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From rescue to recovery, to transformation and growth: building a better world after COVID-19

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The COVID-19 pandemic has underlined the fragility and dangers of the old growth path. There can be no going back to the old normal, argue Amar Bhattacharya and Nicholas Stern.

London's financial district during the COVID-19 lockdown.
(Credit: Amarjeet Singh Hardeepsingh/iStock)

The importance of resilience and the dangers of ignoring the links between nature, pandemics and climate have come to the fore as this pandemic has taken hold. The crisis has also underscored the importance of inclusion and social cohesion, and of internationalism.

At the same time the need to respond to the threat of climate change remains just as urgent, with mounting emissions and evidence on the rising costs and risks of climate change (including the Intergovernmental Panel on Climate Change's **Special Report on Global Warming of 1.5°C [https://www.ipcc.ch/sr15/]** of 2018). While there has been progress on many different fronts and by different players on climate action, collectively the world is falling far short of what science tells us is needed to respond to the threat of climate change.

The current crisis presents the risk of a major depression. We are in a moment more like the post-WWII era, with its dislocated economies and risks of mass unemployment, than any global financial crisis, including that of 2008–09. An extraordinary collective response from the world is needed to get through, as was necessary in the 1940s.

The challenge is to avoid a depression *and* to set off on a new path of growth that responds to the climate threat.

Of course, the COVID-19 pandemic is still unfolding. So far the impacts have been primarily on North Asia, Europe and North America, but it has now spread to all parts of the world. There has not yet been a rapid acceleration of the disease in the developing world, but the outlook remains uncertain, given unknowns on the nature of the spread and the ability to contain it. Beyond its evident profound human costs and great loss of life, the pandemic is enacting enormous economic and social costs, even in countries that have not experienced large numbers of infections.

Confidence takes a battering

The pandemic and the necessary lockdowns have resulted in a sharp contraction of aggregate demand, supply disruptions, loss of revenues for many service sectors, and unprecedented increases in formal and informal unemployment. Many economic actors face severe financial difficulties of both *liquidity* and *solvency*; and, of special importance for many developing and emerging market countries, sharp declines in commodity prices, remittances and tourism, and reversals in capital flows. All of this has fuelled a *deep loss of confidence* and exacerbated vulnerability to other potential shocks. This will likely shackle the recovery, of both consumption and investment, without strong action.

The demand, output and employment impacts are expected to be much greater than in the 2008 financial crisis and to be much more severe this time for developing countries and emerging markets. The impacts on these jurisdictions are potentially immense and will unfold in the coming months with potentially long-lasting and deeply damaging consequences.

Three phases of response: rescue, recovery, transformation to a new growth model

Beyond the stabilisation phase, we must act to create a strong recovery that can support job creation and hence consumption, and re-design, not just restart, investment. The response to COVID-19 will fall into three phases which overlap and interweave, but essentially involve different kinds of priorities. These are *rescue, recovery* and the *transformation to a new form of growth*.

In addition to a concerted response to the medical emergency, the world will need to act boldly to tackle the threat of a collapse of confidence and a sustained loss of employment. This is what Keynes understood so well, and what we must do now.

Strong and sustainable investment, across the world, must be at the heart of a recovery that is strong enough to protect the world from the serious risk of a great depression. Both nature and scale matter. On the former we need investment in physical, human and natural capital. If investment is to be of the necessary magnitude, both to avoid a depression and to set off with a new form of growth, then it must be across the world and, in particular, in the large emerging market countries, where the bulk of investment, particularly in infrastructure, will take place.

Recovery has to be driven by an expansion of demand but has to be part of a story of sustained investment, innovation and growth. The world has excess savings and, as we have said, is potentially at the beginning of a great depression. There will be pressure on the public finances of every country, and pressure on the balance sheets of multilateral development banks (MDBs), the IMF, and the development finance institutions. It is crucial that the world does not slip back into austerity as it did after the financial crisis of 2008: the challenge is to grow out of this one.

We will likely need to commit to 'no austerity' and thus to major deficits for a while (and some monetary financing of these deficits) if the confidence about growth, which is necessary for both consumption and investment, is to be there. And that confidence about growth would be generated by a clear sense of direction, as is embodied in the **Green Deal in Europe [https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal_en]** and the drive to the zero-carbon economy. A clear strategy for investment and innovation is critical to save the world economy and its climate/environment.

The recovery has to be much more than green – and design and implementation need to happen soon

The recovery has to be green but also it has to be a path to a better economy, to better health and wellbeing, to inclusion and a just transition, and with respect for planetary boundaries.

We must start designing stimulus packages now and move to implementation soon.

The stimulus packages must be shaped by the scale and urgency of the challenge, and with a clear sense of direction. They must be anchored in the target of net-zero emissions and greater resilience, with supporting plans for sustainable infrastructure, pricing (including carbon pricing and elimination of fossil fuel subsidies, taking advantage of low fossil fuel prices) and smart regulations. Stimulus packages can be built to exploit transformative opportunities in energy transition (energy efficiency, renewable energy, grid development), sustainable transport (electro-mobility, mass transit, rail electrification), cities (pedestrian walks and bicycle paths, upgrading buildings and green spaces), and investment in natural capital (land restoration, forests and landscapes). There are many examples of green investments and activities that can be launched quickly and conducted safely with good practices.

Stimulus packages should also invest in people to boost productivity and wellbeing (health, education). They should target support to employment-intensive segments of the economy, especially small and medium enterprises. We must invest in the jobs and skills of the future. That is the only path to decent jobs and job security. Dirty investments will bring stranded assets and stranded labour. As economies move from rescue to recovery, it will be important, therefore, to support companies that move forwards, not backwards. This includes energy and transport companies that are committed to the low-carbon transition. We must accelerate the phase-out of dirty and polluting capital and ensure that we do not add to that stock through dirty fossil fuel investments such as coal.

Preparing 'shovel-ready' programmes, policies and finance

Well-designed recovery packages can boost aggregate demand and employment in the short term, boost productivity and competitiveness in the medium term, and bring about the transformation needed for inclusive, sustainable and resilient growth. An early start to stimulus packages can boost confidence, counteract the contractionary pressures in the economy through direct and spillover effects, and create much needed jobs.

The recovery has to embody very big investment in the infrastructure and technologies of the future. It must also support jobs and incomes to stimulate consumption and embody the inclusion and equity vital for social acceptance after a very difficult experience, where the poorest have suffered badly and many low-paid workers have made huge contributions. Boosting employment will boost consumer confidence, and strong recovery packages can boost investor confidence.

To enable early implementation of robust recovery packages, countries need to prepare: a) 'shovel ready' programmes and investments that can be scaled up; b) 'shovel ready' policies that can draw through the right investments and curb wrong ones; and c) 'shovel ready' finance to mobilise the scale of financing needed and ensure that the financial system can be a powerful force for transition.

International collaboration and support can greatly enhance the efforts of individual countries. Tackling the pandemic will require strong global cooperation on containment and the medical response, including treatment and vaccines.

As in the case of the 2009 response, there is strong benefit from macroeconomic policy coordination on the design and implementation of stimulus packages. Collaboration will be particularly important in helping developing countries respond to the adverse social and economic impacts. This includes tackling the debt burdens of developing countries and ensuring that both emerging markets and developing countries have access to finance for investment and transformation – which will require something similar to a Marshall Plan, but of even greater ambition and scope. The UN and the international financial groupings (such as the G7 and the G20) and institutions must come together to shape and implement such an ambitious plan.

Harnessing the private sector

Already there are powerful examples of private sector leadership in the face of the COVID-19 crisis. The private sector will be central to the recovery of employment and consumption and for investment and innovation to drive economies forward. Confidence in the strength of government policy, in the clarity of its direction, and in its steadiness over time will be crucial.

To finance a sustained recovery, the financial system must create the right kind of finance at the right scale at the right time. We have both negative interest rates in global financial markets and rising risk premiums, especially for emerging markets and developing countries. The financial system will have to manage, reduce and share risk to bring down those premiums. Development banks can play a vital role in helping to take programmes to scale and in catalysing private finance, given the problems of confidence in these uncertain times.

The imperative of choosing the right path

While we have the knowledge and the means to emerge out of this crisis stronger and better, there is a significant risk that we could go the other way.

A prolonged depression would be the most dangerous path of all. It could lead to a rise of extreme politics. It would not involve the new investment and innovation (in all types of capital) desperately needed for tackling climate and environment. It would lead to great deterioration of health and loss of life flowing from unemployment and poverty. And it would potentially undermine the social discipline that we will need to manage risks of second and third waves of COVID-19. Austerity and/or an attempt at a 'brown' recovery would be very dangerous.

Global solidarity and leadership have never been more important.

The response to the global pandemic and the need to shape a recovery that avoids the threat of a prolonged depression and delivers a sustainable future for people and the planet calls for unprecedented international solidarity and urgency of action. Now is the time to recommit to the UN and the Sustainable Development Goals; to step up support and unleash the potential of the international financial institutions (IMF, OECD, MDBs, IDFC); for the business sector to build on recent momentum to play a leadership role in driving the transition to a better growth path; for leadership and solidarity from world leaders, especially from the largest countries and the most important groupings; to strengthen and use coalitions of economic decision-makers such as the Coalition of Finance Ministers for Climate Action and the Network for the Greening the Financial system, and to foster coalitions of cities and local governments to accelerate ambition, learning and actions; and for global citizenry and civil society to exert their pressure for an adequate response that delivers a sustainable and inclusive future.

Only with collective mobilisation and solidarity will we overcome the crisis and build a better world – strong, inclusive, sustainable and resilient.

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