August 5, 2021

FSVC Report on FSVC/KAS Webinar "Restarting the Engine after Covid-19: Regional Perspectives for Economic Recovery Programs"

On July 15, 2021, the Financial Services Volunteer Corps (FSVC) hosted with the Konrad-Adenauer-Stiftung (KAS) a third webinar under the program "Fostering Economic and Political Cooperation Among Key Countries in a Post-COVID-19 Environment". The webinar compared the economic recovery programs launched by the European Union (EU) and U.S. to restart their economic engines after COVID-19. The main presenters were Sabine Lautenschläger, former Executive Board member of the European Central Bank, and Alastair Fitzpayne, Senior Fellow and Advisor at the Aspen Institute and former Assistant Secretary for Legislative Affairs at the U.S. Department of the Treasury. Syaru Shirley Lin, Compton Visiting Professor in World Politics at the University of Virginia and Nonresident Senior Fellow at the Brookings Institution, offered a perspective from the Asia/Pacific region.

The webinar helped to identify similarities between the economic recovery programs and to highlight clear differences in priorities, reflecting underlying issues in the societies and economies. A common trait has been the enormous size of the programs. In terms of priorities, the EU programs have focused on climate change, green deal and the need for growth. On the U.S. side, the creation of "good jobs" has been a recurring theme, as well as reducing income inequality and the return to full employment. While there have been subtle differences of emphasis in the EU and U.S. strategies, they appear strikingly similar when compared to the description of the recovery in Asia. There has been generally a more positive outlook from the EU and U.S., reflecting relatively high vaccination rates and signs of economic recovery. In the Asia/Pacific region, low vaccination rates and a new wave of infections have crippled the beginnings of economic recovery, and the outlook has been more pessimistic. There was consensus, however, that there is an urgent need: 1) to get as many people vaccinated globally as possible; 2) to increase global cooperation, including around vaccination efforts; and 3) for recovery initiatives to be part of a broader strategy to tackle longer-term challenges (e.g., climate change). Key observations included the following:

Significant Economic Impact of COVID-19 in EU – In the EU, the pandemic has had a substantial impact on the economy: -6.1% GDP growth in 2020. Prior to the pandemic, the EU already suffered from low GDP growth, due largely to structural issues that will need to be addressed to ensure economic recovery and growth. These issues include: structural impediments to investment; less developed capital markets than in the U.S.; the lack of a single EU market for the services sector; inefficient public administrations in many EU member states; and judicial systems that are too slow and too complex. In 2021 and 2022, GDP is expected to rebound to 4.22% and 4.5%, respectively.

€1.211 Trillion EU Response – The EU put together a €2.018 trillion plan that includes the Multiannual Financial Framework or MFF (€1.211 trillion), which is the EU's 7-year long-term budget, and NextGenerationEU (€806.9 billion), a temporary instrument for post-COVID-19 recovery. The MFF highlights new priorities for the EU: 50% supports the modernization of the EU through research and innovation, via climate and digital transitions, preparedness, recovery and resilience. 30% will be spent specifically to fight climate change. Part grants, part loans, the NextGenerationEU funds represent approximately 5% of the EU's GDP. The EU Commission expects to disburse the funds between 2021 and 2026, with repayments to take place until 2058. The NextGenerationEU funds also highlight new and reinforced priorities for the EU, including green transition and climate change (32-37%) and digital (20%) initiatives. The EU's approach to the crisis is different from its approach to past crises, demonstrating more solidarity as funds are paid out based on need, not population size.

Criteria for EU Recovery Success – Each EU member state must submit for approval a national recovery and resilience plan to the EU Commission, which must include milestones and targets to be met prior to the disbursement of funds. It will be critical for the EU to enforce conditionality, for small and large EU member states. Furthermore, while the MFF and NextGenerationEU funds are a very good response to the economic crisis, they are only part of the solution. More reforms will be needed to ensure more growth, investment and productivity in the EU, and for it to remain competitive with the rest of the world in the longer term. Public administrations in EU member states will also need to be modernized to quickly adjust, implement reforms and meet milestones.

Lesson Learned in U.S. from Great Recession: Go Bigger – The Biden administration believes the response to the 2009-2010 Great Recession was too small, with a quick pivot toward fiscal austerity and a lack of bold policies to address the recession. The slow recovery resulted in a slow labor market recovery. The Biden strategy therefore is to take advantage of the Democrats' control of Congress to be bolder in policy proposals. Similarly, the Federal Reserve has been more aggressive on the labor market front, tolerating higher levels of inflation in part to regain lost jobs. U.S. GDP growth is now expected to be 7.5% in 2021, driven by a recovery from the pandemic, and strong fiscal and monetary support. The labor market recovery is also picking up. There are, however, significant concerns about all the stimulus and economic growth, and the $2 trillion in excess savings that Americans have accumulated since March 2020. There is also a debate about whether the Federal Reserve needs to address inflation more urgently (currently 5.4% year-over-year).

5 Key Goals of Biden Recovery Proposals –

1. **Labor market recovery:** A key driver in fiscal and monetary policy is to return to full employment in the short term. The U.S. lost 22 million jobs in March and April 2020 alone, and has regained approximately 15 million of those jobs.
2. **End wage stagnation:** There is profound income and wealth inequality in the U.S., and the Biden administration is focusing policies on reducing wage stagnation among low- and middle-income workers.
3. **Creation of "good jobs":** The Biden administration estimates that 40% of jobs in the U.S. are low-wage jobs. Many of its policy proposals therefore aim to create higher-wage jobs with good benefits and opportunities to join unions, and to transform traditionally low-wage jobs (e.g., elderly caregivers, childcare workers) into higher-wage jobs with better benefits.
4. **Move toward industrial policy:** As a result of the pandemic, the Biden administration has emphasized the need for more resilience in supply chains and investment in critical industries/segments (e.g., advanced batteries, electric vehicles, wind turbines).
5. **Promote competition:** The Biden administration has initiatives (e.g., anti-trust policy) to promote competition as it is skeptical of large businesses, including their impact on consumer prices.

Massive U.S. Relief and Recovery Programs – Prior to President Biden taking office, $3.5 trillion of fiscal support had already been enacted by Congress to combat the impact of COVID-19, and the Federal Reserve had lowered interest rates to nearly zero. The Biden administration has pursued an additional $1.9 trillion COVID relief plan (American Rescue Plan), more concerned about the risks of doing too little than of doing too much. This bill includes stimulus payments to individuals, expanded unemployment insurance and dozens of other proposals targeting individuals and sectors/industries, such as $350 billion to state and local governments, assistance to small businesses, and targeted assistance to restaurants and airlines, among other proposals. These funds are expected to be spent very quickly: $1.1 trillion in 2021 and the rest in 2022. This is therefore a short-term initiative that aims to dovetail the Biden administration's longer-term recovery proposals, including the American Jobs Plan ($2.2 trillion) and American Families Plan ($1.8 trillion). The American Jobs Plan includes a significant amount of industrial policy, traditional infrastructure spending (e.g., roads, bridges), social infrastructure investment (e.g., broadband) and $400 billion for the care economy as part of its "good jobs" initiative. It is also very focused on research and development, in part to remain competitive with China. The American Families Plan includes significant spending for education, childcare and a child tax credit. The child tax credit could amount to $1 trillion over 10 years, and help cut child poverty in half in the U.S. There are tax proposals for both corporations and high-net worth individuals to pay for these programs.

Signs of Trouble in China – While second quarter growth in 2021 was strong (7.9%) in China, there are signs of impending problems. Structurally, the economy is slowing down due to cyclical issues but also long-term issues associated with low-quality growth. Key challenges include a slowdown of exports (in part due to shortages in semiconductor chips), weak consumption and rising bad loans. The government recently announced a 50-basis point cut in the reserve requirement for all banks, which will release 1 trillion yuan ($154 billion) in long-term liquidity into the economy. This is a major shift in monetary policy, and has raised concerns about the ability of the government to maintain economic growth. Monetary policy is being deployed to combat the fallout of inflation on small businesses and help banks clean up past excess lending. These developments highlight the challenges of growing an economy while moving away from the low-quality growth of the past.

Poor Outlook for Rest of Asia/Pacific and Dependency on China – During the second half of 2020, the Asia/Pacific economies began to pick up, and strong global export demand combined with a rebound in domestic consumption created significant growth. But this recovery momentum has slowed due to the Delta variant, which has hit all the economies in the region very hard. At slightly more than 20%, the vaccination rate across the Asia/Pacific region lags significantly behind that of the U.S. and EU. Even in countries with greater access to vaccines (e.g., Japan), there are very high levels of skepticism about vaccines. Governments therefore are facing waves of new infections and, in the past two months, have grappled with how to balance public health and economic growth. Furthermore, the more protracted and gradual the economic recovery is, the more important China will be for other countries in the region. China is critical to the global supply chain but it is also exporting capital through its Belt and Road Initiative. These developments make it harder for many countries to solve the "China dilemma", particularly as rivalry between the U.S. and China is stronger now, as reflected in recent policy initiatives and rhetoric from the Biden administration.

Cross-Cutting Emphasis on Green – The EU recovery programs have emphasized green initiatives. It is also a priority for the Biden administration and many Congressional Democrats, but less so for the Republican Party. Some climate-related provisions were therefore taken out of recent bills. In the Asia/Pacific region, it was noted that most countries had become wealthy through exports and are now struggling to adopt a radically different approach to turn their brown economies into green economies. China, though, is providing leadership in this area, committing to carbon neutrality by 2060 even if it comes at a huge economic cost.

Consensus on Need for Greater International Cooperation – The lack of international coordination of measures to tackle the COVID-19 pandemic was raised by participants. Every country is focused on its own issues even though many measures require more international coordination to be effective. There are also clear differences in approaches. For example, the U.S. government is leaning toward not insisting on intellectual property rights pertaining to COVID-19 vaccines, while the EU insists they are important for future innovation. This difference of view plays a significant role in how Western countries may be able to assist poorer countries to fight the pandemic. There was also discussion about the economic benefit of helping everyone gain access to COVID-19 vaccines. The Biden administration has pledged to help the world get vaccinated, committing recently to provide 500 million Pfizer doses over the next two years. Significant work remains to be done in making the international distribution of vaccines more equitable.

Appendix I – Biographies of Speakers

Sabine Lautenschläger

Sabine Lautenschläger served as a member of the Executive Board of the European Central Bank (ECB) and as Vice-Chair of the Single Supervisory Mechanism of the ECB (2014 - 2019). She was formerly Deputy Governor of the Deutsche Bundesbank (2011 - 2014) and a member of the Executive Board and Chief Executive Director of Banking Supervision at the German Federal Financial Supervisory Authority (FFSA). Ms. Lautenschläger spent over 15 years at FFSA and its predecessor. She served as a member of the Basel Committee on Banking Supervision (2008 - 2018), and as a member of the Financial Stability Board (2015 - 2019). She served as Chair of the European Retail Payments Board and as Chair of the Euro Cyber Resilience Board for pan-European Financial Infrastructures. She was a member of the Management Board and Board of Supervisors at the European Banking Authority and observer to the European Single Resolution Board. She is currently a member of the Board of the Dubai Financial Services Authority.

Alastair Fitzpayne

Alastair Fitzpayne serves as a Senior Fellow and Advisor at the Aspen Institute. He previously served as Executive Director of the Aspen Institute Future of Work Initiative. Prior to his work at the Aspen Institute, he served as Chief of Staff at the Department of Health and Human Services (HHS) under Secretary Sylvia Burwell. In addition to serving as Chief of Staff at HHS, Mr. Fitzpayne held a number of senior roles at the Department of the Treasury during the Obama administration, including Deputy Chief of Staff and Assistant Secretary for Legislative Affairs. He has also served on Capitol Hill, in both the Senate and the House, as an economic advisor to Sen. Evan Bayh and Rep. Rahm Emanuel, respectively. He has also worked at the White House Office of Management and Budget and Abt Associates, a public policy consulting firm. Mr. Fitzpayne holds a BA from Vassar College and an MPP from the University of California-Berkeley.

Syaru Shirley Lin

Syaru Shirley Lin is a Compton Visiting Professor in World Politics at the Miller Center of the University of Virginia and a Nonresident Senior Fellow in the Foreign Policy Program at the Brookings Institution. She teaches at the Chinese University of Hong Kong, Tsinghua University in Beijing, and National Chengchi University in Taipei. Her book, Taiwan's China Dilemma, on the impact of the evolution of Taiwanese national identity on cross-Strait economic policy, was published by Stanford University Press in 2016 and in Chinese in 2019. Ms. Lin is currently working on the challenges facing high-income societies in East Asia. Her commentaries frequently appear in both English and Chinese media. Previously, she was a partner at Goldman Sachs, where she led the firm's private equity and venture capital efforts in Asia.