COVID-19 'should not necessarily foreshadow an economic downturn'

16 March 2020, by Sarah Whitebloom

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Market hysteria over coronavirus may have seen hundreds of points wiped off indexes around the world this week, but Oxford University experts maintain the COVID-19 crisis should not necessarily foreshadow an economic downturn.

Professor Simon Wren-Lewis, economist and expert in the impact of pandemics at the University of Oxford, maintains that modelling he undertook after the 2008 global financial crisis, shows the coronavirus crisis should have a short-term impact and need not have a long-lasting effect on the UK economy. This view was echoed by Rishi Sunak, the new Chancellor of the Exchequer, during this week's Budget speech [11 March], when he said the impact of the coronavirus will be "temporary."

Professor Wren-Lewis says: "Ever since the global financial crisis (and perhaps before) we have become obsessed with markets and, in particular, their imagined predictive power."

He added: "Looking at the markets, it appears the economic impact of coronavirus will be huge and permanent. In contrast my own study, and others we refer to, suggest something very different: that coronavirus will lead to a large negative shock that will be short term, and certainly will not be permanent. So who is right?"

Based on a three-month virus crisis, Professor Wren-Lewis said his modelling study showed, there is a danger of firms going bust, as we have already seen in the airline sector. But, this week, the banks have said they will support hard-hit businesses and the 2009 study showed that, once the virus is over, firms will become viable again.

It has been widely claimed firms will be vulnerable if they lose production, as workers fall ill or have to take on child care duties because schools are shut. In a blog this week, Professor Wren-Lewis says unwell workers may lead to falls in production but that: "Firms have ways of compensating for this…This 'direct' impact "[from the effect on the workforce]" of the pandemic in the UK, will reduce GDP in that quarter by a few percentage points."

His blog says: "The impact on GDP for the whole year following the pandemic is much less at around 1% or 2%, partly because output after the pandemic quarter is higher as firms replenish diminished stocks and meet postponed demand."

He continues: "Even with all schools closed for three months and many people avoiding work when they are not sick, the largest impact we got [based on the study's findings] for GDP loss over a year was less than 5%. That is a very severe one-quarter recession, but there is no reason why the economy cannot bounce back to full strength once the pandemic is over."

This could still mean that there are short-term problems of supply, with supermarkets unable to keep their shelves stocked with everything. But a decline in demand, caused by people self-isolating and not consuming, could have a more significant impact.

With consumers changing behaviour and avoiding social spending on restaurants, pub visits or entertainment, the leisure industry could be hit hard. These will not be made up after the crisis has passed, with consumers unlikely to eat multiple meals out, in order to compensate for those not eaten during any period of isolation. As part of the Budget, the Chancellor announced special measures to alleviate the impact on the leisure industry, with business rates being lifted and support for the sector.

Professor Wren-Lewis says: "If people start worrying about getting the disease sufficiently to cut back on this social consumption, the economic impact will be more severe than any numbers discussed so far. One reason it is severe is that it is partly a permanent loss."

Nevertheless, according to the economic modeling, the largest fall in annual GDP was 6%. "It is in this light that we should view the collapse of stock markets around the world. In macroeconomic terms this is a one-off shock," according to Professor Wren-Lewis.

He adds: "Markets dislike uncertainty, and so you are likely to see an overreaction." But, he says, this should not be allowed to distract policymakers from following the best medical advice.

Some of the measures Professor Wren-Lewis said would alleviate the situation for the economy have been taken, "although more could be done to encourage low-paid or self-employed workers to self-isolate."

Banks have extended lending and given mortgage-holidays to customers in need. Chancellor Sunak maintains that he will be having regular meetings with the banks. And the Budget contains a series of measures, aimed at protecting businesses and individuals from the potential economic impact of the coronavirus.

Provided by Oxford Science Blog