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Economic policies for COVID-19

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ABSTRACT

Economic Policies for COVID-19[1]

This note describes some of the early policy developments in the UK and the way in which the framing and understanding of a novel economic problem evolved to include a focus on livelihoods combining social protection and business support orientations. It highlights various points including the rapid iterative nature of policy development based on consultation in the face of uncertainty, as well as a trade-off between risk-sharing with commercial banks to limit adverse selection and the rapid prevention of insolvencies. We consider some of the policy-making lessons to date and conclude with suggestions for issues that policy makers might consider to support workers in the near and medium term.

JEL Classification: A1, D7, D8, J00, H, P1

Keywords: COVID-19, furlough, fiscal response, labour market policy, workers, social contract

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[1] I am particularly grateful to Ken Mayhew, Heidi Allen and David Stuckler for comments on earlier versions. To reiterate, this note is no new empirical analysis but rather a contribution to discussions about the economic understanding of public policy.

1. Introduction

COVID 19 has been described as a twin pandemic, for health and economic activity. It is a moving target that throws up new decision problems for economic advisors to government on a daily basis. In this briefing note, partly informed by discussions with colleagues in government as well as those in academia, we describe some early emerging experience and offer ten recommendations. The policy experience on which we draw is largely from the UK though parallel issues can be found in many other high income countries.[2] Following a short discussion of this experience, which we hope to discuss in more depth and comparatively elsewhere, ten recommendations for economic policy making related particularly to employees are proposed.

2. Some Policy Experience

In March 2020, the UK government took a number of dramatic steps to bolster economic activity as it was threatened both by the risks of COVID and measures to reduce transmission of the virus. The Bank of England on 19 March reduced its base rate to 0.1%, the lowest rate in the central bank's 400 history and announced it would also support liquidity in the economy by buying government bonds. Given the ambiguity facing firms and consumers about the impacts and duration of the COVID pandemic, the emphasis of these activities appeared to be geared more towards positioning the economy to benefit from recovery when the time came rather that changing behaviour in the immediate term.

At the same, the Chancellor of the Exchequer announced starting March 11 what has been described by the media as three budgets in nine days. The first announcement comprised a package of fiscal measures including government underwriting of 80% of loans to businesses by commercial banks, sick pay rebates to small firms, abolition of business rates to retailers, small cash grants to small businesses, additional contributions to a local authority hardship fund and statutory sick-pay for anyone in self-isolation. These measures were described as costing between £30-£50 bn while the loans to large businesses, announced in March 17, were capped at £350 bn which potentially sounded large given the government's total spending of £848 bn in 2019.

In the days that followed, a number of concerns began to arise. For one thing, there was some concern about what was seen as a bias towards business and away from employees, a point made by union representatives at national level. Secondly, there were several concerns about loans schemes to businesses. Would they be attractive to directors if they had to spend a couple of years paying them back? Would banks be interested in making the loans if they had little way of judging whether a company would be solvent in even a few months' time?

On March 20, Chancellor Sunak announced further measures including a temporary employment subsidy of 80% for furloughed workers up to £2500 per month, a move that was without historical precedent in the UK.[3] In doing so, he noted 'this is not a time for ideology and orthodoxy…I want to reassure every British citizen this government will give you all the tools you need to get through this.'[4]. There were, however, concerns about those who were

[2] Issues related to funding in Europe and in low and middle countries are discussed in Dell'Arricia et al (2020) and Bénassy-Quéré et al (2020).

[3] Some figures for responses from the Office of National Statistics faster indicators are presented in Table 1 at the end. By April 5, about one quarter of responding companies had temporarily ceased trading and of those remaining, 68.9 % had either laid off staff or decreased staff.

[4] BBC 2020, March 17.

self-employed, about 5m workers, or on zero-hours contracts in the gig economy (another 1 m people) – and it took another fortnight to design a policy for the self-employed.

These narrowly defined economic policy changes which suggested the need for borrowing and funding on a scale that were not expected from a conservative government should be set against the human development crisis to which they were a response. On the health front, epidemiological models were suggesting possible mortality rates of between 1%-3% which if simply replicated across the population could have resulted in a doubling of the country's mortality. Concerned about the limited impacts of social distancing by keeping two metres away from others, the government announced on March 23 rules to limit trips away from home to one per day for exercise, work if home-working was not possible and occasional visits to food retailers – the UK's version of lockdown.

At the time of writing, some lessons for and about policy-making were already beginning to emerge. The human costs, due to the mitigation of exposure to COVID 19 either voluntarily or by following government instructions, are but not included in the models on which the government relied, Manski (2020). Indeed, several economists have noticed that it has taken some time for policy-makers to find ways to frame and articulate the trade-offs, opportunity costs and actual financial costs of response in ways that reflect them accurately. As the economic philosopher, John Broome noticed, the rule of rescue is a strong motive that dominates others and as a result, individuals tend to be more egalitarian in the health domain than in others. In any case, it has become clear that the shift from concern about prospects of a recession to a potential existential threat to national and global economic systems was rapid. Patterns of impact were and will continue to be unevenly distributed across the economy and range from the decline of revenues and substantive business opportunities in passenger transport, restaurants and other leisure venues through to elevated demand for food, some aspects of health and communication services.

In many key dimensions of quality of life, what people are able to do has been constrained, Anand et al (2011). Routine health services were postponed by hospitals and Janke et al (2020) have documented how chronic illness is set to rise as incomes fall. Parental withdrawals of children combined with reduced teacher numbers through illness and self-isolation contributed to the closure of schools to most parents though this brought into stark relief their additional roles of facilitating child-care for working parents and mitigating consequences of child-poverty through free school meals. However, the facts that private schools were able to continue with less disruption, educated parents were better placed to provide home schooling while poor households may be sharing online access have all contributed to poorer and more unequal education, Burgess and Sievertsen (2020). For the most part, the small number of chains that dominate food retail have prevented price-gouging and been able to manage demand and access to food items though fresh fruit and vegetables produced within country may yet experience price spikes if migrant and other replacement labour is unable to harvest crops in the normal way. Concerns about gender and other inequalities have also been significant. Women's charities have reported dramatic rises in cases of domestic abuse and otherwise empty hotel-chains across Europe have made rooms and food available in response. The police have also reported new forms of online fraud. For the moment, housing evictions appear not to be a major issue of concern as government early on negotiated with banks 3 month mortgage holidays and subsequently similar protection for tenants.

The UK is thought to embody a version of capitalism somewhere between the US and European models and one of the most important research questions concerns the success with which

different economic systems are able to protect the various dimensions of human wellbeing. Currently UK government and economy are responding to the shock in several ways: initial policy proposals have been modified in response to representations by business, unions and civil society; the effective labour force has been expanded flexibly by the NHS calling health-care professionals out of retirement, a government call for volunteers quickly oversubscribed and the employment of unemployed workers by food retailers. The experience with commercial banks has been more mixed and suggests that moral suasion has some use but limits also. The rapid agreement to mortgage holidays is an important contribution to the prevention of wide-scale evictions but the application of normal lending criteria to business lending has had some limiting impacts on the effectiveness of loan schemes for business. There are problems of asymmetric and uncertain information which might be better addressed by debt-for-equity provisions which are only workable for larger companies. To save smaller businesses, addressing the drying up of cash-flow is key, and doing this may involve a trade-off between standard checks and balances which and the maintenance of liquidity, which in turn might require consultation between political parties and between treasuries and national audit offices.

The emphasis on UK policy has been to hold as many of the economic relations together in the immediate term, to put the economy into hibernation while the health pandemic is brought under control and plans are put into place to unwind stay-at-home orders.[5] Support for these is high at time of writing but likely to decline as time goes on. Epidemiologists make a plausible case that a policy of testing tracing and isolating is key to a successful to normal (economic) life (see also Chen and Qui (2020) and Quah (2020)). In addition, and in some countries, there is a move to open up primary schools which have a low connection to transmission. It there is to be phased unwinding, there are different considerations that it should take into account. One is to focus on the age profile of those with greatest mortality risk which suggests finding more effective ways of shielding of those close to retirement age and above. Another is to focus on job roles – those in the broader frontline which includes shop workers, bus drivers, the police and waste disposal workers as well as medical and care staff who meet with members of the public on a repeated basis. Yet another is to focus on activities – and consider ways, where they exist, in which they could be adapted – low density sittings in Parliament being one approach. In any case, protection is warranted both on grounds of society's duty to protect employees and by the fact that some of these roles are primary transmission mechanisms. While steps have been taken to protect some staff, it seems that it would be socially optimal to encourage more innovation and resourcing of the protection of this broad frontline.

It has been hoped that there will be a v shaped recovery and perhaps this is still feasible but it is also likely that the real economy will take time to recover. China's recovery is being described as sluggish: consumers are likely to be cautious in their spending, firms will be waiting to see if investment plans need to be revised and exporters will still be suffering from the impacts of a global lockdown – with some exceptions including those manufacturing relevant medical supplies. In the UK, employment levels have often taken about five years to recover from spikes in unemployment. Following the last financial crisis, the US economy took about seven years for employment levels to recover. Furthermore, this time round, recovery will take place against a background of increasing use of artificial intelligence with more hope than clear visibility about the quality of the new jobs that will emerge as a result. Even if the stock market has already recovered to some extent, the real economy (or least certain sectors)

[5] Policy measures taken have not differed so much compared with those in Germany, Bosch (2011) and Bofinger (2020) with perhaps the exception that reduction of working hours which is not being used as a policy instrument in the UK.

may not do so as quickly and so we should be preparing now policies for the prospect of millions of workers without meaningful access to decent employment for years to come. In this final section, we offer therefore ten recommendations for policies that should be considered to alleviate some of the worst impacts on workers.

3. Priorities for Economic Policy

Several lessons and issues for economic policy-makers are beginning to emerge. In the first place, the decision problems faced by policy designers are characterised by uncertainty as well as risk, and have evolved rapidly over time. What seemed like the prospect of recession transformed within weeks into concerns about an existential risk to economic systems. While the COVID 19 pandemic has been described as a rare kind of shock to the economic system, it constitutes the second global economic crisis in just over a decade. In response, the UK has developed novel policies, borrowing from elsewhere, including German experience from the financial crisis, and differential timings have enabled all countries to learn from each other as events unfold. However, the approach to policy-making (both in health and economics) around the world can best be described as reactive and it seems appropriate to suggest that in future, economists in government and academia devote more attention to the preparedness for such economic shocks.

Secondly, responding to the pandemic has raised questions about how most rapidly and effectively economic agents can be supported. Choosing mechanisms, such as universal credit and the taxation system with which firms and workers are familiar has emerged as an important consideration. However, this has left open some important gaps, such as the coverage of workers who are undocumented (about 7 m workers in the US) or the treatment of those in the UK on zero-hours contracts not currently protected by job retention schemes. Related also to policy delivery are questions about the efficacy of government support for firms being tied to risk sharing with commercial banks. In principle, the requirement that banks keep 20% of the loan default risk incentivises them to address problems arising informational asymmetries such as adverse selection. However, normal banking lending processes take weeks and for a number firms this may be too long. Moreover, given the radical uncertainty about the nature and speed of any economic recovery, it is inherently difficult for banks to make commercial judgements about loan viability. As a result, the UK government has just switched to a simpler system, similar to that used in Switzerland, in which smaller firms make a simple application and government assumes all the risk.

Finally, at a more foundational level there are psychological and political changes underway that will indeed have profound impacts on how we think about the economy for years to come, Carlin (2020). The sustained efforts of health-service workers to save life, and the personal risks being taken, are, for example, being applauded (literally) by populations around the world who have for weeks been told to stay home and save lives. At the same time many businesses have embraced offers of support from government and all of these experiences will inevitably cause a rethink of ‘what we owe to each other’ as the philosopher Tim Scanlon has put it. Hopefully, societies and economists will focus more closely on the human outcomes of economic activity and in any case, basic facts about the interactions between markets and governments will need to be updated. In any case, and gainst this background, we conclude with some more concrete steps that need to be considered.

1. Scrutinise all government policies and expenditures in terms of contributions to employment.

Given the massive amounts of un- and underemployment that now exist, helping households to recover their ability to earn a living through productive work must be a priority. In general growth may serve to reduce or increase employment so scrutinising more explicitly likely employment implications of major government projects. Increasing references to livelihoods in the media suggest that their protection has quickly risen up in salience and significance for both voters and policy makers. Furthermore, there is evidence from macro-economic simulation models, Faia et al (2013) that polices such as hiring subsidies (see also 2 below) can be cost-effective.

2. Reduce costs to business of employing workers.

Already governments have picked up substantial responsibility for the costs of employees in the short term through furlough schemes. There may well be a need to extend this support longer term and, without a rapid global recovery, which is not looking very likely at time of writing, there may be a continued need to reduce the cost of employment to business. Merkl and Weber (2020) also argue that hiring subsidies are likely to be valuable in this case as they are unlikely to compete with hires that would have been made otherwise, and are automatically directed to those parts of the economy that are recovering.[6]

3. Protect front-line, customer facing workers.

There are many types of front-line workers - in health, care, transport, schooling, retail and the police for whom the work place now offers a significant additional hazard. The nature of associated hazards varies significantly with risk and workplace setting suggesting that a variety of mitigation measures need to be developed. This has happened to an extent but it is possible that more can and should be done to protect some categories of workers in particular settings – for example bus drivers working in areas where most passengers pay for fares in cash. Unions representing a wide range of clinical and non-medical professions and trades have played an important role in identifying details of work-place interactions that if modified could make significant contributions to the reduction of transmission. Such modifications involve an appreciation of detail that could be a blindspot in strategy formation (see also West et al (2012).

4. Monitor and address employment and income inequalities due to sex, ethnicity and disability, age and educational status.

Long standing inequalities can be associated both with health outcomes associated with COVID 19 as well as the lockdown to reduce transmission. Monitoring carefully and in detail both sorts of inequalities may give clues both about priorities to be addressed as well as pathways to addressing them. It is said that history teaches that will always be financial crises but they tend to have their own character. Generally those in lower paid, part-time work and in certain ethnic grouping suffer disproportionately and we know already that other low paid and zero hours contract workers in restaurants and hotels are suffering this time around.

5. Encourage constructive engagement between local and national government, employee representatives and business.

[6] Such policies probably need to be time-limited and undertaken when unemployment is high if they are to avoid deadweight costs.

The general impression to date, is that labour unions in the UK have made positive contributions to the protection of employees and their relations with employers in the workplace and also policy-shaping at national level. Presence in the workplace combined with voice at national level provide a basis for informing workers of rights and responsibilities as well as shaping government thinking and policy. Constructive relations between these parties are a valuable economic asset and should not be undervalued, Keep and Mayhew (2011).

6. Encourage workers and students to address structural change needs by developing skills in shortage areas such as IT and STEM.

The fact that firms and individuals have been forced to go online indicates the way in which economic trends already underway are accelerated by the crisis. Different countries may have different shortages (Manning (2019)), and these shortages may be quite specific (for example IT skills in lower paid business support workers) but governments could help individuals make appropriate switches. It is, however, perhaps worth studying in more detail what the needs really are that arise from the digitisation of economic and social life. Older workers might need to develop basic IT skills and confidence whereas younger workers might need more experience of using developing related non-cognitive skills – for example using IT to support team working. (A broad-brush approach not attuned to individual and cohort differences in workers might not be effective.)

7. Prepare plans to deal with large numbers of 'discouraged' workers that may include volunteering and skill development.

A substantial increase in workers who would like work but are not actively looking ('discouraged workers') is likely if the rise in numbers of those unemployed is not reversed rapidly in coming months. There is evidence the issue can be significant (eg Dagsvik (2013)) and if experience from the previous financial crisis, or previous unemployment spikes in the UK over the past century can be a guide, it might take between five or ten years for employment rates to recover. Some limited ability to train or volunteer whilst in receipt of social protection could contribute to the quality of life of such individuals.

8. Embrace public deliberation and avoid siloism and reactivity in policy design.

Social and other digital media are facilitating public deliberation of social and economic priorities on a daily basis in a manner that is rare in economics but perhaps conducive to the transparency and inclusiveness that Sen (2009) and others have argued for. The trade-offs between livelihoods, and lives, around the world are becoming more fully understood and articulated. There is also evidence that government consultation with subject experts needs to be broadened out beyond the obvious. For example, pandemic modelling in future is likely to combine inputs from economics as well as from epidemiology: conversely economic policy design might include inputs from social welfare and behavioural psychology. The need to avoid siloism in the development of relevant expert advice has been increasingly acknowledged in health and seems important also in economics given the practical uses to which the subject is put, Kaufman et al (2014).

9. Promote international trade but also develop some within country core manufacturing capacities.

Early on in the pandemic, it was suggested that value chains may be reduced as a method of making countries more resilient to such shocks. Currently, the dependence on out of country inputs from personal protection equipment to skilled workers might suggest that countries will develop some manufacturing capacity that can be rapidly switched over to emergency supplies should the need arise. In any case, the role of trade and travel in particular and its contribution to human safety needs now to re-evaluated given the different approaches adopted by national governments and the World Health Organisation.

10. Pursue business support policies that accelerate the creation of new environmentally sustainable infrastructure.

It has been suggested that Europe needs a new kind of Marshall Plan[7] as the post WW II experience was positive for economic growth particularly for Germany the UK and France. What are the infrastructure needs at this point? However slowly, the world is converting to a low carbon economy so it is worth asking whether governments and businesses should now seek to accelerate this process perhaps by helping to make homes more energy efficient or expediting the roll-out of national infrastructure for electric vehicles, which will in turn accelerate the use of vehicles based on alternative fuels. Impacts on unemployment short-term are not likely to be large but it may still make a contribution worth having.

If we allowed ourselves an eleventh priority, it would be the acceleration of tax reform so that a fairer balance of taxation from online business resides in the communities where individuals live and work. This has been on the OECD's agenda for some time but if the crisis accelerates advantages to digital-rich businesses, then resolution of the issue will become a more pressing priority. In any case, the above recommendations suggest there are several courses of action that government can and should consider to protect and sustain livelihoods in the event that national economic recoveries are slow.

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[7] Crafts (2011) suggests the Marshall Plan's direct impacts were probably positive and modest and that less direct impacts might have been more beneficial.

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Table 1 Workforce related Actions taken by firms continuing to trade by industry.

Which of the following measures has your enterprise taken to cope with the impact of coronavirus (COVID-19) on its workforce?

Industry	Increased working hours	Decreased working hour	Laying off staff in the short term	Recruiting staff for short term	Other	No measures have been taken
Manufacturing	16.2%	28.7%	32.6%	10.5%	24.9%	18.5%
Water Supply, Sewerage, Waste Management And Remediation Activities	11.6%	31.9%	52.2%	7.2%	14.5%	11.6%
Construction	5.1%	34.4%	63.6%	1.0%	15.9%	12.8%
Wholesale And Retail Trade; Repair Of Motor Vehicles And Motorcycles	12.1%	29.5%	45.0%	10.7%	22.7%	14.6%
Accommodation And Food Service Activities	12.6%	50.5%	42.1%	8.4%	20.0%	9.5%
Transportation And Storage	8.4%	37.3%	54.8%	4.9%	19.8%	10.3%
Information And Communication	4.8%	14.4%	23.4%	1.7%	28.2%	40.7%
Professional, Scientific And Technical Activities	4.0%	20.5%	36.8%	1.2%	28.4%	26.1%
Administrative And Support Service Activities	14.6%	38.9%	54.9%	8.1%	17.7%	12.1%
Education	9.3%	23.7%	20.1%	2.5%	36.9%	28.7%
Human Health And Social Work Activities	33.9%	15.6%	22.0%	26.6%	21.1%	16.5%
Arts, Entertainment And Recreation	4.4%	37.8%	40.0%	2.2%	22.2%	17.8%
All Industries	11.1%	28.6%	40.3%	6.9%	23.8%	19.5%

Notes:

Final results, Wave 2 of ONS Business Impact of Coronavirus (COVID-19) Survey that are continuing to trade. (n = 4,650).

Real Estate Services, Other Services and Mining and Quarrying have been removed due to their low response rate, but their totals are included in ‘All industries’.
The percentages in this chart will not sum to 100% as businesses were able to select multiple options

Source: ONS faster indicators