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Ten years later—the financial crisis cost every American $70,000 in lifetime income

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In a recent article, "The financial crisis at 10: will we ever recover?" (*Economic Letter*, Federal Reserve Bank of San Francisco, August 13, 2018) economists Regis Barnichon, Christian Matthes, and Alexander Ziegenbein argue that the last financial crisis cost every American about $70,000 in lifetime present-value income.

A possible reason for this loss of lifetime income lies in the decline of U.S. GDP following the financial crisis of 2007–09. In figuring out the reasons for the lost output, the researchers said that the effects of financial market conditions on the economy are asymmetrical. That is, a financial shock will slow down economic growth in good times, but favorable financial conditions will not necessarily stimulate economic activity in bad times. Based on previous trends, the authors state that GDP might not revert to the level indicated by its precrisis trend.

The authors modeled the relationship between financial conditions and GDP over the course of a typical business cycle. By testing this economic model under various stress conditions, the authors found that during recessions, the overall desire for risk normally decreases as the financial sector becomes more risk-averse or has less money available to lend. Further, they conclude that without the massive financial shocks of 2007 and 2008, the economy likely would have trended closer to the post-1991 recessionary period, when GDP fell by just 1.5 percent before bouncing back a few years later.

Data indicate that actual U.S. GDP is running about 12 percentage points below where it would have been had the crisis not occurred. The recession lowered output by so much (about 7 percentage points more than in a mild recession) and for so long, that the average American will take a $70,000 hit to their income over their lifetime. To come up with this figure, the authors took the GDP-per-person reading from 2007, about $50,000, and assumed an annual 5-percent discount rate.

Barnichon, Matthes, and Ziegenbein conclude that much of the gap between current output and what would be expected under precrisis trends is attributable to the financial crisis, even 10 years later. The authors point out that financial-market disruptions can have large costs in terms of societal welfare by causing persistent losses in the level of GDP. America has yet to make up the ground it lost in the 2008 financial crisis, and the researchers doubt that the country will ever regain the lost ground. The authors suggest that preventing future financial crises, and finding ways to contain those that do occur, is an important research and policy priority.