The Economic Outlook: Pandemic and Recession

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Shutdowns and other measures are slowly bending the COVID-19 curve

Cumulative Deaths from COVID-19

Source: European Centre for Disease Prevention & Control; Macrobond; author's calculations.
But containment measures (and choices to stay home) are causing a plunge in economic activity

Unprecedented drop in consumer demand for many services

Sharp slowing in production of many goods as employees cannot get to work and supply chain disruptions take hold

Knock-on effects include liquidity crises, drops in asset prices, and surge in unemployment
The pace of the rebound depends on 3 key factors

How dangerous and contagious is the virus?

How quickly can countries build capacity for testing, tracking, and other means of reducing contagion after shutdowns are eased?

How much can aggressive policy responses limit the damage to economic structures during the shutdowns?
Pandemic causes a sharper global slump than the financial crisis, with significant recovery thereafter.

Real GDP Growth

Percent Change, Annual Average

<table>
<thead>
<tr>
<th>Region</th>
<th>2019</th>
<th>2020</th>
<th>2021</th>
</tr>
</thead>
<tbody>
<tr>
<td>World</td>
<td>-20</td>
<td>-20</td>
<td>-20</td>
</tr>
<tr>
<td>United States</td>
<td>-10</td>
<td>-15</td>
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</tr>
<tr>
<td>Euro area</td>
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<td>Japan</td>
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</tr>
<tr>
<td>United Kingdom</td>
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</tbody>
</table>

Many vulnerable households and businesses but fiscal policy response aggressive

Hit harder than the US by drop in trade because of greater trade dependence

Huge SME sector and trade dependence will be a significant drag

Public health missteps and EU links worsen 2020 but vigorous policy should pay off in 2021


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Pandemic causes a sharper global slump than the financial crisis, with significant recovery thereafter.

Real GDP Growth

Percent Change, Annual Average

Early successes but recent experience suggests recovery will be slow and uneven
Informal sector comes back more quickly but financial stress casts lingering shadow
2020 activity held back by lower oil demand; health care diverts resources that might otherwise support recovery
Recovery likely to be hindered by weak underlying state of economy and social unrest

In the United States, hard data about the severity of the recession is emerging.
An “check mark” shaped cycle is most likely

**U.S. Real GDP**

Chained 2012 Dollars (Trillions)

Note: Dashed segment is forecast.
Source: Bureau of Economic Analysis; Macrobond; author's calculations.

**U.S. Real GDP Growth**

Percent Change, Annual Rate

Source: Bureau of Economic Analysis; Macrobond; author's calculations.
With the unemployment rate rising to the highest level since the Great Depression

Unemployment Rate

Percent of Labor Force

Note: Dashed segment is forecast.
Source: Bureau of Labor Statistics; Macrobond; author's calculations.
Many households in the middle and lower part of the distribution have little financial buffer.

The graph illustrates the median financial assets across different income quintiles. The x-axis represents the "Normal" income quintile, while the y-axis shows the weeks of "Normal" income.

- **Total Financial Assets:**
  - Lowest Quintile: Approximately 2 weeks
  - Second Quintile: Approximately 4 weeks
  - Middle Quintile: Approximately 18 weeks

- **Liquid Financial Assets:**
  - Lowest Quintile: Approximately 2 weeks
  - Second Quintile: Approximately 2 weeks
  - Middle Quintile: Approximately 2 weeks

Note: For households with heads age 25-54.
Source: Survey of Consumer Finances (2016); author's calculations.
Some were already encountering greater financial difficulties and many more will likely do so.

**Serious Delinquency Rates for Selected Types of Debt**

- **Credit Card**
- **Mortgage**
- **Auto Loan**

**Debt Delinquency Expectations, Income Less Than $50,000**

Mean Probability of Not Being Able to Make Minimum Debt Payment Over the Next 3 Months

Source: Federal Reserve Bank of New York; Macrobond.
Many small businesses are operating on thin margins

43% of small firms reported challenges paying operating expenses in 2019.

30% reported challenges making payments on debt.

Note: Cash buffer days measured from 2013 to 2017.
Source: JPMorgan Chase & Co. Institute.
The United States has taken aggressive monetary and fiscal policy steps

Dramatic action by the Federal Reserve:

– Cut in policy rate and large-scale asset purchases
– Lender-of-last-resort interventions building on financial crisis playbook, including liquidity facilities aimed at domestic strains and swap lines with other central banks

Unprecedented expansion of fiscal policy:

– Address public health needs
– Limit damage to the economic structure
– Protect the vulnerable
– Stimulate demand
Fed policy response—commitment to “whatever it takes”

Federal Reserve System Balance Sheet, Total Assets

Billions of Dollars

Note: Shaded regions denote recessions.
Source: Board of Governors of the Federal Reserve System; Macrobond.
The CARES Act

- Enhanced Unemployment Insurance Benefits, $260b
- Direct Payments to Households, $290b
- Small Business Loans (incl. Payroll Subsidies), $444b
- Support for Federal Reserve Lending, $454b
- Direct Treasury Lending to Affected Industries, $46b
- Spending for Hospitals, FEMA, & Infrastructure, $260b
- Aid to State and Local Governments, $181b

Note: Excludes about $345b in tax relief, social safety net funding, and other miscellaneous spending.
Source: Committee for a Responsible Federal Budget; author's calculations.
US fiscal policy response—what comes next?

Implementation of the CARES Act is challenging and crucial.

Automatic stabilizers will also buffer the downturn and widen the budget deficit—by about $1 trillion this year.

Phase 4 of fiscal relief will probably include more funds for small business lending, more support for state and local budgets, an extension of expanded UI benefits, and more.
US federal debt will jump upward, but financing costs are very low and are unlikely to rise sharply.

**U.S. Federal Debt Held by The Public**

- **Percent of GDP**
  - Historical
  - Very approximate projection with more COVID spending and no later deficit reduction

**10-Year Treasury Yield**

- **Percent**
  - Source: Board of Governors of the Federal Reserve System; Macrobond.

Note: Assumes $3 trillion of additional COVID-related measures, extensions of existing fiscal measures, and extension of 2017 tax cuts.
Source: Congressional Budget Office; Office of Management and Budget; Macrobond; Jason Furman’s calculations.
US Inflation will be buffeted by cross-currents but the net effect of crisis is likely to be negative.

Supply constraints will raise the price of some goods.

At the same time, we are already seeing softness in prices in some services and goods sectors where demand has dropped sharply.
Confidence bands for the global economic forecast are especially large now

Neither epidemiologists nor economists have any analogous experiences in modern times on which to base their forecasts.

Indicators to watch include:

- How quickly deaths and hospitalizations flatten out in Europe and the United States.
- The extent to which countries in South Asia, Africa, and Latin America become infected.
- China’s success at rebooting its economy.
- The rate at which testing increases in the United States.
# Addendum: Real GDP Growth Rates

<table>
<thead>
<tr>
<th>Real GDP Growth (Y/Y)</th>
<th>2019</th>
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<th>2021</th>
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<td>Global Output Growth</td>
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