EDITORIAL

THE CORONAVIRUS AND THE PROFILE FOR GLOBAL GROWTH IN 2020: V, U OR L?

From an economic perspective, the coronavirus epidemic represents a combination of a demand, a supply and an uncertainty shock. The weight of China in world economy, its contribution to global GDP growth and its role in global value chains imply that the international repercussions are more far-reaching than during the SARS crisis in 2003.We have to brace for poor data in February and March, so the real test is whether April sees a pick-up in business surveys. Absence thereof would fuel concerns that the impact is more lasting in nature which would put us in a U-type scenario. An L-type scenario looks unlikely as yet whereas a V-type recovery would supposes a swift decline in new cases.

At the start of the year, it looked like we were heading for a J-type recovery of global growth.. Not a steep J, more like flattish growth in the early part of the year followed by a gradual pick-up in the second half, on the back of better business surveys, reduced uncertainty and accommodative monetary and financial conditions. The outbreak of the coronavirus has changed the scenario and the question now is whether the recovery will be V, U or L-shaped.

From an economic perspective, the epidemic represents a combination of three shocks: a demand, a supply and a confidence shock. On the demand side various transmission channels can be distinguished. Chinese household consumption declines because people have to stay home, suffer an income loss, feel uncertain and hence postpone big ticket purchases. Foreign travel declines as well as purchases of foreign goods, so imports decline. Public spending will increase slightly –investment in health care facilities- or perhaps more significantly to support growth. Corporate investment will decline because of reduced demand but in particular, increased uncertainty.

In terms of impact on the rest of the world, the decline of Chinese imports and tourism represents a direct spillover effect. Sector effects can be huge, think of tourism, restaurants, the IT sector, commodities or the automobile industry. . Countries which experience a decline in Chinese demand will in turn import less intermediate inputs that go in their exports. The relevant metric in assessing the exposure to a growth shock in China is how much value added from a given country is embedded in Chinese final demand -domestic and exports. This in turn can be related to the country's GDP. As shown in the chart, this weight is for most countries very small. It is estimated that the SARS epidemic in 2003 represented a hit to Chinese GDP of 1%. Of course, the weight of China in global GDP now is a multiple of what it was in 2003 [1], but even assuming a considerable drop in Chinese growth, the table indicates that the effect would be small. Clearly, this does not take into account the indirect consequences such as negative multiplier effects, a drop in confidence and supply disruptions. Concerning this last point, the situation is very much different compared to 2003 when there were no factory shutdowns in China. The global repercussions are also of a much bigger scale due to the integration of China in global value chains. Mounting anecdotal evidence at Western companies suffering from disruption of supplies coming from China –e.g. mobile phone, automobile sector- may even lead to an overestimation of true macro impact.

An epidemic is a temporary shock so the question is how the recovery will look like. V in case the number of new victims declines swiftly, which would mean that uncertainty drops quickly, unleashing pent-up demand in China and restocking, with positive global repercussions. U if the peak in new victims is reached several weeks later, in which case both consumption and production will be disrupted for a longer period. Global uncertainty would increase, weighing on corporate investment, financial markets, hiring decisions. L would be a more extreme version, with an initial hit to growth and no recovery in the foreseeable future. Such a scenario seems as yet quite unlikely. We have to brace for poor data in February and March, so real test is whether April sees pick-up in business surveys. Absence thereof would fuel concerns that the impact is more lasting nature which would put us in a U-type scenario.

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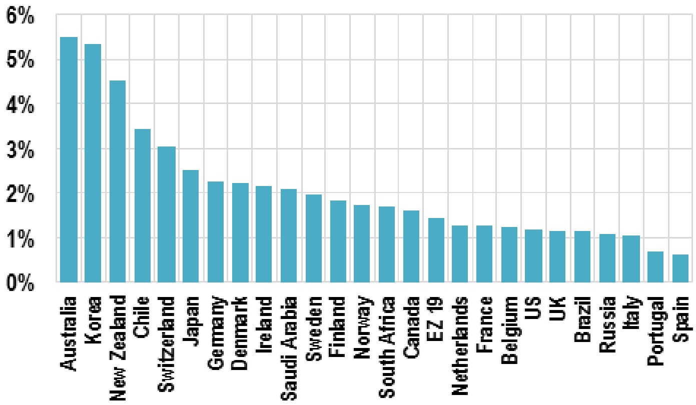
VALUE ADDED IN CHINA'S FINAL DEMAND BY COUNTRY OF ORIGIN (IN % OF GDP OF THE COUNTRY OF ORIGIN)



SOURCE: OECD, BNP PARIBAS

1. Based on IMF World Economic Outlook data, China represented 4.3% of world GDP in 2003 and 16.5% in 2019

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