

## **Briefing – Economic Impact of Coronavirus – Michael Taylor, ACCA chief economist**

The coronavirus outbreak has rapidly escalated into a significant global economic risk. Early reassurances that this virus had a much lower mortality rate than the SARS outbreak in 2003 have given way to increasing concerns about the rapidly rising numbers contracting the virus in China – and its spread overseas.

### **The Economic Impact**

Economic shocks such as this virus outbreak tend to have temporary effects on economic activity, which is then recovered quickly once the crisis has passed. This was the case with the SARS outbreak in 2003 for example. For now, this is our central case – **whatever the short-term effects, we expect activity to recover, such that by the second half of 2020 global economic activity is growing at the rate it would have been if the coronavirus outbreak had not occurred.** But a prolonged crisis could result in a more long-term reduction in growth for example, if there were significant job losses that further reduced consumer confidence and spending.

### **China**

The restrictions on travel within China, the extended New Year holiday factory closures and the shutting of retail outlets and tourist attractions will have a significant effect on the Chinese economy. **Consumer spending – now a key driver of economic growth – will be very weak in the first few months of this year.** Capital Economics, an economic consultancy, has cut its forecast for annual GDP growth in the first quarter from 5.5% to just 3%. Note that recent efforts by the authorities to boost liquidity are designed to help companies manage short-term cash flow. They are not an attempt to stimulate the economy: the virus represents a supply shock, not a demand shock, so there is little point in trying to boost demand.

### **Outside China**

The SARS outbreak in 2003 did have economic effects outside China but these were relatively limited and confined mainly to the East Asia region. **China's significance in the global economy is now much greater than it was 17 years ago.** Its share in global GDP and goods exports has roughly doubled over this period to 19% and 13% respectively and China now plays a vital role in many global supply chains. (Hubei Province, the source of the virus, is an important region for manufacturing and supply chains.) The potential for the coronavirus to have a global economic impact is therefore much greater than it was 15 or 20 years ago. This has already been felt in the oil market where prices have fallen by 20% since early January, reflecting China's position as the world's biggest oil consumer.

**An extended and significant slowdown in the Chinese economy caused by the coronavirus would reduce world GDP growth and put the recent stabilisation in global trade volumes into sharp reverse.** An interruption in global supply chains caused by extended factory closures in China would also have a significant negative impact on several Asian economies, with Vietnam, Taiwan, South Korea and Malaysia particularly vulnerable.

There has also been a surge in overseas Chinese tourists in recent years, boosting the service sector exports of many countries, albeit modestly in most cases. But in Cambodia and Thailand spending by Chinese tourists accounts for around 5% and 3% of GDP respectively – so the potential for economic loss here is significant.

### **Policy Response**

As discussed above, China can do little to offset the short-term economic impact of the coronavirus other than providing extra liquidity to prevent corporate distress. However, **other economies in the region can attempt to boost their domestic economies to offset the coronavirus's headwinds.** For example, Thailand and the Philippines are likely to cut interest rates later this month. Last year several Asian economies mitigated the effects of a slowdown in China with monetary and fiscal ease which helped to support overall GDP growth. A similar response is possible this year especially if the crisis persists. Major central banks such as the US Federal Reserve and the European Central Bank are not likely to respond with easier policy. But by adding to near-term downside risks to the global economy the case for maintaining the current easy stance of policy is strengthened.

**To sum up, the short-term economic effect of the coronavirus will be significant in China with spill-over effects on other Asian economies. A comparison with similar episodes in the past suggests that lost economic activity will be recovered quickly – provided efforts to control the spread of the virus are successful.**

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