

Treasury Committee

Oral evidence: Economic impact of coronavirus, HC 271

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Members present: Mel Stride (Chair); Rushanara Ali; Mr Steve Baker; Harriett Baldwin; Anthony Browne; Felicity Buchan; Ms Angela Eagle; Mike Hill; Julie Marson.

Questions 740 - 795

Witnesses

I: Laurence Boone, Chief Economist and G20 Finance Deputy, OECD; Gita Gopinath, Chief Economist, Economic Counsellor and Director of Research Department, IMF.

Examination of witnesses

Witnesses: Laurence Boone and Gita Gopinath.

Q740 **Chair:** Welcome to our latest session of the Treasury Select Committee, looking into the economic impact of the coronavirus. I am delighted to be joined today by two important economists as witnesses: the chief economists for both the IMF and the OECD. Perhaps I could ask them to very briefly introduce themselves to the Committee.

Laurence Boone: Hello, everyone. Thanks for the invitation. It is a pleasure and an honour to be here. I am Laurence Boone, the OECD chief economist and representative for G20 finance. I head a team of about 200 economists who are working on both country-specific and cross-country policies; it is basically the research department.

Gita Gopinath: Thank you also for inviting me. I am the chief economist of the International Monetary Fund. I wear two hats. I am the economic counsellor at the fund and also the director of the research department. We do several things. We do multilateral surveillance and come out with our World Economic Outlook; we put out an update just last week. In addition, we engage with our members on important policy issues.

Q741 **Chair:** Thank you very much indeed and a huge welcome to both of you. We are extremely grateful. We know how busy you both will be at this difficult time for many countries around the world, and we are very grateful that you are giving your time to us this afternoon. The questions will be asked by members of the Committee in sequence. Each member will have about 10 minutes to ask you questions. I would just remind members to try to direct their question at either one of our two panellists or to both panellists to answer, but to indicate which one they would like to answer first.

With that, I will start with the first question. When it comes to the global crisis, what would be of interest to the Committee is if you could help by characterising how you see that global crisis, both in terms of how it is now and how it might evolve through time, and how you see it as being different from the 2008-09 financial crisis. Specifically in the case of the United Kingdom, how do you see the outlook as perhaps being different from some of the other advanced economies? Where are those differences, why are they there and how do you think we might best address them? There is quite a lot in that but I would like to start with Gita first, please, and then go to Laurence.

Gita Gopinath: We describe this as a crisis like no other for the simple reason that none of us, in our lifetimes or even before, has experienced something like this. This is, first and foremost, a health crisis—a pandemic, as we all know at this point—and in the absence of a solution to the health crisis, there is no solution for the economic crisis. That is the first important distinction.



Secondly, this is a large, real shock. If I think of the global financial crisis, it was triggered by subprime mortgages, so there was a real shock involved, but it was much smaller in scale than anything we are seeing. That means that the risks in terms of solvency are just that much higher this time around as opposed to the global financial crisis.

The third is in terms of how policies work. This crisis has required countries to be put in lockdown in order to mitigate the spread of the virus. That has meant that the fiscal support that has been put in, which is substantial at this point, at over \$10 trillion in the global economy, has been more about ensuring that the web of economic relations remains. This is not a standard stimulus as we would think but more about making sure that, once the recovery starts, it is going to be much faster.

What this means in terms of the path forward is, first, tremendous uncertainty. The health shock has not gone yet. We can have second waves, and that is something that can prolong this crisis. In the absence of that, we could say that the first half of this year was one of the deepest contractions we have seen. As countries are reopening, we are seeing signs of recovery, so we could say that, at least for now, the worst is maybe behind us in many economies. We are seeing a recovery but that is not guaranteed; the strength of the recovery is not guaranteed. We would expect to see a spurt in activity initially, but all our projections are for a much more gradual recovery by the end of this year.

Q742 **Chair:** Gita, on that specific point, Andy Haldane, who is, as you may know, chief economist at the Bank of England, has just said today that, based on some of the information that they monitor—electricity consumption, the movement of goods and various other things—it feels like, in the UK, we might be bending back towards more of a V-shaped recovery than many of the macroeconomic forecasters might have imagined. Is there any possibility of that or is that just an outlier of an observation?

Gita Gopinath: At this point, many things are possible. My fear is that, at the beginning of the recovery, all these paths will be observationally equivalent, so the sense is that we would see an initial spike. Going forward, we could then end up much flatter. It is a little too early at this point to project what the rest of that path would look like.

In terms of our tracking ability around the world, we are seeing that, for many countries, this is going to be somewhat of a prolonged recovery, with countries remaining below their pre-crisis levels even by the end of 2021. There are, of course, upside risks to it. Better news, especially in terms of treatments and vaccines, can trigger much more confidence and more spending, but I would be a little hesitant at this point to describe what the rest of that curve would look like.

In the case of the UK, we have our recent projection that we put out last week of around -10% growth in 2020 and +6.3% growth in 2021. That is very comparable to what other advanced economies' numbers look like.



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We had a significant downgrade relative to April and that reflects the fact that lockdowns have just been much more prolonged than we had anticipated, including in the UK, and the intensity of the effect, especially in the second quarter, is somewhat worse than we had anticipated.

Because we do not have a health solution at this point, we expect that there will be more persistent social distancing in the second half of this year, and the scarring that comes with that. Ours is a much slower, prolonged recovery as of now, but there are both upside and downside risks, for advanced economies especially.

Q743 Chair: You mentioned the 2020 and 2021 projections in terms of the GDP, with the UK at -10.2%, moving to a growth of 6.3% in 2021. You have France at -12.5%, so a little steeper than us on the downturn, and then stronger growth, by a percentage point, the following year. What is the reason for that difference?

Gita Gopinath: The reason we have different impacts across various economies is, first, how the virus has been spreading in these economies, how much containment has been needed and how long the lockdowns have been needed. That is one factor, but there are many other factors, including the reliance of the economy on tourism. The more dependent on tourism the economy is, the bigger the hit. France relies heavily on tourism, as does the UK, but still there could be relative differences. The amount of policy spending that happened depends again on countries' fiscal policy space. There are several factors that come in. I would not make a huge distinction between -10% and -12% at this point, given the considerable uncertainty around these numbers.

Q744 Chair: Laurence, could you say a few words on the question and perhaps particularly focus on this issue of scarring for us? We know that it is going to take some time to get back up to where we were before. There will be an output gap across the world—the estimates are of the order of \$12 trillion—so a lot of substantial damage will have been done. Where would you see the scarring specifically in the UK? What sort of measures should the UK be looking at in order to avoid or ameliorate the effects of that scarring from occurring?

Laurence Boone: At this stage, we have two scenarios, given the uncertainty described by Gita. We published our economic outlook about two weeks ahead of the IMF. We used two scenarios because we still do not know much about the virus, as you know. Given that there is no reason to believe that there will not be a second scenario, there is no reason to believe that there is more probability that there will be a scenario.

In these two scenarios, the UK is among the OECD countries, together with France, Spain and Italy, being particularly hurt, in part because of the strict confinement that Gita mentioned, and in part because of the importance of services in the UK, on top of the other factors that have been described before.



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Looking ahead, which is what I guess you were getting at, our health department at the OECD estimates that it usually takes six to seven years to get a vaccine or a new treatment. There is an amount of research in the world that makes it very likely that we will get something much more speedily, but if we assume—and this seems reasonable—that, at a minimum, we have to wait between 12 and 24 months, that means two things for this period. First, we will have to live with physical distancing, which is particularly affecting aeronautics, which we have not yet mentioned, on top of all the services that have more difficulties operating with physical distancing.

It also increases the operating costs of a number of industries. In the beginning at least, we run the risk of having an economy functioning at 90% or 95% of its capacity over the long and medium term. In fact, by the end of 2021, we think that the total accumulated output lost is likely to be between 6% and 10%, depending on the country.

We are in phase two of the crisis, where some support is still needed for some firms and people, even as the economies reopen. At the same time, policymakers will want to facilitate the transition from those sectors that will be affected for a long time towards those sectors that will thrive again in the Covid world. You can think of sectors that the UK is good at, like e-commerce, but there is also the issue of care. Across countries, these sectors will likely be beefed up and restructured. You can think of a number of others, like energy transition, which the UK is doing a lot about.

This has two implications. One is to be able to screen which companies are viable in the medium term and those that need to be restructured, and a review of the restructuring or solvency processes for firms may be of the order. The other one is to be able to train people who have to transition to new jobs as well as providing income support to those who do not have enough income.

In terms of the UK, the extension of universal basic credit was welcome and will likely have to stay for a while, but there is a lot to do—and I do not know if you want to get into this now—in terms of labour market reform and solvency, and how to address those firms that will have benefited from guarantees, of which there have been many in the UK.

Chair: We will get a bit more into the labour market stuff and other areas later. Thank you for that answer.

Q745 **Rushanara Ali:** Good afternoon. I wanted to focus my questions around international issues and co-operation. Starting with Professor Gopinath, I was wondering if you could just talk us through the emerging and low-income economies and the kinds of challenges that they have faced. Which ones have been hit the hardest by the outbreak? Which are the most vulnerable? What sorts of interventions are most effective for those countries?



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Gita Gopinath: This is a truly global crisis, unlike the global financial crisis, where we had advanced economies in recession but emerging and developing economies growing. This time, everybody is in recession. Emerging markets, developing economies and low-income countries are being hit on multiple fronts. It is a health crisis but, for several, there is a big drop in their commodity export prices, which is having a very large effect. Several of these countries rely very heavily on tourism and are being hit very hard. They rely very heavily on remittances, and the kinds of job losses that we have seen are usually tied to migrant workers, who are being hit very hard. In the period of March, when we had these very volatile financial market conditions, they were hit hard in terms of foreign financing.

The risks to these economies are very large. They have large financing needs. About half of the low-income countries entered this crisis with debt already in distress or a high likelihood of being in distress. As this crisis has called for more spending, many emerging markets have had to incur bigger deficits, causing debt-to-GDP to rise as the economies have contracted, and so they are now also entering the space of being very vulnerable on the debt front.

In terms of what works, the first thing is that this is a crisis where spending needs to be made. There are critical spending needs in the health sector and in ensuring that people have livelihoods. The first need is emergency financing, and that is what we have done at the IMF. About 70 countries have received rapid financing from us. That is the first requirement.

Secondly, several of these economies have their debt payments coming due, and this is not the time for them to be making those payments. They should have that income for other purposes. Initiatives such as debt relief and debt suspension are very important, and the IMF has done debt service relief for some of our poorest members, of which there are more than 25.

I suspect, however, that there will be continuing need for concessional financing and for financing in the form of aid and grants to several low-income countries for a prolonged period. This is not going away any time soon. They will also need technical expertise to deal with this crisis, particularly those with poor health capacities.

For a large number of emerging and developing economies, there was the March turbulence but, right now, because financial markets have rebounded in a lot of places, and because of the very large support from many major central banks and the swap lines, we have seen borrowing costs and spreads come down, so they are in a situation where their external borrowing is not under stress. I would say that the priority is to ensure that the international environment is such that they are able to access liquidity at reasonable rates and to make whatever spending is



required. That is the difference between emerging-market and low-income countries.

Q746 Rushanara Ali: Dr Boone, could you set out what would happen if the wealthier countries that provide billions of pounds of overseas development assistance and support started to go into retreat? In our own country, we are seeing the merger of DFID with the Foreign Office. There are concerns that, if there is a rolling back of overseas aid—emergency as well as development aid—that will make matters worse.

Given the interdependencies around this pandemic and how we tackle it, what is your sense of what would happen if development aid was in retreat around the world, particularly in some of the poorest economies?

Laurence Boone: Overseas development assistance in particular has played a key role, as you know, in promoting health and social protection systems in developing countries. We have been looking at what happened in previous recessions, and especially the financial crisis.

In fact, it is difficult to see a depression of the ODA level because members of the Development Assistance Committee have tended to maintain their contributions, even though they usually state their ambition as being a share of GNI or GDP, as you know. During the last Development Assistance Committee, they again confirmed that they will try to protect their ODA budget during the Covid crisis. Many of the ODA budgets were finalised before the Covid-19 outbreak, so there will need to be some revisiting of this because, as I said, they are expressed as a proportion of GNI.

Q747 Rushanara Ali: In your view, what would be the impact if countries started to cut back because of domestic pressure? We can understand where the political pressure might come from, and we are certainly feeling it. What is the impact on those economies and on those countries if there is a shift away from what you have at the moment?

Laurence Boone: I can think of two immediate impacts that would be of very high concern. One is on the funding of healthcare systems, which needs some of this money. The other is all the informal workers. We have seen how some emerging-market economies have developed or used digital tools to reach out to informal workers who fall through the social safety net, and we fear that they would be much more affected if we did not get this support.

Looking ahead, it will be super-important to ensure that, once a vaccine is developed, it is manufactured and deployed in large quantities also to those countries.

Q748 Rushanara Ali: I have one last question. This is in relation to some of the issues around UK retail companies, but it applies to European and American companies as well, in sectors like garment factories in countries like Bangladesh, that have been involved in the practice of not paying for contracts or for orders that have been made. In a country like that, over



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80% of exports are in the garment sector.

What can be done at the international level to address these types of issues? There will be parallels for other sectors as well. Are you playing a role in ensuring that this is addressed? There are two sets of issues, because some of these companies will be under financial pressure. Others do not have financial pressures but have cancelled contracts or orders, and this is putting millions of people at risk.

Laurence Boone: As you know, we have Aid for Trade, which would help to address some of these barriers that limit the contribution of trade to growth. A committee is working on this. It is a major concern for us, so we are trying to put pressure and increase Aid for Trade, as I was saying, especially for very small enterprises that tend to be priced out of the international market very quickly. That is the example that you were highlighting.

Gita Gopinath: I just wanted to add to your question about the need for aid. If you look at the projections of what is going to happen to poverty in these parts of the world, it is really sad.

If you look at, for instance, the World Bank numbers for people who will live with less than \$3.20 a day, that number could increase by about 40 million to 150 million. You are going to see deep distress. A country like the UK having a negative growth rate of 10% is very different from a low-income country having a negative growth rate of 10%, having started out with very low per-capita incomes, and the debt distress is tremendous.

Q749 **Felicity Buchan:** Hello, and thank you for taking the time. My questions are on the global economic policy response. I will ask Laurence the first question. Would it be fair to say that the international economic policy response has not been as strong as it was in the financial crisis? What would be the difference if we were to see a series of actions like we had at the 2009 London summit?

Laurence Boone: What you say is fair. We have seen tremendous national policy responses, learning from the financial crisis in particular. Governments have been very swift and efficient in beefing up their healthcare systems and then shielding people and firms.

At the international level, it is true that we have not had the equivalent of the London summit. There has been a lot of discussion about co-operation but the most concrete action that we have seen is the debt service moratorium that Gita mentioned earlier for low-income and developing countries. It is a success in itself because China came along, which was achieved by the Paris Club, for the first time in history.

Let me just make three remarks. The first is that, as we said before, this is first and foremost a health crisis. We need co-operation for two reasons. First, as long as the virus exists in some countries, we will not get back to something that looks like a normal situation. If only out of



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self-serving interests, the advanced economies should do something for emerging-market and lower-income countries.

Secondly, one thing that we have not mentioned is how much this crisis is widening all sorts of inequalities within people because of the way it affects people, which we can come back to, but also within countries. One of our big fears is that some emerging and low-income countries deescalate from the convergence process that they were on, not only because they do not have the same healthcare system but because they are very much integrated into the global value chain and that helps them catch up, and also because, when you have such numbers of informal workers who have to wake up in the morning to work during the day in order to have dinner at night, confinement is just not possible and the social safety nets are not the same at all. If only for health and these reasons, a lot more needs to be done.

Q750 Felicity Buchan: Gita, you have already alluded, in your responses to Rushanara, to the huge needs in emerging-market economies. There has been talk of an increase needed in special drawing rights, as we saw in 2009. Is that the solution and are we likely to see that?

Gita Gopinath: To compare at least the IMF's standing to what happened in the global financial crisis, on the eve of the global financial crisis the IMF had a lending capacity of about \$250 billion. Thanks to the actions taken by the members, the IMF now has a lending capacity of \$1 trillion, so we are in a much stronger position entering this crisis than we were entering the global financial crisis, which is an important distinction to make. In terms of the kinds of financing that have been needed, our strategy has been to try to push on levers that can deliver results most quickly. Those have been the rapid financing facilities that we have provided.

On your specific question around the SDR, this was discussed and, at this point, there is no broad consensus on having new SDR allocations. There is consensus on better use of the existing SDR allocations through a transfer from higher-income members to lower-income members. That is something that we are working on.

In terms of resource needs, as of now, given where financial markets are, in much more stable phases as compared to the real economy, we have about \$250 billion committed and are left with about \$750 billion, so we have a considerable amount. Given the current environment that we have, we are well resourced. If there is a major second wave and greater market turbulence, those resources could be seriously tested and, at that point, we would have to see what the international appetite is for doing more.

Q751 Felicity Buchan: Laurence, perhaps I can come back to you. Could there be circumstances where advanced economies may need international support?



Laurence Boone: Another feature of this crisis is the amount of uncertainty that we have and, at the same time, for advanced economies, how much support has been provided by the state. This raises the debt-to-GDP ratios of all countries. It is a big-level jump in debt that will likely be of the order of between 15 and 20 percentage points, depending on the economies, or perhaps higher.

If we have a second wave, my view is that, as long as we are not on a strong recovery path with declining unemployment and better-performing labour markets, Governments should still be in support. It is raising concerns in some instances about public debt but we should make the distinction between a jump in the level and the dynamic of the debt itself. That is the reason we are not recommending blanket support to both firms and people, but rather, as we get out of this phase of the Covid crisis into confinement, better targeting and adjusting of the parameters of labour-market support and the support of firms during the evolution of the pandemic and the economic side of it.

Once we are on much more known and stable ground, there will be reasons to revisit what we call sustainable public finance and how we reach new sustainability. To sum this up, the jump in the level might not be so worrying if it is across the world. Even so, we will also have to assess that because it will be an unreached level in these times. I am even more concerned, however, about the dynamic of the debt, and that is where we should be very careful.

Q752 **Felicity Buchan:** If you had one wish from the international community and specifically from the UK Government in terms of international policy response, what would it be? I will ask Gita first.

Gita Gopinath: My number one would be to deal with the health crisis much more globally in terms of making sure that all countries have the scale of testing and medical capacity that they need. Also, much more needs to be done now, so that, when treatment and a vaccine are available, they are globally available and affordable to all countries.

Laurence Boone: Everything related to health has to be at the top of the wishlist. The only thing that I would add is that there has been a rise in barriers to trade during the crisis, which has prevented the delivery of protective equipment, medicines, drugs and treatments to developing and emerging economies, as well as advanced ones. These barriers should disappear for the benefit of everybody.

Q753 **Anthony Browne:** I have a question about trade, but I just want to ask about a domestic issue first. Both the IMF and the OECD compare the economic policies of different countries. I am just wondering what you think of the UK's economic response to the crisis and the lockdown, and how that compares to other countries.

Laurence Boone: Like most OECD Governments, the UK has really deployed a vast array of measures. We look at three types of measures



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for each country: its health, its jobs and its people, and its firms. In terms of health, we can praise all Governments for the speed and extent of the increase in healthcare-system capacity that has been realised in what will appear a very short period of time, once we look back.

When we look at the labour market, as I said before, the reaction of the UK Government, like many other OECD countries, has been very prompt, both in maintaining a link to employment and in subsidising wages. There has also been a lot of support, extension and more accommodation on the universal basic credit, even though there may remain some holes here and there. However, the stepping up and the extension is very welcome.

In terms of corporate support, the array of instruments has also been very comparable to many countries. Again, a lot of it is guarantees but, when you look across the OECD, most of the support to firms is off public finance balance sheet and in the form of guarantees. That is why the period ahead of us is much more complicated and much more crucial in terms of the medium-term impact that it will have and in terms of the speed of recovery.

Gita Gopinath: I would concur with what Laurence said. The UK has given substantial, timely, targeted support for the economy, co-ordinated across fiscal, monetary and financial policy. This has been very important for ensuring that there is not a massive increase in unemployment and job losses. The take-up rate in the job retention scheme has been very high, and it has been quite successful. In terms of the coverage and generosity of that scheme, it is quite comparable to other European schemes, but the UK did not have this in the first place and they had to design and implement it very quickly. That was a very good initiative.

The challenge for the UK, as well as all other economies, is how to deal with these policies, when to phase them out and how long to keep them in the system as a function of the recovery. The guiding principles have to be that, first, it has to be a gradual phasing out, because there is tremendous uncertainty here and you could have countries going back into lockdowns.

The second principle has to be that, in the strict containment phase, it was about keeping people away from work while ensuring they have an income; the next phase has to be about encouraging people to return to work and less about protecting the job itself, especially over time, and encouraging a reallocation of resources. That would mean relying much more on unemployment insurance, for instance. In the case of the UK, you could make a case for temporarily increasing the support under that, because the UK has one of the lowest replacement rates among advanced economies in terms of unemployment insurance.

The measures that will be needed include a shift towards encouraging hiring, taking the form of targeted, not blanket, hiring subsidies—wage



subsidies—providing more unemployment insurance and encouraging reskilling and retooling.

Q754 **Anthony Browne:** Turning to international trade, there has been a lot of concern that supply chains have been disrupted during this crisis. Quite a few countries are looking at onshoring their supply chains so that they have resilience in medical produce. Is there a risk that protectionism becomes more pronounced now and that could slow down economic growth?

Laurence Boone: Let me just complete one thing on the previous question. On top of the cyclical policy to help people find a job and to provide incentives to people to find a job, it is often the case that single mothers, second-income earners or poor people do not have the means to get a job, either because they have to take care of a child or it is not great from a tax perspective. Those are two things that may benefit from being reviewed in the current period.

In terms of trade, trade tensions existed before and there will likely be more pressure in terms of onshoring firms. There are a couple of things that I would like to say here. Let me take the example of masks to start with. At the time, there was a shortage of global supply in the face of the surge in global demand. It has very little to do with what countries are able to manufacture. Even if we each had had our mask-manufacturing plants operating at normal levels before the pandemic, it is fair to say that none of us would have been prepared for this. There is some pragmatic explanation to make here.

There are three implications from that. First, we probably did not have enough stock in any of our countries. Secondly, the solution is not always to bring things home because, as I said, as would probably have been the case for masks, it takes some time to diversify sources of input into the global value chain. Clearly, there is a case for stress-testing value chains for some firms, as we do with banks or insurance, and the insurance balance sheet is, as you know, usually as complicated as a supply chain.

The last point that I would like to make is on something that you may wish to look at. Advanced economies and most of the northern hemisphere all got into this crisis together, so we confined at the same time together, meaning that there was little supply-chain disruption because the entire supply chain was in hibernation.

When we look ahead, the risk is what is happening today in the UK and in Germany: there is a cluster in a city and the area is closed, as with meat packaging in Germany. That has the potential to disrupt the supply chain a lot more than during the fully fledged confinement period. I say this because stress-testing and checking how firms are doing will be super-important.

The last point before finishing is international co-operation, which somebody else asked me about. For the sake of the recovery, being very



aware that trade barriers will be an impediment to global recovery and will not only impair the healthcare system of a lot of countries but will also deprive them from export growth, it would be a lot better if we could get some reduction in tension at the global trade level.

Q755 Anthony Browne: Gita, are you worried about increasing trade barriers in the wake of the crisis?

Gita Gopinath: Absolutely I am worried about it. There are tremendous risks to global trade such as rising protectionism; that was true even in the run-up to this crisis. We saw a reversal of trade integration. If you look at measures that have been put in place, that was a concern, and this crisis is going to trigger that even more. There is a temptation to localise production and a desire to put export restrictions on so-called essential or strategic goods. That is a main concern.

Another issue is that the global community has not made much progress in opening up trade in new or more dynamic areas, such as the services trade or electronic commerce. Those—especially electronic commerce—are going to become a much bigger part of the global economy going forward. It is a big concern, and the right approach would be to start building on these new areas and showing the potential benefits of greater trade integration and, as Laurence said, simply not having restrictions on the export of medical equipment and so forth.

Q756 Ms Eagle: Professor Gopinath, you wrote a recent blog in which you were praising the policy support that “has helped avert worse real outcomes” as part of the pandemic. At the same time, you observed that a “disconnect between real and financial markets raises concerns of excessive risk taking and is a significant vulnerability”. How do you see these vulnerabilities? Are they going to crystallise? What needs to be done to try to prevent that from happening?

Gita Gopinath: The substantial policy actions, especially by advanced economies around the world and by major central banks, ensured that there was no financial crisis alongside the real crisis. That was certainly very helpful. It prevented real outcomes that were worse even than the dire numbers that we have out there. That was super-supportive in that direction. What that has also done—this is the way that policies work—is to raise asset prices, which we have seen. We have seen recoveries in asset prices and reductions in credit spreads, and that has also been helpful for emerging and developing economies that are able to access markets without rates going through the roof.

That said, there is this concern about disconnect. If I think of where that disconnect might come from, I can think of three. First, the fact that policy support and the expectation that interest rates will stay low for the foreseeable future is one very important factor.

A second factor is that there is tremendous uncertainty about what this recovery will look like. We have both upside and downside risks, so the



markets are taking a more optimistic view on the recovery path. It is not a zero-probability event, so people can disagree. Thirdly, in terms of the effect on economic activity, it is affecting a lot of small and medium enterprises, as well as microenterprises, that do not show up in the stock market. That is another source of disconnect.

In terms of vulnerabilities, that is an important concern. In the run-up to this crisis, there were very large increases in corporate debt. Several countries had very high pre-existing debt levels already. We are projecting the highest public-debt-to-GDP in history for this year and next, so we are in that territory.

Q757 Ms Eagle: Are you worried not only about corporate indebtedness but also about the fact that the public policy responses increased levels of debt-to-GDP ratios for Governments as well, which makes it less likely that they will be able to respond in a coherent way if we get a serious second wave or, God forbid, swine flu comes back and we get a different pandemic?

Gita Gopinath: The response varies across countries. For many advanced economies, as of now, putting second waves aside, given the projected path for their recoveries, debt levels are projected to go up quite substantially this year but then stabilise and then come down gradually over time.

What helps is the fact that interest rates are projected to stay low for long, alongside the fact that this is a crisis that, regardless of how bad it is, has a bit of a V shape initially, whereby you are going to see growth spurt back up. Of course, that does not guarantee that there will not be financial market turbulence, and there are economies that are not reserve currency issuers and for whom there is a major risk in terms of what can happen if interest rates go up. I am worried about that.

On the plus side, compared to the global financial crisis, the banking system around the world is in better shape. It has more capital buffers and liquidity buffers, and the stress has shown that they can survive some very negative outcomes. The world is in better shape but there is a very serious likelihood that firms could become insolvent and require restructuring as this crisis plays out. The more prolonged the crisis, the greater that risk.

Q758 Ms Eagle: Are you as worried as some of us about the non-bank financial institutions? They are non-regulated. They were the cause of the 2008 financial crisis and are still around and unregulated. Do you worry about the effect that the non-bank institutions have? Should they be more supervised?

Gita Gopinath: It is important that there is more oversight over the non-bank financial institutions. There has been a push for that, but much more can be done on that front.

Q759 Ms Eagle: How would you see that being achieved, especially given that



we are in a period where there is a decline, rather than growth, in global co-operation to deal with these issues, and more protectionism? How would you see non-bank-financial-institution regulation coming about practically?

Gita Gopinath: There are some areas of global co-operation that are still holding up quite well. In this particular case, for instance, in terms of the committees that exist on financial regulation and so on, that co-operation still exists, at least for now. That would be the platform from which to do it.

Q760 **Ms Eagle:** One of the surprising things that the IMF changed in the way in which it approaches its analytics of countries and their economic prospects in the last few years, if I could characterise it this way, is the shift away from the Washington Consensus and towards ideas of inclusive growth.

In our response to the health pandemic, where the health of one is the health of all, and the pandemic is causing higher death rates in poorer areas and, therefore, inequality is also a huge issue, how can the IMF's concept of inclusive growth be more understood and perhaps have more of an effect on the way that economists and policymakers across the world regard the outcomes that they want to see from their policy—in other words, I would say, moving towards fairer, more equal and more sustainable societies?

Gita Gopinath: All three things you mentioned are essential, even from a pure growth perspective. There are very relevant concerns that high levels of inequality are dampening demand around the world and keeping growth and investment at low levels. These are very intricately linked.

An important legacy of this crisis has to be that, when you come out of this, it is important that there are good social safety nets in place, as well as access to healthcare, opportunities across the board and a lack of discrimination. These have to be the legacies of this crisis. It is good, not just from an equity perspective but even from a growth perspective.

Q761 **Ms Eagle:** Laurence Boone, how do you think the idea of inclusive growth and sustainability can be baked into the policy responses that we need in order to increase the prospects of a faster rather than a slower recovery from the recession—or even depression—that the Covid-19 pandemic is causing?

Laurence Boone: I will make two points on this. First, this crisis is, as you know, most impacting some sectors, such as hospitality, leisure, entertainment and sport. It is in those sectors, across countries, where you find the most non-standard forms of work and contracts. They are younger people and are the highest proportion of low-income earners. They are going to be the ones who will be most affected by this crisis. By the way, it is also in those sectors that firms are most indebted and where the debt-to-equity ratio is the highest. This is where firms run the



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risk of insolvency and where the highest unemployment rates are going to be seen.

All the programmes that we were talking about to support people should especially target these people, and not only the young ones in those firms but also the middle-aged people, who usually have less access to training when they get unemployed or when they are infirm. That is a real area where there is scope for any Government to look at.

The other one is the big and real effect of inequality on growth. Perceptions are also hugely important. For example, as we know, opening trade has been beneficial for most of the world and has lifted about a third of the world out of poverty; however, we also know that it has left some people behind within some advanced economies, so inequalities have risen within countries, which is now, in turn, leading to protectionism.

One of the areas where the necessary perception of fairness is important is when it comes to the taxation system. Nationally, progressivity matters a lot, but it also does internationally. The co-operation on international taxation, and the inclusive group working on international taxation in the digital age—and Gita mentioned ecommerce—will be especially important in sending a strong signal that policymakers are paying attention to inequality.

Q762 Julie Marson: I would like to direct my questions to Laurence, please. They relate to the global response to developing a vaccine. We have discussed the enormous economic costs arising from the lockdown. Would it be fair to say that you feel that Governments should spare no expense in looking at all candidates for possible vaccines, even if we end up looking at options that turn out not to be viable or going down dead ends?

Laurence Boone: Yes, we should spare no expense at all. As long as the virus is around, we will not be able to live with the same mobility as before. Some sectors will not work. A lot of people will be affected. As I said, it takes at least six or seven years to manage to develop a vaccine, and there are some pandemics for which we have not managed to develop a vaccine. We also know that we do not have a readily available molecule for treatment, and that we will also have to work on that. Given the magnitude of the shock we are going through, it is super-important that we achieve something as quickly as possible.

First, this requires international co-operation. Secondly, an example of something that works really well when it comes to research and development is co-operation, which is an area where we should continue to foster that. There is a scheme that helps in the context of how it is financed, which is DARPA, where you have a lot of teams working on different projects that have been carefully selected by very scientific people. It is encouraging research. I hope that that will continue but, as we both mentioned before, it is not only about discovering the vaccine



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but about manufacturing it on a massive scale and then making it available to most people at a price that they can afford.

Q763 **Julie Marson:** The OECD has posited an international response via an advanced market commitment to get the coronavirus vaccine across the world. Could you give us more of an idea of how that would work in practice, in terms of funding and overseeing the funding?

Laurence Boone: The inspiration is what happens when it comes, for example, to security of energy provision, whereby Governments commit to purchase a certain amount of energy over the years to come, so as to give some certainty to the provider, and then show that they will be able to benefit from this electricity over many years. There is a buffer on what could happen. It will be important to have a pre-commitment from Governments, so that they can distribute this.

There is the question of emerging and lower-income countries, for which international support will be required as well. An initiative was first launched in Europe for Covid, handled by France and Germany. There is also the global initiative that was initially launched in the US by a foundation that would make it. Any support that can go to those foundations that have a global outreach would be very helpful, because we do not have an international organisation in a position to deploy a vaccine everywhere, which may also be an area to look into.

Q764 **Julie Marson:** Is it fair to say that one of the major beneficiaries of this international effort and spending would be the major pharmaceutical companies?

Laurence Boone: This is an interesting topic in two respects. The first is to strike the right balance between the fact that you are trying to foster innovation, which is why we have intellectual property rights, and what happens when there is a global pandemic of the magnitude and the strength that we are facing. In this case, there is a global agreement that we should not repeat the mistakes of the past. We are talking about a global public good here, not a niche market where we should reward the research of some pharmaceutical companies.

Q765 **Julie Marson:** How do you feel the UK Government can help to catalyse and lead the international response to finding a vaccine?

Laurence Boone: The UK has certainly been one of the most vocal advocates of global co-operation and research on this, and has pushed for this initiative, the name of which escapes me at the moment. The UK is absolutely the place for leadership on this.

Q766 **Julie Marson:** If it was the case that the UK proved successful in developing the vaccine, would you say that the Government should prioritise our own domestic rollout or should it prioritise an international rollout, even if that took longer?



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Laurence Boone: That refers to what we were saying about barriers to trade and how some people tried to protect their markets in the past. I will give you a couple of examples that do not involve the UK but which expose what is happening quite well.

In continental Europe, as you know, there is some discussion about bringing back the manufacturing of paracetamol, which is manufactured mostly in India and China. The best answer to that is that the companies that manufacture most diabetic drugs are based in continental Europe. What happens if India and China respond to the barrier of bringing paracetamol production to continental Europe by doing the same with diabetic drugs? When we start making this type of fragmentation and barriers, everybody is a loser. We should really strive to make everybody a winner in this crisis.

Q767 **Julie Marson:** When we look at the pandemic that we are facing, what can we learn for the future in terms of funding to mitigate this kind of risk in the future?

Laurence Boone: That has been one of the lessons and something that we also look at internally in the OECD, in terms of striking the right balance between efficiency and being prepared for this type of event. There are things that we can do at the national level, as well as things that we should do at the international level.

At the national level, like others have, we have recommended more efficiency in the healthcare sector, which is something that perhaps needs to be reviewed. An expression that I like is a move away from "just in time" to "just in case", which well represents what we should do. There is a need to review healthcare preparedness. When we compare what is happening in Europe with Korea, for example, which was really prepared not only in terms of beds but also tests, isolation methods and so on, the cost to its economy is lower than the one we are all facing.

At the international level, there is merit in going into deeper co-operation in terms of pandemic preparedness. Because we were not prepared globally, we had all these barriers that were erected and slowed down the travel of protective equipment such as ICU machines. We were not even able to account for the dead in the same way, which is also slowing research. It really is a disaster, so there is a much more co-operation to be done at the global level.

Q768 **Rushanara Ali:** I wanted to focus on the issues around employment and how this crisis affects households. Just to kick off, can you give us a sense of the scale of unemployment that we are likely to see in the coming months, across Europe and globally? Could you also say a bit about what it means for youth unemployment? In the last financial crisis, we saw youth unemployment soar not only in the UK, but it was very high also in Spain and other countries.



Gita Gopinath: This crisis is leaving very unique imprints on the workforce. First, workers who are most impacted are low-skilled, low-income workers. In several cases, within those it tends to be women and minorities who are being affected in large numbers.

In terms of what this implies for unemployment rates, given the number of schemes that are in play for job retention, we are not seeing unemployment numbers directly. US unemployment rates have gone up quite substantially and are projected to go up and stay high, in double-digit numbers. For many other countries, however, especially in Europe, we are not really seeing a big jump in unemployment, because of the kinds of schemes that are there for keeping people in jobs.

Q769 **Rushanara Ali:** As they taper off—we are going to move away from them—how do you see the scale of unemployment across Europe?

Gita Gopinath: An ILO report tried to quantify the jobs that were lost. People are matched but they are not exactly producing or doing work. It was of the scale of 300 million workers, which is a very large number. This is a crisis that will have big consequences in terms of employment, because most of the sectors that have been affected are highly job-intensive.

As we know from previous crises, young people are particularly badly affected. We know that people who enter the labour force in a crisis like this take a long-term hit to their incomes. Entering in a recession is not a good thing. In this crisis, older workers could also be much more substantially affected: first, because of the health crisis, they might want to stay away from work; secondly, if this crisis goes on for a long time, people will have to retool, which is just that much harder for older workers.

That is what the landscape will look like. Part of the reason why we have a prolonged recovery is because we expect unemployment rates to come down but only gradually, just going from what we know from the past.

Q770 **Rushanara Ali:** From international experience, what kinds of interventions would help businesses and Governments to enable people to move from jobs and reskill quickly after a crisis like this? What would you point us and other Governments towards, as well as businesses?

Laurence Boone: I am completely in line with what Gita said on all this. There are a couple of things. First, in terms of training, there is a lot of inspiration. For once, I am not going to quote Denmark, which we usually quote when we come to talk about workers' support. Sweden has a very organised and deep organisation to take people by the hand and put them back in work. As we were describing, the risk that we see now is that some firms will become bankrupt and some workers will need to be retrained quickly and helped to find a job.

In Sweden, there is an agency that is not the usual kind of job support agency, but which works with firms before they complete the bankruptcy



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process in order to assess the skills of the workforce onsite, to assess the need for reskilling where it exists, and then to accompany people in reskilling them and then helping find them a job. This can be a short job and, when it is over, they start the process again. There is a huge amount of support that can be done here.

I would say a few other things quickly. First would be to keep the extension of universal basic credit that we mentioned for the most vulnerable people, and the other would be to move to wage subsidies that are linked to getting a new job in certain sectors. In that way, you do not have firms using the system to get some money, but rather hiring somebody when they need it.

The third is apprenticeship and vocational training. In most countries, this is restricted to the private sector but there may be room for having some in the public sector at the time of this crisis, and also ensuring that it targets not only lower-skilled people but people of all skills, in order to avoid any stigma.

Paid sick leave may also be something that you want to keep and review during the transition period. As we have seen in this crisis, a lot of self-employed people lost their jobs or moved into jobs involving delivery, care or ecommerce. There might be a need to review their social protection and access to training.

Q771 Rushanara Ali: Given what we know about the impact on young people, one generation already had to live through the global financial crisis. This is likely to be another generation that is going to be hurt very badly. Is there a case for targeted interventions to give them minimum-income guarantees alongside training and support?

Certainly, in our experience in the UK, it has been quite hit-and-miss in terms of the apprenticeship schemes and various programmes that successive Governments have introduced. From international experience, are there good examples or emerging examples where Governments are considering much more radical measures to ensure that young people do not end up facing the scarring effect that then has a knock-on effect on the economy going forward?

Laurence Boone: From international experience, there is no universal solution. It depends on each country's social set-up. Spain is, as you know, extending minimum income for younger people. In particular, because their social benefit system is such that it benefits higher-income earners, this is a levelling of what they were doing.

Once again, the extension of the universal basic credit may be something that you want to better target towards younger people, but I totally agree with you that this should go hand in hand with further training. Something that a lot of countries are doing, and did during the financial crisis, is to consider how to extend the education of young people who are about to graduate from university or other forms of education in



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order to ensure that they do not land in the job market now, where, as we have seen from previous crises, they usually start working in bad conditions, with lower wages and less recognition of the degree that they may have.

Gita Gopinath: I would add just a couple of points. We learned from the global financial crisis that targeted hiring subsidies help. If you have hiring subsidies targeted at people who are at risk of becoming long-term unemployed, it does work and did benefit jobseekers.

The second thing is in terms of the recovery. If the recovery involves public investment, and especially infrastructure investment, those recoveries also tend to be much more job-rich. One could think of a scenario where countries with fiscal space make public investments that also address the need for a greener planet at the same time as a job-rich recovery.

Q772 **Rushanara Ali:** How big does that infrastructure recovery plan need to be in a country like ours? For instance, we had an announcement of about £5 billion of infrastructure investment towards the recovery, but what scale is required to reverse the likelihood of a 9% unemployment rate, for instance, later this year?

Gita Gopinath: I do not have an immediate answer for you, but I know that our team in the IMF is going to be working on the new Article IV for the UK, and I am sure that this will be part of the exercise that is being done. We know that the multipliers on this kind of investment can be quite substantial, especially when we are in a period of low employment.

Q773 **Mr Baker:** Thank you very much for the evidence that you have given us so far; it has been fascinating. I want to explore your corporate view on preserving and recapitalising business, particularly with reference to what that means for the relationship between the state and individuals and private enterprise.

You will both be well aware of the range of interventions that the British Government have brought forward. How well have those been working? How long can they go on for before the burden of debt, both for the state and for private actors, becomes so great as to be counterproductive?

Laurence Boone: One of the striking things about this crisis is how similar the policies that each Government have implemented have been, across countries and across policies, both for people and for firms. For firms, there are three factors: mortgage or electricity bill deferrals, and the deferral of tax and other charges; a lot of guarantees; and, in some cases, equity injection.

If there is a slight remark to be made when we compare what countries have been doing, it would be that there have been more guarantees in the UK than in other countries, but that does not mean that there has been a massive distortion or anything like that at all. In the period that we have just come through, with a blanket guarantee, everybody did



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their best. In fact, guarantees are the single policy measure that has been most used by the largest number of countries.

What is difficult now is how to move away from this period where you provide this guarantee and into one where you want to let those firms that have a future thrive, and to let go of those that need to restructure. I do not have a definite answer to that, but I can give the direction that we are looking at.

The first thing is how you determine which firms are viable and which are not, and how Covid has affected the probability of firms' survival. Depending on the country, it may be the tax system that is used to look at the financial life of firms; it may be the banks, when it is very intermediary. The UK has used banks a lot to shelter firms.

The other thing is insolvency procedures. At the moment, we are comparing the speed and possibility of doing out-of-court solvency procedures or mediation—otherwise, we are going to see courts being very encumbered by this—and having a simplified fast-track process, for which there is no model in the world at the moment. Even the simplified procedure for US SMEs starts from Chapter 11, which produced something very complex for SMEs, so it is not applicable. A fast-track process with some out-of-court mediation, without stigma, for the people managing the firm is super-important, so that they can start again.

In terms of equity injection, we have a hub where we have policy briefs—

Q774 **Mr Baker:** I am sorry to interrupt you, but I want to come on to equity investment in a moment. I have one important follow-up question on what you have said. Very early on, you talked about the similarity of Governments' policies, which seemed to surprise you. To what do you attribute the similarity of different Governments' policies?

Laurence Boone: Our job—both mine and Gita's—is to identify best practices across countries and across economic episodes. Frankly, it is true that, for health, for labour and for firms, we learned a lot from the previous crisis in terms of how to shelter things. Policymakers have done this on an unprecedented scale this time.

Q775 **Mr Baker:** I wondered whether the OECD was going to take credit for having inspired Governments around the world to do similar things.

Laurence Boone: If that was a trap, I hope I did not fall into it!

Mr Baker: No, I am not setting any traps today. Professor Gopinath, how do you think the UK's policies are working and how long can they go on?

Gita Gopinath: As Laurence said, the UK policies are quite similar to what many other economies are doing in the form of credit guarantees, making sure that loans are more easily available. In the beginning, in the initial part of the crisis and during peak containment, clearly that was the thing to do.



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Giving firms access to more liquidity helps if the problem is a liquidity problem; it does not really help if it is a solvency problem. The more prolonged this crisis is, and depending on which sector the firm is operating in, you could see that this quickly becomes a solvency problem for many firms. In that case, there are only two options. One is debt restructuring, and the other is equity infusion or you provide them ways of raising their profitability by giving them wage subsidies and so on for a prolonged period.

The best possible policy, regardless of how the world plays out, is one where countries improve their bankruptcy procedures as best as possible. That would be the number one need of the hour. Regardless of how long this crisis goes on for, having sound, quick, fast-track bankruptcy practices, as Laurence said, is a big deal. Especially as the longevity of this crisis increases, that is going to be important.

There are some strategic or systemically important firms that would be hard to have exit and then re-enter in peacetime. Those would be ones where, if they fail, because they have very big linkages, many other firms that are tied to it fail. That would call for equity injections by the Government, making sure, of course, that taxpayers get the upside of the recovery when they make that kind of investment.

An important challenge for policymakers will be where, when a large number of loans have been made, several of these firms might go under. You want to avoid a banking crisis, so how do you make sure that that does not happen? Banks have many more buffers at this point and have been stress-tested. The fact that Governments continue to help firms helps with this situation, but this is going to be a challenge going forward, especially if this crisis lasts much longer.

Q776 Mr Baker: You have both given very full answers, which has been very interesting, but we are now running a bit short of time. I want to drill in on the key point. At different times, in written and oral evidence, you have both talked about the need for taxpayers to see the upside. Of course, I want to see taxpayers looked after but I want to see all investors looked after and getting a just return on their money.

It just strikes me that there is an issue here that particularly those businesses forced to shut down for longer—like the hospitality sector, to pick an example, or airlines—have their losses imposed on them, in a sense, because the disease was, in many cases, uninsurable and the state has forced them to be shut for longer; that is particularly the case for the hospitality sector.

Is there something of a tension there: that private investors are going to be suffering losses because the state's policy is to keep them closed? Are you not offering them a double whammy if you then say that the taxpayer must see a considerable upside to any bailout?

Gita Gopinath: First, even countries and regions that have not imposed lockdowns have seen activities go down. Regardless of what countries put



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in place, people have chosen to self-distance, and these sectors that include hospitality, personal care and so on have taken a big hit.

I agree that this is not a crisis that firms have brought upon themselves, but the question is what the best way is to move forward, to the extent that countries have good resolution mechanisms and the social costs of shutting down firms and reopening them are small. The longer this crisis goes on, that would be the strategy to follow. In places where that is not the case, that would require more Government support going forward.

The question of protecting taxpayers' investment is going to be important. The details of it and how exactly that is going to be done will matter in terms of the implications for the private investor. I am not giving specific details here but that will have to be carved out.

Q777 Mr Baker: You certainly indicated that it is a tricky problem. We are over time but, Laurence Boone, do you have a brief word on this particular tension?

Laurence Boone: I would just add that, as we said, we do not know how long this going to last. For some of those firms in the hospitality sector—airlines are different—a lot of Governments are looking at how to change the guarantees or loans that were made into tax deferrals or some sort of equity type of thing, so that you can give them another chance, help them get through and see if they can survive.

It will be unfair on some people, but wherever you can fine-tune the parameters to help filter those firms that are viable, that would have lived otherwise and that can reinvent themselves from those that would not have lived even before the crisis, that should help a little.

Q778 Mike Hill: It has been a very enjoyable session. Thank you, both. Many countries are easing themselves out of their lockdowns. They are setting out their own exit strategies and hoping to enter economic recovery. How responsive are economies proving to the easing of lockdown? What factors make an economy more responsive?

Gita Gopinath: Over 75% of countries are now in the reopening phase. In several of them, the number of cases of the virus continues to grow; despite that, there has been a reopening. What we are seeing in terms of the recovery is what I would call an uneven recovery, where some sectors are seeing activity return much more quickly.

On the other hand, sectors that require much greater contact, such as hospitality, personal care, leisure and tourism, have remained subdued. You can see that even in China, which is one of the countries that exited the earliest and has had the most number of days since reopening. We saw a quick increase in manufacturing and industrial production. Private consumption expenditure has remained subdued, although you are seeing a recovery.



In terms of how this recovery goes forward, a lot is going to depend on the news on the virus front and how much it gives people the confidence that, if there is going to be a second wave, it will be well managed and hospitals are not going to get overcrowded, because that will hold back spending.

What is important in terms of the reopening is continued widespread testing and contact tracing. We are seeing that Governments are able to do widespread testing and to communicate the facts about what is happening with the virus. If a lockdown has to be put in place, it is a smarter one that is more targeted to the particular locality where it is happening, or to particular vulnerable groups such as older people. Those might be the approaches that would work better and have less economic disruption as opposed to the first half of this year.

Q779 Mike Hill: Laurence, it is all about establishing and restoring consumer confidence. In general, has lockdown been restraining pent-up demand or will lifting the lockdown restrictions achieve very little until that confidence is restored?

Laurence Boone: You have raised a point that I would have added otherwise. What you say is very important. Once again, let me illustrate this with three points. If we compare Sweden and Denmark, very good studies show that consumption declined in Denmark by 29% during the confinement. In Sweden, which, as you know, did not have confinement to the same extent at all, it declined by 24%. The difference between the two is tiny, and consumer behaviour is super-important. A lot of consumers and households will have seen their saving ratio increase—not the lower-income earners but the others have much higher savings today, which we want to trigger into consumption.

As Gita was saying, consumer confidence comes from healthcare news, both real time and from the fact that you can be reassured about how further clusters will be treated. It is about massive testing and tracking, but also tracing and isolating, as well as protective equipment and physical distancing. The whole package is super-important, together with clear and transparent information on what is going on and how it is being addressed. That gives the most certainty on the situation.

I have two other quick points. In terms of monitoring what is happening on the economic side—and this is something that we do—it is super-important to use all the data that one can get from the digital economy, such as Google Mobility Trends or LinkedIn data. I am not saying that you have a stable relationship with GDP, since we do not have a long enough time series, but we very much see the correlation in real time with other data, and they show this V-shape recovery but at a much lower level than what we had before. They also help to contrast what is happening across countries, which is important.

Thirdly, the situation of the social relationship between employers and employees is key for a more rapid confinement. Let me give you the



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example of two of your neighbouring countries, and one sector in particular. The construction sector in Germany continued working into confinement because the relationship between social partners made workers confident that they could work safely, and the employers confident about their legal responsibilities. Cross the Rhine and go to the French side, where construction was totally shut down during confinement. Anything that can reassure employers about their responsibilities in terms of Covid, and employees about their safety, will be key in the face of the recovery.

Q780 Mike Hill: Gita, we have come on to the issue of stimulus. In terms of fiscal stimulus, would that backfire and result in inflation or cause debt dynamics to become unstable, if it is implemented far too quickly?

Gita Gopinath: Before I answer that, I just wanted to say one more thing about the recovery that we are seeing. Income support schemes have really worked. If you look especially at the recovery in the US in terms of low-income earners, we have seen pretty much a recovery to their pre-crisis spending, which tells you that the support that was given to them has helped.

To your question about the risks of fiscal policy, and policies in general, on inflation and debt dynamics, I would say that the prospects of runaway inflation are pretty muted at this point. We are looking at an environment where there is tremendous uncertainty. That is usually associated with some increasing precautionary savings and with a decline in investment spending, so we expect to see demand to remain subdued for a while. Therefore, inflationary pressures should remain subdued. Again, given the large output gaps or very low employment levels, pressures on wages will remain muted.

We have seen co-ordinated action by central banks and fiscal authorities, where the central banks have been purchasing Government debt on the secondary market. The question is whether that is a concern about debt monetisation that is going to end up having inflation through that channel. What is very important here is that, right now, it makes complete sense for central banks to do what they are doing, but if you are in an environment where you start seeing inflationary pressures come up, that has to be the number one target of the central banks. The independence of the central banks has to be maintained to make sure that goes forward.

In terms of whether these very high levels of debt somehow set countries up for major risks, there are a couple of factors of concern. Interest rates are expected to stay long, and this is a crisis that has growth picking up, even if it is only a partial recovery. That said, countries differ in terms of their pre-existing conditions in terms of their debt front and their fiscal space, and they will need a medium-term fiscal consolidation plan. That includes actions on both the revenue side and the expenditure side.

Q781 Mike Hill: Gita, you moved into the area of co-ordinating fiscal stimulus.



Finally, therefore, could I ask Laurence to comment on that? What benefits, if any, would the co-ordination of fiscal stimulus have?

Laurence Boone: There are spillovers between countries. If one country does fiscal stimulus, there is some leakage because they import from other countries. If the stimulus is co-ordinated across countries, the leakage goes both ways and everybody benefits from higher growth without necessarily a stronger fiscal stimulus. I would not be at the OECD if I did not say that this will give a kick to the economy, but we get much better results when we have fiscal stimulus and structural reforms at the same time.

Q782 **Harriett Baldwin:** I am going to try to touch on some of the subjects that have not already been touched on. When you get to this end of the session, it becomes harder and harder. I wanted to start with Professor Gopinath and ask about the timing in terms of reprioritising the levels of debt that the world has increased so sharply. Do you have a strong view as to when that reprioritisation should start to occur?

Gita Gopinath: As of now, countries are still in the midst of the crisis, so now is not the time to implement plans for consolidation, but now could certainly be the time for planning for what would look like a more medium-term fiscal consolidation going forward.

As of now, borrowing rates are very low, and we are expecting growth in many of these countries to pick up in 2021, which will help stabilise the debt levels. That itself will not be enough and there will be more that needs to be done to bring down debt to more pre-crisis levels. It is important to plan for that now but I would not say that now is the time to implement a consolidation.

Q783 **Harriett Baldwin:** The target should be to get back to pre-crisis levels. What about the euro area? Is there is a risk of this crisis reigniting some of the pressures that we saw in the financial crisis in the euro area?

Gita Gopinath: The response this time in the euro area has been really unprecedented and substantial. The actions by the ECB and the new schemes that they have put in place have had a material impact on countries in terms of their borrowing costs, and that has helped with their fiscal needs. Similarly, at the EU and European Commission level, there has been EU-wide support, with \$440 billion put in play in May. The proposed EU recovery plan being discussed is also quite substantial, at €750 billion. All these measures will help to trigger a sustainable and strong recovery in Europe and the euro area.

Q784 **Harriett Baldwin:** Picking up on Mike's questions around inflation risks, what is the IMF's view on the discussions that some countries are having around nominal GDP targeting?

Gita Gopinath: That has been discussed quite a lot even before this crisis. In an attempt to bring inflation back to target, the question is whether we need to redefine the target and talk about returning to



nominal GDP. There are communication challenges associated with that. It is a proposal to consider but it is not obvious that it will deliver the silver bullet to bring inflation back up to the level that you want it to be.

What is clear is that, given what central banks have learned from the previous crisis, it can be particularly challenging to bring inflation back up to your target. My sense is that they probably wait until they see inflation durably above target before they start moving on interest rates.

Q785 Harriett Baldwin: Dr Boone, in terms of the OECD's view, I presume you agree that, at some point, economies are going to have to start dealing with their fiscal situations. Do you have a preference as to whether that is done through tax rises or through spending cuts or freezes? What is your view at the OECD on that?

Laurence Boone: There is no one-size-fits-all view on this. I would say a couple of things. It is quite likely that, if the economy gets better in 12 or 18 months' time, there will be pressure to adjust and consolidate public finances. However, at the same time—and this is what we discussed at the beginning—there will likely be pressure for more healthcare spending and for more care spending. Across the world, care homes were in very dramatic situations. There will be pressure on education and retraining. There is also pressure on climate change and energy transition.

In the '90s, there were a lot of public spending reviews. At the OECD, we think that there will be scope to do such spending reviews. For example, Canada did a very good one in the '90s. At the same time, we also talk a lot about the perception of inequality. There should be an opportunity to review the tax system in order to ensure that it is progressive, and perhaps to allow a more climate-consistent tax system, like the one that the UK has. I am not even talking about digital taxation. For me, it is not just about taxes or spending but about having a block and ensuring progressivity.

Q786 Harriett Baldwin: I think Canada did a zero-based budgeting exercise in the '90s. That is my recollection. Is that what you are referring to?

Laurence Boone: Yes. You may remember that, at the same time, they had signed a trade agreement with the US, and their currency was also depreciating, which helped with the boom in exports. That reinforces the case for looking at things as packages rather than in isolation.

Q787 Harriett Baldwin: Looking at the UK from your perspective at the OECD, what steps should the Chancellor follow first as he thinks about how we pay for the increase in our deficit?

Laurence Boone: I am not in his shoes; I am not in the Treasury. However, perhaps this is an opportunity for me to add a couple of things. We have talked about the long-term trends of digitalisation and energy but not about demographics, and there is a lot to do on the pensions and care side of the equation.



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At the same time, both the digitalisation and what we have seen in terms of social support around some categories of people probably also deserve to be revisited. I am thinking in particular about two things: first, as we discussed, universal credit income; and, secondly, the relationship between the different levels of Government and how much tension has been triggered by the crisis.

Q788 Harriett Baldwin: Professor Gopinath, I wondered if you had any thoughts on what steps you would be taking to address the ballooning deficit, if you were Chancellor of the United Kingdom.

Gita Gopinath: Again, I do not want to pre-empt my colleagues, who are going to do an article for a mission soon, and their discussions, but broadly on the question of how Governments can bring down debt levels, one is the unwinding of the stimulus that has been put in the system. You are going to have to do that, once the crisis is over, and the temporary measures have to be unwound.

In terms of which specific countries, it depends on where their tax or spending system has deficiencies. For instance, some countries have very high spending-to-GDP ratios; some of that is just wasteful spending that they need to cut back on. You could see a situation where, with very low fuel prices going forward, some countries have very regressive fuel subsidies that can be rolled back. On the flipside, carbon pricing and carbon taxes are another tool that they can use.

Q789 Harriett Baldwin: You are being very tactful. We have had Article IV reports done on the UK system in the past, so it would be really helpful to the Committee if you focused on the UK example.

Gita Gopinath: Yes, we did have an Article IV consultation with the UK in 2018, but my colleagues at the IMF would be quite upset if I were to make specific recommendations at this point without them going through the 2020 Article IV. We will have those for you but just not today.

Q790 Harriett Baldwin: When will we get them?

Gita Gopinath: It is in the works, so maybe in the next few months.

Harriett Baldwin: By the autumn?

Gita Gopinath: Let us see.

Laurence Boone: I would just add that the OECD survey is completed, so you should get it in the summer.

Q791 Harriett Baldwin: What date in the summer?

Laurence Boone: I do not know. It depends on the Treasury.

Harriett Baldwin: We can ask them.

Q792 Ms Eagle: Given that both the OECD and the IMF are now very interested in promoting inclusive growth and we have to move to a more



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sustainable environment, not least because the origin of the virus is in the exploitation of nature and species destruction, which is already occurring due to climate breakdown, how can that be done, given the structure of economic theory that we have at the moment, which basically tells Governments to keep their hands off the market and then redesign and balance things out afterwards?

Surely, we need, for example, a much more interventionist industrial policy or a more interventionist policy to promote a green industrial revolution. It will not just happen spontaneously. That seems to go against the economic theory that has been the king for the last 40 years. Gita, do you have any thoughts on whether we need a more interventionist state presence?

Gita Gopinath: What we have learned over the last 40 years are many examples of market failure, and we all understand that very well. For instance, a very important aspect for greater equality is greater access to opportunity. This comes when you think about education, healthcare and skill training. We all know that this is not something that is provided just by the free hand of the market; this is also how modern capitalism works. I do not necessarily see a tension there and there is a lot more that countries can do on that front in making sure that people have equal opportunities.

Similarly, when it comes to inequality, for instance, that comes because of a concentration of corporate market power, it is another example of market failure, which is the fact that it could reflect, but not necessarily, a failure of market power, with a monopoly power in markets. Again, that is why we have antitrust and those regulations in place.

These are the kinds of things going forward. Inequality shows up on many fronts: in terms of access to opportunity, in terms of discrimination, and in terms of making sure that firms do not have monopoly or monopsony power in markets. All those sit very well with the other virtues of having a market economy but those have to be addressed.

Q793 **Ms Eagle:** In a more positive way, there are public goods, are there not? We could think about vaccines or R&D for health purposes, for example, or having a circumstance where we are not releasing pathogens into the air by burning forests, or living too close to or exploiting animals, which create the circumstances where these pathogens can come into being.

However, we do not have a very robust international commentary on the right to provide public goods. We have, all too often, got into socialising the risks when they materialise and privatising the rewards of economic activity.

Laurence, how can we make sure that that is not the case going forward, so that we can begin to rebalance the way our societies operate? We cannot just rely on the invisible hand of the market, can we?



Laurence Boone: As Gita mentioned, there have been interventions in the past to correct for market failures. A huge change is being brought with this crisis, which is that the role of Governments in all sectors has massively increased de facto, because of all the support that has been brought. It would have been a lot easier to put that in place than to withdraw it. Therefore, there will be occasions or opportunities, depending on how you see this, for Government intervention in some of the things that you mentioned.

Once again, the demand for health and for more climate resilience will be very high and, on this, UK climate action has really been a leader in the action plan for dealing with climate change. There might some missing targets, but it is important. We are doing quite a lot of work to assess the impact of environmental protection on productivity. It has been published and shows that, as it stands, there has been no negative impact on productivity or employment, which should raise people's confidence that we can continue in that direction, having a cleaner and more sustainable economy and at the same time remaining productive.

Q794 **Ms Eagle:** Is there a role for things like a citizens' dividend, which Mariana Mazzucato has talked about, or public wealth funds like the one done in Alaska, to try to socialise some of the benefits of success when it is being funded by Government actions such as R&D and innovation, rather than having all that success privatised into the corporate sector and communities not really being able to share in it? Are you looking at some of these new mechanisms to try to encourage a more equitable distribution of benefits from economic activity?

Laurence Boone: There have been a couple of initiatives to move into that direction. One that I would mention is the Business for Inclusive Growth initiative that started with some businesses across the world, including some UK firms, where you can see some of the first firms moving towards governance that involves people much more.

It is true that, around the world, we are seeing some policy variations where employees can participate in the benefits of the firm more widely, but it is also done in a number of countries. Something we did not have time to discuss is the good governance of firms that are being partly nationalised as well. In doing that, one wants to make sure that the taxpayer also receives their money back when the Government exit the firm in which they have injected funds.

The one thing to keep in mind—and perhaps I will make the link with monetary and fiscal policy here—is that the allocation function of policymaking is very much with fiscal authorities, which are democratically elected, and much less with technocratic bodies. The example that comes to mind is the central bank, for example, when people talk about central banks providing cash for direct investments. They should remain independent from this point of view.



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There is some analysis that deserves to be looked into. Some of it has already been put in place. Others have to make sure that democratic rights are preserved.

Q795 Ms Eagle: Gita, can this acceleration into greener and more sustainable areas for the economy be accelerated by public policy and new structures such as, for example, a public wealth fund, so that we can get there faster and try to take some benefits from the opportunities that have been put out by the interventions that we have had to make to deal with the pandemic?

Gita Gopinath: Absolutely, yes. This is a crisis that has shown everybody what can happen when you have a national disaster of a magnitude that we have not seen in a while. This is also not going to be the last one. Given the projected levels of carbon emissions and the heating of the planet, these risks are going to be out there. There is no option. Countries have to deal with it.

This is an opportunity because, for many countries, we can see a very good argument for them to undertake public investment spending, because this is going to be a crisis where people will hold spending back for a while; the private sector will hold back spending for a while, so there is a role for public investment. Greening the environment and reducing carbon emissions will play a very important role. Public green infrastructure has to be an important part of countries' recovery plans.

Secondly, if you want to incentivise people to shift towards greener choices, the public sector will have to play an important role. You have to make sure that there are sufficient alternative clean energy sources available; otherwise, there will be no incentive to move. You then combine that with carbon taxation and carbon pricing. You will require these kinds of interventions to bring about the change that is needed.

Chair: We have survived not having to put up with a vote, which is very good news, but we are still, nonetheless, at the end of our session. Thank you both, Gita and Laurence, very much indeed for the evidence that you have provided to us today. You have answered our questions excellently and in detail.

Perhaps one of few positive features of the crisis is the fact that people are now more normally drawing themselves together by using technology and bringing people together from far-flung and different places, and we have certainly benefited from that in being able to benefit from your evidence today. Thank you very much indeed for giving us your time.