

# COVID-19 RESPONSES FOR EQUITY (CORE) KEY ISSUES GUIDE



Kantamanto market, Accra, Ghana. West Africa's largest market for second-hand clothing and shoes, most of which are imported from the United Kingdom, the United States, Canada and China.

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## Shockproof and inclusive fiscal policies

### Summary

The Covid-19 pandemic has had a significant impact on the economies of most countries. What differed is the intensity of the impact, which ranged from mild economic contractions to devastating recessions and downturns. From a generic perspective, it is obvious to assume that high-income countries (HIC) would have faced lesser economic destruction than low- and middle-income countries (LMIC). However, a closer examination reveals that there are several factors that determined the impact of the pandemic on a country, as well as influenced its ability to respond. For instance, the existing economic structures and weaknesses strongly affected the countries' ability to provide adequate fiscal stimulus. These weaknesses are following pro-cyclical policies and not creating fiscal buffers that would help build more resilience. An interesting finding that emerged was that the credit rating of a country was found to be the most important determinant of its Covid-19 fiscal response. This is one major area where HICs had a significant advantage compared to LMICs. Another key challenge that disproportionately affected LMICs was the lack of

digitisation and access to the internet, which hampered economic growth as well as affected the countries' ability to quickly disburse cash transfers and support.

Research supported by the Covid-19 Responses for Equity (CORE) Programme – which is supported by the International Development Research Centre (IDRC) – has revealed some emerging lessons and recommendations to address these challenges and improve the resilience of countries to future shocks. One of the first and foremost recommendations is for countries to invest strongly in social protection and healthcare systems for its citizens, which would help build their resilience for future shocks. Adopting free trade policies and avoiding protectionism has also been an important lesson from the pandemic. Another key lesson is to employ a gender lens to fiscal and monetary policies as women have been disproportionately affected by the pandemic. Countries should also adopt expansionary monetary and fiscal policies as far as possible to increase the demand. Finally, countries also need to strengthen their financial institutions and mechanisms and reduce political interference, that would help maintain the asset quality of the banking sector.



## Key issues

### Heterogeneous economic impacts of the pandemic

It is well known that the pandemic has had a negative impact on the global economy and individual countries. The levels, however, varied significantly with high-income countries (HIC) being able to withstand the shocks much better than low- and middle-income countries (LMIC), and some variation even within LMICs. For instance, Raga and te Velde (2022) found that, based on pre-pandemic forecasts, Peru was supposed to grow by 3.6 per cent. However, the pandemic led to an actual contraction of the Peruvian economy by 11 per cent – suggesting a 15 per cent loss of growth due to the pandemic. Similarly, Sri Lanka was forecast to grow by 1.5 per cent but the pandemic led to a -3.6 per cent economic contraction in 2020 – the worst in the country's 73 years of independence. Meanwhile, Tanzania grew by 4.8 per cent in 2020, which is only about 1 per cent lower than pre-pandemic forecasts. The reasons for this differential impact ranged from varied containment policies, pre-pandemic economic pressures, different sizes of fiscal packages, and pre-existing social vulnerabilities.

### Existing weaknesses of economic structures and policies

Evaluation and studies by researchers suggest that one of the key issues that hampered a country's ability to respond effectively to the pandemic was the structural challenges in the economic system. For instance, Adeniran (2020) notes that the pandemic exposed structural hurdles facing low-income countries (LIC) in Africa, such as weaknesses in the digital economy, a lack of financial and social inclusion, and poorly developed domestic financial markets. Furthermore, contrary to conventional economic thinking, many LICs follow pro-cyclical policies – i.e., not saving during an economic boom – which hinders their preparedness and ability to respond effectively to a sudden economic crisis (Adeniran 2020). A long-term approach should be adopted to strengthen the systems that underpin the delivery of the responses, including strengthening social protection and public health systems, formalising the labour market, and creating fiscal buffers. In the context of Nigeria, Ekeruche and Adeniran (2021) also suggest that streamlining governance structures for countries with a high cost of governance is a policy option towards building fiscal buffers.

### Role of credit ratings in determining fiscal response

A key but rather less discussed issue that determines a country's fiscal response is its credit rating. Benmelech and Tzur-Ilan (2020) write that pre-crisis sovereign credit ratings were the most important factor affecting a country's fiscal policy during the Covid-19 pandemic. This holds true not only for LMICs but also high-income countries (HIC), i.e., even among high-income, advanced economies, a country's credit rating affects



Public service workers provide health services to internally displaced persons in camps and host communities in Northeast Nigerian states.

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its ability to pursue expansionary fiscal policies. The Covid-19 pandemic has triggered rating downgrades in seven sub-Saharan African countries since March 2020, including some of the region's biggest economies, due to factors such as an immediate economic contraction, the initial debt-to-gross domestic product (GDP) ratio, the accumulation of new debt (which widens current fiscal deficits) and the real interest repayment on debt (Shipalana, O'Riordan and Prinsloo 2021). Thus, Shipalana *et al.* recommended that credit ratings agencies can suspend their assessments for developing countries until global production and supply chains return to pre-pandemic levels (*ibid.*). Such steps can be taken for future shocks and economic crises.

### Lack of digital penetration and financial inclusion

Countries that had a low digital penetration among its citizens struggled to provide quick support. For example, in the context of Nigeria, digitisation is a key structural issue that hinders the country from reaching its economic goals – noting that individuals with access to the internet as a share of the population was only 7 per cent in 2017 (Ekeruche and Adeniran 2021). Thus, LMICs which have a large informal population need to effectively leverage digital technologies to ensure that basic financial services are available to its population (Shipalana *et al.* 2021). In this regard, countries must learn lessons from Kenya which leveraged its well-developed financial technology platforms as a channel to stimulate liquidity and widen financial inclusion during the pandemic. For the majority of 2020, charges for transactions up to KSh1,000 (USD8.8) were waived, the limit of daily mobile money transactions per person was increased up to KSh150,000 (USD1,326) from previous KSh70,000 (USD619) limit, and monthly mobile money transactions limit per month was eliminated (Raga and te Velde 2022).

## Emerging lessons

### More investment is needed to enhance social protection and safety nets

The first emerging lesson is that governments should invest strongly in social protection mechanisms and education and health policies. This is particularly crucial to build the economic resilience of vulnerable groups such as women, youth, and the elderly to prevent them from falling below the poverty line and build their resilience from long-term shocks. For example, the Tanzania Social Action Fund (TASAF) piloted an e-payment programme in 16 districts in which over 65 per cent of Productive Social Safety Net Programme recipients have been women (Mashindino and Kazi 2022). Not only do these measures have the potential to boost economic growth while keeping public financial accounts solvent, but they aim to Build Back Better after the pandemic by enhancing productivity, reducing income and social inequalities, and kick-starting the creation of a social protection system capable of shielding all citizens from external shocks (Jaramillo and Escobar 2021).

### Employing a gender lens to monetary and fiscal policies

It is widely recognised that the Covid-19 pandemic had varying levels of impact on men and women as female-dominated professions faced greater shocks and disruptions than male-dominated sectors, as found in Ethiopia (Tekleselassie *et al.* 2023). Thus, there is a strong need to employ a gender lens in monetary and fiscal response policies. In the context of Zimbabwe, Mabugu *et al.* (2022) recommend that concerted efforts to increase capital stocks in subsistence farming, where women are highly represented, could help enhance earnings. Furthermore, Papadavid and Pettinotti (2021) argue that alternative monetary policies – such as earmarking specific provisions to target specific sectors or groups – could have gender-equalising effects if those measures predominantly benefit women. For example, a lowered interest rate in the agricultural sector in Bangladesh may impact women working as daily labourers. Given that women constitute more than 50 per cent of the agricultural labour force, there is the

possibility that the loan would spur more investment on farms and more demand for hired labour of whom many will be women doing, for instance, weeding or harvesting (*ibid.*).

### Adopting free and open trade policies

Another key lesson that emerges is that countries should revamp their trade policies and mechanisms. Reviewing the evidence from Sri Lanka, Kenya, and Tanzania, Raga and te Velde (2022) suggest that boosting regional trade, attracting foreign direct investment, trade diversification, free trade agreements, and preserving trade openness can reduce vulnerabilities to future shocks and stimulate a 'rainbow recovery'. Furthermore, in the context of LICs in the African continent, Adeniran (2020) suggests that intra-Africa trade is one area that can be leveraged for stronger resource mobilisation and growth. The opportunities created by the African Continental Free Trade Area can be tapped by LICs to improve their economic growth.

### Need to adopt expansionary monetary and fiscal policies

Researchers have found that a commonality between countries who were mildly successful in managing the pandemic's economic impact was that they adopted expansionary monetary and fiscal policies which helped to boost aggregate demand. For instance, in the context of Uganda, the government adopted policies such as reducing the central bank rate, reducing the reserve requirement ratio, and encouraging regulatory flexibility at central bank-supervised financial institutions (SFIs) that extend loan-restructuring services on a case-by-case basis among others (Okumu, Kavuma and Bogere 2021). However, caution must be exercised especially in the case of LICs, where expansionary policies can lead to increased inflation.

### Strengthening financial institutions and maintaining their independence

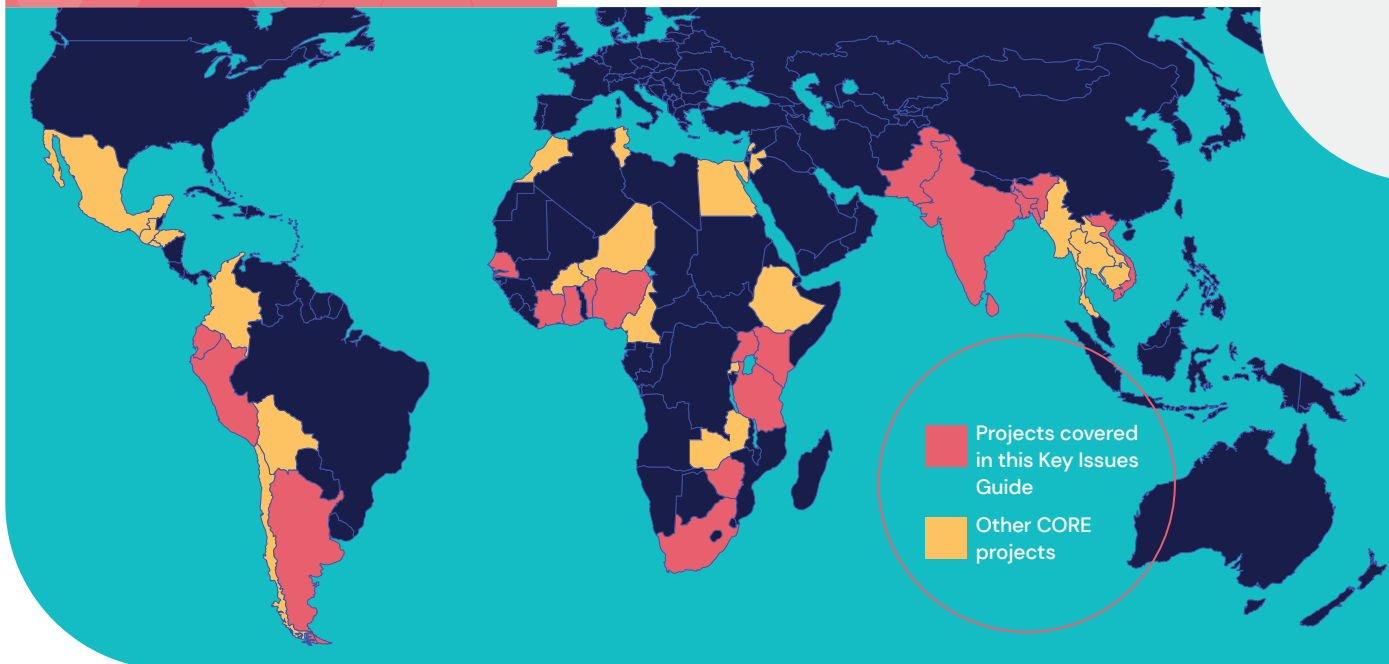
The third important lesson is that countries should strengthen their financial institutions and regulators, and enable them to dominate policymaking without interference from politicians. The independence of monetary institutions is critical for fiscal sustainability and controlling inflation. These structural bottlenecks impeded the effective implementation of economic policies in LICs, so addressing them is necessary (Adeniran 2020). Having strong financial institutions can also help maintain asset quality, which can be a crucial factor in determining the amount of fiscal support that can be provided during crises and shocks. For instance, in Kenya, the International Monetary Fund (IMF) assessed that the pandemic has exacerbated the pre-existing weaknesses of asset quality in the banking sector. The banks' non-performing loan ratio rose from 12.7 per cent in February 2020 to 14.1 per cent in December 2020 (Raga and te Velde 2022), which affected the country's ability to respond adequately to the pandemic shocks.



Women working in a textiles factory where they are sewing garments for export in Dhaka, Bangladesh.

PHOTO: © G.M.B. AKASH/PANOS PICTURES

## Highlighted projects



### **Covid-19 Macroeconomic Policy Response in Africa**

This project generated evidence to support policymakers, specifically finance ministries, to promote equitable socioeconomic and sustainable environmental policies and interventions, in the short- and long-term. The project supported peer learning and capacity building among targeted policymakers and policy think tanks, for strong pandemic responses on fiscal and monetary measures, financing and programming options to support vulnerable groups, and how they can contribute to climate-resilient, sustainable and inclusive rebuilding of economies.

#### **COUNTRIES**

• Benin • Nigeria • Senegal • South Africa • Tanzania • Uganda

#### **RESEARCH PARTNERS**

• [South African Institute of International Affairs \(SAIIA\)](#) • [Centre for the Study of the Economies of Africa \(CSEA\)](#)

### **Shaping the Macro-Economy in Response to Covid-19: A Responsible Economic Stimulus, a Stable Financial Sector, and a Revival in Exports**

This project aimed to contribute to the knowledge on macroeconomic policies that are key for low-income countries' responses to the Covid-19 pandemic. The impacts of the pandemic on the economies of these countries are significant, contributing to growing poverty and hunger. There was an urgent need for credible data, analysis, and advice for the economic policies and fiscal and monetary measures required to mitigate the impacts and promote an inclusive and sustainable recovery.

#### **COUNTRIES**

• Bangladesh • Kenya • Peru • Sri Lanka • Tanzania

#### **RESEARCH PARTNERS**

• [Overseas Development Institute \(ODI\)](#) • [Institute of Economic Affairs \(IEA\)](#)

### **Simulations and Field Experiments of Policy Responses and Interventions to Promote Inclusive Adaptation to and Recovery from the Covid-19 Crisis**

This project focused on the impact of the Covid-19 pandemic and the effectiveness of current and potential policies in 11 developing countries to identify more effective and inclusive policy responses. In nine countries, it used simulation modelling to explore the likely impacts of various policy responses at different stages of the crisis: epidemic and lockdown, gradual re-opening, and full recovery. In two countries, ongoing experimental impact evaluations were extended to assess specific pandemic-response interventions. The research was guided by questions relating to the impacts of the pandemic on national economies and populations, and the results will guide national decision-making.

#### **COUNTRIES**

• Argentina • Benin • Côte d'Ivoire • Ecuador  
• Ethiopia • Ghana • Kenya • Nigeria • Pakistan  
• Vietnam • Zimbabwe

#### **RESEARCH PARTNERS**

• [Partnership for Economic Policy \(PEP\)](#)



## Further reading and references

### Further reading

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### ABOUT THIS GUIDE

This Key Issues Guide was written by **Devanik Saha**, Research Officer at the Institute of Development Studies (IDS). It was produced as part of the Covid-19 Responses for Equity (CORE) Knowledge Translation Programme, which supports the translation of knowledge emerging from the CORE initiative. Supported by the International Development Research Centre (IDRC), CORE brings together 20 projects to understand the socioeconomic impacts of the pandemic, improve existing responses, and generate better policy options for recovery.

The views expressed herein are those of the authors and do not necessarily represent those of IDRC or its Board of Governors, or IDS.

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