Recovery from the Pandemic Crisis: Balancing Short-Term and Long-Term Concerns

Norman V. Loayza, Apurva Sanghi, Nurlina Shaharuddin, and Lucie Wuester

The COVID-19 pandemic crisis combines the worst characteristics of previous crises. It features a simultaneous supply and demand shock; domestic, regional, and global scope; a projected long duration; and a high degree of uncertainty. What can be expected for recovery from the pandemic crisis across the world? This brief first assesses the projections of economic activity in 2020 and 2021 and the domestic and international conditions that will constrain and drive a possible recovery. It then discusses the potential shapes of the recovery (or lack thereof) for specific country conditions. Finally, it explores the need to balance short-term and long-term concerns, arguing in favor of policies that focus on sustained recovery, rather than quick but debt-fueled and short-lived gains. Drawing on the lessons from past crises, the brief concludes that sustained economic recovery is possible only when the underlying causes are addressed and the foundations of growth are protected. For the pandemic crisis, this implies mitigating the spread of the disease to manageable levels while keeping the economy sufficiently active. In the short term, economic policy should focus on preventing further poverty, averting unnecessary business closures, and avoiding lasting damage to human capital and productivity. In the long term, policy reform should address the structural vulnerabilities that the pandemic crisis has exposed. This includes reforms to expand labor and business formalization; to improve the coverage and adequacy of social protection; to extend financial inclusion to elderly, rural, and poor people; to promote digital transformation across society; and, most basically, to improve access to and quality of public health care.

A Crisis Like No Other

The COVID-19 pandemic crisis shares some similarities with other crises such as those stemming from natural hazards, wars, macroeconomic mismanagement, and international financial meltdowns (World Bank 2020a). However, this pandemic crisis arguably combines the worst features of all these crises. One way to see this is by assessing the shocks that different crises create. Table 1 presents a taxonomy of crises and associated shocks, with the latter organized by their mechanism, scope, duration, and certainty. The COVID-19 pandemic combines a simultaneous supply and demand shock; domestic, regional, and global scope; a projected long duration; and a high degree of uncertainty. According to Global Economic Prospects, it is “the most adverse peacetime shock in over a century” (World Bank 2020a).

Growth impacts and perceived uncertainty are two indicators of crisis severity. The current crisis is expected to bring about the largest contraction in global GDP per capita since World War II. In addition, it has the highest share of economies experiencing a recession in modern times (figure 1). Moreover, the pandemic is associated with extraordinary uncertainty (Altig et al. 2020). The World Uncertainty Index shows that the level of uncertainty associated with COVID-19 exceeds that of any other crisis experienced since at least 1960 (figure 2) (Ahir, Bloom, and Furceri 2018).

In this context, what can be expected for recovery from the pandemic crisis across the world? The magnitude and persistence of the economic downturn and the shape of the recovery will depend on smart public health policies to mitigate the pandemic, economic policy responses to support households and businesses during the crisis, and the discovery and delivery of an effective vaccine or treatment. This brief first presents the projections on economic activity in 2020 and 2021 and the facts that will likely constrain and drive a possible recovery. It then discusses the potential shapes of the recovery (or lack thereof) under various conditions. Finally, it explores the need to balance short- and long-term concerns, arguing in favor of policies that focus on achieving resilience for sustained recovery.

Growth Projections: Rebound May Not Be Recovery

The pandemic crisis is affecting virtually all countries, though with substantial differences across them. A comparison with the most similar worldwide economic event in recent history, the 2009 global financial crisis, is striking—although that earlier crisis was lower in magnitude and different in origin. Figures 3 and 4 compare the global, regional, and national patterns of decline and recovery for the 2009 global financial crisis and what is expected for the 2020 pandemic crisis. A look at global and regional averages (figure 3) reveals several disturbing observations. First, the decline in global

### Table 1. A Taxonomy of Crises and Associated Shocks Ranked by Severity and Uncertainty

<table>
<thead>
<tr>
<th>Characteristics of shocks</th>
<th>Mechanism</th>
<th>Scope</th>
<th>Duration</th>
<th>Certainty</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Supply</td>
<td>Demand</td>
<td>Domestic/Regional</td>
<td>Global</td>
</tr>
<tr>
<td>Pandemics</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Wars</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Macroeconomic mismanagement (e.g. hyperinflation)</td>
<td>X</td>
<td>X</td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>International financial crises</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Natural hazards</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
</tbody>
</table>

Source: Authors’ formulation.


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GDP growth projected for 2020 is three times worse than the corresponding decline in 2009. Second, whereas in 2009, three large regions (East Asia and Pacific, South Asia, and Sub-Saharan Africa) experienced little change or even an increase in GDP growth, all regions around the world will experience a contraction in economic growth in 2020. Third, regarding recovery, after the global financial crisis ended, a large increase in global and regional GDP growth occurred right away (in 2010), with only advanced countries experiencing a sluggish bounce-back. In contrast, the recovery for 2021 is projected to be much less strong, with most regions and countries regaining only a fraction of what had been lost during 2020. Fourth, focusing on the projected recovery during 2021, there are significant differences across countries and regions: East Asia and Pacific is projected to be the best performing region in terms of absolute growth. Countries in this region as well as in Sub-Saharan Africa are expected to regain most of the losses incurred during the crisis. On the other hand, although they are expected to grow during 2021, advanced countries and developing countries in Europe and Central Asia, Latin America and the Caribbean, Middle East and North Africa, and South Asia are estimated to regain only a fraction of the losses they incurred in 2020.

Focusing on cross-country data (figure 4), one striking observation is the contrast in the correlations of the growth rates the year of the crisis and one year later. In the context of the global financial crisis, countries that grew the most the year of the crisis tended to grow more the year after, rendering a positive correlation in growth rates. The opposite is expected to happen in the pandemic crisis: countries that experienced a larger contraction in 2020 are projected to have larger expansions during 2021. Whether these projections reflect excessive optimism on the resolution of the pandemic and the ability of countries to manage the crisis remains to be seen. Naturally, there are important differences across countries and regions. Advanced countries’ growth rates are expected to drop the most in 2020 and expand the most in 2021, possibly because of the resilience of their economies and their capacity to secure a vaccine as soon as it is available. Developing countries that suffered large contractions in 2020 but have strong fundamentals are projected to recover more strongly. Other countries suffering from structural problems, declining growth rates, or whose capacity to recover from a deep recession is doubtful are expected to have a weak recovery or a further contraction in 2021. Nevertheless, for nearly all countries, the bounce back in 2021 is expected to match only a fraction of the decline in 2020 (as indicated by figure 3).

Early evidence on recovery based on community mobility data—Europe leads the pack. Exploring economic activity during the crisis is difficult because of limited production or income data available across countries at monthly or even quarterly frequencies. Real-time data (from cell-phone location and mobility patterns) can proxy some economic activity, but with caveats (The Economist 2020a). Figure 5 shows an index based on the Google COVID-19 Community Mobility Report 2020, comparing mobility at the peak lockdowns, both relative to mobility during January and early February and adjusting for variation in temperature differences across countries. Some observations arise. Although mobility picked up in late (Northern Hemisphere) summer, there is wide diversity across countries. European countries have moved faster than the rest in recovering some of their pre-crisis mobility. They have been joined by some countries from other regions that have dealt well

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**Figure 1. Crisis Severity and Growth Contractions, 1871–2020**

The COVID-19 pandemic has the highest share of economies experiencing a recession in modern times and is expected to bring about the largest contraction in global GDP per capita since World War II.

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**Source:** Authors’ adaptation from World Bank 2020a. Data from Bolt et al. 2018; Kose, Sugawara, and Terrones 2019, 2020. Note: 2020 uses forecast data. Grey shaded areas refer to global recessions. Sample includes 183 economies, though the sample size varies significantly by year. For crises that last for more than a year, the annualized average of the cumulative contraction of GDP per capita growth during the crisis is used.
The negative external shock, exacerbated by other shocks, will linger for the foreseeable future. The global response to the pandemic has been and is likely to remain chaotic and uncoordinated, with cycles of outbreaks and lockdowns, until a vaccine or effective treatment is made available. With the continued threat posed by the pandemic, it is very likely that international borders will remain restricted and global economic activity will stay low and volatile. This implies that negative external shocks will persist in the near future, affecting even countries that are able to reduce the public health risk posed by COVID-19. Box 1 provides a summary of the various external shocks facing countries around the world. The adverse external situation is aggravated by the ongoing and worsening trade and technological disputes between China and the United States. Global coordination and cooperation could greatly reduce the human and economic cost implied by the pandemic by providing financial support to governments in need, facilitating trade and capital flows, and developing and deploying a COVID-19 vaccine (Athey, Hoyt, and Kremer 2020; OECD 2020a). The latter benefit is worth underscoring: even when an effective vaccine is discovered, the logistical and political challenges of securing and administering it at scale in the developing world could delay the recovery and should not be underestimated (IMF 2020a; World Bank 2020a; WHO 2020). Pre-existing conditions matter. On the domestic front, countries with favorable demographic profiles and those able to implement sustainable measures to deal with the pandemic will fare better on health and economic dimensions (see map 1). Developing countries will have to navigate the crisis with lower health care capacities, larger informal sectors, smaller scope for home-based work, and dwindling fiscal space (Hevia and Neumayer 2020; Loayza and Pennings 2020).
The decline in global GDP growth is much worse than the corresponding decline in 2009 and affects all regions, not just some. Recovery is projected to be much less strong and take much longer, and to vary considerably by region.

### 2009 global financial crisis

#### a. World and regional output growth

#### b. Extent of national recovery worldwide and by region

<table>
<thead>
<tr>
<th>Country/Region</th>
<th>2009 Global Financial Crisis</th>
<th>2020 Pandemic Crisis</th>
</tr>
</thead>
<tbody>
<tr>
<td>World</td>
<td>0%–50%</td>
<td>&gt;100%</td>
</tr>
<tr>
<td>Advanced</td>
<td>50%–75%</td>
<td>&gt;75%–100%</td>
</tr>
<tr>
<td>East Asia &amp; Pacific</td>
<td>0%–50%</td>
<td>&gt;75%–100%</td>
</tr>
<tr>
<td>Europe &amp; Central Asia</td>
<td>0%–50%</td>
<td>&gt;75%–100%</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>0%–50%</td>
<td>&gt;75%–100%</td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>0%–50%</td>
<td>&gt;75%–100%</td>
</tr>
<tr>
<td>South Asia</td>
<td>0%–50%</td>
<td>&gt;75%–100%</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>0%–50%</td>
<td>&gt;75%–100%</td>
</tr>
</tbody>
</table>


Note: “Advanced” represents countries that are advanced economies based on IMF grouping. Regions follow the World Bank classification excluding advanced economies. Growth data in 2020 and 2021 are projections from World Bank (2020a). Countries that were not featured in the report use projections data from IMF (2020a, 2020d). Panels a and c, regional aggregates are weighted averages using GDP in constant 2010 US dollars. Panels b and d include only those countries that experience a decline in GDP growth from the preceding five-year average. <0 shows the percentage of economies that experience negative growth after the corresponding recession year. 0–50% shows the percentage of economies that recovered less than half of the losses they incurred in the contraction in the recession year. 50%–75% and >75%–100% show the percentage of economies that recovered 50% to 75%, and more than 75% to 100%, of losses they incurred in the contraction in the recession year, respectively. >100% shows the percentage of economies that recovered more than 100% of the losses they incurred in the contraction during the recession.

On the external front, countries that depend more on international merchandise and services trade and financial flows will be more affected by the global dimension of the crisis (see box 1). Against the backdrop of subdued trade performance in 2019, the sharp downturn of trade caused by the COVID-19 crisis will hit those countries with disrupted global value chains and with high dependence on a limited range of products and markets especially hard. This group includes most developing countries, many of which will also suffer the brunt of plummeting revenues from tourism and remittances (Bosson and Natarajan 2020; Monahov 2020; UNCTAD 2020; World Bank 2020b, 2020c; WTO 2020b). Services trade continued to decline globally in April and May 2020, driven by the reduction in travel and transport, with international arrivals estimated at 3 percent of 2019 levels (World Bank 2020d). Globally, the loss in tourism receipts is estimated to amount to 1.5 percent to 4.2 percent of GDP, with countries such as Jamaica and Thailand losing about 10 percent in the most optimistic scenario (UNCTAD 2020). Developing countries involved in global value chains may experience a lasting decline in participation as advanced countries reshore and source internally, posing a risk of early deindustrialization (UNIDO 2020). Commodity exporters have seen prices falling to record lows, further eroding their fiscal positions, external balances, and foreign exchange buffers (UN DESA 2020).

For oil exporters, having drawn on their buffers during the oil price
plunge in 2014–16, the current crisis hits them when they are especially weak (Wheeler et al. 2020).

The Shape of Recovery: An Alphabet Soup of L, W, V, or U?

Although there is a great deal of uncertainty regarding when and how economic recovery will take place for various countries, a basic taxonomy of recovery patterns may be instructive. The type of recovery will depend on how severely countries have been hit by the pandemic and the external shock and on the policy responses that governments are deploying (macroeconomic, financial, and social protection policies). Although the following taxonomy is a conceptual exercise, it is based on the lessons from previous crises (see box 2) adapted and applied to the characteristics of the current pandemic crisis.

**Lack of recovery (L):** This is unfortunately possible for countries that are not able to get the pandemic under control and that squander their public resources with failed attempts at mitigation and recovery, allowing the pandemic crisis to morph into a macroeconomic, debt, and financial crisis. In this case, the COVID-19 crisis may have a permanent effect on GDP via lost investment during and after the crisis, a loss of human capital, a deterioration of fiscal capacity, and a slowdown in productivity growth (Sheiner and Yilla 2020).

**Volatile recovery (W):** A volatile recovery may occur in countries that address public health concerns with strict but unsustainable measures, leading to a cycle of openings, outbreaks, and lockdowns. This may also happen to countries that, because of their structural characteristics, are very dependent on external conditions, which are likely to be volatile. A recovery with a double-dip recession has been relatively rare (Barthélemex, Binet, and Pentecôte 2020; Reinhart and Rogoff 2014). It may, however, be a common feature of the pandemic crisis, reflecting the risks associated with renewed outbreaks and an exceptionally volatile international situation.

**Quick recovery (V):** A quick, V-shaped recovery is in theory the best scenario after a shock. It is, however, unlikely for most countries because of the depth of the crisis (which has affected growth fundamentals) and the high degree of uncertainty surrounding the crisis. This is true even if a vaccine becomes available in early 2021. Moreover, attempting a quick recovery by opening without proper public health measures in place and by pumping government stimulus packages where fiscal multipliers are low can be counterproductive (Loayza and Pennings 2020). Evidence indicates a disconnect between expectations in the financial market and patterns in the global economy, whereby the former suggests a V-shaped recovery while indicators for the latter portend a deeper-than-expected downturn (IMF 2020a; World Bank 2020e).

**Gradual recovery (U):** A gradual recovery may be the most pragmatic scenario for most countries in the next few years. It may require a period of resilience, where smart public health measures are in place and economic activity resumes, albeit at a lower level, and where vulnerable households are supported and excessive destruction of firms is prevented. Recovery would occur based on resilient fundamentals, at a pace driven by the resolution of the pandemic (vaccination or effective treatment) and the normalization of global conditions (Furman 2020).

Box 3 applies this conceptual framework to data on the evolution of the pandemic, the public policy response, and the social and economic vulnerabilities in order to assess the possibility and shape of economic recovery for various countries and regions around the world.

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**Figure 4. Comparing GDP Growth Contraction and Recovery for the Global Financial Crisis and the COVID-19 Pandemic Crisis**

Unlike after the global financial crisis, countries that experienced a larger contraction during the crisis are projected to have larger expansions the following year—but recovery is expected to be limited and vary widely by country.

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**Source:** World Bank 2020a, World Bank 2020g World Development Indicators; IMF 2020a, 2020d.

**Note:** “Advanced” represents countries that are advanced economies based on IMF grouping. Regions follow the World Bank classification excluding advanced economies. Data labels use the International Organization for Standardization (ISO) country codes. Growth data in 2020 and 2021 are projections from World Bank (2020a). Countries that were not featured in the report use projections data from IMF (2020a, 2020d). Being above (below) the 45-degree line (gray) indicates that the difference of growth and the average of the preceding five years improved (worsened) in 2010 and 2021. The red line represents the linear trendline.
Beyond Quick Recovery, Long-term Resilience as a Goal

While a quick resumption of growth is everyone’s wish, a gradual recovery may be a more sensible policy goal. This approach would consider both the uncertainty of the pandemic crisis and the limits of what can be achieved by active government interventions. It would set long-term resilience as its goal (Hammer and Hallegatte 2020).

Why would the pursuit of a quick recovery be misguided? First, it can lead to repeated waves of the pandemic. Abandoning containment and mitigation measures prematurely may lead to an initial upsurge in economic activity but at the cost of rising infection rates, as is happening in Australia, India, Mexico, and Spain (The Economist 2020b). This, in turn, raises the risks of a persistent recession (Acemoglu et al. 2020; Eichenbaum, Rebelo, and Trabandt 2020). Hence, after implementing supply-restricting containment measures, the turn toward recovery needs to highlight the dual challenge posed by economic decline and the continued risk of contagion. In order to preserve lives and livelihoods, the combination of pragmatic and effective economic and public health measures is crucial, in line with the realities and conditions in each country.

Second, a pursuit of quick recovery can result in large fiscal deficits without a significant and steady increase in economic activity. The debt overhang can be large. In severe cases, this can lead to an unsustainable fiscal situation, resulting in debt and financial crises. Central banks and governments have quickly ramped up large-scale monetary and fiscal measures in response to the economic downturn (World Bank 2020a). This is justified to the extent that it serves to prevent a collapse in household income, widespread business closures, and mass unemployment. It is not justified, however, to stimulate the economy while it is naturally constrained by the pandemic and mitigation policies (Loayza and Pennings 2020). In this case, increased spending and reduced revenues can exacerbate the fiscal risks posed by worsening macroeconomic conditions amidst plummeting commodity prices, currency depreciations, and widening sovereign spreads (IMF 2020b). Even as financial pressures are easing, risks of unmanageable debt levels persist (Alberola et al. 2020; IMF 2020c; World Bank 2020e). Emerging market economies face greater vulnerabilities and more binding borrowing constraints, implying painful postcrisis adjustments that can be exacerbated by a debt overhang (Daly, Gedminas, and Grafe 2020; Kose et al. 2020).
What does long-term resilience require?

Long-term resilience and sustained recovery require that the fundamentals of economic growth remain solid, even during the crisis. This requires restoring “wealth,” which broadly understood includes physical, human, natural, social, intangible, and financial capital. In this framework, economic growth is an annual return on this cumulative wealth stock, mediated by how productively it is used. Lange, Wodon, and Carey (2018) provide a measure of national wealth that includes physical, human, and natural assets. According to their calculations, for advanced countries, human capital is the largest component of wealth (70 percent, in high-income OECD countries), and for low-income countries, it is natural capital (around 47 percent). On the path to recovery, it is crucial to preserve all these forms of capital while grasping opportunities to boost productivity growth. In this way, the path to recovery can also lead to long-term resilience.

Third, pursuing a quick resumption of growth may transform emergency measures into regular practice. While these measures may have been necessary at the peak of the crisis, they are harmful or risky in normal times. For instance, the practice of central banks buying sovereign bonds to provide stimulus could do away with central bank independence and inflation control, the cornerstones of macroeconomic stability for most developing countries. Another example deals with lax financial policies. Regulators have “eased prudential limits on banks and allowed lenders to indulge in creative accounting” (The Economist 2020b). These measures have interrupted or even reversed reforms for better micro- and macroprudential practices in financial markets. Rescuing firms and financial institutions is necessary when governments are forcing supply restrictions to contain the spread of COVID-19. However, policymakers need to write off certain loans and allow some firms to fail when their solvency beyond the current crisis is questionable (The Economist 2020b).

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First, human capital needs to be preserved and strengthened throughout and after the crisis, focusing especially on children’s and
young adults’ health and education. Indiscriminate lockdowns and school closures of several months lead to learning losses that could last a lifetime, resulting in an earnings shortfall of about US$10 trillion, or 11.4 percent of GDP globally (World Bank 2020f). It is unlikely that online and remote learning in general can be adapted to prevent large human capital losses, especially for children in poor and disadvantaged households. Reopening schools, as safely as possible, should be seriously considered. Human capital formation in the workplace has also been curtailed. Although adaptation to new and largely digital working processes offers opportunities for development, early evidence suggests that the transition to new business practices and the associated productivity effects are uneven (Bartik et al. 2020; Baldwin, and Forslid 2020; Financial Times 2020).

Second, physical capital can be preserved by maintaining projects of high-quality public investment and by encouraging private investment by reducing policy uncertainty and avoiding crowding out by large fiscal deficits. The type of investment matters in its effect on long-term resilience: rushed decision making to boost demand in the short term can lead to dubious investment projects (Foster et al. forthcoming). Moreover, excessive debt borrowing raises concerns over sovereign credit risk and results in an increase in sovereign bond yields and borrowing costs, crowding out private investment (Corsetti et al. 2013; Huidrom et al. 2019). High-quality public investment, policy certainty, and fiscal moderation may be at least as important as the credit guarantees and interest rate reductions that dozens of developing country governments have implemented to boost investment since March 2020 (The Economist 2020b; World Bank 2020a).

Third, natural capital captures both nonrenewable sources (such as fossil fuels) and renewables sources (such as forests). Commodity exporters have borne the brunt of the crash in oil and gas prices during this crisis, affecting their stocks of natural capital. However, their large share of carbon-based wealth faces increased risk due to future price uncertainty and large-scale attempts at global decarbonization. This puts a premium on deepening the role of nonrenewables, while managing volatility in commodity prices in the short term through appropriate macrofiscal management.

Fourth, the current crisis has demonstrated the role that social capital plays in building resilience. In seven European countries, areas with high social capital registered between 12 percent and 32 percent fewer COVID-19 cases from mid-March until mid-May (Bartsher et al. 2020). Anecdotal evidence from various corners of the world underscore the importance of community structure, trust, and family and kinship structures in providing essential food and supplies, as well as monitoring and implementing social distancing measures.

Finally, productivity, which determines how effective factors of production are in yielding growth, faces a drastic fall because of the destructive nature of the pandemic crisis. This can be mitigated only by avoiding excessive business closures, providing continuity of public infrastructure and services, and maintaining macroeconomic stability. The adaptation of innovative and digital business practices could offer a boost to productivity growth, offsetting some of the inherent losses that are resulting from the crisis. For instance, Argentina, China, Italy, Japan, and South Korea, among other countries, have introduced measures (such as subsidies, credit lines, toolkits, and free advisory services) to encourage the adoption of technologies for a range of new online-based business practices, especially in small and medium-sized enterprises (OECD 2020b).

However, the current pressure against globalization, labor mobility, and small firms pose serious threats to such growth (di Mauro and Syverson 2020). In the long term, structural reforms are needed to promote a growth-friendly macroeconomic, regulatory, and institutional environment (Dieppe 2020; Kim and Loayza 2019).

Conclusion: Leveraging the Crisis to Promote Necessary Reforms

Although it is hard to see the positive side of an ongoing crisis, crises have begot reforms with lasting beneficial effects in the past and may do so again now (Alesina, Ardagna, and Trebbi 2006; Bruno and Easterly 1996; Drazen and Grilli 1993). The pandemic crisis has exposed areas of great vulnerability in developing countries, and reforms are needed to address them. Some of them include reforms to expand labor and business formalization; to improve the coverage and adequacy of social protection; to extend financial inclusion to elderly, rural, and poor people; to promote digital transformation in schools, businesses, and government; and, most basically, to improve access and quality of public health care.

Box 1. The Different Dimensions of External Shocks Facing Countries around the World

The COVID-19 crisis has brought about numerous shocks, via supply and demand channels, which have affected trade in goods and services—especially commodities, travel, and transport—remittances, and capital flows, globally. Naturally, economies that are dependent on these sectors face greater vulnerabilities to these shocks. Common characteristics among these economies include a low degree of export diversification and—especially with respect to tourism—remoteness and small domestic markets (UNCTAD 2020). The shocks have affected regions and income groups to different extents, notably in line with infection “waves” and containment policies but also because of differences in economic structures (see figure B1.1).

The trade shock has differed across regions, with exports from East Asia declining by 13 percent in May 2020, year on year, compared with a 37 percent drop in North America and South Asia (World Bank 2020d). Yet, international tourism has collapsed in all regions, although the brunt of the shock will affect small island developing states, which are most vulnerable not only because of their high dependence on tourism receipts, but also because a shock of this magnitude is particularly hard to manage for small economies (Coke-Hamilton 2020). Countries dependent on inflows of remittances are located in diverse regions, with the largest recipients, including Tonga, Haiti, South Sudan, Kyrgyz Republic, and Tajikistan, receiving around 30 percent of GDP through this channel (World Bank 2020b). The loss of remittances affects households and trade balances, also leading to a reduction in consumption, which will hit countries that experience capital outflows and tight financial conditions especially hard (Sayeh and Chami 2020). In turn, flows of foreign direct investment (FDI) are projected to decline by more than 30 percent in 2020, especially affecting developing countries, where a larger share of FDI is accounted for by the primary and manufacturing sectors (OECD 2020c).
a. Trade disruptions lead to lower export receipts...

Merchandise exports 2019, percent of GDP

- Advanced
- Latin America & Caribbean
- Europe & Central Asia
- Middle East & North Africa
- Sub-Saharan Africa
- South Asia

Source: World Bank 2020g World Development Indicators; WTO 2020a.
Note: Change in merchandise exports (percent of GDP) in annualized form based on data available for January–May 2020.

b. ...with a particularly adverse effect on commodity exporters

Merchandise exports 2019, percent of GDP

- Advanced
- Middle East & North Africa
- East Asia & Pacific
- Europe & Central Asia
- Latin America & Caribbean
- Sub-Saharan Africa
- South Asia

Source: World Bank 2020g World Development Indicators; WTO 2020a.
Note: Bubble size reflects the export values of fuels and mining products as percent of GDP based on 2018 WTO and World Development Indicator (WDI) data.

c. Dependence on tourism brings sharp losses in this crisis, with greater vulnerabilities for small economies

Tourism receipts 2018, percent of GDP

- Advanced
- Latin America & Caribbean
- Europe & Central Asia
- Middle East & North Africa
- Sub-Saharan Africa
- South Asia

Source: World Bank 2020g World Development Indicators; IMF 2020e.
Note: Projected change in travel receipts 2019–2020 (percent of GDP) estimated by IMF 2020e.

d. Declines in remittance inflows are adding to income losses, especially in vulnerable emerging markets and developing economies

Remittances inflows 2019, percent of GDP

- Advanced
- East Asia & Pacific
- Middle East & North Africa
- Latin America & Caribbean
- South Asia
- Europe & Central Asia
- Sub-Saharan Africa

Source: World Bank 2020g World Development Indicators; World Bank 2020b; IMF 2020e.
Note: Projected change in remittance inflows 2019–2020 (percent of GDP) estimated by IMF 2020e, based on World Bank 2020b regional estimations.

e. On average, emerging markets and developing economies are expected to see FDI inflows decline by over 20 percent

FDI net inflows 2019, percent of GDP

- East Asia & Pacific
- Europe & Central Asia
- Latin America & Caribbean
- Middle East & North Africa
- South Asia
- Sub-Saharan Africa

Source: World Bank 2020b; World Bank 2020g World Development Indicators; IIF 2020.
Note: Projected change in FDI inflows 2019–2020 (percent of GDP) estimated by IIF 2020.

f. Estimated current account changes reflect these external shocks and the impact of dependencies on trade, tourism, remittances, and foreign capital flows

Estimated change in current account, 2019-2020

- Advanced
- East Asia & Pacific
- Europe & Central Asia
- Latin America & Caribbean
- Middle East & North Africa
- South Asia
- Sub-Saharan Africa

Source: World Bank 2020g World Development Indicators; IMF 2020e.
Note: Projected change in current account 2019–2020 (percent of GDP) estimated by IMF 2020e.

Note: Projected changes as percent of GDP. Actual changes may differ based on other factors and on the dynamics of the pandemic in 2H:2020. Estimations are provided by different sources (IMF 2020; IIF 2020; World Bank 2020a) and therefore include different country samples. Data labels use the International Organization for Standardization (ISO) country codes. "Advanced" represents countries that are advanced economies based on IMF grouping. Regions follow the World Bank classification excluding advanced economies.
Box 2. Lessons from Past Crises

Several key lessons for recoveries can be drawn from past crises, taking into account the nature of the shock (table 1). First, initial conditions (such as fiscal space and governance capacity) can increase vulnerability and pose challenges to the implementation of recovery measures (Bandaogo 2020; Felbermayr and Gröschl 2014; Kumar and Woo 2011; Panizza and Presbitero 2014; Romer and Romer 2018, 2019). Successful experience dealing with similar crises is an important condition. Second, before embarking on a path of recovery, the underlying shock needs to be addressed and resolved to avoid a sudden return to emergency management and an inefficient allocation of resources. Third, once some degree of crisis resolution has been reached, economic management needs to focus on strengthening the factors of production most affected by a crisis. Fourth, as crisis management turns into recovery policies, measures need to emphasize sustainability and future resilience to similar shocks.

**Pandemics and epidemics** have been associated with a trade-off between health and economic harm. Public health policies are crucial to protect society and the economy from further losses. In the recovery phase, long-term health and human capital impacts need to be addressed. In countries affected by past epidemics (SARS, MERS, Ebola, Zika), investment and output per worker remained on average 9 percent and 4 percent lower, respectively, over the next three years relative to other comparable countries (Dieppe 2020). In addition, past pandemics and epidemics have been associated with sharp productivity losses, which call for policies promoting investment in human and physical capital and a productive reallocation of resources, as well as structural and institutional reforms (Dieppe 2020).

**Wars** pose stark challenges to recovery, particularly through weakened state capacity and destroyed physical, human, and social capital, as well as being obviously threatened by the recurrence of conflict (Collier 2009). Evidence shows that a gradual recovery from such a crisis is feasible once wars end and lasting peace begins (Chen, Loayza, and Reynal-Querol 2008). Post-conflict reconstruction is often sensitive. Local context and economic potential should be carefully considered, with the aim of strengthening domestic factors of production. In addition to the usual fiscal, monetary, and exchange rate policies, recoveries have tended to be more successful where inclusive growth was driven by employment and business environment policies (UNDP 2008).

**Natural disasters** tend to have especially severe economic consequences for small, less-developed countries (Loayza et al. 2012; Noy 2009). During the recovery phase, the central element is reconstruction, which should be phased and sustainable (Benson and Clay 2004). Especially in countries with frequent events, implementing forward-thinking risk management and response strategies can improve the speed and quality of reconstruction. This has proven successful, for instance, in Indonesia, where institutions and funds were prepared for this purpose following the 2004 earthquake and subsequent tsunami (Hallegatte, Rentschler, and Walsh 2018). The availability of information plays a key role to promote prevention, which can reduce human and economic costs (World Bank 2010).

**Financial and banking crises** bring about severe output losses. In countries with high public debt levels before the crisis, lack of fiscal space not only constrains the government’s ability to implement countercyclical policies, but also undermines the effectiveness of fiscal stimulus and the quality of fiscal performance (Botman and Kumar 2006). Importantly, the literature documents that expansionary fiscal responses lead to sustained economic recoveries after the crisis only when the financial sector’s vulnerabilities are addressed without endangering fiscal sustainability (IMF 2009; Baldacci, Gupta, and Mulas-Granados 2012). During the global financial crisis, exchange rate flexibility acted as a shock absorber, while a shift to inflation-targeting regimes in several emerging markets and developing economies helped lower inflation in the run-up to the global recession. Countercyclical policies are no substitute for vigorous reforms in support of long-term growth, as shown by experiences of financial and external shocks. Thus, structural and governance reforms are important (Kose and Ohnsorge 2019).

Box 3. Assessing a Country’s Ability to Start and Sustain a Recovery from the Pandemic Crisis

Sustainable economic recovery is possible only when the underlying problem has been addressed and has to a certain extent been resolved. For the pandemic crisis, this implies mitigating the spread of the disease to manageable levels (that is, preventing health systems from being overwhelmed and avoiding excessive deaths) while keeping the economy sufficiently active (that is, preventing worsening poverty, averting unnecessary business closures, and avoiding lasting damage to human capital and productivity). The policy challenge is easing the difficult trade-off between saving lives and livelihoods.

Saving lives and livelihoods requires a combination of supportive economic policies targeted at the most affected households and businesses, along with smart public health policies that rely less on indiscriminate lockdowns and more on sustainable mitigation measures (such as focalized quarantines; testing, tracing, and isolating the infected; and wearing face masks in public places) (Loayza 2020). However, addressing the underlying problem is a necessary but not a sufficient condition for sustained economic recovery. The two major threats to economic recovery are the recurrence of waves of infection and adverse external and domestic economic shocks. These threats are, in turn, dependent on social and economic vulnerabilities to the pandemic crisis.

Figure B3.1 attempts to combine all these factors—the evolution of the pandemic, the public policy response, and the social and economic vulnerabilities—to help determine the possibility and shape of economic recovery for various countries and regions around the world. It relies on proxies—admittedly imperfect indicators. For the evolution of the pandemic, the figure uses the infection rate, the case fatality rate, the rate of positive tests, and the mortality rate of COVID-19 as officially reported. For the public policy response, the figure uses indicators of lockdown stringency, lack of testing, tracing, and isolating; lack of economic support; and infrequency of mask wearing. For social vulnerability to the pandemic, the figure uses measures of the prevalence of elderly populations, labor informality, urban slums, and overcrowded dwellings. Finally, for economic vulnerability, the
How can this information help assess a country’s ability to start and sustain a recovery from the pandemic crisis? First, we can consider the evolution of the pandemic: if rates of infection, case fatality, positive tests, and mortality are comparatively low, the country seems to have the pandemic under control, at least currently. Second, we can check the public policy response, looking for evidence that lockdowns are easing, smart public health policies are in place, and vulnerable sectors are receiving support. For example, if the pandemic is under control and public policies are conducive to a resumption of social and economic activity, then the country has the right environment to embark on the recovery from the crisis. In contrast, if the pandemic is raging and the country is in lockdown, the country is not ready for recovery and should focus on emergency and relief measures: that is, implementing smart policies to mitigate the pandemic and alleviate the economic fallout. Third, we can assess the vulnerabilities that signal the risks of a sluggish or volatile recovery. The social vulnerability to the pandemic is given by the country’s demographic profile, with older populations being more severely affected by the disease; and by working and living conditions, with higher labor informality and more overcrowded cities and dwellings being more conducive to infections. The economic vulnerability is determined by available fiscal resources, depleted in the context of high deficits, and by dependence on external conditions likely to remain volatile. For example, if a country has the pandemic under control and is starting recovery, it would need to remain vigilant if its social vulnerability to the pandemic is high and it would need to adjust its programs and expectations if its deficit is projected to be high and is dependent on external conditions.

This analysis can be applied to individual countries and groups of them. As an illustration, figure B3.1 presents the typical cases in advanced countries (as a group, worldwide) and developing countries in various geographic regions.

- **Advanced** countries have been able to avoid the worst of the pandemic with a combination of public health and economic measures but are still facing high infection rates. These countries remain vulnerable to the disease because of their older...
populations. Recovery will be slow and erratic if they need to resort to repeated lockdowns. These could be avoided with more intensive testing, tracing, and focalized quarantines.

• **Europe and Central Asia** emerging and developing countries have been mildly successful in controlling the pandemic, suffering, nevertheless, a relatively large number of infections and fatalities. Their old populations are an important vulnerability, though their relatively well-advanced working and living conditions can help control the rate of infections and fatalities with increased reliance on smart health policies. Their recovery will likely be tied to Western Europe and the rest of the world, particularly so for commodity exporters (such as Kazakhstan and Russia).

• **East Asia and Pacific** countries have, once again, forged ahead of other developing countries in handling the pandemic crisis. Their infection and fatality rates are among the lowest in the world. The relative youth of their populations and, possibly, their experience with previous pandemics have been to their advantage. Their fiscal and external accounts seem to be relatively strong. Their recovery will be gradual, linked to external conditions for countries that depend heavily on trade (such as Vietnam), commodities (Malaysia), and tourism (Thailand).

• **Latin America and the Caribbean** countries have been unable to control the pandemic, with rampant and growing infections and fatalities. Their strict lockdown strategy, still in place in many countries, has not yielded the expected results. They remain vulnerable to the pandemic because of poor living conditions and high informality. Any hope of flattening the epidemic curve and prevent a further collapse of the economy relies on being able to implement more sustainable public health policies. The situation is especially difficult for countries with low fiscal space and high commodity dependence. Rather than focusing on economic recovery, they should concentrate on preventing a further collapse.

• **Middle East and North Africa** countries are struggling to manage the pandemic, with high rates of infections and fatalities. There is a high uncertainty as to whether they will be able to control the spread of the disease. An important advantage is the youth of their populations. On the negative side, the most remarkable feature for the region is the deterioration in fiscal and external accounts, particularly for commodity exporters. Without these resources, it is doubtful that they will be able to continue their lockdown policies. Their recovery is likely to be volatile and erratic, not only because of the pandemic but also because of their domestic political conditions.

• **South Asia** countries are also struggling to mitigate the spread of the disease, and their low testing coverage puts the reported numbers in doubt. The youth of their populations is a big advantage, somehow compensating for poor living conditions and high informality. Their lockdown measures would need to be replaced by more sustainable policies based on testing and focalized quarantines. Their fiscal accounts are in a difficult situation, and they may not have the resources to support low economic activity. Their recovery will be gradual and, given the large size of most economies in the region, dependent on internal conditions.

• **Sub-Saharan Africa** countries have low infection rates but relatively high fatality rates. This is likely to indicate insufficient testing. They have among the worst living conditions and labor informality, making them vulnerable to the spread of the coronavirus. Possibly more than in all other regions, the young population in African countries plays in their favor. Some countries in the region have imposed strict lockdowns with questionable results. All countries in the region would benefit from more testing and focalized quarantines. Their fiscal and external accounts have deteriorated, though not as drastically as in other regions. A gradual recovery for Sub-Saharan countries is probable, provided they avoid a cycle of lockdowns and reopenings, and conduct moderate economic policies.

References


