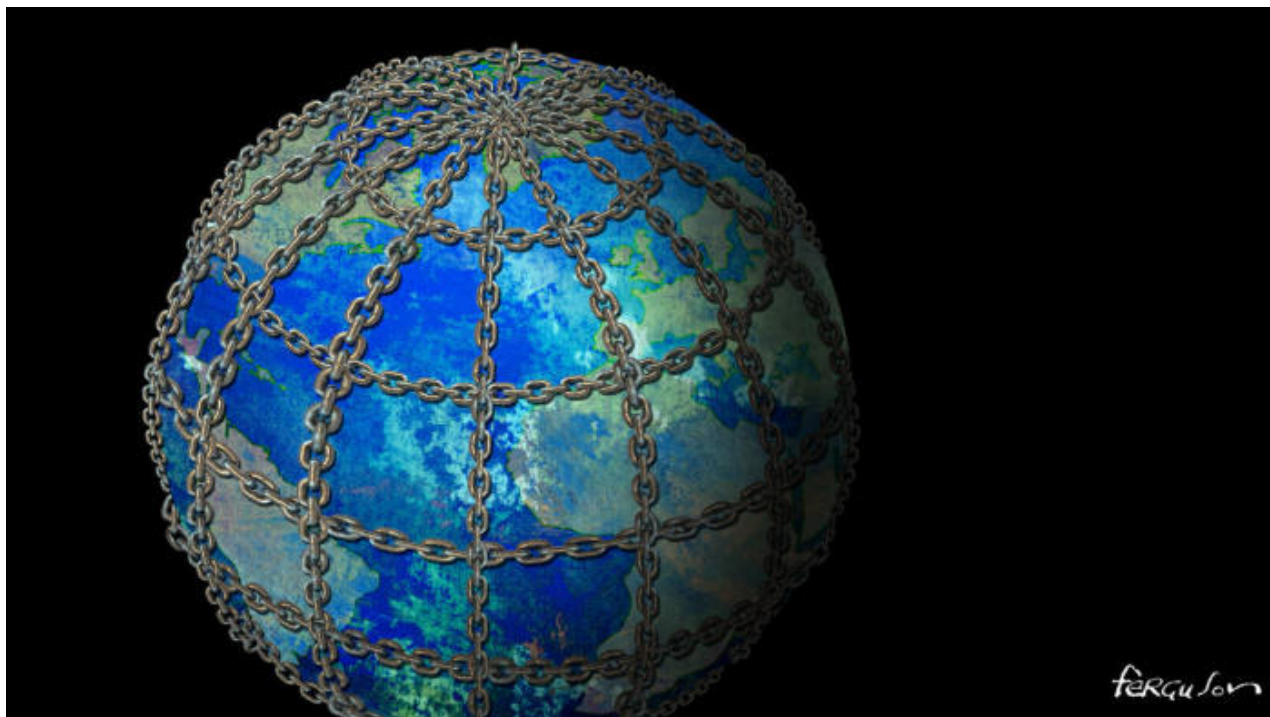


The world economy is now collapsing

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Martin Wolf, *The Financial Times*, April 14, 2020

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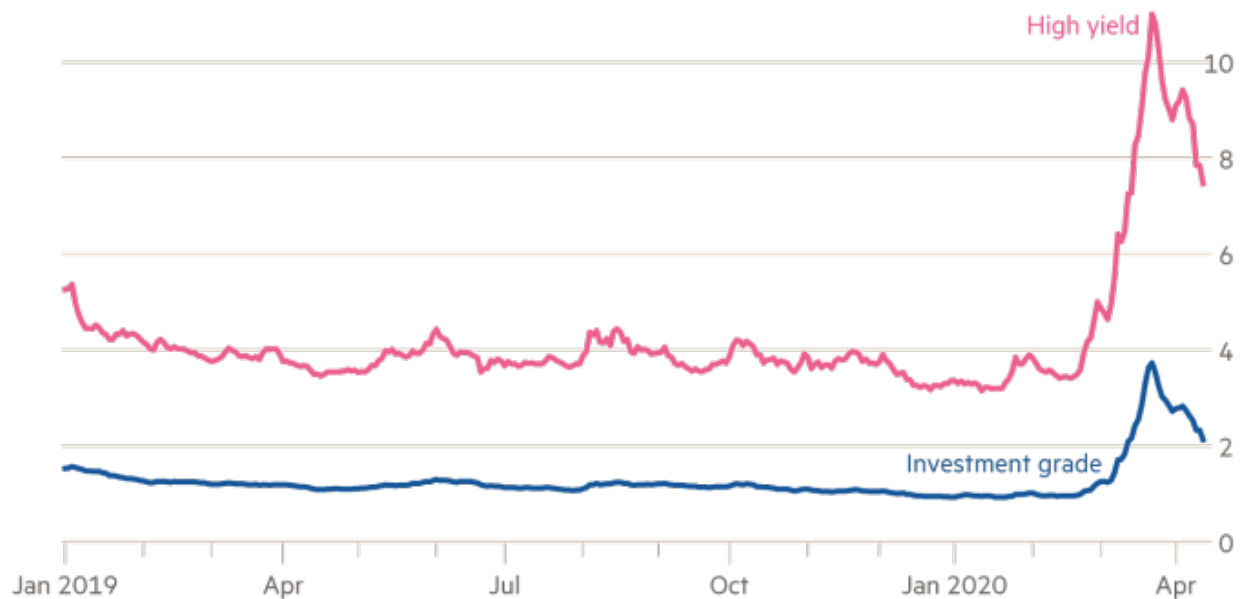
In its latest World Economic Outlook, the IMF calls what is now happening, the “Great Lockdown”. I prefer the “Great Shutdown”: this phrase captures the reality that the global economy would be collapsing even if policymakers were not imposing lockdowns and might stay in collapse after lockdowns end. Yet, whatever we call it, this is clear: it is much the biggest crisis the world has confronted since the second world war and the biggest economic disaster since the Depression of the 1930s. The world has come into this moment with divisions among its great powers and incompetence at the highest levels of government of terrifying proportions. We will pass through this, but into what?

As recently as January, the IMF had no idea of what was about to hit, partly because Chinese officials had failed to inform one another, let alone the rest of the world. Now we are in the middle of a pandemic with vast consequences. But much remains unclear. One important uncertainty is how myopic leaders will respond to this global threat.

Rising spreads show flight from risky assets in developed countries

Credit spreads on US corporate debt

(option-adjusted spreads over US Treasuries on Bloomberg Barclays indices, % points)



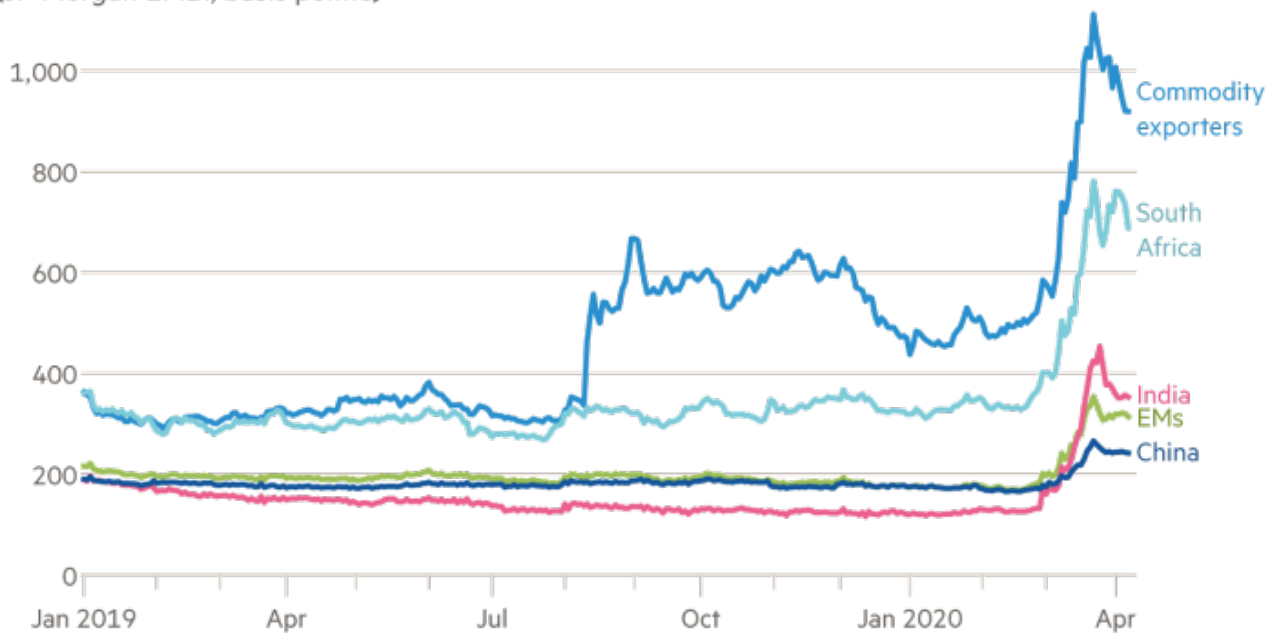
Source: Refinitiv
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For what any forecast is worth, the IMF now suggests that global output per head will contract by 4.2 per cent this year, vastly more than the 1.6 per cent recorded in 2009, during the global financial crisis. Ninety per cent of all countries will experience negative growth in real gross domestic product per head this year, against 62 per cent in 2009, when China's robust expansion helped cushion the blow.

In January, the IMF forecast smooth growth this year. It now forecasts a plunge of 12 per cent between the last quarter of 2019 and the second quarter of 2020 in advanced economies and a fall of 5 per cent in emerging and developing countries. But, optimistically, the second quarter is forecast to be the nadir. Thereafter, it expects a recovery, though output in advanced economies is forecast to remain below fourth quarter 2019 levels until 2022.

Rising spreads also show flight from risky assets in emerging economies

Emerging market sovereign bond spreads over US Treasuries
(JP Morgan EMBI, basis points)



Source: IMF
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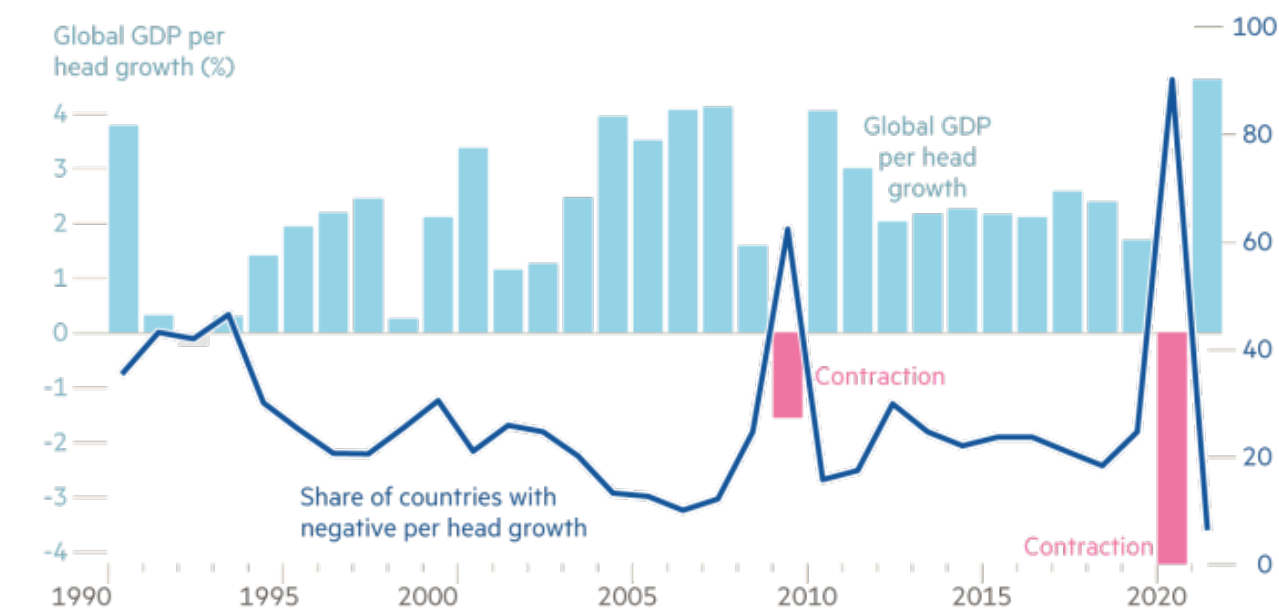
This “baseline” assumes economic reopening in the second half of 2020. If so, the IMF forecasts a 3 per cent global contraction in 2020, followed by a 5.8 per cent expansion in 2021. In advanced economies, the forecast is of a 6.1 per cent contraction this year, followed by a 4.5 per cent expansion in 2021. All this may prove too optimistic.

The IMF offers three sobering alternative scenarios. In the first, lockdowns last 50 per cent longer than in the baseline. In the second, there is a second wave of the virus in 2021. In the third, these elements are combined. Under longer lockdowns this year, global output is 3 per cent lower in 2020 than in the baseline. With a second wave of infections, global output would be 5 per cent below the baseline in 2021. With both misfortunes, global output would be almost 8 per cent below the baseline in 2021. Under the latter possibility, government spending in advanced economies would be 10 percentage points higher relative to GDP in 2021 and government debt 20 percentage points higher in the medium term than in the already unfavourable baseline. We have no real idea which will prove most correct. It might be even worse: the virus might mutate; immunity for people who have had it might not last; and a vaccine might not be forthcoming. A microbe has overthrown all our arrogance.

The depth and breadth of the coronavirus recession will be far worse than in 2009

Growth in global GDP per head and recessions

Share of countries with negative per head growth (%)

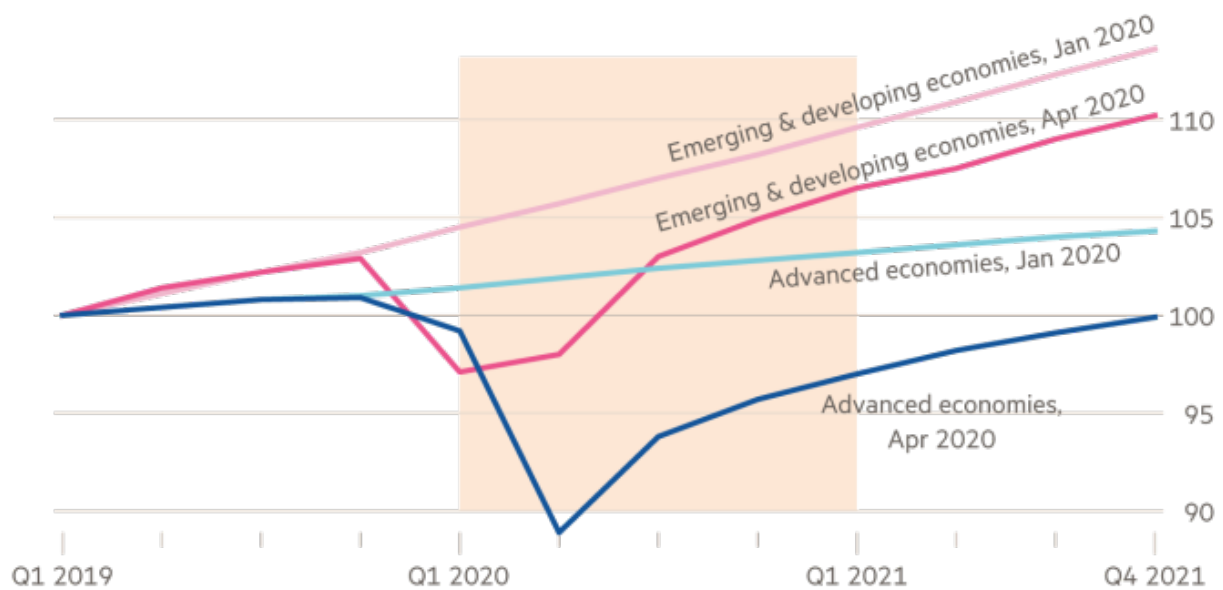


Source: IMF
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What must we do to manage this disaster? One answer is not to abandon the lockdowns before the death rate is brought under control. It will be impossible to reopen economies with a raging epidemic, increasing numbers of dead and pushing health systems into collapse. Even if we were allowed to buy or go back to work, many would not do so. But it is essential to prepare for that day, by creating vastly-enhanced capacities to test, trace, quarantine and treat people. No expense must now be spared on this, or on investment in creating, producing and using a new vaccine.

The baseline forecast is now for deep recessions this year

Global GDP forecasts (Q1 2019 = 100) - IMF forecasts in January and April 2020

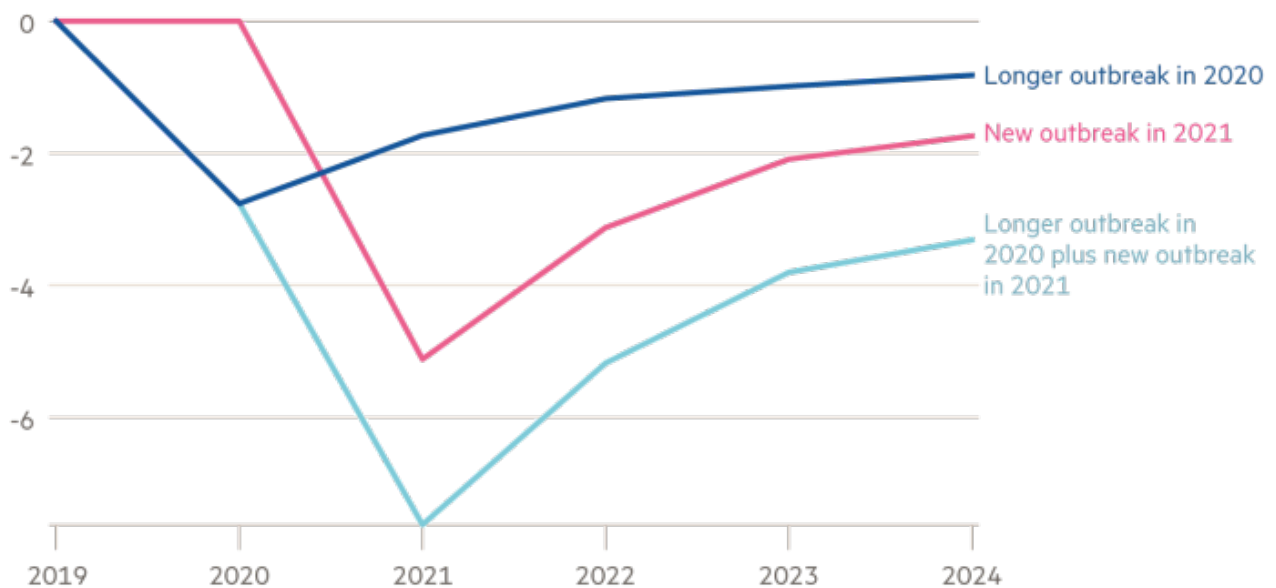


Source: IMF
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Above all, as the introductory essay to a report from the [Peterson Institute for International Economics](#) in Washington on the essential role of the Group of 20 leading countries states: "Put simply, in the Covid-19 pandemic, lack of international co-operation will mean that more people will die." This is true in health policy and in ensuring an effective global economic response. Both the pandemic and the Great Shutdown are global events. Help with the health response is essential, as Maurice Obstfeld, former IMF chief economist, stresses in the report. Yet so too is economic help for poorer countries, via debt relief, grants and cheap loans. A huge new issue of the [IMF's special drawing rights](#), with transfer of unneeded allocations to poorer countries, is needed.

Scenarios suggest outcomes could be far worse than in the baseline in advanced countries

Impact of differing Covid-19 scenarios, advanced economies
(GDP deviation from baseline, %)



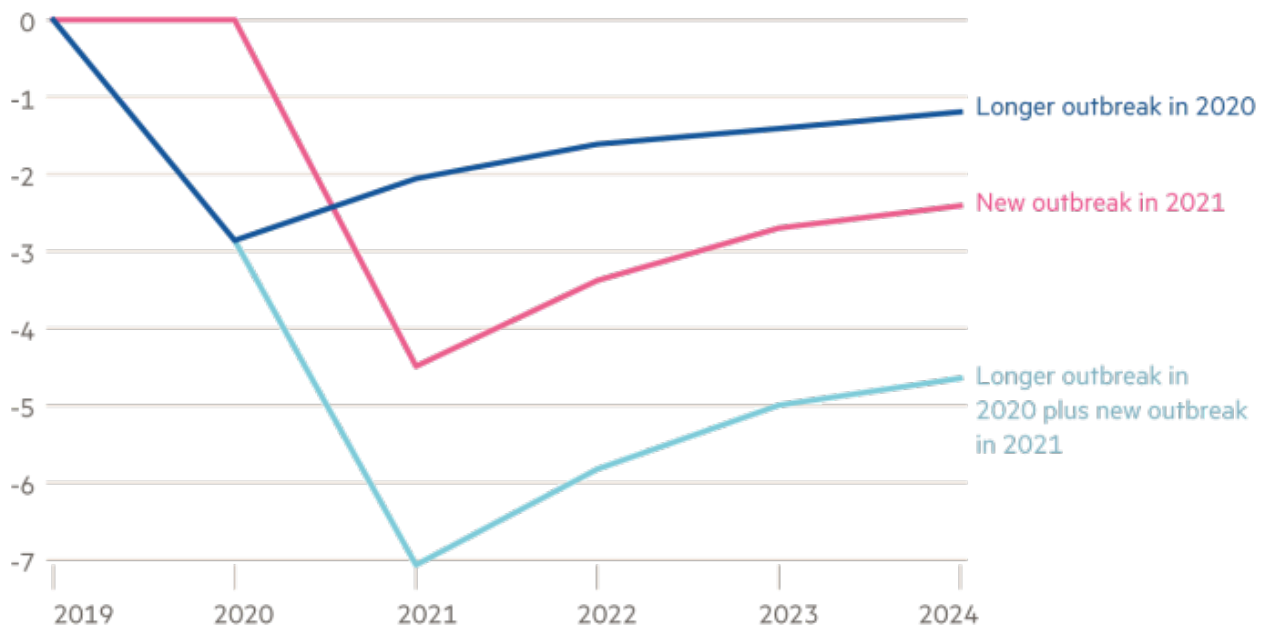
Source: IMF
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The negative-sum economic nationalism that has driven Donald Trump throughout his term as US president, and has even emerged within the EU, is a serious danger. We need trade to flow freely, especially (but not solely) in medical equipment and supplies. If the world economy is broken apart, as happened in response to the Depression, the recovery will be blighted, if not slain.

We do not know what the pandemic has in store or how the economy will respond. We do know what we must do to get through this terrifying upheaval with the least possible damage.

Outcomes could also be far worse in emerging and developing countries

Scenarios in the fight against Covid-19 - Emerging & developing economies
(GDP deviation from baseline, %)



Source: IMF
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We must bring the disease under control. We must invest massively in systems for managing it after current lockdowns end. We must spend whatever is needed to protect both our people and our economic potential from the consequences. We must help the billions of people who live in countries that cannot help themselves unaided. We must remember above all that in a pandemic, no country is an island. We do not know the future. But we do know how we should try to shape it. Will we? That is the question. I greatly fear our answer.

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