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Keynote speech

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The Covid-19 pandemic started the worst world economic crisis since Second World War. For the first time after the Great Depression of the last century both advanced economies and emerging and developing economies are in recession.

Preliminary GDP estimates for the main countries for the second quarter of 2020 (table 1) show double-digit negative signs for the largest European countries and the euro area, as well as a slightly less dramatic -9.5 percent for the American economy (reported by the Bureau of Economic Analysis and therefore in the media in annualized terms as a minus 32.9 percent). In all cases, however, these are unprecedented data and are added to the already heavily negative numbers recorded in the first quarter of the year (and reported in the first column of the table). By combining the changes in the two quarters, it is possible to calculate the loss of GDP in mid-2020 compared to the end of 2019 (net of seasonal

and calendar components). The data (third column) show cumulative losses of around 10 percentage points in the United States and an average of around 15 percentage points for European countries. Thus, the US economy has so far contracted less than the European ones. Within the euro zone, Germany is the least affected country (-12 percent) and Spain the most affected (almost 23 percentage points of GDP decline), with Italy and France suffering GDP decreases between 17 and 18 percent. If the analysts' forecasts are confirmed, the greatest decline in GDP will be recorded in the United Kingdom. On the other hand, the second quarter data shows that China - the economy most affected in the first quarter - has fully recovered the loss thanks to the rapid recovery experienced in the April-June period.
The forecasts for the third quarter indicate an expected rebound of the main economies, in particular China, followed by the USA and to a lesser extent by Europe. However, there is a prevailing opinion that the recessive impact of the pandemic has by no means worn off and the consequences of the crisis will be long-term.

The reasons derive from the nature of the crisis we are experiencing and the context in which it takes place.

The current crisis originates from an almost simultaneous shock of supply and demand, created by a sort of freezing of the economies due to lockdown and social distancing measures adopted all over the world and which however threaten to continue to some extent even after the emergency.

Table 1 – GDP Growth

	First quarter 2020 (%)	Second quarter 2020 (%)	GDP level at the second quarter end (4th quarter2019=100)
Eurozone	-3,6	-12,1	84,7
Germany	-2,0	-10,1	88,1
Italy	-5,4	-12,4	82,9
France	-5,9	-13,8	81,1
Spain	-5,2	-18,5	77,3
United Kingdom	-2,2	-20 * (* estimate Trading Economics)	78,2
Usa	-1,2 (-5,0 annualizzato)	-9,5 (-32,9 annualizzato)	90,7
Cina	-10,0	+11,5	100,3

It will be crucial how fast the governments of all the major countries will be able to restore the negative expectations of citizens and companies, by announcing and, above all, quickly implementing, expansive fiscal and monetary measures.

The goal was to find a way to finance immediately the necessary spending on health and the measures aimed to ensure that people are able to meet their needs.

Simultaneously, the governments had to support the production systems disrupted, by compensating the losses of the companies caused by the economic shutdown.

We are aware that immediately after it is necessary to finance a massive recovery plan, that is investments mainly on health and infrastructures.

To prevent companies' bankruptcies many European countries adopted the mechanism of the temporary transfer to the government of the largest part of the wage bill of companies forced to halt their production.

These measures - together with credit guarantees, liquidity facilities, granting of grants - had to avoid that firms went out of business creating unemployment that risk to become permanent or long lasting, because we know from previous crisis that the firm-specific skills of workers quickly depreciate. In other words, while the pandemic does not destroy physical capital, it can destroy both human and entrepreneurial capital.

Some of these policies have been adopted so far with asymmetric intensity, timing and efficiency by almost all countries.

However, the depth and the long-term consequences of the pandemic depend also on the fact that the countries that have been particularly hit are the countries more integrated in transnational supply chains, that is to say the countries that depend on intermediate inputs produced around the world, and the countries that are suppliers of commodities and raw material, as oil.

Seven countries that are, or have been, at the top of the infection rankings (China, US, Japan, Germany, France, UK and Italy) represent almost 60 percent of the world GDP, 65 percent of the world manufacturing product and over 50 percent of the world manufacturing exports. Each of these countries is an important supplier of industrial inputs to each other and to third countries and they are at the heart of a myriad of international supply chains. This implies a kind of "supply side contagion" via international supply chains that represents one of the greatest uncertainty factors of the global recovery.

For this reason, we face tremendous uncertainty on how deep and how long will be the recession and how big is the risk of a prolonged economic global depression. For the same reason getting out of the crisis would require the maximum international cooperative game, even if the pandemic has also highlighted the vulnerability of the current hyper-globalization phase and has offered arguments to pre-existing anti-globalization sentiments.

Above all, it is important to avoid that the asymmetric impact of the health emergency among countries, and their different financial strength in supporting their companies, is used for a sort of beggar the neighbor policy. In other words, for aggressive competitive restructuring of transnational production and commercial chains.

Global trade is a complex network of exchanges of intermediate inputs regulated by international commercial, financial and insurance contracts, in addition to national and international norms.

What we need is that the private and financial sectors must find ways to sterilize the current risks on global value chains deriving from potential temporary interruptions of these numerous interconnections by adopting, perhaps in innovative ways, the necessary adjustment and compensation mechanisms. A private sector response may not necessarily be sufficient on its own, and may entail stability risks around the World, and for the long term.

It would be also risky a reaction by countries that follow the demand to reduce the global connections between economies, under the psychological pressure of pandemics and in response to political arguments for achieving national self-sufficiency in the provision of essential goods.

Restructuring the supply chains in ways that make production costlier would show limited awareness of the interconnections between national economies in the global market.

It must not be forgotten that one of the positive effects of an interconnected world is the production of global public goods, like the fight against climate change and pollution, the diffusion of knowledge and education, scientific progress, human rights, the conquests of medicine and the global fight against endemic illnesses.

More attention and concern must be placed in addressing expectations and fears that could determine drastic changes in populations sentiment and could condition the strategic investment choices on a global level.

International coordination will be also crucial because the potential impact of the crisis on the financial and monetary markets is yet unknown.
In fact, the use of financial markets by both sovereign debtors and companies will necessarily be massive and protracted over time.
In particular, the governments debts, which are already very high in most countries, risk to grow larger, with foreseeable growing pressure on financial markets, not only to cope with the current phase of economic emergency but also in the subsequent phase.
Sovereign debts are, in fact, the main instruments that all countries necessarily have to activate to inject resources into the economy and stimulate productive recovery, going beyond monetary expansion policies, which have already reached the limits of their effectiveness through mere reduction in interest rates.
We remind that even before the Covit-19 pandemic, a great debate took place in Europe on the limits of the monetary policy and on the need of a more expansionary fiscal policy in European countries with fiscal space.

However, under the current conditions we must ask ourselves whether and to what extent it is possible to avoid a global explosion of public debt. In fact, recourse to debt, including European debt, appears necessary to support monetary policy and inject resources into the economy, but at the same time its unlimited growth creates the danger of a global collapse of the sovereign bond market and is probably not indefinitely sustainable.

The answer can be to channel monetary resources created by central banks towards financing specific pandemic mitigation measures and targeted public investment programs.
A monetization of the additional investment expenditure would allow governments to contain the growth of their debts also in the recovery phase. This direct monetary financing of public expenditure can be achieved in different ways.
In fact, all major Central Banks, including the European Central Bank, are already buying massively sovereigns and corporate bonds, even if the ECB purchases of sovereign bonds cannot be considered as monetization of debt or direct financing of government as in the case of other Central Banks.
These purchases of sovereign bonds by the ECB are not purchases characterized by debt cancellation or by an indefinite renewal commitment at their maturity and ECB did not announced what action it will take next (the so-called "exit strategy"). In other words, these are not transactions equivalent to direct treasury financing to governments by issuing money.
However, in the face of the explosion of sovereign debts, the relative benefits and costs of instruments aimed at attenuating or eliminating the ordinary nature of public debt of the sovereign bonds issued, through the

partial or total elimination of the reversibility of their underwriting by central banks, should be considered.
In the case of ECB, an instrument of this kind could consist in a form of temporary monetization of the golden rule, through the purchase of irredeemable public securities, or with an indefinite repurchase commitment, issued to cover actual expenditure incurred in implementing public investment programs. Compared to current expenditure, investments have the characteristic of creating real assets as a counterpart and offer guarantees to creditors since the expected return on investments will make it possible to honor the payment promises.

I argued, in previous occasions, the need to overcome the taboo of monetizing a vast program of European investments, in order to finance what was not then allowed by European rules, that is, a good debt. The argument was that we were often worried, and rightly so, not to transfer to future generations a financial debt incurred today, if not by creating the conditions for that debt to be repaid, but we were not concerned that the alternative to creation of debt, for a good and correct use, risked being the progressive impoverishment of human and social capital as well as the deterioration and progressive reduction of the stock of infrastructures essential for production and for society as a whole.

The damage for future generations, and in general for those who are young today, would be no less than that caused by the financial burden of the debt. Today, it is more necessary than ever, therefore, not to be afraid of a good debt, even if the effects of the pandemic and the uncertainties we face impose on the government, whatever it is, great discipline as well as great determination. I think this is the rational of the Next Generation EU plan.

However, in this context, coordination between monetary and fiscal policy requires also international coordination of monetary policy between central banks to stabilize international financial markets and to ensure liquidity for economies and governments worldwide.

The recent announcement made by Jerome Powell, chair of Federal Reserve, to the other central bank governors that US monetary policy change will have consequences. The Fed has stated that the employment goal will prevail over the inflation control goal. It was not just a matter of acknowledging that inflation is no longer dependent on the natural unemployment rate of the individual country and that therefore the monetary expansionary policy will not stop in the face of the reabsorption of current American unemployment, as it happened in the past. By stating that the policy of low rates and liquidity expansion will continue for a long time even if the inflation rate were to exceed the 2 percent threshold, the Fed announces that it will go its way by looking only to the pursuit of maximum employment.

This confirms that we are entering unknown territory. Not only because we do not know how we will be able to return from ultra-expansionary monetary policies around the world, but because we are moving away from the idea that international coordination of macroeconomic policies, monetary in the first place, is necessary to exit the crisis caused by the pandemic.

On the contrary, each large country will go on its own, looking internally and without considering the external repercussions on foreign exchange. We do not know what the consultations between the ECB and the Fed are today on how to maintain relative exchange rate stability but, if there is a divergence between monetary policies, the problem will arise. Therefore, the problem posed by a long tradition of economic theory returns to be of importance: it is difficult to contain global imbalances if a national currency is used as an international currency that reflects the internal political needs of the issuing country. Especially if there is no explicit or implicit international coordination.

In conclusion, we have to look at the pre-Covit existing three global trends: the retreat from hyper-globalization, the relationship between market and government with a growing role of the latter, evident also in Europe, and a falling growth rate.
Regarding these three trends, the Covit-19 probably will not be a game changing event but probably a game accelerating event.