

# Intelligence MEMOS



From: Mark Zelmer

To: Bill Morneau, Minister of Finance

Date: April 2, 2020

Re: **MANAGING THE ECONOMIC CONSEQUENCES OF THE CORONAVIRUS PANDEMIC**

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The social distancing intended to slow the spread of the coronavirus has shut large segments of the Canadian and global economies, disrupting the ability to produce, consume and pay for goods and services.

High uncertainty about how long it will take to contain the virus, how severe will it be, and what the world will look like post-virus means that it may become impossible for households and businesses to access credit on normal commercial terms.

The primary focus for governments at this stage has been on taking steps to contain the financial damage to households and businesses so that the economy has a better chance of staying intact and recovering when the pandemic eventually passes.

This is appropriate. But gaps remain, and policymakers and central bankers should continue to be vigilant to the need for further intervention in every area.

## Overview of Government Measures Announced So Far

With the benefit of hindsight, it is tempting to argue that Canadian governments have been slow to respond to the pandemic. However, we must bear in mind we live in a liberal democracy not an authoritarian regime.

Governments are very mindful that introducing measures to combat a pandemic and protect public health constitute major intrusions on the rights and liberties of Canadians. The introduction of such measures needs to be based on objective evidence and the public needs to be brought along. Such measures can only succeed if they enjoy widespread public consent.

Hence, the over-riding objective of the economic measures announced to-date (see [here](#) as of March 30<sup>th</sup>) has been to alleviate as much as possible the economic and financial damage to Canadians and Canadian businesses during the pandemic so that they have a chance to survive financially and participate in the eventual economic recovery when the pandemic abates.

So, the key question at this stage is whether enough has been done.

## Remaining Gaps & Where do We Go from Here

Speed is of the essence in a crisis like this, as is the need to be bold.

While government responses are becoming bolder, even more radical steps may be needed before we are done.

For example, in the case of the business sector, governments have started to move from supporting credit flows on commercial terms to entertaining outright government guarantees for credit to small and medium-sized businesses. Those programs may need to be expanded both in scope and size if the ability to extend credit on commercial terms evaporates.

Similarly, the Bank of Canada's willingness to expand its balance sheet in support of the Government of Canada securities market is welcome and will give it more flexibility to support the financial system. But, again, if conditions deteriorate further it may need to contemplate doing the same in support of other parts of the financial system.

At some point governments will also need to confront the question of what is to be done for critically important firms in deep financial distress where loan guarantees may not be enough – think airlines and oil and gas firms. Who to subsidize, on what scale, and on what terms will be important challenges.

Finally, there is the question of how do we pay for all of this. This is not a pressing issue at this stage because governments can borrow in financial markets at close to zero interest rates. They are not exactly crowding out private borrowers in this environment. And, if worse comes to worst, the Bank can finance the federal government in Canadian dollars.

But when the pandemic subsides this issue will come to the forefront.

At first glance, the choices for paying the bill will boil down to some mix of higher taxes, reduced government spending and possibly inflation. Unhelpfully, our starting point is not great given our society's high level of indebtedness. However, if interest rates on the additional government debt are lower than economic growth after the pandemic subsides, as was the case pre-COVID, we should be able to cope with the additional burden over time.

Governments and central banks have reacted forcefully to this unprecedented shock. Filling in these gaps as new needs arise is the next critical phase.

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