

# Governments will determine the economic consequences of COVID-19

March 25 2020, by Sarah Whitebloom

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Credit: AI-generated image ([disclaimer](#))

Measures taken by governments in the coming months to control COVID-19 will determine the impact of the pandemic on the global and national economies, according to Oxford professor of economics Simon Wren-Lewis. In his latest blog, Professor Wren-Lewis argues: "It is impossible to predict what the full year impact will be until we know

what controls are essential and what controls can be relaxed while maintaining an effective test/trace/isolate regime."

His work modeling the impact of a pandemic—which anticipated a 6% fall in GDP over 12 months—was based on the crisis lasting just three months. But, with COVID-19 set to be present in the community for a longer period, the way that the response is managed and implemented will be critical to its [economic impact](#).

"We assumed the pandemic was just a three-month affair. If we look at our severe pandemic case, including falling social consumption, we had GDP in the pandemic quarter falling by 30%. There was a similar fall in consumption. However, because our severe pandemic lasted for just one quarter, GDP for the year as a whole fell by only 6%. So how good a guide are those numbers to this coronavirus pandemic?"

Professor Wren-Lewis says the predicted fall of 30% "does not look obviously wrong and may well be an underestimate." But he emphasizes that "this is not a precise figure."

It is what comes next that is crucial. Key to the economic impact will be 'the strength of social distancing controls, the degree of business and worker support from governments and whether governments can relax social distancing before three months are up."

Professor Wren-Lewis says: "Once the number of cases are brought right down, it is likely governments will do what China is currently doing, and move to a strict contain regime," he writes. "This involves a very stringent regime to test those who might still get the virus and the isolation of known contacts, combined with some continuation of social distancing controls... I think this will inevitably be how other countries deal with the virus once numbers are down."

But he warns: "Some will do it well, and others may not, leading to controls being reintroduced."

Despite the expected longer term presence of COVID-19, the theory behind the earlier modeling essentially holds true, according to Professor Wren-Lewis. The main supply side impact comes from school closures which, as he says, now look set to last until the summer. Meanwhile, workers will be reluctant to use grandparents—unlike the assumptions in the study.

The study had predicted a fall in social consumption and a heavy impact on the leisure industry—which has been borne out. But, Professor Wren-Lewis says: "There is a limit to how far GDP can fall because we will not eat less, and we will not spend less on housing or heating. Expenditure on clothing and particularly durables may be delayed to some extent, as people avoid personal contact, but online purchases should continue."

This is why the action that governments take now is so critical. Professor Wren-Lewis says: "We assumed there would be no attempt at suppression beyond school closures... This coronavirus pandemic will not be a one-quarter affair, because governments quite rightly have not been prepared to see a short, sharp peak where their health services will be overwhelmed."

Talking about initial responses to COVID-19, he continues: "Nearly all Western governments underestimated how quickly the virus would spread."

But he says, "It is easier to control the virus by relaxing controls than creating such controls from scratch... The key issue for the economy once numbers come down is how many controls can be reduced or eliminated while keeping a lid on new case numbers."

At the heart of this, on the supply side, will be whether schools reopen and on the demand side, what parts of social consumption can be made safer. Professor Wren-Lewis says, "Because some relaxation will almost certainly be possible, then GDP growth will partially bounce back, but how much it will bounce back is very unclear at present... our study, which had GDP being above the no-pandemic case in the second quarter, does not apply to the [pandemic](#) we are now in.

"As a result, our study is much too small to predict the first year GDP impact of a 6% fall. It is impossible to predict what the full-year impact will be until we know what controls are essential and what controls can be relaxed while maintaining an effective test/trace/isolate regime. We will get some idea from China."

Provided by University of Oxford

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