac{30}{31} q_t^b = \frac{1 + \delta E_t[q_{t+1}^b]}{1 + r_t^a}.$$

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The government funds its expenditures through debt and taxes, subject to the following budget constraint:

$$^3 \quad ^4 \quad (1 + \delta q_t^b)B_{t-1} + G_t + S_t = \tau_t w_t N_t + q_t^b B_t,$$

where S_t are payments⁵ for unemployment insurance and other transfers.

For all stimulus⁶ policies, except tax cuts, we follow [Auclert et al. \(2020\)](#) and allow the tax rate to adjust in order to stabilize the debt-to-GDP ratio:

$$^8 \quad ^9 \quad \tau_t - \tau_{ss} = \phi_B q_{ss}^b \frac{B_{t-1} - B_{ss}}{Y_{ss}}$$

10

where ϕ_B governs the speed of adjustment.

For the tax cuts, we assume government expenditures adjust following:

$$^{13} \quad ^{14} \quad G_t - G_{ss} = \phi_G q_{ss}^b \frac{B_{t-1} - B_{ss}}{Y_{ss}}$$

where ϕ_G governs the speed of adjustment of government spending in response to debt.

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A.7 *Monetary Policy*

The central bank follows a standard Taylor rule that responds solely to inflation:

$$^{21} \quad i_t = r^* + \phi_\pi \pi_t,$$

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where ϕ_π is the coefficient on inflation. Inflation is given by $\pi_t = P_t / P_{t-1} - 1$, and r^* is the steady state interest rate.

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A.8 *Equilibrium*

An equilibrium in this economy is a sequence of:

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- Policy Functions $(c_{it}(m))_{t=0}^\infty$ normalized by permanent income.
- Prices $(r_{t+1}^d, i_t, q_t^b, w_t, h_t, \pi_t, \tau_t)_{t=0}^\infty$.
- Aggregates $(C_t, Y_t, N_t, \Theta_t, B_t, A_t)_{t=0}^\infty$.

Such that:

¹

- $(c_{it}(m))_{t=0}^{\infty}$ solves the household's maximization problem given $(w_t, \eta_t, r_t^a, \tau_t)_{t=0}^{\infty}$.
- The final goods producer and intermediate goods producers both maximize their respective objective functions.
- The nominal interest rate is determined by the central bank's Taylor rule.
- The tax rate is set according to the fiscal rule, ensuring that the government budget constraint is satisfied.
- The value of assets is equal to the value of government bonds:

¹³

$$A_t = q_t^b B_t.$$

¹⁴

- The goods market clears³⁵:

¹⁶

$$C_t = w_t N_t + G_t,$$

¹⁷

where $C_t \equiv \int_0^1 \mathbf{c}_{it} di$.

- The labor demand of intermediate goods producers equals labor supply of labor agency:

²¹

²²

$$L_t = N_t.$$

²³

²⁴A.9 Calibration of Non-Household Blocks

The elasticity of substitution is set to 6, and the price adjustment cost parameter is set to 96.9 as in Ravn and Sterk (2017, 2021). The vacancy cost is set to 7 percent of the real wage as in Christiano et al. (2016).³⁶ The matching elasticity is

³⁵Note if profits were not held by firms then the goods market condition would be $C_t + G_t = Y_t - \kappa v_t - \frac{\varphi}{2} \left(\frac{P_t}{P_{t-1}} - 1 \right)^2 Y_t$. In particular, since firm profits are $D_t = Y_t - w_t N_t - \kappa v_t - \frac{\varphi}{2} \left(\frac{P_t}{P_{t-1}} - 1 \right)^2 Y_t$, then the goods market condition would become $C_t + G_t = w_t N_t + D_t = Y_t - \kappa v_t - \frac{\varphi}{2} \left(\frac{P_t}{P_{t-1}} - 1 \right)^2 Y_t$.

³⁶The range of plausible values lie between 4percent and 14percent Silva and Toledo (2009)

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1 TABLE 9. Calibration

2 Description	Parameter	Value	Source/Target
Elasticity of Substitution	ϵ_p	6	Standard
Price Adjustment Costs	φ	96.9	Ravn and Sterk (2017, 2021)
Vacancy Cost	κ	0.056	$\frac{\kappa}{w\phi} = 0.071$
Job Separation Rate	ω	0.092	Match $\pi(eu)$ for Highschool group
Matching Elasticity	α	0.65	Ravn and Sterk (2017, 2021)
Job Finding Probability	η_{ss}	0.67	$\pi(ue)$ in section 3.3.1
Vacancy Filling Rate	ϕ_{ss}	0.71	den Haan et al. (2000)
Real Wage Rigidity parameter	ϕ_w	0.837	Gornemann et al. (2021)
Government Spending	G	0.38	Gov. budget constraint
Decay rate of Gov. Coupons	δ	0.95	5 Year Maturity of Debt
Response of Tax Rate to Debt	ϕ_B	0.015	Auclert et al. (2020)
Taylor Rule Inflation Coefficient	ϕ_π	1.5	Standard

0.65 following Ravn and Sterk (2017, 2021). The job separation rate is set to 0.092. As in section 3.3.1 we set the job finding probability in the steady state for the unemployed η_{ss} to 0.67. Along with the job separation rate, this gives a probability of transitioning from employment to unemployment within a quarter of 3.1 percent which is the value we use for the Highschool group in section 3.3.1. The quarterly vacancy filling rate is 0.71 as in den Haan et al. (2000) (and together with our other choices, this pins down the matching efficiency χ). The degree of wage rigidity ϕ_w is set to 0.837 following Gornemann et al. (2021). The tax rate is set to 0.3 and government spending is set to clear the government budget constraint. The parameters that dictate the speed of fiscal adjustment, ϕ_B and ϕ_G , are set to

0.015, the lower bound of the estimates in Auclert et al. (2020).³⁷ Furthermore, the decay rate of government coupons is set to $\delta = 0.95$ to match a maturity of 5 years.³⁸ Finally, the Taylor rule coefficient on inflation is set to the standard value of $\phi_\pi = 1.5$.

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³⁷The speed of adjustment parameter is set to the lower bound to ensure that the policies evaluated in the HANK and SAM model are almost entirely deficit financed.

³⁸The duration of bonds in the model is $\frac{(1+r)^4}{(1+r)^4 - \delta}$

72 REFERENCES

APPENDIX B: RESULTS IN A MODEL WITHOUT THE SPLURGE

Full appendix PDF available at: GitHub: Subfiles/Appendix-NoSplurge.pdf

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Click any section title below to view it online in HTML:

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B.1 *Introduction*

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B.2 *Matching the iMPCs without the splurge*

B.3 *Estimating discount factor distributions without the splurge*

B.4 *Multipliers in the absence of the splurge*

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