Covid and climate – building a strong and sustainable recovery

The UK and the world have been transformed by the Covid crisis. Beyond its tragic human costs and loss of life, the pandemic and the necessary lockdowns have resulted in a sharp contraction of aggregate demand, supply disruptions, loss of revenues for many service sector businesses and unprecedented increases in unemployment.

The demand, output and employment impacts are expected to be much greater than the 2008 financial crisis, with truly global reach. The impact on many developing and emerging market countries could be immense and with potentially long-lasting and deeply damaging consequences. It has meant 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.

Climate action must now be examined in the context of a real risk of a great depression. The immediate focus has to be in shaping and implementing rescue plans, with commensurate international support for countries that need it, and carefully designed lockdown exit strategies. But beyond the immediate emergency measures, governments will need to introduce more comprehensive, longer time horizon stimulus packages to promote recovery. There is an opportunity for investment in sustainable growth to be at the centre of a recovery strategy for the world, both in terms of restoring confidence and securing strong, resilient and inclusive growth and development that respect planetary boundaries. It will require focus and leadership, but a unique window is now open.

Well-designed recovery packages can boost aggregate demand and employment in the short term, and grow productivity and competitiveness in the medium term. But there is a real risk that recovery packages try to return the economy to the old model that has proved unproductive and dangerous (including in the sense of making pandemics more likely). This would make climate action much more challenging in the years and decades ahead.

Previous studies, such as the New Climate Economy, Better Growth, Better Climate reports and LSE research (see here, here, here and here), have outlined the opportunities associated with low-carbon, resource-efficient growth. Three key actions will be central to locking in better growth and avoiding the dangerous models of the past.

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First, getting the biggest bang for every policy buck. The evidence suggests that every dollar of spending funded by public borrowing during a severe downturn is likely to raise output by $2-$3 by leveraging private spending and 'crowding in' productive capacity. Sustainable investment policies perform particularly well. In the short run, clean energy infrastructure is particularly labour intensive, creating twice as many jobs per dollar spent as fossil fuel investments. Construction projects like insulation retrofits and wind turbines are less import-intensive than many traditional stimulus measures and lead to higher multipliers, while lowering long-term energy cost. By generating growth, the public debt becomes sustainable and more easily repayable.

In the long run, sustainable investment expands capacity and fosters productivity growth faster than investment in resource-intensive high-carbon sectors. Clean innovation, working with the technologies of the future, is particularly effective at generating economies of scale in production and discovery. We already had a glimpse of this in the dramatic declines observed in the costs of renewable energy, battery storage and electric vehicles. There are many more opportunities for cost reductions in clean technologies.

Second, there is a need to invest global savings in a broad range of productive complementary assets including not only physical and human capital, but also knowledge and intangible capital as well as natural and social capital. Covid-19 has reminded the world of the urgent need to strengthen the quality and resilience of natural assets. Investment in social and institutional capital is also necessary to deliver effective and functional government with popular support, as well as to reinvigorate the cash-starved social sector (e.g. charities and enterprises with social objectives), which generated up to £200 billion of value to the UK economy, or around 10 per cent GDP in recent years. At the same time, public money should not be spent propping up fossil-fuel intensive assets with limited productivity potential, except to ensure a just transition for workers and communities impacted by their inevitable decline.

Third, there is an urgent need for a coordinated response, in the UK and internationally, to avoid a global depression and build back better. This requires strengthened institutional arrangements at home in the UK, including national investment banks with a sustainability mandate to leverage private finance, and also multilateral coordination from the OECD, IMF, World Bank, regional development banks and development finance institutions. Sound institutions can boost confidence, reduce the cost of capital (by sharing and reducing risk) and help steer the economy onto a more sustainable growth path. So too will clarity of strategy and credible policy. By contrast, looking backwards, policy delay, inaction or uncertainty will have devastating economic and social effects.

Other Covid-driven changes can also help lock in a better growth path. For example, in many countries the state is likely to have increased its role in the economy through the process of rescue, with loans to or shares in many companies. That puts it in a position to be active in industrial policy because as the rescue-loans are unwound or extended, and/or as a significant shareholder, the state could tilt its influence in these firms towards a sustainable, resilient and inclusive recovery, utilising supportive public policies. Many will have also found ways of doing things more efficiently; the reaction to the crisis has shown the possibility of rapid change in ways of doing things.

There is a unique window for the UK and the world to act fast and lock in a more sustainable, inclusive and resilient growth path. Public support is high. If we miss it, the legacy of the Covid pandemic could lead to a whole series of damaging social, environmental and economic emergencies. The consequences of a prolonged global depression could be profoundly damaging and unmanaged climate change catastrophic.

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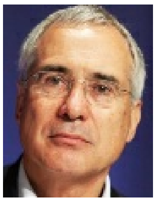

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