

Economic policy

Additional Course Assignment

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Corona crisis of 2019-20

economic perspective

The coronavirus pandemic is an outbreak of the newly emerging respiratory disease COVID-19. This disease had first become noticeable in December 2019 in the megacity Wuhan in the Chinese province of Hubei, developed into an epidemic in China in January 2020 and finally spread worldwide. The outbreak was triggered by the previously unknown corona virus SARS-CoV-2. This virus is also known as a new corona virus.

On January 30th, 2020, the World Health Organization (WHO) announced the international health emergency in order to counteract the spread to countries without efficient health systems. From February 28th, 2020, the WHO's reports assessed the risk at global level as very high.^{1 2}

On January 13th, 2020, the first laboratory-confirmed infection was reported from Thailand, outside the People's Republic of China. On January 23, 2020, the first case of infection outside of Asia was reported in the United States of America. On February 23, 2020, the first two Europeans to died.^{3 4}

Italy increasingly became the new centre of the pandemic; on March 19, more deaths were reported here than in China for the first time. On March 19, more deaths were reported here

¹ WHO Statement Regarding Cluster of Pneumonia Cases in Wuhan, China, WHO, 9. January 2020

² Elena Erdmann, Coronavirus: „Wir wissen nicht einmal, wie viele Fälle es heute gibt“, in: Die Zeit, 29. February 2020

³ Coronavirus deaths exceed Sars fatalities in 2003. BBC News, 9. February 2020

⁴ Kristian G. Andersen, Andrew Rambaut, W. Ian Lipkin, Edward C. Holmes, Robert F. Garry: The Proximal Origin of SARS-CoV-2. In: virologica.org, 17. February 2020

than in China for the first time. At the end of March 2020, the number of infections in the USA rose sharply; the United States, along with Europe and China, became the new centre of the pandemic.^{5 6}

In April 2020, France, the United States, the United Kingdom, Iran, Belgium and Germany were among the countries that reported more deaths than China. In many countries, the pandemic is now characterized by massive cuts in public and private life as well as an economic crisis.⁷

Within a few months, the global economy has entered a crisis that is unique in many ways. The health emergency and the measures to curb the spread of viruses hit the global economy abruptly from the supply and demand sides and overshadowed the decline in overall economic output triggered by the financial crisis in 2009. The effects are widespread, both geographically and in comparison, to other industries. The economic policy response came in a short time and on a large scale in many developed countries. However, the measures are less of a stimulant than of a saving character, because the demand-side impulses are currently of little use to the current lockdown. The situation is even more dramatic in many emerging and developing countries, especially since the state's financial scope is often limited. Capital flight of historical proportions and health emergencies paint the overall socio-political and economic picture.⁸

This situation has prompted the International Monetary Fund (IMF) to revise its historical scope. The decline in global economic output as a result of the lockdown, which is forecast for 2020, is said to be the largest since the Great Depression. The IMF divides economic policy

⁵ Gesundheitsexperte bemängelt Versäumnisse der Bundesregierung bei Corona-Virus. in: Deutschlandfunk.de, 25. February 2020

⁶ Coronavirus in Deutschland: Zahl der Infektionen sprunghaft gestiegen. in: tagesschau.de. 28. February 2020

⁷ Julia Köppe: Neues Coronavirus: Suche nach Patient X. in: Der Spiegel, 18. February 2020

⁸ Martin U. Müller, Claus Hecking, Simon Hage, Kristina Gnirke, In Chinas Häfen stapeln sich die Container. in: Der Spiegel, 22. February 2020

responses into two phases: containment and stabilization, followed by the recovery phase. Quarantines, bans, and social distancing remain critical to slow transmission in the first phase so that the healthcare system can cope with the increasing demand for its services.^{9 10}

However, these measures also give researchers time to develop therapy and vaccines. While parts of the economy are closed, policymakers need to ensure that people are able to meet their needs and that companies get a handle on the acute phase and related liquidity constraints. Targeted fiscal, financial and monetary measures are necessary to secure economic relationships as well as economic and financial structures. Advanced economies with strong governance, well-stocked health systems, and the privilege of spending reserve currencies are better placed to manage this crisis. In contrast, several emerging and developing countries are currently experiencing health, economic and financial crises at the same time and will urgently need help from advanced economies and international institutions. Multilateral cooperation is central to this global problem and, in addition to sharing equipment and expertise to strengthen health systems, can include financial support for many emerging and developing countries, including debt moratoriums and restructuring.^{11 12}

The IMF economists revised the forecast for the development of the global economy in 2020 down by 6.3 percentage points to 3.0 percent. According to the forecast, global economic output is likely to recover somewhat in 2021 and grow by 5.8 percent. Nevertheless, the pre-crisis path will not be reached in the coming year. The forecast is corrected across the board.¹³

⁹ Brutal: Welche Folgen das Virus für Deutschland und die Weltwirtschaft haben könnte, in Focus Online, 28. January 2020.

¹⁰ EU-Kommission fordert freie Fahrt für den Warenverkehr. in: tagesschau.de. 16. March 2020

¹¹ Corona-Krise: US-Arbeitsmarkt im freien Fall. in: tagesschau.de. 2. April 2020

¹² Gwang-Chol Chang, Satoko Yano, UNESCO's Section of Education Policy: How are countries addressing the Covid-19 challenges in education? A snapshot of policy measures. UNESCO, Global Education Monitoring Report, 24. March 2020

¹³ Erholung 2021 unter Vorbehalt: IWF erwartet globale Rezession. in: faz.net, 30. March 2020

In the past, German exports followed the development of world trade with a slight tendency to overshoot in times of crisis. The global trade volume in the crisis year 2009 fell by almost 13 percent, while price-adjusted German exports fell by a good 14 percent in the same year. When the growth rate of global trade, partly driven by the dotcom crisis, declined from 13.9 percent in 2000 to 2.9 percent in 2001, the rate of expansion of German exports slowed considerably. In the following years 2002 and 2003 in particular, they experienced a much smaller increase than the global trade volume.¹⁴

Even in the current crisis, German exports are likely to follow the development of world trade and suffer heavy losses. The figure shows the IMF forecast for the fifteen most important export destination countries in terms of export sales of German companies. A particularly sharp drop in economic output in 2020 is expected at -9.1 and -8.0 percent for the countries severely affected by the virus spread, Italy and Spain. A total of 8.4 percent of German goods exports flow to these two countries. For China, the IMF expects overall economic output to increase by 1.2 percent in 2020, but at the same time this means a decline in economic growth of almost 5 percentage points compared to the previous year. And the other four in the top five of the German export destination countries, the USA, France, the Netherlands and the United Kingdom, are likely to experience sharp drops in economic activity of up to 7.5 percent.^{15 16}

The integration of the German economy into the global economic structures has led to a considerable increase in prosperity in the past decades. The current crisis will require a reassessment of the risks associated with international value chains. The advantages of the

¹⁴ IWF: Weltwirtschaft wird "schwere" Rezession erleben, in: Süddeutsche Zeitung, 30. March 2020

¹⁵ Welthandel könnte um bis zu ein Drittel einbrechen, in: spiegel.de, 10. April 2020

¹⁶ IWF senkt Prognosen wie noch nie - Weltwirtschaft vor dramatischer Rezession. in: dw.com. 14. April 2020

international division of labour have to be taken in consideration as well. The discussion about the systemic relevance of certain products and the associated claims to industrial and trade policy support or protection measures in the relevant sectors opens the door to a new wave of protectionist measures and requires thorough analysis. However, in order to maintain the achievements of trade liberalization in recent decades and to better counter global crises in the future, more multilateralism and not protectionism is the order of the day.¹⁷

The measures against the coronavirus pandemic include more than just a health policy. Their socio-political and economic consequences are so enormous that they will shape the fate of mankind in the long term.

In principle, economists must now accept that health policy comes first. We must therefore keep the inevitable economic impact as limited as possible. But the effects of the protective measures can be compared to an artificial coma of the entire economic system. Economic policy is therefore focused to harm the economic system as little as possible in the long term.¹⁸

In the short term, this primarily means measures to ensure liquidity. This includes tax deferrals and comprehensive government guarantees for loans to bridge liquidity shortages. The instrument of short-time work benefits plays an important role in Germany. This enables companies to reduce the working hours of employees and receives an increase in wages and social security contributions from the Federal Employment Agency (normally 60 percent of the basic salary or 67 percent for households with children).^{19 20 21}

¹⁷ Die Rezession beschert der Welt die noch viel größere Katastrophe, in: welt.de, 8. April 2020

¹⁸ Kampf gegen Coronakrise: EU und Mitgliedstaaten haben 3,4 Billionen Euro mobilisiert. In: Der Spiegel. 20. April 2020

¹⁹ 650.000 Betriebe haben Kurzarbeit angemeldet, morgenpost.de, 10. April 2020

²⁰ Deutsche-Bank-Chefvolkswirt: Coronavirus kostet Deutschland 1.500.000.000.000 Euro, in Focus Online, 30. March 2020

²¹ "Kurzarbeit: Germany bets on tried-and-tested tool for coronavirus jobs crisis". The Local. 1 April 2020

But securing liquidity is only the first line of defence. Since the crisis will continue to accompany us for at least four to six weeks, the state must compensate for the loss of income for companies and many freelancers by making direct cash payments. In the short term this can be done through concrete subsidies.

As a comprehensive solution a model of negative income tax should be considered. Companies and freelancers received a certain proportion of the income or corporate tax already paid for 2019 from the tax authority. In order to avoid deadweight effects, the 2020 tax return could be used to check whether the profit actually decreased significantly compared to 2019. If this decline were less than maybe twenty percent, the negative income tax would be reversed.

Without such extensive transfer payments, the entire economy, especially the financial system, would suffer long-term damage which would prevent a rapid economic recovery after the end of the pandemic. Since the restrictions causes enormous household costs for the economy, the question is often asked whether the states are even able to raise the necessary financial resources.

One answer to this is provided by modern money theory. In principle, there are no funding restrictions for large countries, according to their key message. A historical example of this is the financing of wars: data from Great Britain and the United States show that the ratio of debt to gross domestic product increased significantly during the two world wars. But this did not create major inflation problems.

Large countries are able to compensate for the loss of income due to the corona virus through extensive, direct payments to companies, workers and freelancers without having to cut back financially. And if it is not possible to have the additional government debt financed by private

investors on the capital markets, the central banks are ready to buy government bonds in principle, indefinitely. This was expressly confirmed by the United States Federal Reserve and the European Central Bank.^{22 23}

Critics of modern money theory emphasize the risk that high deficits could lead to inflation.

Problems arise especially for countries that cannot borrow enough in their own currency. In Europe, this is particularly true of the heavily indebted countries in the Eurozone like Italy. Other solutions for financing have to be found. Eurobonds could be an option. These funds are not paid out to the individual Member States as loans, but in the form of transfer payments.²⁴

All in all, the coronavirus crisis is probably the biggest challenge for the global economy since World War II. It will take a huge effort through out the hole world to manage this crisis.

Academia could contribute to solving the present and upcoming crisis by checking unconventional theories like the new monetary financial theory for their practicability and if possible, develop new approaches.

²² Anja Ettl, Holger Zschäpitz: EZB holt im Kampf gegen das Virus eine neue Bazooka raus. in: Welt.de. 19. March 2020

²³ Was im Corona-Paket der EU steckt. In: n-tv.de. 10. April 2020

²⁴ Union läuft Sturm gegen Corona-Bonds. in: n-tv.de. 9. April 2020

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