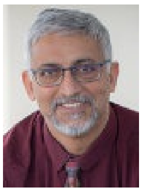
Who pays for Covid-19? Assessing seven potential options



The Covid-19 pandemic has motivated huge levels of spending from governments across the world. But once the pandemic is over, how will these measures be paid for? **Arvind Ashta** *assesses the feasibility of seven potential options.*

While statistics on the daily number of infections and deaths caused by Covid-19 are available from many sources, there is absolute silence on the bill that is being prepared to finance all the emergency action. On 13 March, the EU provided its thoughts on coordinated economic measures and followed this up on 2 April and 22 April with further statements, all while pointing out that the EU's budget is rather small. Elsewhere, India just announced that it would spend 266 billion dollars (10% of its GDP) on stimulus measures. All of this begs the question: where will the money come from?

The simple explanation from modern monetary theory would be to print more money and pay with a smile. However, this approach seems to have been tried by Nicolas Maduro in Venezuela with few real results and at the cost of excessive inflation – a contagion of its own kind. Second, with interest rates being so low, there is excess money in the economy and not a deficit of liquidity. This is one reason why financial markets may have done well in stagnating economies (pre-Covid). Without this financial euphoria, we may have all been driven to depression. Even with a mild easing of lockdown measures, financial markets are ready to bounce back to their pre-Covid numbers because, as we all know, financial markets reflect future cash flows and not past ones.

Seven options

There are at least seven potential options available to fund Covid-related spending. A higher personal income tax comes first in our list since this concerns a wide middle-class population. Perhaps, everyone is expecting this and tightening their belts in preparation. This belt-tightening of course will not help the economy, as we all know if we have read our Keynes. Therefore, if we want any relaunch, we should first assure the middle classes that personal taxes will not increase.

The second proposal would be to raise corporate taxes, especially in relation to businesses that have clearly benefitted from the virus. To some extent, those with higher profits will already pay more taxes: this would include all social media platforms, for example, as well as those who will profit from supplying medical equipment of various kinds. But governments could also look at taxes on insurance companies that have accumulated reserves over recent decades. By invoking trustee-based leadership concepts, we could argue that these reserves belong to society and should be given back in times of need such as this.

However, some insurance companies may already be settling claims for events cancellations and business interruptions – a crude estimate of these is $100 billion. Most companies are going to find themselves in times of trouble and any general increase in corporate income tax could simply be the final straw on the entrepreneur's back. The closing down of these enterprises would generate even more unemployment to be financed by welfare spending. As such, it might be advisable to look elsewhere for a solution.

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A third option is to look at indirect taxes. Fortuitously, we do not have far to look because crude oil prices have crashed. If governments just tax the difference between retail prices and crude oil prices, they could make a windfall gain that could largely finance the Covid-19 expenses. Assuming crude prices fall by $30 and consumption is 100 million barrels a day, this saving is more than a trillion dollars per year. Certainly, there is a tradeoff: lowering petrol prices may kick start some industries. However, since the economy is based on expectations and moods, this tax is the least likely to kill consumer optimism. Keeping crude prices low requires breaking the cartel.

Fourth, there is the option of the State providing subsidies to struggling firms and bailing them out. This may be a mistake. Shareholders take risks and should bear risk as far as bankruptcy is concerned. This includes pension funds who have taken risks – they can't just have gains. Therefore, all these troubled enterprises should raise equity capital issued at a lower share premium. The IPO markets should therefore boom and instead of paying taxes, people should be investing in companies with risky returns. The EU document mentioned above does suggest recapitalisation, with the State investing and later exiting. The inconvenience is that the burden of the difference between entering price and exiting price is often left for the taxpayers of the future.

A fifth solution, and here we go back to the monetarists, is to take on debt. But even debt must be repaid eventually. Otherwise, why are we looking aghast at Italy? Why did we bother about Greece? The burden for the repayment of debt then goes to our children and to our grandchildren. The argument is that we would have overcome the immediate problem, and a more powerful economy could pay for the debt later. We have already mentioned the modern-day monetarists who feel that we just don't have to pay money back, and this author pleads ignorance as to whether the pigeon that closes its eye will be eaten by the cat or not. The question of the organisation of this debt, and provisions for bad debts and bad banks rushing to finance the public aggregates when they would not finance private individuals, also needs a lot of reflection. Clearly, for some countries, sovereign risk may have surpassed private risk.

A sixth solution is charity. This could be charity from rich individuals or from rich states to poor states. The only difference between charity and tax is the former is voluntary while the latter is considered involuntary. After all, if rich individuals can finance the reconstruction of Notre Dame, they could surely come forth to pay for the suffering of the millions affected by Covid-19. What is true of rich people can also be true of rich states. But experience in the past shows that very few countries are even willing to contribute 1% of GDP as foreign aid. And even what they do contribute is often tied aid and goes to consultants who have relationships with international organisations.

However, if we are dreaming of a solid Europe, it must be *solidaire*, an opinion clearly expressed in a recent paper on Greece I have co-authored with Christine Sinapi. Without this solidarity, and without everyone gaining from trade, either through profits or through equalisation payments, a European Union with open markets cannot thrive. This response would then acknowledge those who suggest that Germany or northern European states, who are richer than the rest, pay for those in southern Europe. At an even wider level, if the US is the major superpower, we might say let the US be great again and pay for the rest of the world. And if China wants this mantle, let China pay.

The final option would be a tax on financial markets. Since they thrive on liquidity, they certainly have the capacity to pay. This argument comes back to the proposal of the worldwide Tobin tax attributed post-mortem to a comment the Nobel Laureate James Tobin had made when alive. The problem with such a tax is financial capital would flee the country that imposes it. However, it can work if the whole world were to impose it. So, we need a world federation with taxing powers, and which distributes the proceeds of the tax in a manner that is economically and socially healthy. Coming back to Keynes, what is economically healthy is that the poorest people with the highest marginal propensity to consume get the money to boost aggregate demand. Fortunately for us, this would be socially healthy too.

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Note: This article gives the views of the author, not the position of EUROPP – European Politics and Policy or the London School of Economics. The author would like to thank Milford Batemen, Stuart Brown, N.K. Jain, Sandeep Kumar, Dirk Lebe, Chris Macrae, Gilles Mesnard and Avinash Wadhwani for comments and encouragement.

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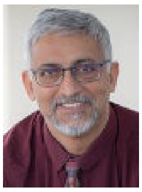

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