

## DROP IN DATA CONFIRMS NEED FOR STRONG POLICY REACTION

The measures to stop the spreading of the pandemic have a profound impact on the economy which increasingly shows up in the economic data. Record declines in business sentiment illustrate the necessity of the forceful policy measures which have already been taken. The lifting of the lockdowns will, mechanistically, trigger a rebound in activity but additional stimulus will probably be needed to maintain the momentum.

We are in an atypical recession. Robert Kaplan, President of the Federal Reserve Bank of Dallas calls it a self-mandated recession<sup>1</sup>. The necessary measures to stop the spreading of the pandemic have a profound impact on the economy causing a recession which is expected to be deep and short.

Recent economic data which have been gathered when lockdowns had been introduced start to show the extent of the hit. The flash purchasing managers' indices<sup>2</sup> for March showed big declines, in particular in services and as far as export orders are concerned. In Germany, the ifo business climate had the biggest monthly decline on record and the same holds for its French equivalent produced by INSEE. In the US, initial jobless claims jumped to 3.3 million - the highest on record - and is expected to increase further in the near term. This number didn't stop Wall Street from rallying strongly, which may reflect optimism about the impact of the USD 2 trillion stimulus package - about 10% of GDP - which had been voted in the Senate but it might also show that investors are 'looking through' very poor data, considering that a self-mandated recession will end swiftly once the lockdown is lifted.

This shifts the debate on the economic costs of the lockdown. These costs depend on how long it will be maintained and under which conditions. INSEE communicated this week that the loss of activity due to one month of confinement, could lower annual GDP by 3%<sup>3</sup>. A confinement of two months would have an impact on annual GDP of 6%. The ifo Institute calculated that in case of a partial standstill for two months "the costs will range from EUR 255 to 495 billion, depending on the scenario. That means output for the year will shrink by 7.2 to 11.2 percentage points"<sup>4</sup>.

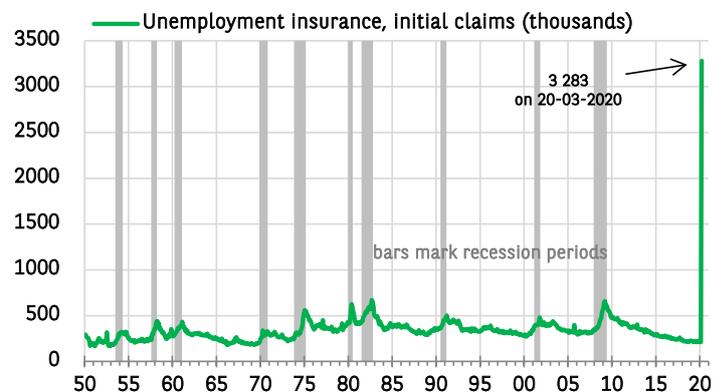
These estimates illustrate how crucial it is to comply with the measures to stop the spreading of the virus: strict compliance increases the likelihood that lockdowns would be lifted sooner rather than later thereby limiting the human cost but also the economic impact. In many European countries as well as in the US, measures have been taken to attenuate the impact on companies, in particular SMEs, so as to avoid that a liquidity problem would end up becoming a solvency problem, thereby inflicting lasting damage to the economy. In addition, income support to households or, as seen in several European

countries, measures to facilitate the use of part-time unemployment whilst limiting the impact for the people concerned, should avoid that household spending declines even more.

Once lockdowns are lifted in various countries, activity will, mechanistically, rebound as people will be able to spend and travel again and companies to offer their goods and services. However, that does not mean that companies will rush to start investment plans which previously had been put on hold or even canceled altogether. Likewise, the sudden increase in unemployment will take time to go into reverse. As a consequence, a second wave of fiscal policy support will probably be needed to keep the momentum going.

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US INITIAL CLAIMS FOR UNEMPLOYMENT INSURANCE  
(MONTHLY DATA)



SOURCE: US DEPARTMENT OF LABOR, NBER, BNP PARIBAS

1. Interview on Bloomberg Television, 27 March 2020.
2. The data are for the US, the eurozone, France, Germany, the UK and Japan.
3. <https://www.insee.fr/fr/information/4471804>.
4. ifo Institute: *Corona Will Cost Germany Hundreds of Billions of Euros*, press release, 23 March 2020.

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