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FGV IIU Flash Notes

Post Covid-19 Economic Recovery: is there a sustainable alternative?

Renato G. Flôres Jr.

FGV IIU International Intelligence Unit

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FGV IIU
npii@fgv.br

Director: Renato G. Flôres Jr.

FGV   Praia de Botafogo 210 ; Rio de Janeiro, Brazil.

Voice: +55 21 3799 6220 (Licia)

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1. Introduction: three lines of enquiry and the search for optimistic prospects.

The question about the prospects for sustainable development once the pandemic is clearly under control is vast and complex. Nowadays, at the middle of 2021, all regions are still under stress and nobody can say that things will soon get back to normal. Uncertainties are manifold and, while the pace of global vaccination pays witness to the appalling lack of solidarity of most developed economies towards the less favoured regions, new varieties of the corona virus regularly threaten supposedly improving contexts, keeping hysteria and fear at high levels.

Meanwhile, economic disruption sails through and bottlenecks, shortages, disturbing gluts and fiscal debts, social and political tensions steadily proceed. In order to adequately frame the context of the recovery, this text contemplates three key dimensions that will strongly condition it. It first looks at the recovery packages on the table and their potential effects in boosting international exchanges to, at least, previous levels. Secondly, disruptive effects that almost daily take place are addressed. They can easily jeopardise or delay many positive initiatives, creating further, unexpected problems that unfold in other problematic outcomes. Thirdly and finally, the geopolitical context cannot be left aside. The pandemic cleared stage for previously latent confrontations and disagreements morph into open rivalry, even if, in many instances, not all parties involved desire radical outcomes. At present, however, it seems that divisions and splits will progressively take shape in the international order, creating additional difficulties to freer and more intensive exchanges of goods, services and capital.

Along the discussion, attention focusses on the different world regions, notably the EU and South America. In any case, it is hard to envisage better times or an encompassing

♣ This Note is an expanded version of a presentation in the above-mentioned virtual event, during "Panel 4 - Transborder Economic Flows from an Atlantic Perspective. Post Covid-19 Economic Recovery: is there a sustainable alternative?".

recovery that would bring back (supposedly) good old times. The paper concludes in a pessimistic, though not catastrophic mood.

2. The recovery packages and associated measures.

Two main packages in the Western world are worth mentioning. The first is the ambitious EU programme the NextGeneration EU (NGEU) initiative, supposed to last from 2021 to 2026, during which period 1,8 trillion euros will be spent in the form of grants and loans to all 27 members. The biggest beneficiary is Italy, supposed to receive € 191,5 bn, with a country like Spain getting 140 bn, equally divided between grants and loans, and a small member as Portugal able to get 16,6 bn.

The whole budget has a EU basis, loans must be paid under generous though not over-generous conditions and the initiative will be partially funded by new taxes[1] and euro-bonds issued by the Union itself. The programme is project-based and members must submit specific projects that may qualify for the loans or grants. Priority is given to endeavours related to either the green or the digital economy, though resilience and connectivity are also addressed.

The package is broadly positive as well as its emphasis on being fully EU based, even in its financial aspects, though in a debt-ridden Europe, inflationary pressures will be unavoidable due to the mechanism designed for securing NGEU. It is not without unknowns either. Basically, it is a recovery package, with an uncertain impact in terms of transnational exchanges.

Many projects will deal with infrastructure and administrative recovery of the state machinery and institutions. As for the latter, there is always fear that the governmental sector, being closer to the Union bureaucracy and controlling, to some extent, the domestic implementation of the initiative, will end by capturing large shares of the individual members's allocations, attenuating the impact of the programme on the domestic (micro-) economy. Regarding the former, the different shortages and uneven demand patterns created by the pandemic have raised prices in civil construction and many items related to

[1] New taxes will include a carbon border tax and a fee to be paid by the main digital platforms operating in the EU, among others. They face opposition by some members, segments of the public opinion and the US itself, in the case of the digital tax.

infrastructure works, sometimes dramatically changing cost forecasts and schedules of originally conceived projects.

Moreover, the EU disparities also raise doubts on the net outcome. Brussels asks that 37 percent of the funds be used in projects to reduce carbon emissions, something that in the Eastern members -Poland and the Czech Republic, for instance[2]- seems a far-fetched goal.

In the US side, the amount of money already spent and still to be delivered for avoiding recession, unemployment and (re-)boosting the economy has and will be far superior than that in the EU. Infrastructure and green projects are again top priorities, together with the digital. Advanced electronic technologies -chip manufacturing, for instance, and supercomputing- are also strategic sectors of concern.

Inflationary pressures are once more unavoidable, and the extent and pervasiveness (through the economic sectors) of the dynamic potential of the green label is debatable.

The above applies worldwide, as a recurring present narrative is that there is plenty of available investment money -thanks partially to the constant decrease in interest rates and the increased financial sector volatility- to be matched to the needed and alluring green infrastructure needs[3]. However, green investment presents several unpleasant facets and can be rather costly.

To begin with, demand for specific and ticklish inputs will heighten. Minerals like copper and special varieties of steel and wood, rare earths will require much more intensive mining and environmentally problematic activities. The supply of rare earths -a highly polluting activity- had been left to China and select developing or underdeveloped countries, but must be assumed in large part by the US and a few other countries that relied on the Chinese supply. Wind turbines also require specific kinds of wood, found in the Amazon region, notably in Ecuador, and their short 20-25 years life poses serious problems of disposal and environmental degradation. Bottlenecks and capacity constraints can easily take place; when not, ironically, green restrictions to green investments.

It is no wonder that, many of the proposed investments up to now, both in the EU and notably in the US, boil down to a mixture of job generating ventures with disguised protectionist endeavours to recover heavily hurt sectors.

[2] According to a latest survey by Eurobarometer, only 17 and 15 percent of the Czech and Polish, respectively, against 31 percent of the Germans, consider the environment "nowadays' most pressing question".

[3] See, for instance, Otaviano Canuto's views in www.policycenter.ma/opinion/matchmaking-private-finace-and-green-infrastructure#.YOXIXehKgsE.

Overall, both packages will maintain a minimal ability to sustain trade flows.

Moving to other regions, like Africa or Latin America, in some countries, moderately successful macroeconomic policies have managed to alleviate the economic downturn, but as the economies continue to be hardly hit by the pandemic, funds and strategies are becoming scarce, and many previously balanced situations are deteriorating.

Asia, particularly Southeast Asia, stands perhaps as the region that will relatively sort out in better shape. China, Japan, South Korea and a few ASEAN countries will have a faster recovery and seem more able to re-ignite transborder economic flows. They will make for the main, triggering buying surge, fuelling a partially export-led recovery in other areas. The US may either join in or come in second place; America will not exactly be back.

3. Disruptive effects.

The prolonged status quo imposed by the pandemic, with alternating lockdowns and a systematic closure of several activities, provoked a depletion of stocks at the end of numerous production chains, be they of final or intermediate goods. But many inputs for diversified production processes started to lack, together with ruptures in intermediate points of value chains that obliged a halt in the process.

At the same time gluts and jams caused either disruption or backlogs in key logistic and transportation networks.

The outcome is a disparate increase in prices of different goods, without apparent logic, but indeed reflecting the irregular, if not chaotic shocks of the pandemic in the world production system. This puts any recovery effort in a half-schizophrenic situation. In one hand, they must address immediate jobs and even survival needs of specific sectors, either in manufacturing or services, on the other hand, the restoration or full replacement of damaged global value chains and connectivity networks is a must. In many cases, though not in all, these will be competing if not openly conflicting objectives.

The way to cope with this challenge is a careful and co-ordinated planning of the recovery endeavours, something missing until now. Instead, a traditional Keynesian rhetoric, without support on a serious analysis of the world production mesh and its present gaps and holes, is heard in most official statements, conveniently wrapped in the mandatory icing of "sustainable development principles".

But another elephant is in the room. Inflationary pressures have been mentioned in the previous section, as a result of the two main packages described. Care was taken in not mentioning inflation. Broadly, because despite inflation there will be, there is scope for keeping it at moderate levels, and also because wages will not go up, controlled as they are and will remain -a *transitory inflation* is what optimists expect. Notwithstanding, several analysts start to challenge this hope[4].

A scenario in which prices go up but disposable income is roughly fixed means a higher-profits one, higher rents to the super-rich and large corporations, contributing to the continued increase in inequality due to the pandemic. Good -in a superficial, short term view- to big business and transnational suppliers, bad, if not frightening, as regards social and political tensions.

Evidences of the above are multiple. According to the Credit Suisse, for instance, during 2020, 5.21 million people passed the personal income threshold of US$ 1 million, making for 56 million people in the world, or 1.1 percent of the total population having 45.8 percent of the global world wealth[5].

Things can still become worse if one remembers the total lack of solidarity clearly displayed, particularly by the majority of the advanced economies, during the pandemic. The outrageous vaccine policy, with several displays of uncooperative behaviour by the Western powers, while China, Russia and -up to its possibilities- even India struggled to spread their creations and ease their local production, is a major and sufficient example. The US, the EU and the frustrating GAVI and COVAX alliances got enmeshed in self-centred policies, inefficient bureaucracy, vapid statements and unwise disregard that a pandemic can only be brought under control in a global basis, through policies involving the greatest possible number of affected countries,

Within this context, everything gets to be more difficult. Encompassing decisions, like the harmonisation of sets of standards or practices, crucial for facilitating several endeavours,

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[4] See, among others, Mohamed El-Erian (*Goldilocks-like view downplays inflation threat;* Financial Times, 1 July 2021) and Lena Komileva (*Covid legacy will be more than a spike in inflation;* Financial Times, 7 July 2021).

[5] 2020 Report on Global Wealth, Credit Suisse, Genève.

from faster and easier investment procedures to more complementary macro-policies or tax attempts, become impossible dreams.

These disruptive effects, coupled with the unequal and partial elimination of the pandemic and the active though selfish behaviour of big business and several powers will worsen the post-pandemic prospects.

4. The geopolitical context.[6]

With the heightened US rivalry towards China, in which the new administration wants to rally the EU, Japan, South Korea, ASEAN and India -among other nations and groups- in an openly aggressive stance against China, there is no doubt that the geopolitical context will become more complex and twice less co-operative. Despite doubtful how far the US will be successful, given the immediate and long run interests, as well as geographical imperatives related to the other actors it wants to engage, a world with plenty of fault lines is unavoidable.

In the short run, there will be no significant separation of the productive mesh, but the duality of the production poles will progressively become noticeable. This may also harden the possibilities of common endeavours -harmonisation of standards and practices among them, as previously mentioned- so needed for a comprehensive sustainable development effort.

The new productive arrangements, determined by the interests of the two superpowers, will not necessarily be in those of other countries. For many Atlantic nations a likely reduction of export markets might be envisaged.

5. Conclusion.

Provided the pandemic is, until the end of 2021, brought under control, prospects for a retake of sustainable development are uncertain. If the two major Western economic poles are engaged in offering ambitious growth packages, where green investments and activities are predominant, doubts on how they will perform beyond sheer domestic recovery instruments

[6] The points in this section are further elaborated in the Author's book "The World Corona Changed: the US, China and Middle Powers in the New International Order" out with Routledge, London, in September 2021.

exist in both areas. Adequate planning, heavy bureaucracy and the divergent views of EU members are some of the unknowns in the European side, while the diversified and fractured social-political situation in the US plays a similar role in that country. In both areas, though at present inflation risks do not seem worrisome, there is no guarantee of a smooth macroeconomic scenario for the coming years[7].

Disruptive realities created by the pandemic, together with a less friendly and more aggressive international environment, thanks to the recent US rhetoric towards China, add further difficulties and, in not a few cases, bottlenecks and impediments.

Sustainable development cannot be divorced from the social dimension. Significant price changes, not followed by corresponding wage adjustments will enhance profits already enjoyed by the well-offs and larger corporations, widening the income gap in a world and country basis.

It is difficult to envisage a globally positive future in the next years. As democracies differ in many substantial aspects -Indian democracy, with its specific party, states and institutional dynamics, is not the US democracy, for instance- and, at the very inside of so-called democratic enterprises like the EU, largely ruled by a combination of technical autocracy and supranational bureaucracy, members disagree on their views of the concept and on the amount of effective power to give to an already established Parliament, the role of the resurgent socio-political conflicts cannot be disregarded.

Advocates of universal solutions, like 'capitalism', 'democracy' or 'free trade', usually forget that the masses in general, constituencies and countries as well need a roughly common vision of the future for moving in unison towards any major goal or pursuit. Abstract ideas, attractive or logically right as they might seem, coupled with debatable economic packages, need something else to mobilise changes and actually rebuild a new and better normal. Hungry, jobless and sick people do not care for great issues or principles, but rather for food, a minimally decent job and health conditions. Fear, as seen during the pandemic, may be a great engine of change; hate and the feeling of injustice also.

[7] The discussion in this Note is centred in the Western hemisphere, the effects of a Chinese likely faster recovery, as well as of those in other Asian economies, have not been taken into account.