

Turning hope into reality

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For the first time since the pandemic began, there is now hope for a brighter future. Progress with vaccines and treatment have lifted expectations and uncertainty has receded. Thanks to unprecedented government and central bank action, global activity has rapidly recovered in many sectors, though some service activities remain impaired by physical distancing. The collapse in employment has partially reversed, but large numbers of people remain underemployed. Most firms have survived, albeit financially weakened in many cases. Without massive policy support, the economic and social situation would have been calamitous. The worst has been avoided, most of the economic fabric has been preserved and could revive quickly, but the situation remains precarious for many vulnerable people, firms and countries.

The road ahead is brighter but challenging. At the time of writing, the global death toll has risen to $1\frac{1}{2}$ million, subsequent waves have hit many countries and the first one continues unabated in others. While waiting for effective vaccinations to be widely distributed or some breakthrough in

treatment, hopefully in the course of 2021 for most, managing the pandemic will still impose strains on the economy. Economic activity will continue with fewer face-to-face interactions and partly-closed borders for a few more quarters. Some sectors will regain strength, others will be on standstill. Developing or emerging economies, where tourism is important, will continue to see their situation deteriorate and will require more international aid. Policies will have to continue to sustain economic activity forcefully, all the more so since the end of the health crisis is in sight.

The global economy will gain momentum over the coming two years, with global GDP at pre-pandemic levels by the end of 2021. After a sharp decline this year, global GDP is projected to rise by just over 4% in 2021, and by a further $3\frac{3}{4}$ per cent in 2022. Scientific progress, pharmaceutical advances, more effective tracing and isolation, and adjustments in the behaviour of people and firms will help keep the virus in check, allowing restrictions on mobility to be lifted progressively. Importantly, policies to support jobs and firms, in place since the beginning of the pandemic, will enable a faster rebound when restrictions are lifted. Together with reduced uncertainty, these improvements should encourage the use of accumulated savings to fuel consumption and investment. The exceptional fiscal relief provided throughout 2020 – and needed beyond, will pay off handsomely. The rebound will be stronger and faster, as more and more activities re-open, limiting the aggregate income loss from the crisis.

We project the recovery will be uneven across countries, potentially leading to lasting changes in the world economy. The countries and regions with effective test, track and isolate systems, where vaccination will be deployed rapidly, are likely to perform relatively well, though the overall weakness of global demand will hold them back. China, which

started recovering earlier, is projected to grow strongly, accounting for over one-third of world economic growth in 2021. OECD economies will rebound, growing at 3.3% in 2021, but recovering only partially from the deep 2020 recession. A striking feature of these projections is the shrinking contribution of Europe and North America to global growth, though that may reverse somewhat should vaccine distribution be fast and efficient.

The outlook continues to be exceptionally uncertain, with both upside and downside risks. On the upside, efficient vaccination campaigns and better co-operation between countries could accelerate the distribution of the vaccine worldwide. Conversely, the current resurgence of the virus in many places reminds us that governments may be forced again to tighten restrictions on economic activity, especially if the distribution of effective vaccines progresses slowly. And confidence would take a hit if vaccine distribution or secondary effects proved disappointing. The toll on the economy could be severe, in turn raising the risk of financial turmoil from fragile sovereigns and corporates, with global spillovers.

Despite the huge policy band-aid, and even in an upside scenario, the pandemic will have damaged the socio-economic fabric of countries worldwide. Output is projected to remain between 4 to 5% below pre crisis expectations in many countries in 2022, raising the spectre of substantial permanent costs from the pandemic. The most vulnerable will continue to suffer disproportionately. Smaller firms and entrepreneurs are more likely to go out of business. Many low wage earners have lost their jobs and are only covered by unemployment insurance, at best, with poor prospects of finding new jobs soon. People living in poverty and usually less well covered by social safety nets have seen their

situation deteriorate even further. Children and youth from less well-off backgrounds, and less qualified adult workers, in particular, have struggled to learn and work from home, with potentially long lasting damage.

Governments will have to continue using their policy instruments actively, with better targeting to help those hardest hit by the pandemic. The fact that vaccines are in sight suggests that this is not the time to reduce support, as was done too early in the aftermath of the Global Financial Crisis. Rather it confirms health and economic policies must work hand in hand. Public health measures have to double down to limit the impact of cyclical virus outbreaks and the associated restrictions. It is also crucial that policymakers ensure continuous fiscal support to keep sectors, firms and the associated jobs alive. The lessons from the last nine months are that such policy action was and remains appropriate. Monetary and fiscal policy will need to continue working vigorously in the same direction, at least as long as the health crisis threatens otherwise viable economic activities and employment.

Heightened policy activism need not be a concern if deployed to deliver higher and fairer growth. Extensive fiscal support is pushing public debt levels to record highs, but the cost of debt is at record lows. A striking feature of the outlook is the absence of correlation between the extent of fiscal support and the resulting economic performance, suggesting not all has been used wisely. Unprecedented monetary and fiscal support cannot be wasted, it must be funnelled into stronger and better economic growth. There are at least three priorities for policymakers. First, investing in essential goods and services such as education, health, physical and digital infrastructure. Second, decisive actions to reverse durably the rise in poverty and income inequality. Third,

international cooperation: the world cannot solve a global crisis through single-country and inward looking actions.

Redirecting public spending towards essential goods and services would signal that governments have learnt lessons from the crisis. The need for enhanced resilience should drive public and private investment in health, education and infrastructure. Better health resilience is not just about vaccine distribution and beds in intensive care units, it is also about health prevention and affordable access to healthcare for all. Enhanced resilience is also about investing in people skills, ensuring better education and labour market outcomes, and ultimately higher trend growth and wellbeing. Walking that talk starts with more and better-targeted resources for early years of education, better paid and trained education staff, as well as better lifelong training support, especially for vulnerable groups including parents in difficulties. Too often previous crises have resulted in lower investment and lasting infrastructure gaps, including in digital and decarbonised energy. This needs to change.

Support to the most vulnerable, especially children, youth and the less-skilled, who have not been fully sheltered from the crisis, will have to intensify. Education systems can improve in many countries, leveraging on lessons drawn from the crisis. Governments must invest to ensure all households, teachers and pupils can access good quality broadband and are equipped for digital education, especially for those in deprived environments. The crisis has shown the urgency to gear up digital skills. It has also unveiled shortfalls in social support systems. Fiscal policy should be better directed to vulnerable groups outside the usual welfare system and who are not eligible for the additional help provided so far, for their own benefit and the benefit of society as a

whole.

Finally, international cooperation has faltered in recent years, just when it is needed more than ever. The “Global” Financial Crisis was mostly a crisis of a few advanced economies, but triggered an unprecedented cooperative response. The pandemic is the first fully global crisis since World War II: it has been answered by massive national responses, but closed borders and little cooperation. Protectionism and shutting frontiers are not the answer: they prevent the distribution of essential goods throughout the world and penalise economies that rely on their participation in global value chains to catch-up. This must be reversed. Wide, rapid and generous production and distribution of effective medical treatments and vaccines must be organised for all countries. Multilateral fora must enhance action on debt transparency and a moratorium where needed, while supervisors need to pay high attention to the indebtedness of firms. The world must avoid the health and economic crisis also becoming a financial one.

When asked what the post-Covid world will look like, let's hope the answer will be: “perhaps mostly the same, but a little bit better”.



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