



***Coronavirus global outlook:
after the outbreak***

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This report was produced on 4 May 2020 by ICAEW's partner Oxford Economics, one of the world's foremost advisory firms. Their analytical tools provide an unparalleled ability to forecast economic trends.

Summary

- The global economy faces a major contraction in growth, coronavirus will make 2020 the biggest global recession in post-war history. Oxford Economics expects global GDP to shrink by 4.7% in 2020. [Read more](#)
- A recovery in the second half of 2020 won't make up for lost activity in the first half of the year, Oxford Economics expects global GDP to return to pre-crisis levels by mid-2021. [Read more](#)
- This shock has already caused mild permanent damage to the global economy. The cost of the virus outbreak, in the medium term, could be in the region of 1.6% of global GDP - though this estimate is subject to a high degree of uncertainty. [Read more](#)
- Governments have unleashed unprecedented support to prevent further long-term damage. Oxford Economics expects government debt levels will rise by 10%-20% of GDP by 2021 in most advanced economies. [Read more](#)
- In the near term the risks around economic forecasts centre around the speed at which lockdown restrictions are eased and the risk of a second virus wave. The length of lockdowns and policymakers' support are vital for the outlook. [Read more](#)

The ICAEW view

This forecast paints a woeful picture of the world economy over the next 18 months. While forecasting in times of such upheaval is incredibly difficult, we can be pretty sure that the trajectory is true. **The report provides the kind of analysis that is increasingly necessary for ICAEW members and others trying to assess the outlook for their operations, for their strategic planning and for disclosure to the markets.**

For example, financial reporting increasingly requires a view of the future. As the crisis will result in more impairments, so organisations will need to look at cash flow projections and economic forecasts to develop these. One challenge, however, from an accountancy perspective is whether this greater focus on forward-looking information can create self-fulfilling prophecies: would overly pessimistic forecasting amplify any crisis? This is particularly true with IFRS 9.

It is important for SMEs and large corporates alike to look at a number of different forecasts, especially given the current levels of uncertainty and, although this forecast is at the gloomier end of the spectrum, it sits comfortably alongside other authoritative analyses. The United Nations Department of Economic and Social Affairs (UN DESA) on 13 May published its *World Economic Situation and Prospects as of mid-2020* with a similar, if slightly less harsh message.

From a business perspective and that of our members, one of the standout figures in the UN DESA report is that 'World trade is forecast to contract by nearly 15 per cent in 2020 amid sharply reduced global demand and disruptions in global supply chains'. As this Oxford Economics report points out, 'global trade was already slowing as a result of the prolonged trade war between the US and China.' **It goes on to note 'This trend towards deglobalisation could likely accelerate after the 2020 coronavirus pandemic.' This retreat into economic nationalism was fuelled by the way that the financial crisis 10 years ago played out undermining belief in international organisations.**

This crisis is, economically, twice as harsh as that of 2007-08 and could well evolve into another financial crisis, and one could imagine the self-reinforcing downward spiral emerging. The OECD has already warned that extra debt being taken on by already heavily indebted governments and companies to tackle the coronavirus crisis will 'come back to haunt us'. This will be of no benefit to our membership, the wider business community or our global society. A strategic approach to managing this so that it doesn't become yet another crisis must be occupying the minds of governments and regulators alike.

There are other issues that can get lost in the current headline measures of the economy. GDP does not capture how wealth is distributed nor how the coronavirus has laid bare and deepened the disturbing pattern of growing inequality across the world. GDP also does not account for the loss of natural capital on which economic and social success depend.

The World Economic Forum's Global Risk Report for 2020, published in January, opens with the following remarks:

'... long-mounding, interconnected risks are being felt. The global economy is faced with a "synchronized slowdown", the past five years have been the warmest on record, and cyber-attacks are expected to increase this year – all while citizens protest the political and economic conditions in their countries and voice concerns about systems that exacerbate inequality. Indeed, the growing palpability of shared economic, environmental and societal risks signals that the horizon has shortened for preventing – or even mitigating – some of the direst consequences of global risks.'

The coronavirus crisis is one chapter of an unfolding bigger interconnected catastrophe of climate emergency, massive biodiversity loss and increasing inequality. The economic crisis that Oxford Economics describes is another chapter. However, capturing that purely in terms of GDP, while it brings

simplicity to what is an immensely complex picture, ignores who will pay the price. Those are the ones least able to afford it: nature itself, whose carrying capacity is being devastated; developing and transitional economies as capital flees; and the poor.

Oxfam's report *Dignity not Destitution* published this April highlights the disproportionate effect the coronavirus is having on the developing world as well as on the vulnerable and women. It estimates potentially half a billion people are being pushed into poverty.

As this crisis evolves, our thinking and action about solutions has to include social, human and natural capital. There has been, and continues to be, a blizzard of calls for a green and fair recovery and a momentum of ambition around that. This needs to be built into forecasts. The decisions we make now as we move from stabilisation to stimulation of our economies will create the path dependencies that will take us either back to where we were or set a new trajectory towards a green and fair world. If we try to repair the colossal damage of the current crisis by returning to where we were, we are setting ourselves up to fail.

There is an emerging consensus among economists and scientists that the recovery needs to be about nature, society and economy. For example, May saw the publication of a report – *Will COVID-19 fiscal recovery packages accelerate or retard progress on climate change?* – written by a team of leading economic and climate change thinkers: Cameron Hepburn, Brian O'Callaghan, Nicholas Stern, Joseph Stiglitz and Dimitri Zenghelis at the Oxford Smith School of Enterprise and the Environment.

The report notes that 'the climate emergency is like the Covid-19 emergency, just in slow motion and much graver' and that 'there are reasons to fear that we will leap from the Covid-19 frying pan into the climate fire'. And climate change is, of course, as we have noted, inextricably linked to biodiversity loss and rising inequality.

This recovery, however, also has to be viewed from an international perspective. The threat of this not happening is very real, as is pointed out in *The Economist* leader article of 14 May, *Globalisation unwound: Has covid-19 killed globalisation?* The lockdowns have closed borders and disrupted commerce, delivering the 'third body blow to globalisation' in the decade, after the financial crash and the Sino-American trade war.

Jayati Ghosh, a development economist and Chairperson of the Centre for Economic Studies and Planning at the Jawaharlal Nehru University, has convincingly argued (*Covid-19 has made one thing clear: Internationalism is not a luxury. It is a necessity*, Progressive International) that international collaboration is a necessary condition for solving the situation we face:

'combined and co-ordinated global efforts are necessary to ensure the survival of the planet and of human life on it ... the Covid-19 pandemic is driving home the urgency of internationalism and not just through the sheer rapidity and force of the global spread of the disease. The unfolding of the pandemic, the national policy responses and the economic impacts, all demonstrate how such processes can dramatically increase inequalities between and within countries, and also that solutions simply cannot be found within any one country.'

We must learn from the last decade and look beyond our borders and the self-interests of our individual nations to solve the current problems.

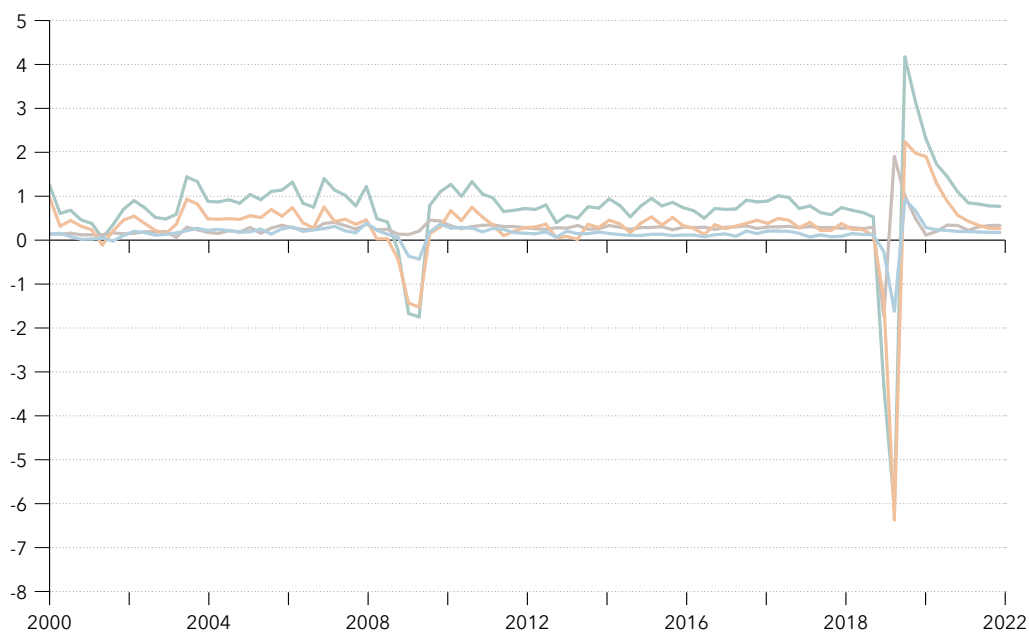
Global economy experiencing unprecedented shock

- Coronavirus to make 2020 the biggest global recession in post-war history
- China's experience paints a glum picture for the rest of the world
- Advanced economies to face the biggest contractions in second quarter

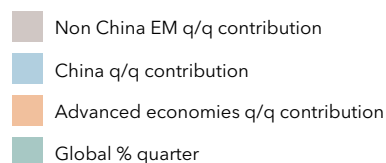
The global economy is about to enter the deepest recession in living memory. The full extent of the contraction in activity in early 2020, which was triggered by containment measures to combat the global spread of COVID-19, remains uncertain. There can be no doubt though that the effects will be massive. **Oxford Economics' baseline forecast projects that world GDP will contract by about 10% in H1, roughly double the impact of the global financial crisis in 2008.**

World: GDP

% quarter



Source: Oxford Economics/Haver Analytics



China lockdown leads to massive economic disruption

As the pandemic originated in China, its economy was the first to suffer a sharp contraction in activity as a result of the COVID-19 outbreak and forewarns what is in store for the rest of the world. The Chinese economy contracted by an estimated 10.7% over Q1, relative to Q4 in 2019.

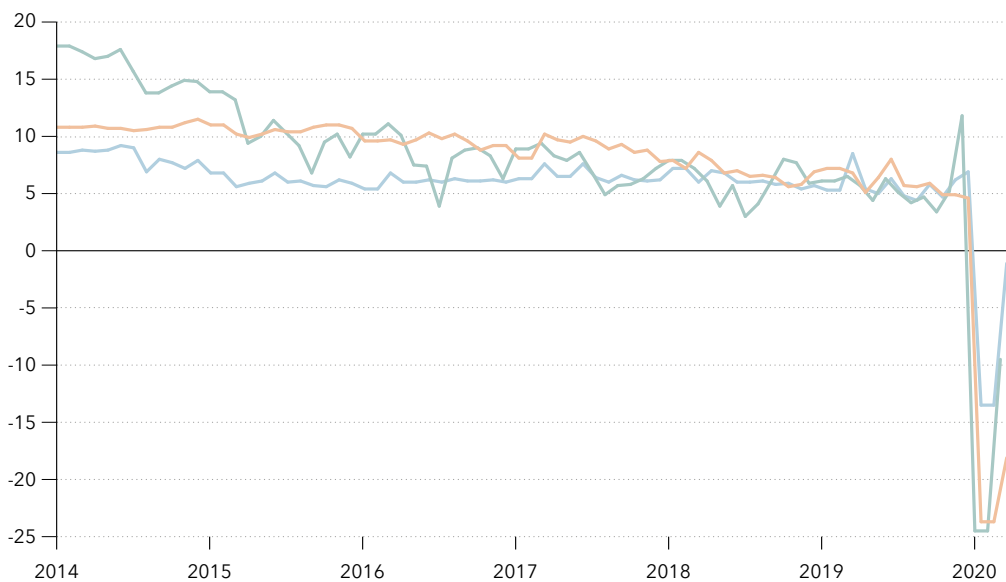
Wuhan province's lockdown began in late January and lasted about 11 weeks, but the length of lockdowns across China varied according to the severity of the outbreak, with the shortest lasting just four weeks. Lockdowns in China were starting to ease through March and then the lockdown officially ended in Wuhan, the starting point of the outbreak, in early April. In January and February combined, industrial gross value added plunged by 13.5% on the same period a year earlier, while the value of retail sales fell by 20.5% over the same period as firms were forced to close and consumers remain at home.

An improvement in economic activity was evident as containment measures eased. In March the official Purchasing Managers Index (PMI) rebounded to 52 (a score of above 50 indicates expanding business), from February's record low of 35.7. The annual pace of industrial gross value added was -1.1% y/y in March, showing the clear improvement from February but underlining that the return to 'normal' would not be immediate.

While the Chinese industrial sector saw a gradual revival in activity, it has not been the same across all sectors. Although people have generally returned to work, voluntary social distancing persists, meaning that non-essential spending on activities that involve social interaction have been slower to rebound. Retail sales fell by -15.8% y/y in March, only a modest improvement on the -20% in January-February.

China: Key cyclical indicators

% year



Source: Oxford Economics/CEIC

Value added industry (real) Retail Sales
Fixed asset investment (nominal)

While weak external demand will affect China in Q2, the ongoing return to more normal levels of domestic spending and a policy-driven boost to infrastructure spending should ensure that China records a healthy rebound in GDP in Q2 - Oxford Economics has pencilled in a 9.3% quarter-on-quarter rise. While this appears to be a healthy short-term rebound, it will still leave the level of GDP in Q2 about 5% lower than they had expected in January, before the scale of the crisis was fully appreciated.

Developed markets can expect a similar experience in Q2

Having seen events unfold across Asia in January and February, most European countries and the US prepared with various levels of success. As a result, many governments have been forced to implement lockdowns of varying stringencies, causing most businesses to scale down their operations, if not shut down altogether.

In Q1 2020, both the US and eurozone economies contracted sharply on the quarter by 1.2% and 3.8%, respectively. Underlying these results were some truly staggering data from both the industrial and retail sectors. Industrial production in the US contracted by over 5% in a single month in March, the largest monthly decline since World War II. In April, US and European business surveys, such as the PMIs, have plunged well below the previous lows pointing to far worse to come. Households are also feeling the squeeze. Consumers in the US drastically reined in spending as a result of stricter lockdowns, unprecedented layoffs and plummeting confidence; resulting in a drop in retail sales of over 8% in March.

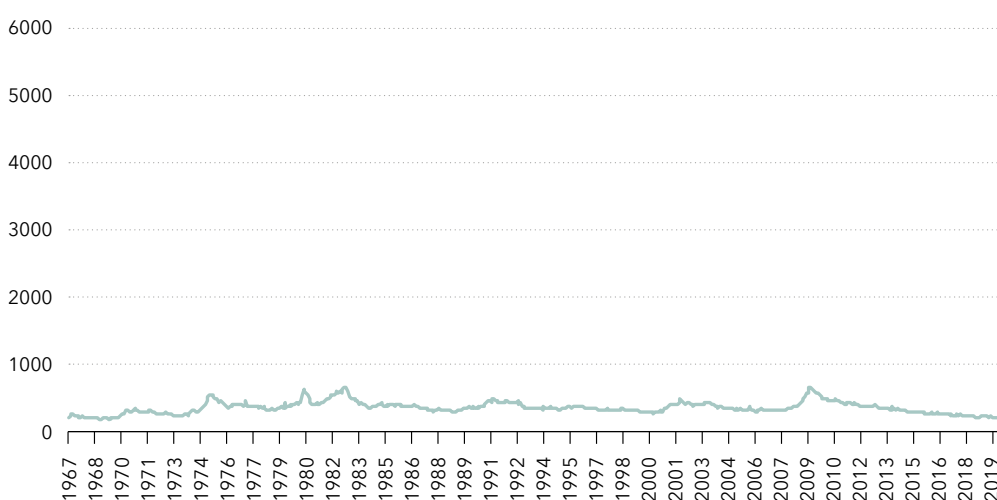
Given that most lockdowns outside Asia only began in March, the exceptionally weak GDP readings were driven by, at most, just one month of economic strict containment measures. The worst is yet to come in the second quarter of the year, with further contractions in GDP forecast of 11% in the US and the eurozone. These are deeper recessions than anything seen in modern times.

The enormity of the crisis is perhaps best reflected in the staggering labour market data that has emerged over March and April.

- In the US, more than 26m people have filed for unemployment benefits since lockdowns began.
- More than a million jobs were lost in Canada, causing the unemployment rate to rise by over 2 percentage points in March; the largest one-month rise during the global financial crisis was just 0.6 percentage points.
- In Germany the unemployment rate rose by 0.8pp to 5.8% in March, the largest one-month rise in almost 30 years.

US: unemployment claims

% year

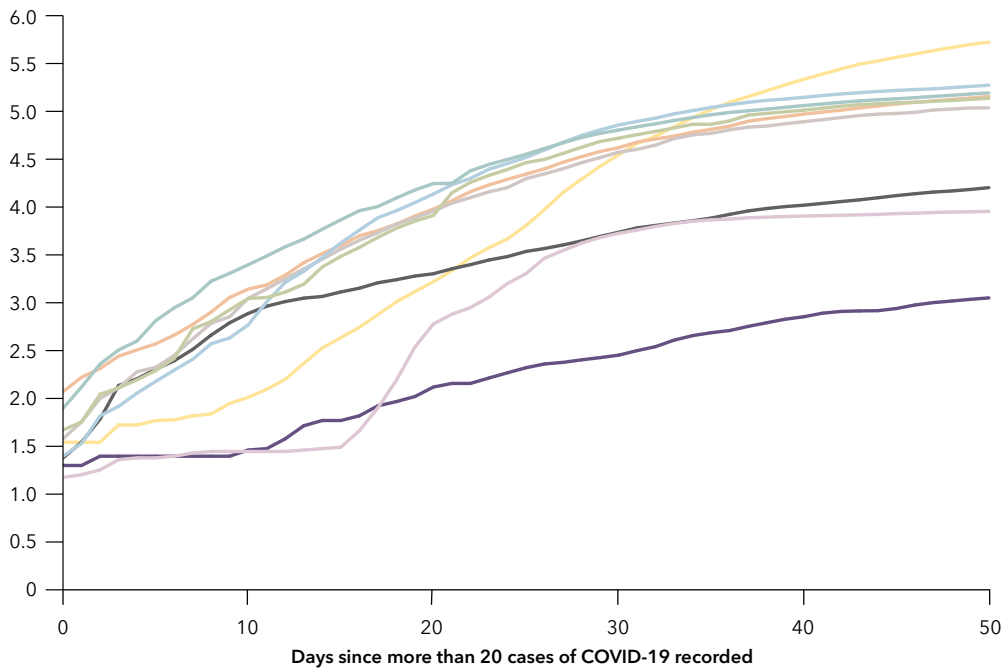


Source: Oxford Economics/Haver Analytics

The good news is that peak lockdown may have been reached at a global level. The levelling off in the number of new COVID-19 cases is already triggering some relaxation in lockdown rules in parts of Europe. Some US states are also starting to loosen restrictions. Most others have partially begun to unwind their lockdown measures in May with further easing expected in June.

COVID-19 cases

Cases (logarithmic scale)



Source: Oxford Economics/Haver Analytics



But for now, policymakers seem to prefer a slow removal of restrictions to minimise the risk of a renewed flare up in the number of COVID-19 cases, implying a slow return to more a normal level of economic activity. The transition to normal may be further tempered by individuals voluntarily choosing to shun situations where close contact with strangers is likely, as seen in China.

Economic recovery will not make up lost ground

- Second half of 2020 won't make up for lost activity in the first half of the year
- A gradual easing of lockdowns to see activity resume in parts of the economy
- The global fiscal expansion is larger than during the global financial crisis

Under the assumption that the gradual unwinding of lockdown restrictions continues and broadens, global GDP is likely to bottom out in Q2. Oxford Economics' forecast assumes that, at a global level, activity rises back to its Q4 2019 local peak in early 2021. For emerging economies such as China, the reversal of the early 2020 falls may be quicker. For typically slower growing advanced economies such as Italy that have been hit especially hard by the coronavirus outbreak, it will take substantially longer for the level of GDP to reverse their losses.

The timing and speed of the eventual economic recovery will depend on several factors including:

- how quickly lockdown restrictions are removed;
- the extent of voluntary social distancing after restrictions are eased;
- the support provided by the monetary and fiscal response; and
- the extent to which the COVID-19 outbreak triggers more sustained changes in behaviour.

In the short term, the speed of the recovery will depend on how quickly economies recover from lockdown. Lockdowns can be thought of as a blunt instrument to contain the spread of the virus when other less invasive forms of containment, such as widespread testing, contact tracing and individual quarantines, are not possible or those systems have become overwhelmed by the number of COVID-19 cases.

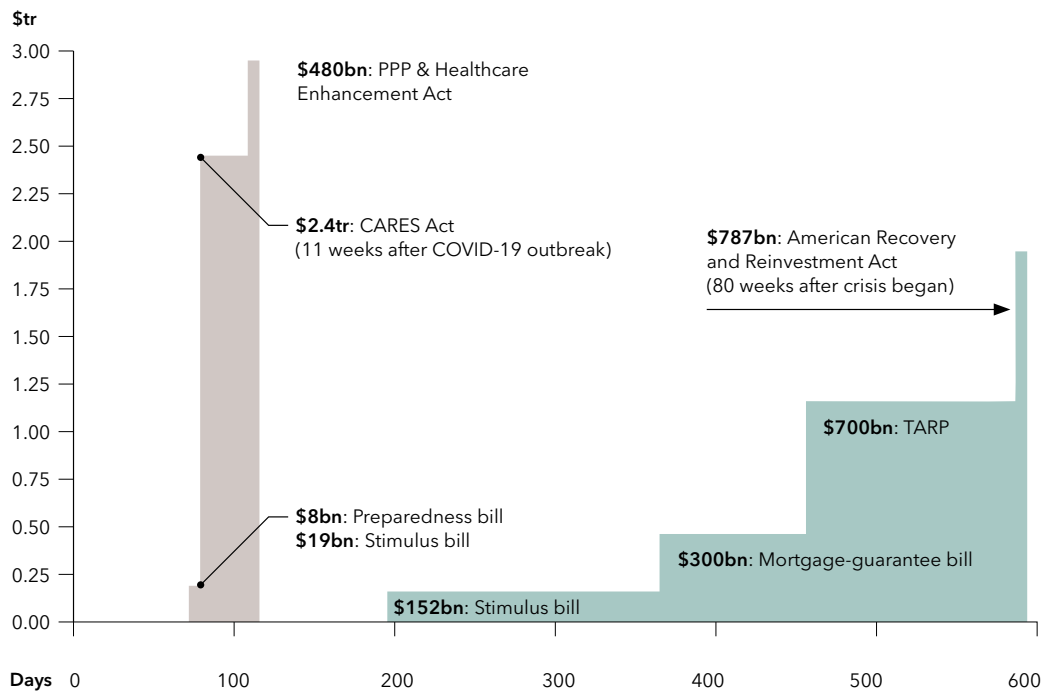
It is highly unlikely that the discovery of a vaccine or dramatic medical developments will occur before 2021. Such developments should eventually come, but without them the easing of restrictions will be gradual and the return to normality will be slow.

The available evidence suggests that some sectors will recover faster than others. Most workers are likely to return to work quickly once this becomes possible, helping the supply side of the economy to bounce back quickly. But individuals may continue to avoid other activities that are deemed non-essential, particularly those involving close contact with other people, such as visits to bars, restaurants and cinemas, suggesting overall demand may pick up more slowly than supply. Some firms that are reliant on complicated international supply chains may also find that they are unable to source components needed to restart production at maximum capacity.

The rebound caused by the relaxation of lockdown restrictions is not the only factor that points to stronger growth ahead. Some of the household spending weakness in H1 will reflect a deferral of spending. The end to lockdowns could thus see some pent-up demand being released. In addition, spending in the second half of the year may be further boosted in oil importing economies due to the recent collapse in the oil price.

Some of the exceptional monetary and fiscal policy support that has been unveiled will also help to boost spending as its full effects begin to be felt. In addition to policy rate cuts and aggressive balance sheet expansion by the Federal Reserve, the US Congress has passed four packages of coronavirus fiscal stimulus response, bringing the total of measures enacted in just over a month to \$3tn, or 15% of GDP. More generally, it is estimated that the global fiscal expansion in response to the COVID-19 outbreak has been larger than that seen during the global financial crisis. Central bank policy rates are also close to or below previous lows.

US: Funds authorized by Congress



Source: Oxford Economics/CBO

- Since China reports first death from Coronavirus (Jan. 11, 2020)
- Since early signs of a financial crisis (Aug. 7th, 2007)

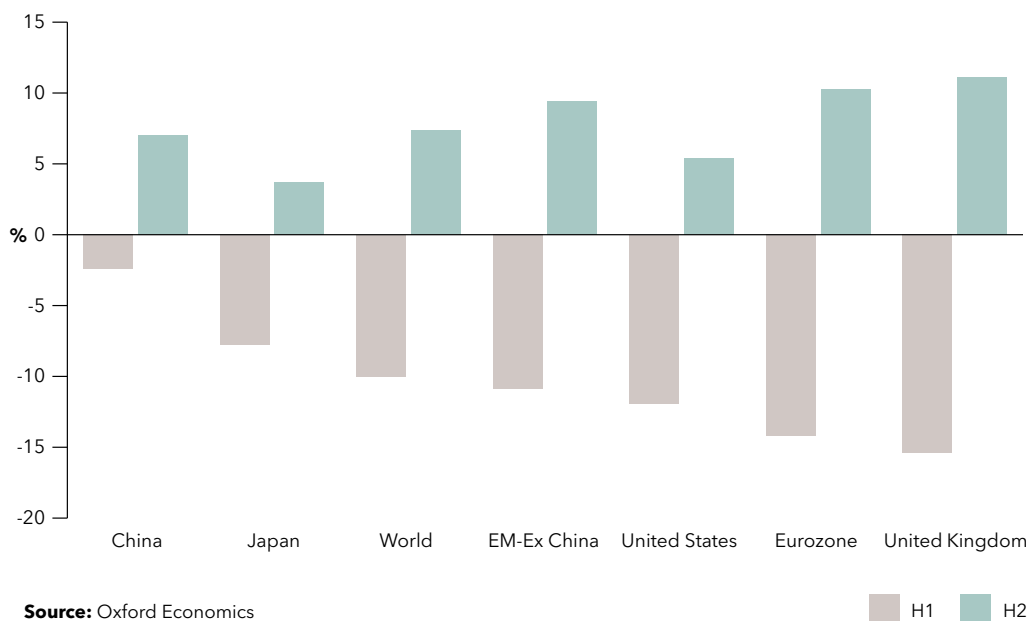
Nonetheless, it will take time for economies to fully reverse the falls in GDP seen in the early stages of this year. While employment should pick up sharply in H2, many industries will struggle with social distancing rules and are likely to permanently lay off some staff. Some businesses that closed down due to the lockdown will never reopen. Given this, and the likely cautious stance of most households and firms due to fears about renewed outbreaks of COVID-19, an immediate rebound in activity to pre-crisis levels is unlikely.

On balance, Oxford Economics expects global GDP to return to pre-crisis levels by about mid-2021.

Normally, fast-growing emerging markets are more likely to reverse the losses in GDP than their slower-growing counterparts. Advanced economies, especially those in Europe, are likely to see the most protracted recovery due to the larger scale of the COVID-19 outbreak and the need for more stringent lockdowns. This will exacerbate the region’s generally lower potential growth and, in some cases, the limited policy response.

However, each region will have its own particular experience with the crisis that will dictate the depth of its recession and the strength of its recovery.

2020 global GDP level change



GLOBAL OUTLOOK

Overall, Oxford Economics expects global GDP to shrink by 4.7% in 2020. This is despite a strong rebound in the second half of the year where they project a 7.4% rise in the last two quarters of 2020. To put this in context, in 2009, the worst year for GDP growth during the global financial crisis, global GDP fell by 'just' 1.1%.

As we move into next year, Oxford Economics expects the quarterly pace of GDP growth to gradually slow to more normal levels. This is compared to as exceptionally weak 2020 which will see GDP growth reach 7% in 2021, the strongest annual growth rate since the 1950s post-World War II economic expansion.

Despite the robust resurgence in activity in late 2020 and throughout 2021, Oxford Economics expects the level of global GDP by the end of 2021 to still be 2% below the level they had expected in January, before the pandemic emerged. This shortfall will continue beyond 2022, reflecting a permanent scar on the economy.

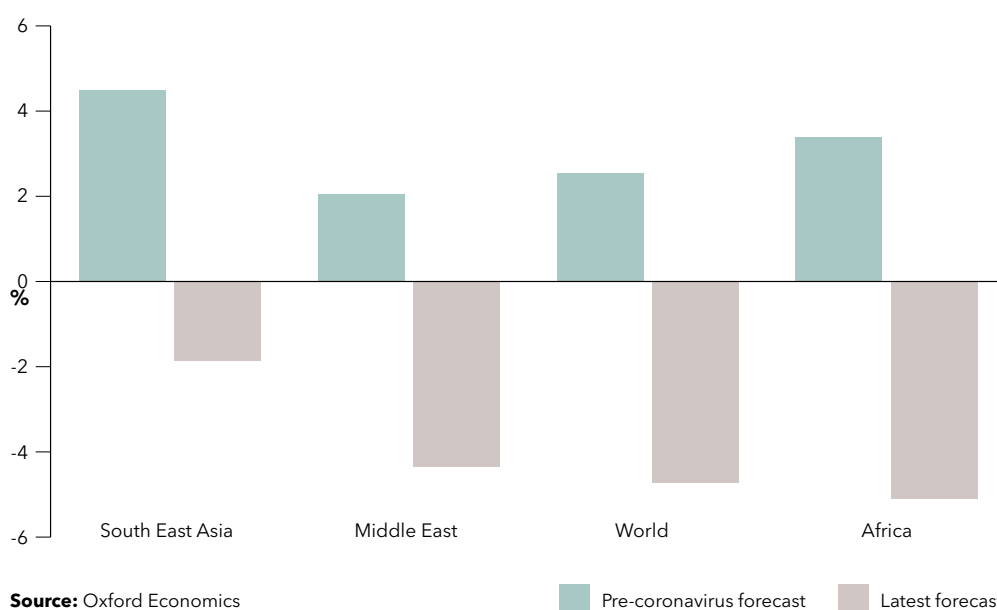
Middle East

The Middle East is set for a sharp fall in 2020 in the face of the dual shock from the coronavirus and unprecedented oil market turmoil. **Oxford Economics forecasts regional GDP to contract by 4.3% this year, the worst performance in recent history,** significantly weaker than the 2% expansion they projected in January. The outlook has deteriorated markedly over the past few weeks. This is particularly the case for the oil-producing countries across the Gulf Cooperation Council (GCC), which have to contend with not only the lockdowns imposed that have slammed the brakes on non-oil activity, but now also the sharp oil output cuts agreed in an OPEC+ meeting in mid-April. The GCC economy is now seen shrinking by 3.9% on aggregate, with all countries experiencing deep recessions. **Oxford Economics still assumes activity will begin to gradually strengthen in H2 as both demand and supply side disruption fade and economic recovery follows in 2021.**

To date, the GCC has been relatively successful in containing the outbreak, with infection and death rates low-to-moderate by international standards. While much of normal activity remains restricted and borders are shut to visitors, the region's two largest economies (Saudi Arabia and the UAE), are starting to unwind virus-related curbs. However, the sharp reduction in oil output, coupled with very low oil prices, is putting pressure on budget revenues, constraining governments' ability to support activity. Support packages have generally been modest in size and narrowly focused, suggesting the bounce-back in demand in key non-oil industries, seen as the primary driver of the expected rebound, may be more gradual. High dependence on travel and tourism and expat workers will also likely weigh on recovery, especially in the UAE and Qatar.

Regional impacts of coronavirus

2020 annual growth (%)



South East Asia

Oxford Economics has slashed the 2020 GDP growth forecast for the South East Asia (SEA) economies amid unprecedented lockdowns that will substantially cut domestic demand, and even weaker exports as global supply chains and external demand are severely affected by the pandemic. Restrictions on exports of some food produce to safeguard domestic food supplies will further dampen export growth. **Oxford Economics forecasts most SEA economies to fall into recession in H1** with Thailand to be the hardest hit, given tourism and travel (directly and indirectly) account for 20% of GDP. The exception is Vietnam, which is relatively advanced in the easing of restrictions and is likely to outperform its Asian peers. That said, it will not be immune to the sharp slowdown in trade flows.

However, after a bleak first half, momentum is forecast to turn the corner in H2 2020 as Chinese import demand and global trade more generally start to recover, although a slower pace of normalisation in travel and tourism will continue to weigh on tourism-dependent economies. Authorities across the region have responded quickly with coordinated fiscal stimulus packages and monetary easing. This should not only prevent an even sharper downturn in domestic demand but also support the recovery in economic growth in H2, with **GDP growth set to rebound to an average 8% next year, after recording a 1.9% contraction in 2020.**

China

In China, Oxford Economics thinks that the worst may have passed as the pandemic appears to have been contained. They expect growth to recover from Q2 onwards as the economy is no longer being held back by supply-side disruptions. However, it is now facing challenges from weak domestic demand and especially faltering foreign demand, as much of the rest of the world falls into a deep recession due to lockdowns. Although they expect a recovery in consumption as daily life returns to normal, lingering fear of a return of coronavirus and uncertainty over income and job losses will weigh on consumption in the coming months. On a more positive note, investment prospects have improved, especially in new industries and infrastructure, which will both benefit from strong policy support. They also expect real estate investment to continue to pick up speed as property developers catch up on housing construction.

Meanwhile, policies rolled out recently such as cuts in taxes and interest rates will begin to support the economic recovery, and more policy support will come, though the easing will remain targeted and modest in size. Indeed, large stimulus remains unpopular in Beijing as it will add to leverage of non-financial corporations that are already seen as a risk to financial stability. Instead policymakers will likely accept low growth this year, given the prospect for a better 2021. **Oxford Economics forecasts GDP to grow 0.8% in 2020**, which would put the level of output 4.7% below their pre-coronavirus forecast. **This will be followed by 8.5% growth in 2021** as both domestic and global economies recover, but the total level of output will remain at least 1.5% below the pre-coronavirus forecast for a few years.

Africa

Like all other regions across the world, Africa will endure a severe economic knock due to the dual global demand and supply-side shocks. Various African countries have imposed measures to curb the spread of COVID-19 but, with the exception of South Africa, lockdown measures have not been as stringent as those seen internationally. Nonetheless, borders being shut and restrictions on the movement of people will hold major adverse implications for these economies that are still characterised by substantial informal sectors that do not officially contribute to GDP, but whose day-to-day operations are critical in sustaining livelihoods for a large proportion of the population. Oxford Economics expects to see a widespread rise in unemployment, with job losses in both the formal and informal sectors. In addition, lower commodity prices and disruptions to global supply chains will compound these challenges, with the continent's economically undiversified oil producers in particular coming under immense pressure.

Governments across the continent have launched various forms of policy stimulus measures which will soften the blow, but aggregate **African output is still projected to contract by roughly 5% in 2020**. African governments don't have the fiscal arsenal available to developed economies and underdeveloped monetary transmission mechanisms in most countries will curtail these support efforts. Pressures are seen easing gradually from Q3 onwards, but the fact that lockdown measures are less stringent in the context of weak healthcare capacity and a population with generally weak immune systems raises the risk that the COVID-19 battle may be more protracted in Africa.

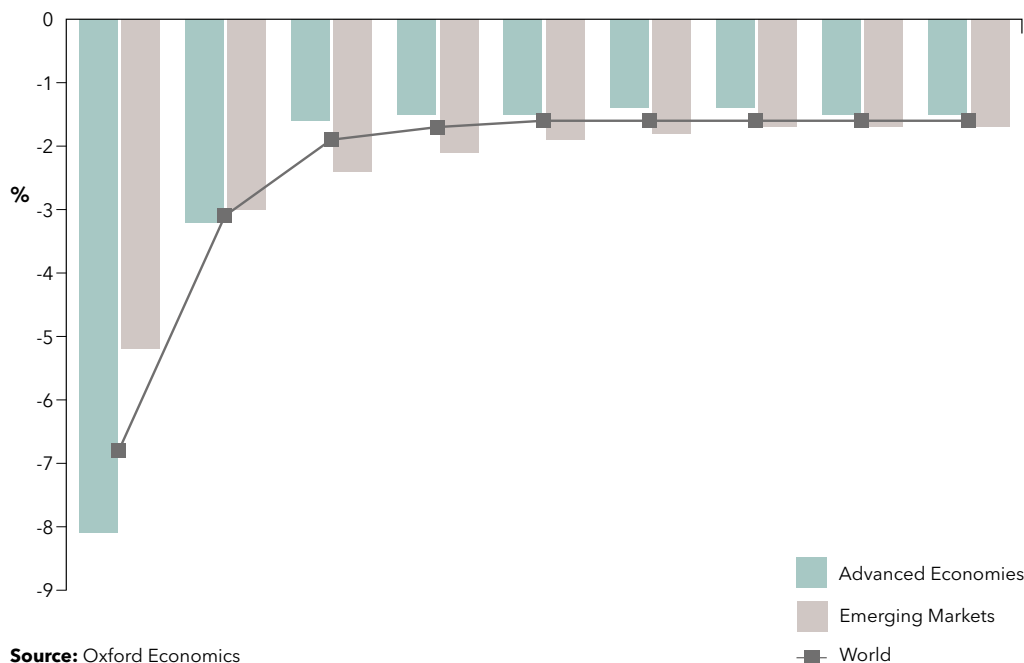
Permanent damage has been inflicted on the global economy

- Coronavirus has caused mild permanent damage to the global economy
- Governments are unleashing unprecedented stimulus to prevent further long-term damage
- Deglobalisation would constrain future productivity

Beyond the shorter term, there is also a possibility that there will be medium-term costs to the global economy in the form of lost activity from the pandemic. **Oxford Economics assumes that the level of global GDP does not fully converge back on the path that they were forecasting before COVID-19, implying that there are some longstanding losses arising from the pandemic. In the medium term, the cost of the virus outbreak could be in the region of 1.6% of global GDP, although this estimate is subject to a high degree of uncertainty.**

Global GDP: medium-term damage

% difference from pre-coronavirus forecast



The degree to which GDP reverts to pre-crisis trends after sharp downturns and historical epidemics and pandemics varies. Historical evidence points to large upfront output losses from pandemics and natural disasters, but the medium-term outcomes are mixed. Large policy responses to such health crises, unsurprisingly, typically result in smaller adverse medium-term effects for the economy.

Unprecedented policy response is aimed at minimising long-term damage

On the face of it, then, the early and aggressive action by policymakers bodes well for medium-term prospects. Nonetheless, much will depend on how quickly policy is tightened once the recovery begins.

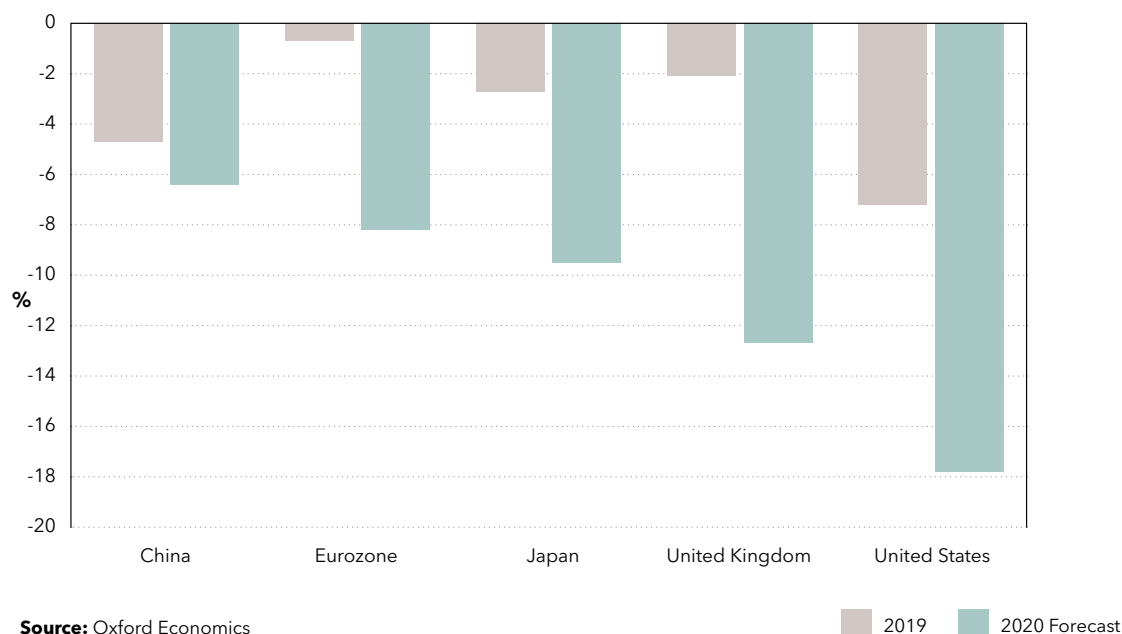
In the short term, government deficits could soar to as much as 20% of GDP due to increased lending and plunging revenues as a result of the lockdown. As a result, Oxford Economics expects government debt levels will rise by 10%-20% of GDP by 2021 in most advanced economies. Record low interest rates means these economies should be able to finance these deficits cheaply, helped by massive quantitative easing policies where central banks such as the FED, ECB and Bank of England attempt to keep financial conditions exceptionally supportive. But economies without monetary independence or more precarious fiscal positions, such as some southern eurozone economies and emerging markets, may find it hard to finance large deficits cheaply for an indefinite period of time.

Given the abruptness of the COVID-19 shock, speedy support is crucial to support the recovery. Economic expansions are typically vulnerable to adverse shocks when they are in their infancy – in the early stages of a recovery, confidence is typically weak, and it may only take relatively small shocks to push the economy into recession. If policymakers begin to reverse the policy measures before the recovery has built significant momentum, due to pressures from financial markets or domestic political factors, then the risk of a ‘double dip’, as occurred in Europe after the global financial crisis, would increase.

Similarly, while the size of the policy support is crucial, the design of the policy is just as important. If emergency loans and transfers take too long to arrive then this will increase the likelihood of firms folding and/or being forced to make redundancies.

Budget deficits

Fiscal budget deficit (% of GDP)



More generally, deep and longer-lasting recessions, especially those involving financial crises, tend to be associated with weaker economic growth subsequently, resulting in larger medium-term losses. Deep and lengthy recessions in the 1970s and 1980s saw 'hysteresis' effects, whereby sharp rises in unemployment and business failures cast long shadows over several years. The 2008 global financial crisis is a prime example of a financial crisis, where the pace of GDP growth in the recovery years persistently underwhelmed relative to pre-crisis trends.

In this respect, there are also some encouraging signs that the shock will not inevitably take a huge toll on the economy in the medium term. **While the recession will be large, Oxford Economics' baseline assumption is that it will be short.** Nonetheless, if the threat from COVID-19 lingers forcing stringent lockdowns to remain in place, or alternatively a relaxation of restrictions triggers a second wave of COVID-19 cases that left governments with little choice but to substantially re-tighten lockdowns, then the recession period could lengthen, increasing the likelihood of more substantial hysteresis effects.

Oxford Economics' baseline forecast assumes that central bank actions will be enough to prevent some form of financial crisis. Recent financial market developments are encouraging in this respect. Nonetheless, it would be unwise to rule out the possibility of the pandemic triggering some form of financial crisis. In such a scenario, the likely medium-term effect on the economy from the COVID-19 outbreak would be more substantial than assumed in their baseline.

Another way in which the crisis may be harmful for GDP in the medium term is if it triggers more structural changes in the private sector. One risk is that households and firms respond to the crisis by trying to reduce debt and increase precautionary savings. While this might be a rational choice it would also lead to a weaker economic recovery and accelerate the shift toward 'Japanification' of major advanced economies - a prolonged period of ultra-sluggish demand despite extensive monetary easing.

Rising protectionism before the outbreak could come back even stronger

The crisis might also exacerbate trends that predated the COVID-19 outbreak. Before the pandemic, global trade was already slowing as a result of the prolonged trade war between the US and China. The imposition of trade tariffs between the two nations, and by the US on Mexico and Europe, caused global goods trade to slow from 6.5% growth in 2017 to just 0.3% in 2019.

This trend towards deglobalisation could likely accelerate after the 2020 coronavirus pandemic, as firms look to insure themselves against further significant supply chain disruption in the event of national lockdown in economies where parts of their supply-chain are located. While this may mitigate future risks, it may result in less efficient production at a global level. In 2019, a decoupling of ideas, a break in consensus views with regards to free markets and trade, and diverging international standards began between the US, Europe and China. This could likely accelerate as firms have to reshape their business model to focus on more localised demand and supply, further reducing economies of scale and adding to inefficiencies.

Longer lockdowns would wipe out substantially more economic activity

- The downside risks are far larger than the plausible upside
- A financial crisis would destroy up to 10% of global GDP
- The length of lockdowns and policymakers' support are vital for the outlook

The risks around baseline economic forecasts are currently especially large and driven by factors, such as the speed with which a vaccine can be found, which are themselves highly uncertain. In the near term the risks centre around the speed at which lockdown restrictions are eased and the risk of a second virus wave. But there is also a high degree of uncertainty over the medium-term costs of the outbreak, reflecting some of the uncertainties highlighted in the previous section. Even if the economic losses from the crisis turn out to be smaller than expected, the level of GDP is unlikely to go above the levels that would have been reached had the COVID-19 pandemic not taken place. In the remainder of the section, we set out plausible upside and downside scenarios.

Downside scenario: Lockdowns persist and irreversibly damage household confidence

In Oxford Economics' downside scenario, they assume that stringent lockdown restrictions remain in place for a more prolonged period in order to bring the pandemic under control, or that an initial loosening of restrictions results in a second wave of infections that forces lockdown measures to be reinstated. **This leads the global economy to contract in Q3 as well as Q4, causing GDP to fall by 8.9% in 2020, compared to a baseline forecast of a 4.7% drop.**

The longer lockdown triggers an even bigger increase in precautionary savings, leading to a weaker recovery and the COVID-19-driven recession exacerbates long-standing structural vulnerabilities, such as overvalued asset prices and high levels of corporate debt. This results in a financial crisis that amplifies de-leveraging in the private sector. As public and private investment fall, productivity growth slows, and potential output diverges from previous trends. **By the end of 2024, world GDP levels are 10% below the pre-coronavirus baseline.**

Upside scenario: Medical advances speed up lockdown easing

In an upside scenario, there is also a possibility that activity can restart more quickly than Oxford Economics anticipates, leading to a faster recovery and less long-term economic damage. It is possible that medical advances – such as increased testing capacity, enhanced therapeutics, and the discovery of a vaccine in the second half of 2020 – lessen business and consumer fear. This would facilitate quicker easing of restrictions and therefore allow activity to resume faster than Oxford Economics' baseline assumes.

Alternatively, using technology, businesses and individuals could find more innovative ways to carry out activities that on the face of it are difficult to do with social distancing in place. This would reduce the burden of ongoing restrictions on economic activity and result in a faster recovery.

In this scenario, private spending and business activity in Q3 2020 would begin to accelerate. However, this process would still be relatively gradual as it will be impossible to completely remove the possibility of infection, even if the risk of serious illness from the virus is reduced. **In Oxford Economics' upside scenario, global GDP still contracts by 2.9% in 2020, but the recovery in 2021 is stronger with growth at 7.3%.**

This would ultimately imply lower precautionary savings in the medium term. **The level of global GDP by the end of 2024 would be 9% higher than in the downside scenario, which illustrates the wide range of plausible outlooks for the world economy.**

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