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EQUITABLE GROWTH, FINANCE & INSTITUTIONS INSIGHT

Private Enterprise after the Pandemic: A Review of Alternative Scenarios

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Abstract

The COVID-19 pandemic has had strong adverse impacts on the private sector in low- and middle-income countries. The future course of the pandemic remains highly uncertain, so consideration of alternative scenarios may be more helpful in assessing investment opportunities and designing policy responses. Based on private sector responses to the pandemic shock, and lessons learned from previous exogenous shocks, this paper outlines two alternative scenarios for private enterprise during the recovery phase. The scenarios consider a stronger as well as a weaker global economic recovery, and both of these are based on the information available as of end-June 2021. Thus, the scenarios do not discuss developments that have taken place since June 30, which include the emergence of the Delta variant of COVID-19, and the evolution of vaccine deployment around the world.



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Abbreviations

COVID-19	a type of coronavirus, which was declared a pandemic by the World Health Organization on January 31, 2020
DFI	development finance institution
EMDEs	emerging markets and developing economies
EU	European Union
FDI	foreign direct investment
G-7	An intergovernmental organization of seven countries that meets periodically to address international economic and monetary issues
G-20	An international forum for the governments and central bank governors from 19 countries across the world and the European Union (EU)
GDP	gross domestic product
GEP	<i>Global Economic Prospects</i> (a World Bank report published twice a year in January and June)
GPT	general purpose technology
GVC	global value chain
IFC	International Finance Corporation
IMF	International Monetary Fund
LAC	Latin America and the Caribbean
MENA	Middle East and North Africa (Region)
OECD	Organisation for Economic Co-operation and Development
PPE	personal protective equipment
SDGs	Sustainable Development Goals (United Nations)
SME	small and medium enterprise
SSA	Sub-Saharan Africa
UK	United Kingdom
UNCTAD	United Nations Conference on Trade and Development
US	United States
WTO	World Trade Organization

Note: Unless otherwise indicated, all dollars are US dollars.



Introduction: How is the Private Sector Landscape Changing?

In emerging markets and developing economies (EMDEs), can the private sector support a vigorous recovery from the impact of the COVID-19 pandemic, and correct some of the ills that afflicted these economies before the crisis? While the pandemic continues to affect lives and livelihoods around the world, we are finally seeing the start of recovery from the worst health and economic crisis since World War II. As a result, international development agencies are discussing the role that private firms and investors could play toward achieving the United Nations' Sustainable Development Goals (SDGs) and, in the process, *build back better*. However, with the pandemic still raging in some countries,¹ uncertainty continues about how the private sector in EMDEs will operate in a post-pandemic world. Will firms adopt new technologies and venture into new industries and value chains, enabling them to boost productivity? Or will the pandemic push more firms into bankruptcy, upend whole industrial segments, and leave deep scars that hamper future growth? Most likely, the future will combine these diametrical opposites, with new opportunities emerging, while the pre-pandemic challenges continue. As the pandemic subsides, better understanding of the future would allow investors, government, and development finance institutions to stimulate economic growth, revive private business activities, and create new jobs.

This note considers alternative scenarios regarding the outlook for economic recovery, and its implications for the private sector. It draws on a large and continuously expanding body of literature that looks, from different angles, at how the pandemic has been evolving; how it has been impacting businesses; and how it is reshaping the environment in which the private sector operates. The note begins by discussing the difficulties in forecasting the future, given the lingering uncertainties of the global economy. The authors then discuss two alternative scenarios regarding the level of optimism in resolving the crisis. These alternatives are based on the state of the global economy at the end of June 2021 and, therefore, this paper does not reflect developments since that date. The two alternative scenarios hinge, to a good degree, on the speed with which the health emergency is resolved; on the effectiveness of individual countries' policy responses in restoring economic activity; and how businesses respond after being hard hit by the pandemic. The note concludes that even under the more benign scenario, some private firms and banks will suffer from scars inflicted by the crisis, and the private sector will continue to face some of the same challenges that existed prior to the pandemic.

¹ The analysis reflected in the present document is based on the data and information that were available as of end-June 2021. Thus, the document does not fully discuss developments after that date, including the emergence of the COVID-19 Delta variant and the evolution of vaccine deployment around the world.



Scenarios Are Built on Shifting Sands

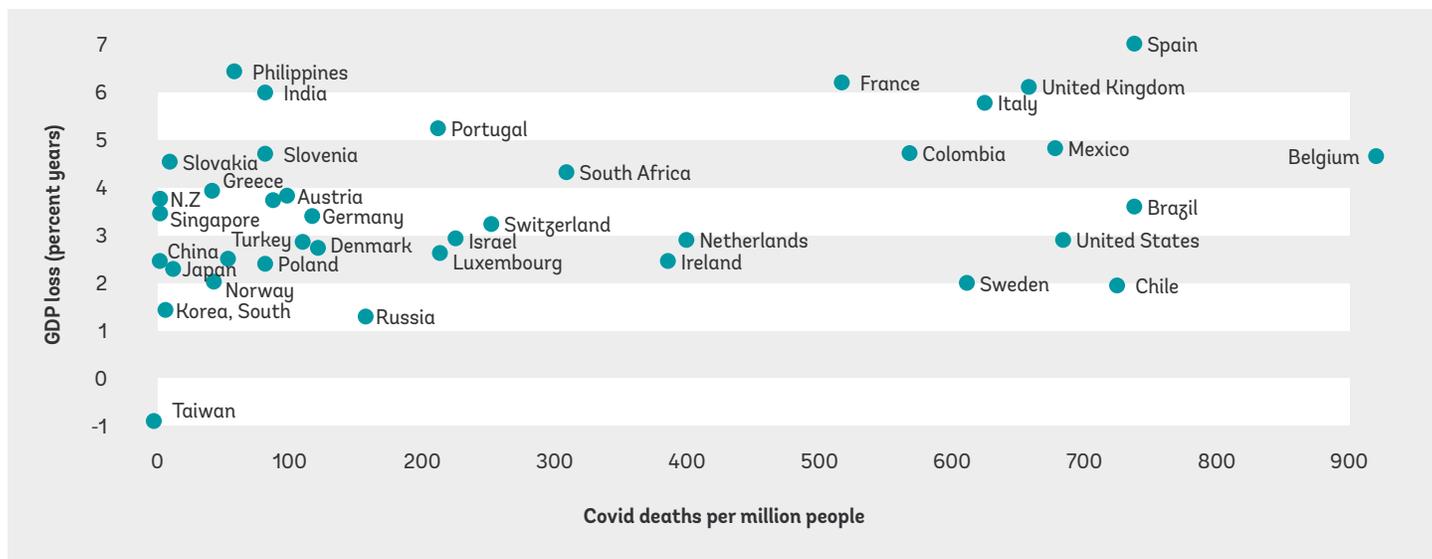
The ability to cope with the health and the economic impacts of the pandemic has varied markedly across countries. To assess macroeconomic impacts, Fernandez-Villaverde and Jones (2020) combined data on gross domestic product (GDP), employment, Community Mobility Reports, and deaths (Figure 2.1). One important finding of their study is that a significant number of advanced and emerging economies initially experienced minimal impacts. In Figure 2.1, these economies are clustered in the lower left-hand quadrant of the graph. Emerging economies such as Cambodia, China, and Vietnam suffered the least in 2020. These countries minimized both the number of deaths and their macroeconomic losses. Other countries including Brazil, Colombia, Ecuador, India, Iran, Mexico, Peru, and South Africa have been hard hit (van Elsland & Johns 2020; Mwai 2021; Overgerg et al. 2021; Rice et al. 2021). Fernandez-Villaverde and Jones (2020) concluded that good outcomes for both GDP and COVID-19 mortality rates are possible if countries have sound policies, enacted by decisive leaders; a capable administration and science; plus a dose of good luck. This would enable more countries in the world to move into the lower, left-hand quadrant of Figure 2.1 where both COVID-19 mortality and GDP losses are lower. Which countries and regions are likely to demonstrate the greatest economic resilience (Noy et al. 2020)? Is it likely that economic recovery will be U-shaped, as it was in past financial crises such as the one in 2008, when private investment and factor productivity remained below pre-crisis levels for several years?²

As epidemiologists warned, starting in the last quarter of 2020, and extending through the first half of 2021, second and third waves of COVID-19 infections and deaths have hammered a number of countries. The severity of these subsequent waves was exacerbated by the emergence of new variants of the coronavirus. By the second quarter of 2021, new and more virulent strains were taking a toll on countries that had eased restrictions too quickly because they thought that the worst had passed, despite having an adult vaccination rate below 75 percent and/or they were some distance from achieving herd immunity. Although the increasing availability of vaccines in 2021 could blunt the momentum of the pandemic, this will depend on how rapidly producing and administering vaccines can be ramped up (Callaway 2021). Up to July 1, 2021, worldwide dissemination of vaccines had proceeded slowly due the unprecedented scale required, and the logistics of getting vaccines into people's arms.³ In Sub-Saharan Africa (SSA), for example, only 1 percent of the population had been vaccinated by the end of June 2021, and the continent had received just 32 million doses (Financial Times 2021).

² Studies looking at the impact of the 2008 Global Financial Crisis include Reinhart and Tashiro (2013), Schularick and Taylor (2012), Barnichon et al. (2018), and Cerra and Sexena (2018).

³ Ahuja et al. (2021) estimate that a monthly worldwide death toll of 300,000 reduces global GDP by half a trillion dollars. Hence, speedy dissemination of vaccines could drastically reduce losses, including health costs and human capital. Torres et al. (2020) noted that ensuring equitable access by all countries will be an issue requiring global cooperation, which, in turn will be influenced by the supply of vaccines. Furthermore, Torres et al. (2020) state "Development of vaccines that meet regulatory and licensing requirements involves high costs in terms of facilities, equipment, and human resources and is a lengthy process that often fails."

FIGURE 2.1. - COVID deaths and GDP losses



Note: COVID-19 deaths are through October 9th, 2020; GDP losses are based on annualizing data from Q1&Q2 of 2020. Source: Fernandez-Villaverde and Jones 2020.

Economic activity and world trade rebounded in the first half of 2021, but normality will only be restored after most of the world’s population has been vaccinated. This may prove to be a great challenge given that a substantial percentage of people, and not only those in affluent countries, may resist vaccination (Eichengreen et al. 2020). Currently, the threat posed by scattered outbreaks makes it advisable to maintain health protocols such as washing hands, wearing a mask, and social distancing, until, and even beyond when the threat of the virus is eliminated. This would reduce the risk of further outbreaks of COVID-19, as well as the emergence of new, and potentially vaccine-resistant variants.

Also, the pace of recovery will vary across countries depending on their degree of economic scarring;⁴ the potential for remote work where employers and infrastructure allow it; the failure of many smaller businesses; and the pace of start-up activities.⁵ Modelling likely outcomes as the pandemic evolves has been challenging according to Murray (2020) because “the quality of the data does not always improve, and key parameters can shift in unpredictable ways.” Some of the predictions voiced in the early stages of the pandemic have proven to be inaccurate. Countries such

as the United States and the United Kingdom, which have advanced healthcare systems, and top ratings on the Global Health Security Index in 2019, fumbled their response to the crisis, and suffered from a high incidence of COVID-19 infections and deaths. Fortunately, predictions based on the Spanish Flu epidemic of 1918, which caused millions of deaths, have been proven wrong (Ionnaidis et al. 2020). So have the many medical practitioners and researchers who predicted that it would take 3–4 years to develop an effective vaccine (Caldwell 2021).

“Prediction is very difficult, especially if it’s about the future.” The COVID-19 pandemic has made prediction doubly challenging because it combines the most worrisome features of past crises. “[It] combines a simultaneous supply and demand shock; domestic, regional, and global scope, [with virtually all economies simultaneously plunged into recession]; a projected long duration; and a degree of uncertainty.” In addition, according to Bloom and DaFurceri (2021), there have been uncertainty spillovers from key systemic economic problems, which are unmatched by past crises (see Table 2.1 and Figure 2.2). This, as Carmen Reinhart (2021) has observed, “makes forecasting little different from guessing.”

4 Scarring is a potential threat with longer-term consequences. (Apedo-Amah et al. 2020; Fuentes and Moder 2021). A study of individuals drawn from a random sample in rural Indonesia showed that those exposed to a disaster tend to become more risk averse because they fear that the likelihood of disasters has increased. On risk taking behavior, see Cameron and Shah (2015). Lockshin, Kolchin, and Ravallion (2020) found that countries with memories of high World War II death rates responded more quickly to the first wave of the pandemic, although they were no more successful in coping with the second wave. However, the 1957 flu epidemic that killed between 70,000–100,000 people, and led to a plunge in U.S. GDP, is barely remembered. (Lokshin, Kolchin, and Ravallion 2020). Regarding evidence of potential long-run scarring effects from past crises, see Apedo-Amah et al. (2020).

5 According to Ma, Rogers, and Zhou (2020), recovery of investment, employment, and trade in countries hit by six pandemics that have occurred since the mid-1960s (1968 flu, 2003 SARS, 2009 H1N1, 2012 MERS, 2014 Ebola, and 2016 Zika) took over five years. Lower potential output can result from a decline in total factor productivity and lower output per worker (Ollivaud and Turner 2015). Jordà, Singh, and Taylor (2020) paint a darker picture. They found that the aftermath of pandemics dating back to the 14th century was prolonged, with real rates of return remaining depressed for decades, and aggregate demand depressed by precautionary saving. Using data from 190 countries, papers by Cerra and Saxena (2008, 2018) corroborate these findings. For people at the bottom of the economic pyramid, banking and political crises can cause long-term economic damage.

The degree of current uncertainty is captured by three measures: the World Uncertainty Index,⁶ which shows perceived uncertainty rising sharply in 2020, and then slipping back to long-run average levels (see Figure 2.3); the World Pandemic Uncertainty Index of the International Monetary Fund (Bloom and DaFurceri 2021); and the World Bank’s COVID-19 Business Pulse Surveys.⁷ Not only has the pandemic battered a world economy that was already in a fragile state due domestic investment slowing since 2010, the growth of global trade is down to half of what it was before 2008. Also, since 2015 there has been a downward shift in the volume of foreign direct investment (FDI), and beginning in 2020, a sharp drop in FDI.

Inevitably, as information is updated, medium-term forecasts are adjusted. Between January and April 2021, global growth

prospects were revised upward. Now for 2021, both the World Bank and the International Monetary Fund (IMF) have projected global GDP growth of 6 percent (IMF 2021a; World Bank 2021a). The economies of both the United States and China, which together account for 41 percent of global GDP, are projected to grow by 7 percent, and over 8 percent, respectively. If their growth is sustained, the strong performance of these two economies will boost growth in EMDEs through 2022, with countries in East Asia leading the rest. However, the IMF (2021c) in its July 2021 projections expected the growth rates of other regions to diverge. The Middle East and North Africa (MENA) Region and the Sub-Saharan Africa Region could turn in the weakest performances in 2021 (4.0 percent and 3.4 percent, respectively), with many countries “expected to lose a decade or more of per capita income gains” (World Bank 2021a).

> > >

TABLE 2.1. - Ranking of the types of crises and the characteristics of shocks

Types of crises	Characteristics of shocks							
	Scope		Scope		Duration		Certainty	
	Supply	Demand	Domestic / regional	Global	Short	Long	Uncertain	Very uncertain
Pandemics	X	X	X	X		X		X
Wars	X	X	X			X		X
Macroeconomic mismanagement (e.g. hyperinflation)		X	X			X		X
International financial crises		X		X	X		X	
Natural hazards	X		X		X		X	

Source: Loayza et al. 2020.

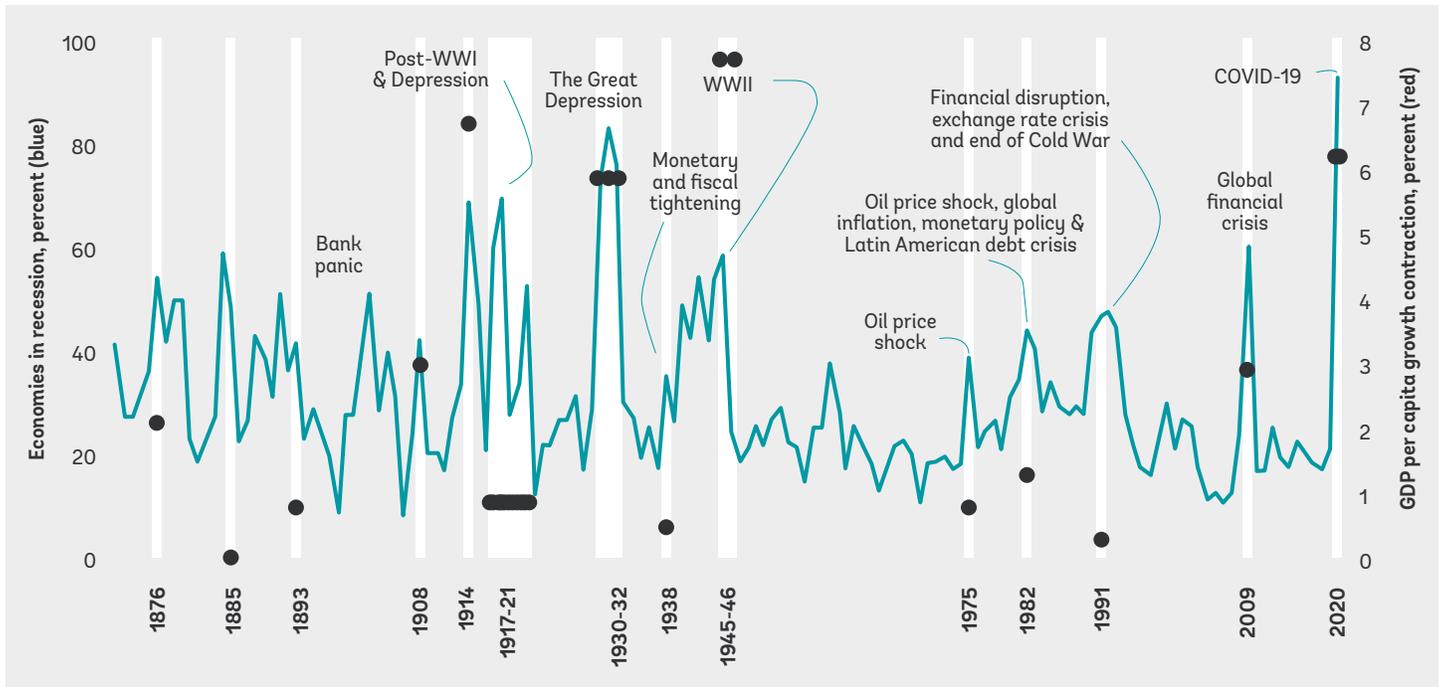
The crisis caused by the pandemic has generated its own ‘alphabet soup’ of recovery predictions, ranging from a V-shaped recovery as the most optimistic, to a middling K-shaped (two-speed) recovery (Ritholtz 2020), and the worst—an L-shaped recovery (Sheiner & Yilla 2020). Given these widely varying predictions, in this report we present both a high- and a low-case scenario, between which the actual outcome may be expected to occur. These are comparable to two of the three scenarios in the World Bank’s Global Economic Prospects (GEP) report for January 2021 (World Bank 2021b)—the pessimistic one and the optimistic one (see Box 1.4 in the GEP). The GEP’s optimistic scenario assumes that rapid deployment of vaccines will be effective in bringing down infections, and that economic activity will revive with assistance from “exceptionally accommodative monetary policy.” The GEP’s pessimistic scenario assumes a persistently high level of cases in leading economies, with vaccinations proceeding at a slower pace, and financial conditions depressing economic recovery.

6 World Uncertainty Index (<https://worlduncertaintyindex.com>).

7 According to Apedo-Amah et al. (2020), the surveys show businesses in EMDEs tended to be more pessimistic about recovery, and their perception of uncertainty was higher.

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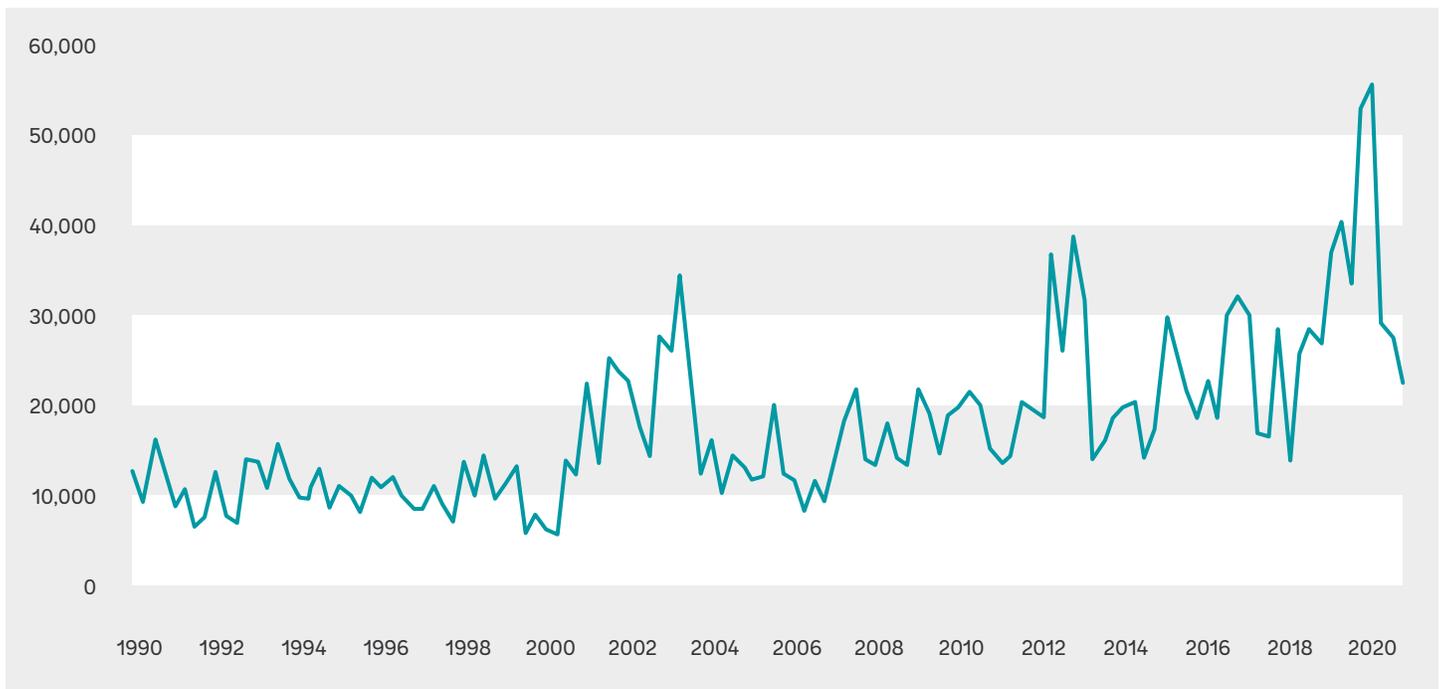
FIGURE 2.2. - Severity and worldwide impact of crises



Source: Loayza et al. 2020.

> > >

FIGURE 2.3. - World Uncertainty Index (through 4th Quarter, 2020)



Note: This figure depicts the percentage of times the word "uncertain" appears in the country reports of the Economist Intelligence Unit, multiplied by 1,000,000. A higher number means higher uncertainty, and vice versa for a lower number.

Sources: World Uncertainty Index (<https://worlduncertaintyindex.com>); Ahir et al. 2021a and 2021b.



Scenario 1: A Global Economy on the Mend

The first scenario comprises the following assumptions, and the rest of this section elaborates on why such a scenario may arise:

- Following the large-scale production and administering of several adequate vaccines in the advanced economies and some EMDEs, starting in the first quarter of 2021, the public health crisis begins subsiding by the third quarter of 2021. The vaccines provide some crossover immunity (Tanne 2021; McCaffrey 2021) and are broadly effective against COVID-19 variants for an extended period.
- Governments avoid excessive fiscal prudence, and the EMDEs manage to skirt debt crises, although debt burdens grow.
- Firms accelerate the adoption of digital technologies, which helps maintain online commerce and boosts firms' productivity.
- There is limited destruction of capital, bankruptcies are checked or resolved, financial fragility is managed thanks to stronger bank balance sheets, and bad debts are written down (Reinhart 2021). Continuation of lending by banks, plus fiscal support, enable broad recovery.
- Services rebound (including some of the hard-hit, customer-facing ones), as do most other industries, many of which have avoided the full force of the crisis (for example, medical supplies and equipment, electronics, food products, and automotive equipment).
- Trade growth resumes; global value chains (GVCs) emerge largely unscathed (although there is some consolidation because of the elimination of marginal suppliers, and measures taken by major GVC firms to enhance their supply chain resilience through diversification and onshoring); trade tensions begin to subside; multilateralism is revitalized (Evenett and Baldwin 2020; Kentikelenis and Voeten 2020; Stiglitz 2020); and the fear of deglobalization is put, at least temporarily, on hold.
- Coordinated action by the G-20 countries continues to speed up recovery.

In the first quarter of 2021, several vaccines became available in quantity from American, European, Russian, and Chinese companies.⁸ Facilities for producing vaccine doses on a mass scale were operating, and solid progress had been made to rapidly qualify, register, package, refrigerate, transport, and administer vaccines. This was mainly in economically-advanced countries, but EMDEs such as Brazil, China, India, and Russia were redoubling their efforts to vaccinate their populations, with India receiving assistance from the United States, the European Union (EU), and others. A waiver on vaccine patents was under consideration in order to augment supplies in countries with production capacity; however, most economists favored high-income countries purchasing vaccines at the prevailing prices, and then distributing them, free of charge, to countries in need. The approximately \$12 billion such a program would cost would be far outweighed by the benefits of worldwide immunity.⁹ Meanwhile, doctors had gained a better understanding of how the virus attacks the body, the efficacy of treatments was improving, and the number of fatalities was declining in the United States and the EU (Ledford 2020; Crow 2020; Kuchler 2020; Budd 2018). New innovations had simplified testing, and the turnaround time for results had been reduced (Billingsley 2021; NIH 2020). In addition, the infrastructure for tracking and tracing people exposed to the virus had evolved, and its workability had been tested by a number of countries.¹⁰

Governments have demonstrated the capacity to engage in expansionary fiscal spending, often on a large scale, and they have also exhibited a readiness—fiscal headroom, and debt and borrowing constraints permitting—to continue using such policies to speed recovery (Gaspar et al. 2020). Varoufakis (2020) rightly observed that “[The pandemic revealed] governments’ inexorable power [to spend].” Fiscal spending will have a significant and continuing role to play over the medium term, and governments with fiscal headroom and external borrowing capacity could expedite the economic turnaround by using the instruments at their

disposal (subsidies, transfers, unemployment benefits, tax relief, infrastructure spending, and procurement) to crowd in private consumption and investment. According to Tomer and his co-authors (2020), investing in infrastructure projects that promise good returns and high job multipliers would be preferable to untargeted income transfers. In addition, to complement public investment, economic recovery programs could prioritize investment in green infrastructure projects through leveraging public-private partnerships (World Bank 2021a). However, measures aimed at supporting firms have been used much more sparingly by lower income countries that are subject to fiscal and borrowing constraints, and support has been primarily directed at well-connected and easier to target, large firms (Cirera et al. 2021).

The pandemic has highlighted the utility of digital technologies. Digital technologies have enabled remote work (Özgüzel et al. 2020; Bartik et al. 2020; Yglesias 2020) by a small percentage of the urban workers who are engaged in professional activities, and know how to use the technology. But this is largely in upper-middle-income countries. E-commerce has enabled many businesses to survive, despite the decline in customers visiting their physical premises. After a lag of several decades, productivity gains from digital technologies could again appear in GDP statistics, with eight sectors, including healthcare, construction, and retail standing to reap significant benefits.¹¹ The shock resulting from the pandemic could also serve as the tipping point for business digitization. Both large and small businesses can now see the advantages of using digital platforms and social media to sell products and services online, as well as settle transactions.¹² This is apparent from the significant rise in online retail sales in developed, as well as emerging economies. In the United States, for example, in the first two months of the COVID-19 crisis, online sales as a percentage of total retail sales, rose from 16 percent to 33 percent (Kotz et al. 2021). In China, the share of online retail sales rose from 10 percent in 2014 to 45 percent in 2020, and online sales are projected to exceed 50

8 Hundreds of thousands of people are receiving vaccinations in Russia and China, and these vaccines are now being made available in EMDEs at attractively low prices. The Russian Sputnik V vaccine is being marketed for under \$10, and 20 countries have lined up to purchase doses (Litvinova 2020; Cohen 2020). Following emergency approval of vaccines in the United States and Europe in December 2020, the vaccination of the general public picked up speed in early 2021 (Zimmer, Corum, and Sui-Lee 2021; WHO 2020; Craven 2021; McKeever 2021).

9 Vaccines developed by Pfizer and Moderna received emergency authorization in December 2020 and similar approvals were obtained in early 2021 for vaccines produced by AstraZeneca, Johnson & Johnson, and others. Chinese and Russian vaccines are also available (Zimmer and Thomas 2020). However, “An ideal pandemic vaccine [should] be acceptably safe for everyone, effective in inducing a durable protective immune response, rapidly scalable, stable at room temperature, single dose and cost effective. None of the current candidates has all these characteristics. Two of the front-runner mRNA vaccines demand (very) cold storage, at least two injections and, in some cases, site-of-care dilutions, raising costs and complicating delivery” (Bingham 2020; Cookson and Miller 2020; and Economist 2020b). “A vaccine with 90% efficacy will require 54%–72% of the population to be vaccinated to confer herd immunity” (Shretta et al. 2020). Regarding the case against waiving vaccine patents, see Vaitilingam (2021).

10 Estonia is one of those countries that has benefitted from a state-of-the-art IT system (Charette 2020). See Huang, Sun, and Sui (2020) and Huang (2020) regarding reservations about such systems’ potential invasiveness.

11 The productivity paradox has aroused much debate. Digital technologies have been diffusing for the past 40 years, and the rate of diffusion has been faster compared to earlier general purpose technologies (GPTs), but diffusion is far from complete, and the productivity gains have not materialized (OECD 2019). In fact, total factor productivity has been declining, worldwide, since around 2010. Some like Brynjolfsson, Rock, and Syverson (2017) and Mokyr (2014) maintain that technological change will be a continuing vital force, and that effective incorporation of a new technology takes time, and requires many complementary changes in organization management and working practices, plus the accumulation of skills and intangible capital. Others such as Gordon (2012, 2018) espouse the view that digital technologies cannot deliver productivity gains comparable to those resulting from, for example, the adoption of electricity and the internal combustion engine. One doubter of the technology revolution has recently expressed second thoughts (Ohnsman 2020), and Kotz et al. (2021) are optimistic that productivity could revive.

12 See Papadopoulos et al. (2020); Chow and Li (2020); and Abanmai (2020). Nigerian health authorities have used Twitter and Facebook to inform the public about COVID-19 symptoms and how to avoid infection (Jiang and Ryan 2020).

percent in 2021 (U.S. Department of Commerce 2021; Gruenwedel 2021; Cramer-Flood 2021; Ma 2021; CIW Team 2021). World Bank (2020b) reports on the Philippines and the Russian Federation also point to the benefits of digitalization for companies, as well as for public agencies.

While firms were forced to cut workers or put them on unpaid leave, this situation has also given firms the flexibility to make organizational changes in order to exploit digital technologies more fully (Brynjolfsson et al. 2017). According to Comin and Mestieri (2018), this should accelerate the diffusion of innovation, and narrow the productivity gap between large firms and small and medium enterprises (SMEs). Thus far, only a small number of firms in EMDEs appear to be taking advantage of digital technologies. According to the World Bank's COVID-19 Business Pulse Surveys in 2021, only one in three firms in EMDEs had increased the use of digital technology in response to COVID-19 (Apedo-Amah et al. 2021). Nevertheless, an experiment in a rural area of China suggests that providing infrastructure, user-friendly platforms, and technical assistance can facilitate the entry of small suppliers in rural areas (Luo 2018; Wang 2017; World Bank 2019). It is also possible to envisage institutional and regulatory innovations that improve the functioning of the public sector. In the EMDEs, the pandemic and the threat of other shocks to come may change the future of work (Baldwin 2020; Seric and Winkler 2020) and drive home the advantages of artificial intelligence (AI), machine learning, and automation, especially for larger, export-oriented firms. As some of these are asset-light investments, firms may be readier to commit to full integration. In addition, firms might also be more ready to embrace greater factory automation so that they minimize the disruption from the shocks that could come in future.¹³ A reversal of the downward plunge in productivity could be possible if firms seize the opportunities to make the needed investments, and increase their research so that they can push technology frontiers.¹⁴ According to di Mauro and Syverson (2020), this would be good for growth and, hopefully, for employment as well, although the distributional consequences are less easy to anticipate. Gordon (2021), for example, has tempered his

past pessimistic forecast for U.S. productivity growth, and now perceives the opportunity for improvement.

The COVID-19 shock has resulted in minimal destruction of capital. This, plus assistance from governments, has allowed many medium- and large-sized businesses in high- and middle-income countries to survive.¹⁵ With some firms exiting the market, the growth prospects for the remaining firms could improve as the global economy revives. Likewise, countries with robust domestic supply chains are capitalizing on the recovery of trade (WTO 2020; Kim 2020). For example, China's exports rose by 3.6 percent in 2020, topping \$2.6 trillion (although the yuan appreciated by 6.1 percent against the dollar). The Wall Street Journal noted in early 2021 that China's economy ended "the Year of the COVID" stronger than when it started, and exports in the first half of 2021 were 28 percent higher than in the first half of 2020.¹⁶ Vietnam's exports were 5.3 percent higher, year-on-year, so that country also entered 2021 on a strong footing (Thuy 2020). Kenya's floriculture industry, which contributes 1 percent of the country's GDP, has seen its fortunes revive, and in January 2021, it was employing more workers than a year earlier (Economist 2021). In fact, global trade, which was initially forecast to decline by 18 percent or more in 2020, actually fell by only 5.3 percent. In 2021, trade showed signs that it will make up for the ground lost in 2020 due to stretched supply chains, and considerable pressures on container shipping from a surge in demand for commodities and manufactured goods. Some consolidation of the hard-hit retail, leisure/hospitality, and transportation industries is likely, and while this could lead to an increase in industrial concentration, and higher profit margins, it may benefit productivity (although doubts have been expressed about this).¹⁷ If larger firms achieve greater scale and harness new technologies, they could more easily mobilize the resources they need to "build back better."¹⁸

Falling oil prices have favored energy importers at the cost of petroleum exporters. Thus, the economies of oil-producing Middle Eastern and North African countries may recover more slowly, although the uptick in oil prices since

13 Firms may be less eager to accelerate the automation of light manufacturing—for example, garment and footwear manufacturers—as there is an abundant supply of low-wage workers who can be laid off in a downturn without incurring high severance costs. Over the medium term, some 40 percent of firms in the EU see the need for more digitalization to adapt their product/services portfolio and improve supply chain resilience (Revoltella and de Lima 2020).

14 The private and social returns from research and development (R&D) are in the double-digit range. Restrictions imposed by the pandemic have affected research in some areas. Luckily, the sectors most affected by the pandemic are among the ones that spend very little on research—retail, real estate, and travel. In the aftermath of the 2008 Global Financial Crisis, the large private firms that undertook the bulk of R&D continued to invest in R&D because their competitiveness hinges on innovation. Since the pandemic began, the information and communications technology (ICT), pharmaceutical, and biotechnology industries with large cash reserves have ramped up their research (Dutta 2020).

15 For more information on government assistance catalogued by the International Monetary Fund, see the IMF's website (<https://www.imf.org/en/Home>).

16 Xie, Jeong, and Cherney (2021) and Cheng (2021). Net exports may have added 0.3 to 0.4 percentage points to China's growth in 2020, which was estimated at about 2.2 percent.

17 Marin (2021) has expressed doubts based on concerns regarding disruption of supply chains and the time taken to absorb new technologies and automate production. 18 While capital is available at low or negative rates of interest, only the larger, bankable firms are in a position to avail themselves of these resources. In 2021 and beyond, assuming that recovery does gather momentum, larger firms should face an abundance of opportunities, and have access to ample supplies of capital. Some of the excess savings resulting from the pandemic will be—and are—mopped up by governments, but this need not crowd out the private sector (Quiggin 2020; Mian, Straub, and Sufi 2020; Dvorkin 2020; UNCTAD 2020).

the first quarter of 2021 could improve their fortunes.¹⁹ Also, according to Buehler (2020), in most countries, bank balance sheets are in better shape thanks to measures taken after the 2008–2009 Global Financial Crisis, plus assistance from their central banks. In emerging markets, economic engines could restart through the combination of selective government assistance to viable firms, and portfolio and direct investors searching for higher yields and growth prospects, plus a fiscal boost, where that is feasible, and aided by low interest rates.²⁰ Given the wide range of new technologies disrupting existing markets, the investment opportunities in a recovering economy are plentiful.²¹

Consumer demand is poised to lead the recovery. The economic cost of the pandemic has been unevenly distributed. Those who are higher on the income ladder, and who are doing white collar jobs and able to work remotely, have suffered much less worldwide (Adams-Prassl 2020). Household savings rose in the United States (Bilbiie et al. 2021); the European Union (Dossche and Zlatanov 2020; Crowley 2020; Galletta and Giommoni 2020; Coibion et al. 2020); India (Bellman 2021); and China, while household indebtedness also fell (Deaton 2021). Conversely, the high percentage of urban people who work in low-wage, manual jobs, and engage in informal activities, have borne the brunt of the pandemic. Income inequality has also risen, although so far if each country is treated as a unit, global inequality may have declined, because the losses in high income countries in the first quarter of 2021 were more severe (Deaton 2021). The divergence of incomes may strain social stability and demand government attention; however, higher savings could fuel consumer spending and speed recovery. This is what happened after World War II, and a surge in spending was already apparent in 2020 (Davidson 2020; Bird 2020; Gagnon 2020; Bossie 2013). Undoubtedly, the sustained recovery of consumer spending will depend on how convincingly the pandemic is brought under control in 2021. The turnaround in China's economic performance in the third quarter of 2020, its 6.5 percent per annum growth in the fourth quarter of 2020, and its even faster growth in the first half of 2021, all suggest that China's performance in 2021 should equal the forecast rate. In addition, in the United States, as has been the tendency after past crises and downturns, employment recovered rapidly (see Figure 12 in Hall and Kudlyak 2020).²² With U.S. unemployment down to 5.9 percent in June 2021, a continuing strong performance of

the economy is likely in the latter part of 2021. In the United States, the passage of a \$1 trillion+ infrastructure bill and a \$3.5 trillion bill to fund family programs, clean energy, and expand Medicare would further add to aggregate demand, and minimize the risk of secular stagnation. A U.S. economy that is growing strongly would be good news for trade-oriented EMDEs.

Both tradable and non-tradable services could rebound rapidly and offer additional opportunities. In some middle- and upper-middle-income countries, thanks to making good use of telemedicine, healthcare is enjoying a boom (Liu 2020). Given the accumulated experience, disruptive innovation in education, which is currently being trialed at scale, could, in a limited way, arrive in the classroom.²³ Business services and export industries capable of remote operation have largely weathered the storm (Espitia et al. 2021). Construction activities, which slowed, have begun recovering quickly. The same applies to many informal activities. Other sectors such as retail, restaurants, entertainment, and hospitality could begin bouncing back, too, because entry barriers and start-up costs are low. But a return to the pre-COVID-19 status quo may not fully materialize until 2022. Barrero and his co-authors (2020) speculate that, given the investment in equipment by the average telecommuting worker, as well as firms' investment in back-end information technology (IT) equipment and support, working from home could persist in advanced economies and some EMDEs, which could result in less spending on meals, entertainment, and shopping in central business districts.

Once the threat from the virus is controlled, and countries take measures to allay the concerns of travelers through insurance, sanitization of facilities, contactless entry/registration, and COVID-19 vaccine passports/certificates, travelers' pent-up demand could revive the tourism sector. This was already apparent from Dubai's surge of visitors at the end of 2020 and into 2021, as a vaccination saturation campaign served as a bulwark against the virus. Going forward, tourists are likely to favor destinations that have credibly demonstrated their ability to bring the pandemic firmly under control, and have proven measures in place to prevent any recurrence. The quality of local transport, IT infrastructure, and the healthcare system will undoubtedly influence the decisions of travelers (IFC EM Compass Note 2020). Educational travel could begin reverting to pre-COVID-19 trends by the fall

19 Troster and Kublbock (2020). In 2021, recovery of MENA countries could be slower than the average for EMDEs.

20 How long these rates will persist is uncertain, but for those borrowers who can avail themselves of low, long-term rates, these rates are a means of financing long-lived infrastructure.

21 In the digital space and in other areas as well—for example, auto components (Kaka et al. 2019 and Barathram et al. 2020).

22 Hall and Kudlyak (2020). Experience from 10 post World War II recessions in the United States, which preceded the recession caused by the 2008 Global Financial Crisis (GFC), shows that real GDP fell by 2 percentage points, and the output gap increased to 4 percent. Following the onset of the GFC, real GDP declined by 5.1 percent by the second half of 2009, and the output gap widened to 8.1 percent (Elwell 2013).

23 For example, education could become more personalized (Barsotti 2020; Amitabh 2020). To date, the results from the use of technology in the classroom have been mixed, with student learning showing no improvement, although computer proficiency rose. (Escueta et al. 2017; Abbasi et al. 2020; Hobbs and Hawkins 2020).

of 2021. However, business travel may be slower to recover,²⁴ including meetings, incentives, conferencing, and exhibitions (MICE) tourism because the use of videoconferencing grew tremendously over 2020 (Curley et al. 2020; Rosen 2020; Frost 2020).

If governments turn their attention to greening infrastructure during the 2021 United Nations Climate Change Conference (COP26), which is scheduled for November 2021, demand for a host of input suppliers could rise (Drescher and Mollame 2020; Barbier 2020). Of the major manufacturing industries, only the aircraft and airline industries might lag behind the others because of reduced business travel. By mid-2021, domestic air travel recovered in the United States and was close to pre-pandemic levels, and in China, vacation bookings were up as well. Tourism, for its part, has long proven to be highly resilient.²⁵ However, the third virus wave affecting the EU, India, and some Latin American countries during the second and third quarters of 2021, could continue dampening intercontinental travel for a few months; but, as the numbers of the vaccinated increase and a system of vaccine certificates/passports is put in place, controls could be relaxed (Markovitz 2021).

The challenges that EMDEs face due to deglobalization (Irwin 2020; Herrero 2019; Altman and Bastian 2019; Ghemawat and Altman 2019); **shrinking global value chains;**²⁶ **and industrial reshoring have been exaggerated** (Fish & Spillane 2020). There is scant evidence that a sharp reversal of globalization is imminent. It has leveled out, but unless the politics in leading countries take a turn for the worse, and trade wars intensify (less likely since the election of U.S. President Joe Biden in November 2020, and the appointment of Ngozi Okonjo-Iweala as head of the World Trade Organization),²⁷ this seems unlikely.²⁸ The signing of the Regional Comprehensive Economic Partnership (RCEP) by 10 members of the Association of Southeast Asian Nations (ASEAN), plus Australia, China, Japan, Korea, and New Zealand on November 15, 2020, indicates that trade liberalization is alive and well, and

global value chains (GVCs) are rebounding.²⁹ There was a dip in trade in 2020 due to problems with GVCs, but the disruption from the pandemic shock is being contained, despite persisting shortages of some inputs and rising prices.³⁰ Some of the decline prior to 2020 was the result of technological change, companies taking steps to consolidate suppliers, localization in China, and creeping protectionism. But little reshoring has actually occurred.³¹ Adidas' inability to successfully operate highly automated shoemaking factories in Germany and the United States, and the subsequent relocation of production to Southeast Asia, is emblematic of the problem (Germano 2019). Undoubtedly, companies will make token efforts to reduce reliance on a single production location. As Shingal and Agarwal (2020) have observed, there was disruption of GVCs following the SARS virus epidemic in 2003. Starting in 2020, companies were again reviewing their China+1 strategies to ensure that they have one other source besides China, and they were looking for producers in Southeast Asia and Central America.³² While companies recognize the advantages of redundancy in the interests of robustness and resilience, the likelihood of massive restructuring of the world's production seems remote.

Similar predictions about the restructuring of GVCs were common following the 2008–2009 Global Financial Crisis, and in 2011 after disastrous floods in Thailand, and the Fukushima earthquake and tidal wave, but very little GVC restructuring actually occurred (Yang 2011; Escaith et al. 2011; Newing 2012; de Treville and Trigeorgis 2010; Baldwin and Venables 2010; Cattaneo et al. 2010). Multinationals have been looking around for alternative suppliers for more than a decade, but they have found few options. For example, many of the components that U.S. companies use to manufacture 3D printers are sourced from China, and technologically advanced hearing aids are now made in Vietnam. However, expanding the production of semiconductors in the United States will take years, and require substantial government incentives. Only in 2019 did a trickle of manufacturing return to the United States, despite the efforts of the Trump administration (Ferry

24 As much as three quarters of airline revenue on international flights accrues from business travel (Hancock and Georgiadis 2021).

25 UNWTO (2020). The revival of tourism is critical for many economies because it accounts for 10 percent of global GDP, and one in ten jobs.

26 Dachs and Pahl (2019). Trade in services is growing faster (Lund et al. 2019; Degain, Meng, and Wang 2017; Kantrup et al. 2020; WTO 2019).

27 Evenett and Baldwin (2021) have suggestions for the new Director General of the WTO, urging Okonjo-Iweala to do her utmost to ensure that the trading system remains open and trade revives.

28 Persistence of the recent rise in protectionism, and efforts by major countries to reduce their dependence on other countries for strategic products cannot be ruled out. But the pandemic has underscored the advantages of trade and cooperation, as well as the limits of self-sufficiency (Dollar 2020 and Evenett; Baldwin 2021). Also see Antràs (2020) and Bloom and Pretzner (2020).

29 The need to source personal protective equipment (PPE) from across the world to make up for local shortfalls during the COVID-19 pandemic, has highlighted the role of GVCs (Bamber, Fernandez-Stark, and Taglioni 2020). The demands for supplies generated by the pandemic also drew attention to the disadvantages of localization. Ariola and van Tongeren (2020) note: "More localization means more reliance on fewer [and more expensive] sources of inputs...When disruption occurs somewhere in the supply chain, it is harder and more costly to find ready substitutes, giving rise to greater risk of insecurity of supply."

30 Espitia et al. (2021) conclude: "While GVC participation increased an exporter's vulnerability to foreign shocks, it reduced vulnerability to domestic shocks. The disruption of production in input source countries more adversely affected export growth in sectors that relied more strongly on imported inputs from these source countries. Similarly, a disruption of production in an exporter's partner countries more adversely affected its export growth in sectors with high shares of imported inputs. But the negative impact of a disruption in domestic production in exporting countries themselves was mitigated by a sector's higher reliance on imported inputs in export production."

31 A study using Spanish data indicated that robotization can lead firms to offshore rather than re-shore production (Stapleton and Webb 2020).

32 Shingal and Agarwal (2020). The COVID-19 pandemic has disrupted container shipping. With trade rebounding, led by consumer demand and the rebuilding of inventories, the shipping business is under severe pressure caused workforce illnesses, quarantining, social distancing, and a shortage of truckers. One consequence is congestion at major terminals, with container vessels having to queue for berths (Steer and Wright 2020).

2020). The tariff barriers the United States erected have failed to significantly shift production back to the country (Krugman 2020; Zumbun and Davis 2020). Cambodia, Thailand, and Vietnam are frequently mentioned as alternatives to China, but, at best, they can absorb only a small slice of the low-tech activities carried out in China. Low labor productivity in Vietnam also diminishes its attraction for multi-national corporations (Viet Nam News 2019; Breu 2012). Indonesia, the Philippines, and Thailand will attract some foreign direct investment, but according to the World Development Indicators database, the falling share of manufacturing in GDP clearly suggests that these countries are unlikely to challenge China's dominance of medium and high-tech product GVCs. The same is true of the Caribbean, Latin America, and South Asia. Manufacturers of semiconductors and telecommunications equipment are exploring the possibility of moving some production to India. For example, at the urging of Apple, the Chinese electronics producer, Foxconn, is investing \$1 billion to expand its capacity to assemble iPhones in India, but the bulk of Apple assembly operations remain in China. It would also be a slow process to shift the processing of cobalt, rare earth minerals, and polysilicon, as well as the manufacturing of advanced magnets from China to other countries. Despite some talk about leaving, U.S. and European companies (Chow 2020; Fang 2020; Payne 2020; Liwei and Guo 2020) are in no hurry to forsake China (Li 2019). In fact, because China's economy has suffered less from the pandemic, it has recovered faster. Moreover, although the renminbi has strengthened (Xie 2021),

China's currency remains competitively priced against both the dollar and the euro (Setser 2020), which is another reason why China will likely retain its grip on value chains for some time.³³ According to Bermingham and Leng (2020), the surge in Chinese exports, starting in the second half of 2020, and extending to mid-2021, is indicative of China's economic resilience and its continuing competitiveness.

In this positive scenario, the resumption of growth in leading economies, and of trade, would “lift most boats (countries)”. The launch of a coordinated effort by the G-7 and G-20 countries to drive recovery of the global economy in 2021 is comparable to the measures they took following the 2008–2009 Global Financial Crisis, and these measures could powerfully reinforce recovery.³⁴ EMDEs, and especially those that are integrated in GVCs; those that are exporters of primary commodities; and some that are dependent on tourism, should all see their economic fortunes improve. Exporters of commodities have already glimpsed the beginning of a new super cycle, with the rise in copper, iron ore, and lithium prices serving as a leading indicator (Bullard 2021). This could be the beginning of a virtuous spiral. The economic data from China, the United States, and the East Asian economies for the fourth quarter 2020, and the first half of 2021, are encouraging, although these signs of recovery need to be treated with caution as the spread of the more infectious COVID-19 Delta variant has aroused worries.

33 China's dual circulation plan, and the persistence of trade tensions—if carried on—could further reduce China's dependence on imports of high-tech items (from the United States, Korea, and Japan), and on exports.

34 See Rooney (2011).



Scenario 2: A Slow, Uneven Recovery

The second scenario comprises the following assumptions, and the rest of this section elaborates on why such a scenario may arise:

- A severe and widespread third, and more waves of the pandemic caused by mutated viruses that are not sufficiently blunted by vaccination on a global scale (IMF 2021b) lead to: more lockdowns (Gros 2020), tightening of travel restrictions, quarantining, a double-dip recession, and spillover effects from the leading economies, which drag others down (Torry and DeBarros 2020; Lane 2020).
- The logistical challenges of EMDEs acquiring, distributing, and administering vaccines are more severe than anticipated, and achieving 70–80 percent coverage of populations proves to be beyond the capability of many governments. In part, this is because of insufficient vaccine supplies, some people refusing to be vaccinated, and difficulties reaching people in rural areas.³⁵
- The scars inflicted by the pandemic, and the uncertainty it generates, depress private investment, potential output,³⁶ FDI, and consumer spending beyond 2021–2022. Over the longer run, the erosion of human capital compounds the losses incurred from 2020 to 2025.
- Business and household financial distress deepen due to both supply and demand shocks, and debt servicing/write off issues tip financial systems into crisis.³⁷
- Debt distress begins afflicting increasing numbers of EMDEs, giving rise to demands for debt restructuring (Spence and Leipziger 2020), and this is exacerbated by corporate distress, credit downgrades, and the default of corporate bonds (EI-Erian 2020).
- Bankruptcies of many SMEs lead to increasing industrial concentration and rent-seeking pressures, with negative implications for innovation and productivity over the medium term.
- Following a sluggish start in the first half of 2021, the growth of global GDP, trade, FDI, travel, tourism, and remittances slows down in the second half; a return to 2019 GDP levels is pushed into 2022, or beyond; key GVCs come under strain (in part because the trade tensions

35 Some African and Asian countries may have difficulty getting access to a sufficient number of doses. There may also be resistance to vaccination in some quarters. Goebel, Mayrhofer, and Schmitz (2020) have found that some people, especially ones with pre-existing conditions, can be reluctant to accept a vaccination: “The decision on getting vaccinated does not depend on how risk-willing or risk-averse someone is but rather on ‘prudence.’”

36 If the pandemic depresses the capital stock by reducing investment or making some capital obsolete as happened in the aftermath of the 2008 Global Financial Crisis, long-term potential output could suffer (Fuentes and Moder 2021).

37 Surveys conducted by the World Bank in the middle of 2020 indicated that the majority of firms in EMDEs could be in arrears by the end of the year if the crisis is not contained, and recovery does not begin (Apedo-Amah et al. 2020 and Crow 2020).

between the United States and China remain unresolved, or worsen); and many suppliers in EMDEs go under.

- Having largely exhausted their fiscal and monetary firepower, most EMDEs are unable to support jobs and businesses, and this leads to a downward spiral of activity and greater unemployment, poverty, and social tensions.
- Social unrest imperils the functioning of states in some of the hardest hit countries. According to Herrera and his co-authors (2020), electorates will vote out governments that do not take adequate measures to control the second or third wave of the pandemic and contain the economic damage. In carrying out their study, Sedik and Xu (2020) found that pandemics and associated hardship can unleash a wave of despair, unrest, and lead to increasing inequality—especially in countries where inequality was substantial before the start of the pandemic.
- The inability of G-7 and G-20 countries to agree on a coordinated plan to share vaccines and other pharmaceutical products to contain the pandemic, or to agree on how to stimulate recovery, prolongs the pain, and the achievement of global herd immunity (MacMillan 2021; Aschwanden 2020).

This scenario points to a sluggish, long-drawn-out U- or L-shaped recovery, extending through 2022 and possibly, beyond—akin to the low growth scenario described in the World Bank’s January 2021 Global Economic Prospects (GEP) report. GDP growth and trade could remain anemic through the middle of the decade because of the damage done to: consumer confidence and demand, private investment, start-up activity, FDI, factor productivity, and the accumulation of human capital. China was already rethinking its investment in the Belt and Road Initiative (BRI) prior to the COVID-19 crisis. China’s outward FDI fell by 8 percent in 2019, and slid further in 2020, with lending by the China Development Bank and the China Ex-Im Bank declining from \$75 billion in 2016, to \$4 billion in 2019 (Wheatley and Kynge 2020a and 2020b; Tanjanco et al. 2020). The high indebtedness and precarious finances of China’s principal low- and lower-middle-income country recipients (Ray and Simmons 2020) is likely to reinforce the reluctance of Chinese lenders to increase their foreign exposure. According to the United Nations Conference on Trade and Development (UNCTAD), FDI from all countries fell by 42 percent from \$1.5

trillion in 2019 to \$859 billion in 2020 (UNCTAD 2021). A further downward slide would be most harmful for countries in Central and South Asia and Sub-Saharan Africa. Over 40 percent of the chief executive officers (CEOs) surveyed by the World Economic Forum in September 2020 thought that recovery would be U-shaped, especially if countries succumb to financial and/or debt crises.³⁸ Only a small minority (except in China) believed that a V-shaped outcome was possible (Table 4.1). A survey by McKinsey in November 2020 indicated that the outlook was improving, but this was before new variants of COVID-19 had begun to appear, and when positive memories of recovery from past crises continued to color perceptions (McKinsey 2020b).³⁹ A survey of CEOs conducted by PriceWaterhouseCoopers (PwC) in March 2021 indicated that the intervening months had strengthened CEOs’ positive sentiments, with 76 percent expressing greater optimism regarding their corporate prospects in 2021 (PwC 2021). However, since the first quarter of 2021, worries have grown due to the resurgence of infections caused by the COVID-19 Delta variant.

As noted by the World Bank’s January 2021 GEP report, the risk to EMDEs is considerable because of countries’ high and rising levels of indebtedness, which have already exceeded sustainable levels. The debt-induced pressures will be even greater if interest rates rise, as some in the United States fear that they will because of the uptick in inflation.⁴⁰ Bulow and his co-authors (2020) contend that “There are reasons for concern about sustained emerging market access to capital markets. The riskiest period may still lie ahead. The first wave of the pandemic is not over...[another wave has started]. Businesses [in EMDEs] have continued to accumulate foreign currency debt...On top of [a] dramatic retreat of private funding... borrowing needs have skyrocketed...and will only rise further as the economic damage mounts...Rising budget pressures have been accompanied by a new wave of sovereign debt downgrades, surpassing peaks during prior crises.” A sudden stop of capital flows to EMDEs could make it harder for them to recover, according to Ahmed et al. (2020). Economic scarring, over the longer term, that depresses output below its potential, was a risk identified by Cerra and Saxena (2008 and 2018) when they used data from 190 countries for the period 1974–2012. These authors observed output losses from recessions inflicted by all types of crises, both economic and political. “On average, the magnitude of the persistent loss in output is about 5 percent for balance of payments crises, 10 percent for banking crises, and 15 percent for twin crises” (Cerra and Saxena 2018).

38 Reinhart and Rogoff (2014). Banking sector distress is a concern for India, which has one of the highest ratios of bad debts in the world, and an economy that has contracted by over 10 percent of GDP. Non-performing loans are projected to increase from 7.5 percent to between 13.5 percent and 14.8 percent by September 2021 (Parkin 2021).

39 Hall (2014) describes and analyzes the damage that the 2008 Global Financial Crisis inflicted on the U.S. economy, which was caused primarily by the slow recovery of employment/participation rates and the downturn in total factor productivity. Also see Krishnamurthy and Muir (2017) and Hauk (2020).

40 Andrews (2019) and Kose et al. (2020). Memories of the taper tantrum of 2012 have not entirely dissipated. See Basri (2016) on the impact on Indonesia. Hence the discussion is underway about whether the U.S. stimulus packages could lead to inflationary pressures and higher interest rates.

TABLE 4.1. - Trajectory of recovery from the pandemic

Region	L-shape	U-shape	W-shape	V-shape
Global (N = 606)	32%	42%	16%	11%
U.S. (N = 103)	26%	42%	23%	9%
Europe (N = 110)	29%	55%	12%	4%
China (N = 122)	25%	43%	11%	21%
Japan (N = 95)	49%	26%	23%	1%
Gulf Region (N = 16)	57%	26%	17%	-

Source: Ghosh 2020.

In this negative scenario, all EMDEs would suffer to varying degrees, depending on their size, openness, structure of their economy, level of development, composition of exports, disruption suffered, the scarring that erodes human capital and depresses future investment (Economist 2020a), and the effectiveness of EMDEs’ responses to the pandemic. High-income and large economies, with greater absorptive capacity and resilience, and less dependence on trade, will find it easier to absorb the damage and recover if they can extinguish the epidemic through vaccinations and other measures—and India and Brazil are two test cases for this. China was the first country to report cases of COVID-19, but it was also the first to rebound because of the decisive actions the government took to control transmission of the virus. Economies such as those of Finland, New Zealand, Vietnam, and Taiwan, China, have also limited the damage. The countries with some remaining fiscal headroom and scope for extending financial support to businesses could use macro-economic policies to revive consumer spending—the main source of aggregate demand—and also encourage private investment. In this regard, China is the best positioned, and has already taken the lead. China has controlled the pandemic, and is using fiscal and monetary instruments to restore economic normalcy. Others such as Brazil, Colombia, India, Mexico, and South Africa are struggling with fresh virus waves of considerable ferocity, but when compared to some of the smaller countries in the Caribbean, Latin America, Sub-Saharan Africa,⁴¹ and South Asia, these five countries have more degrees of macro policy freedom (Lath et al. 2020; Chan et al. 2020; Sankhe et al. 2020).

In recessions, the expectation (embedded in the Schumpeterian theory of growth) is that relatively weaker firms exit, and the productivity of the economy usually increases

(Schumpeter 1912). While this is painful, it is ultimately positive as capital and labor shift from less to more productive activities, assuming that these factors are fungible. Government support policies have, in most cases, not discriminated among firms and, thus, they support weaker, as well as stronger firms. However, there has been less up take by smaller and informal firms. As previous “credit crunches” reveal, firms with perfectly sound business models and strong profitability may be forced to close for reasons that are entirely beyond their control. Furthermore, during the COVID-19-induced recession, the “weaknesses” of many firms, and particularly those in services, result directly from compliance with public health and safety rules and obligations. This has been especially the case for services in high- and middle-income countries. Thus, untimely closures of businesses are not only painful, but this can drive out viable, innovative young firms with growth potential. Indeed, there is growing concern that as countries scale down financial forbearance measures, along with other forms of support to firms that were instituted at the beginning of the pandemic, bankruptcies of otherwise-viable firms will rise (Freund and Pesme 2021).

An increase in market concentration that persists as the entry of new firms slows, would have negative implications for public welfare because this would push prices up, and slow recovery. In EMDEs, this issue will require special attention during recovery, as regulatory protection of existing enterprises in upper-middle-income and lower-middle-income countries is more than 40 percent. And in high-income countries, the level of protection observed is 60 percent. However, in some sectors such as health and education, where there are private providers of public goods and services, a moderate degree of market concentration may be necessary to achieve standardization and quality.

41 The Latin America and Caribbean (LAC) Region, which was growing sluggishly prior to the pandemic, has been hit hard, and is unlikely to return to its pre-pandemic GDP level before the end of 2023. A quarter of all deaths from COVID-19 in 2020 were in the LAC Region, although it has just 8 percent of the world’s population. Recovery is also likely to be constrained by the world’s highest public debt to GDP ratios (FT 2021b).

Countries that are integrated in GVCs face mixed outcomes. Firms in East and Southeast Asia, as well as those Eastern Europe and Central America that produce semiconductors, electrical machinery, telecom equipment, vehicles, pharmaceuticals, and healthcare products, could benefit from strong demand from China, European countries, and the United States. If the recovery of China and the United States continues, it will enable countries in Southeast Asia to regain their economic footing. However, countries such as Bangladesh, Cambodia, Ethiopia, Pakistan, and Sri Lanka, which are integrated in GVCs for garments and footwear, could face a more difficult situation (Becker 2020; Choudhury 2020). This is because demand for these products shrank in 2020, and worse could occur if the global downturn persists. For the same reason, if the recovery is U shaped, suppliers of agricultural commodities and minerals could suffer from lower prices and demand for their products. According to Osterhuber (2020), examples of this include Central American countries (exporters of coffee and bananas); Chile (an exporter of copper); and Cote d'Ivoire (an exporter of cocoa, cashews, and palm oil).

Another group of small economies are dependent on tourism and, arguably, they are among the most vulnerable in a low growth scenario. These comprise countries in Africa, the Caribbean, and South Asia. Several European countries, and others such as Cambodia, Peru, Sri Lanka, and Thailand derive a substantial share of their foreign exchange earnings from tourism. All have taken a severe hit, especially because travel and tourism are among the industries most damaged by the pandemic.⁴² In 2020, real GDP in tourism-dependent African and Caribbean countries was estimated to have fallen by 12 percent, and by as much as 21 percent in Pacific Island nations such as Fiji. The degree of disruption, together with considerable restructuring and consolidation in the tourism sector, means that in EMDEs there will be fundamental and permanent changes that give rise to risks, as well as opportunities.

For the decade before the crisis, the tourism industry was characterized by profound changes: an increase in ultra-long-haul flights; pressure to demonstrate sustainable and responsible business practices; an increase in wellness tourism; a trend toward peer-to-peer accommodation and transportation providers such as Airbnb and Uber (Bakker et al. 2018); and growing use of digital platforms for booking transportation and accommodation. These digital platforms, which allow consumers to search for and book flights and accommodation: facilitate consumers' decision-making (Lopez-Cordova 2020), improve sector competitiveness, and contribute to the growth

of the tourism sector. Pre-COVID-19, the insurance market benefitted not only from the preceding decade's growth in travel, but also from the greater use of online booking platforms. These exploited the opportunities provided by technologies such as global positioning systems and data analytics.

As visibility on the Internet is vital in the tourism sector, firms that do not invest in digitalization are unlikely to survive unless they are specialized, niche operators. Pre-COVID-19, the World Bank (2018) highlighted the problem of EMDE tourism firms lacking the capacity to use digital platforms for promotion and sales because they knew little about digital platforms, and lacked the knowhow and resources to use digital media. Thus, supporting EMDE tourism businesses' use of digital tools will be vital if the global economy continues to languish; and conversely, if the global recovery is V shaped, this will also spur the growth of tourism businesses and the sector.

Peoples' unwillingness to undertake long-haul flights and substituting these with domestic and short-haul travel is expected to persist for some time after the pandemic ends. This is due to the complexities and perceived risks of travel that requires stopovers. Also, peoples' reluctance to travel to geographic regions that are perceived to have poor healthcare facilities and/or where the pandemic is not under control, will continue. Travelers' concerns about catching the virus from others suggests a greater market share for home-sharing business models, and contactless interactions in hotels and restaurants. As noted above, business and scientific conferences and exhibitions may not revert to pre-COVID-19 levels because, like influenza, the virus is likely to become endemic, and technology offers alternatives that avoid the risk of meeting in person (Baldanza 2020). In 2020, the substitution of business and scientific exchanges with digital or virtual conferencing proved remarkably successful, and this is expected to continue. Meetings, incentives, conferencing, and exhibitions (MICE) tourism is likely to evolve into a hybrid form of conferences that integrate online services with smaller, safer, in-person gatherings. There is some expectation in the tourism market that because some professionals will continue to work remotely, there is a market for "long stay" tourism. Barbados, Bermuda, Estonia, and Georgia are among the countries with fragile tourist industries that have created a new visa category for telecommuting foreigners (Mottley 2021). New facilities such as co-living/co-working spaces, camps, and cruises are expected to emerge to cater to these "digital nomads" who are seeking a setting with a safe environment where social

⁴² The travel industry incurred revenue losses equaling \$710 billion (FT 2021a). Bookings Holdings worries that it could take years for travel to return to Pre-COVID-19 levels; Expedia, the travel booking company, noted that international air travel remains "very injured"; and in September 2020, Marriott Hotels announced that global occupancy was running at 37 percent (Forman 2020).

interaction can take place (Thompson 2019). However, this is likely to be a temporary market, and one which is small scale. As the airline industry adjusts to serve relatively more leisure than business travelers (Mason 2020), this will have implications for both the pricing structure and margins of airline companies.

The absence of standardized rules for the movement of people is a barrier not only for the consumption of tourist services, but also for attracting investment. Although the COVID-19 crisis has elevated awareness about the risks associated with travel, most travel insurance policies have been slow to take account of the effects of a pandemic, government shutdowns, travel bans, or pandemic-related medical costs. It is not clear yet if private insurers will be willing or able to address this gap, especially as low interest rates put general

insurers under pressure from the perspective of lower earnings, and the risk of insolvency. In order to increase consumer confidence in leisure travel, it may be necessary for the insurance industry to explicitly assess and improve its ability to absorb ongoing risk.

Many developing countries are exporters of labor, and the remittances of migrant workers significantly augment earnings from other sources. Central Asian countries (for example, Kyrgyzstan) and others such as Cambodia, Egypt, Nepal, Pakistan, and the Philippines⁴³ are in the same league, and all could experience a dwindling of remittances.⁴⁴ Without a V-shaped recovery, the remittances of migrant workers, which have enabled millions to remain above the poverty line, will not be sustained.

43 One in five people in Africa receives remittances from abroad. In 2019 a total of \$81 billion were received. A decline of \$18 billion is projected for 2020 (Aidi, Fatai, and Karingi 2020).

44 World Bank (2020a) and World Bank (2020d). In 2020, remittances to countries in LAC, South Asia, and MENA rose, but those to countries in East Asia and the Pacific, Central Asia, and Eastern Europe declined. Overall, the decline globally was small (only 1.6 percent below 2019 – \$540 billion versus \$548 billion).



Post-Pandemic Challenges, Old and New

The COVID-19 pandemic has inflicted harm. However, developments during the last quarter of 2020 and the first half of 2021 suggest that the building blocks of recovery are coming together. The increasing availability of vaccines, and the apparent effectiveness of some against new variants of the virus; the revival of global trade; the quickening of activity in the East and Southeast Asian economies; the upswing in commodity prices; the positive response of global markets to sovereign and corporate bond issuance by EMDEs; the narrowing credit spreads; and the recovery of the U.S. economy (Torry and DeBarros 2021; Tankersley 2021), are all good omens for 2021–2022.

Nevertheless, questions remain regarding the speed of recovery in many EMDEs because of the structural constraints predating the crisis that constrain growth and jobs, and that have worsened with the pandemic. The economic challenges confronting EMDEs have been exacerbated by: the failure of numerous SMEs; inefficient insolvency regimes; the further weakening of bank balance sheets in cases where banks have been lending to unprofitable firms for some time; the inability of banks in these predicaments to help drive recovery; firms' and governments' heavier debt burdens; pressure on global value chains, and especially on the GVCs for semiconductors and plastics; shortages plaguing the shipping industry and backlogs at ports; and households' greater precautionary savings, which could depress spending over the near term. The crisis has exposed the downside of hyper globalization, and there is urgent need to reverse intra-country inequality, and build resilience against the “known unknowns” and the “unknown unknowns”.

Looking forward, the choice that we confront is whether to be pro-active in launching a private sector development agenda that not only reignites sustainable growth, but one that also builds resilience against “black swans”⁴⁵ and aspires to be equitable. A recovery strategy that lacks the commitment to tackle pre-crisis challenges head-on will, eventually, fizzle out as inequality and environmental degradation continue to grow.

45 That is, a low-probability event with potentially severe consequences.



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