

# THE ECONOMIC IMPACT OF COVID- 19 ON ASIA- PACIFIC

APRIL 2020

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### April 2020

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# EXECUTIVE SUMMARY

**COVID-19 presents an unprecedented threat to both human health and to prosperity in countries in the Asia Pacific region and globally.** The initial and primary concern is of course the impact the disease has on those that suffer and those around them. But the outbreak is also having an economic impact on a scale and speed not seen before. And whereas previous risks to economic growth, such as a trade war or a financial crisis brought about by high debt, are increasingly well-understood, the outbreak of COVID-19 has presented economic policymakers around the world with very different challenges.

**The impact of COVID-19 has evolved from an Asia-focussed supply chain shock to a truly global stoppage in normal business activity.** Economic forecasts published in January and February, when the outbreak was largely contained to Asia, showed a hit to world GDP growth of around 0.2%. China's lockdown measures through February and March took an increasingly heavy toll on the economy though, deepening the economic cost of containing the virus. And as the virus has spread across the globe, lockdowns and restrictions to travel now mean the first quarter of 2020 is likely to have seen the sharpest contraction in world economic output in history, with an even worse fall in output in the second quarter.

**An ambitious policy response has been seen across the globe and is key to containment and rebound.** Over 100 countries had implemented some form of lockdown by the end of March, while governments ramp up spending on testing and treatment, to contain the virus' spread. At the same time, monetary and fiscal policy is being eased across the world, including in several key Asian economies, to try and protect households and businesses from the financial consequences of a prolonged period without income. The focus of fiscal and monetary policy is not to support growth now, but rather on how the economy will look after the pandemic passes.

**Containing the spread, and supporting households and business is critical for a strong recovery.** We are already seeing early signs of a rebound in China, as the spread is contained Authorities have increasingly lifted lockdown measures even in Wuhan, the city at the epicentre of the outbreak, and is now focusing on economic growth. Also, even as restrictions are lifted, relatively strict monitoring, screening, testing, and tracing systems remain in place, including a QR code "passporting" system. Meanwhile, the public remains on high alert for new outbreaks, with new cases extensively disseminated and analysed on social media. This makes it quite unlikely, in our view, that significant numbers of people have COVID19 and are moving about undetected.

**Based on the key assumption the spread is contained through 2020 Q2, and restrictions elsewhere start to ease from 2020 Q3, we forecast a strong rebound for the world economy in 2021.** Our baseline forecast sees the world economy contracting by 2.8% in 2020 and growing 6% in 2021. For China, our forecast is -0.2% in 2020, and growth of 9% in 2021. In Taiwan and other signatories to the Cross-Strait Economic Cooperation Framework, our forecast also assumes renewal of the agreement by September 2020 – failure to do so would pose a particular risk to the recovery in Taiwan.

**But uncertainty is the watchword, and a more severe scenario would prolong the recession and hamper the recovery.** Uncertainty remains in several key areas, including with respect to the rate of spread of the disease across and within economies, the need for further lockdown measures, and policymakers' ability to protect households and firms from the financial consequences of the crisis. We also assess a more severe scenario across these key metrics, and find that under these assumptions, the world economy would contract by 8% in 2020, and China's economy by 5.9%.

# 1. FROM SLOWDOWN TO LOCKDOWN

## 1.1 A COOLING PACE OF GROWTH MOVING INTO 2020

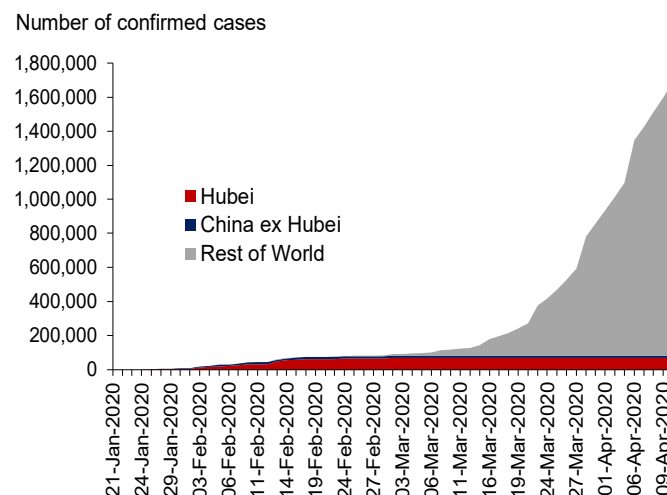
Prior to the outbreak of the coronavirus and its spread across China, then Asia and the world, the global economy looked to be entering 2020 on a reasonably solid footing. Business investment remained tepid against a backdrop of lingering fears of the US-China trade war reigniting. But world trade and industrial output looked to have bottomed out late in 2019, offering hope of a recovery into 2020. Additionally, labour markets remained strong around the world, helping to deliver real income gains for households, and supporting consumer-led growth. Our forecast published in January 2020 was for the world economy to grow by 2.5%, broadly the same rate as in 2019, but set to gradually accelerate through 2020.

## 1.2 EVOLUTION OF A PANDEMIC

But the relatively promising start to 2020 was soon undermined by the rapid spread of COVID-19. The outbreak of COVID-19 has had a major economic impact through its disruption to supply chains, impact on financial market confidence, and most significantly through the restrictions to movement that governments around the world have had to erect to contain its spread.

The virus was first detected in Wuhan, the capital city of China's central Hubei province, and a key cross-China railway hub, with the Wuhan Centre for Disease Control (CDC) identifying a cluster of pneumonia-type cases on 31 December. On 8 January, a new coronavirus was identified as driving the now-growing outbreak. By the end of January, the virus had spread to every province in China. Also by the end of January, cases had been detected in 20 more countries, principally in Asia. On 31 January, the World Health Organisation (WHO) declared the virus a "global public health emergency".

**FIGURE 1 – COVID-19 CONFIRMED CASES BY COUNTRY**



Source : Oxford Economics/Haver Analytics

Through February and March, the regional pandemic evolved into a global pandemic, with serious outbreaks being detected in Italy and Iran around the middle of the month, and then across Europe and latterly in the US.

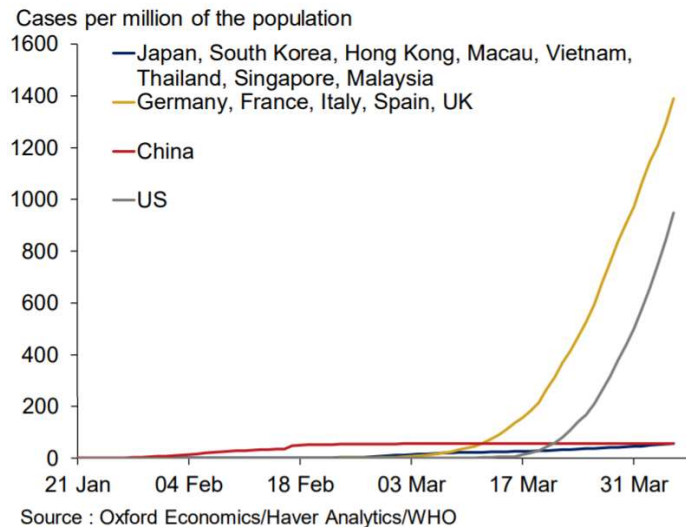


Prior to the outbreak of COVID-19, our forecast was for a gradual pickup in world trade in 2020, complementing a solid rate of household spending growth. World GDP growth was forecast at 2.5% in 2020



In China meanwhile, infection rates started to stabilise through late February, with the number of cases rising from 75,000 on 20 February to a little over 80,000 as of 25 March. By this point however the pandemic had become truly global, with over 460,000 infections detected across 150 countries. European countries have been far more heavily-affected on a per-capita basis, with infection rates many multiples higher than in Asian countries, as the outbreak accelerated through late March and into April. As of 14 April, there were 1.9 million confirmed cases, with 118,966 deaths.

**FIGURE 2 – INFECTION RATES ACROSS GLOBAL REGIONS**



**1.3 CURTAILING THE SPREAD TAKES A HEAVY TOLL IN CHINA**

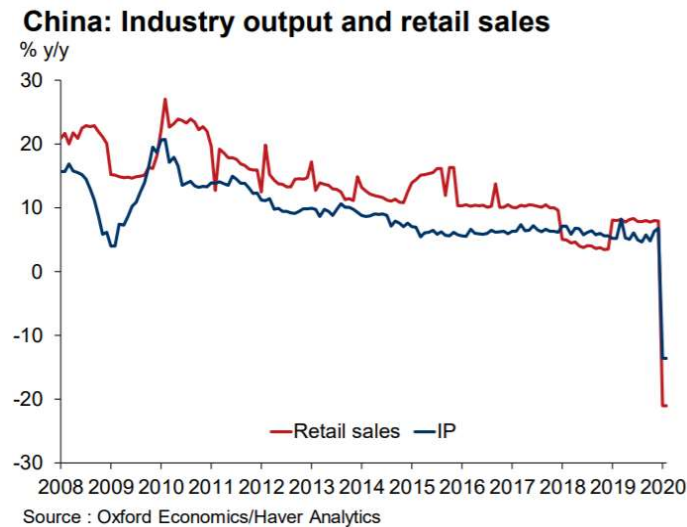
In response to the outbreak, governments across the world have undertaken a range of measures to contain the spread, including increased public health advice and monitoring, restrictions to inbound and outbound travel, and outright lockdown of affected areas.

In China, the government announced a lockdown of several key cities in Hubei province on 23 January, eventually extended to other cities across the country, culminating in Beijing and Shanghai on 10 February. Even following signs that China had made progress with containing the outbreak, local governments continued to err on the side of caution, prioritizing containment of the epidemic over economic growth. This is despite daily new cases of COVID-19 falling to single-digit or even zero in individual provinces. In his COVID-19 media briefing on 11 March, the Director-General of the WHO underlined the “heavy toll” these necessary measures weighed on China’s economy and society – monthly indicators of activity in key sectors such as industry and retailing down by 15-20% or more (Figure 3).

**ff** Lockdown measures in China gave an early insight into the cost of COVID-19 for domestic economic activity, with the WHO recognizing the “heavy toll” paid by Chinese society.

**”**

**FIGURE 3 – IMPACT OF RESTRICTIONS ON CHINA’S ECONOMY**



Nevertheless, even as the lockdown is starting to lift in Wuhan, a broad range of measures remain in place to prevent a second wave. Strict monitoring of residents, screening and testing, and a QR code “passporting” system all remain in place as of mid-April. Moreover, new cases which are being detected are being extensively disseminated and analysed on social media. This makes it quite unlikely, in our view, that significant numbers of people have COVID19 and are moving about undetected.

There has been some recovery in economic activity through March and into early April, with in the region of 80% of employees affected by the shutdown returning to work. But at the end of March the economy was clearly still operating well below normal levels, and our estimate is for an 8.5% fall in GDP in 2020Q1 versus the same quarter last year. Looking into the second quarter and beyond we do expect the start of a more vigorous recovery, but consumer spending in particular will be impacted for many months to come. Our forecast is for China’s GDP to contract by 0.2% this year – unprecedentedly weak in China by the standards of recent decades, but in fact a relatively positive outcome compared to the forecast for many other countries in 2020.

#### 1.4 LOCKDOWNS SPREAD ACROSS ASIA AND THE WORLD

As the outbreak became a truly global pandemic, measures to restrict movement became more commonplace through February and March. Restrictions to international travel were implemented rapidly by a range of governments throughout Asia. By contrast, total national lockdowns have become commonplace across Europe and parts of the US, where infection rates are soaring well beyond those seen in Asia. Across the world, the prevailing sense is one of uncertainty, about: what restrictions might yet be imposed, what impact they will have on curtailing the virus, and when they might be lifted.



**TABLE 1 - MEASURES IMPOSED IN APAC REGION**

	APAC lockdowns due to coronavirus				Internal lockdown	
	Essential services only	Type of lockdown		Entrance restrictions for visitors	National	Regional
		Partial internal lockdown	Minor restrictions			
Japan			X			
Australia		X		X		
S Korea			X	X		
Hong Kong				X		
Singapore	X	X		X	X	
Taiwan			X	X		
China		X				X
India	X	X		X		X
Indonesia			X	X		
Malaysia		X	X		X	
Philippines	X	X		X		X
Thailand	X			X		

## 2. FROM LOCALIZED OUTBREAK TO GLOBAL RECESSION

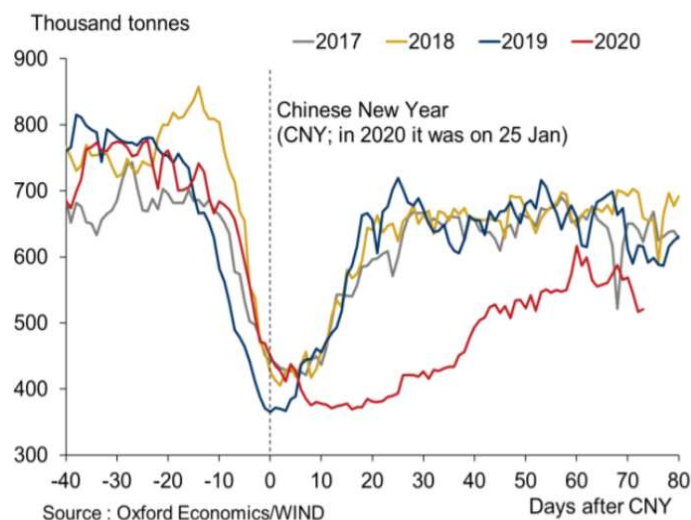
Economic impacts from the COVID-19 outbreak have evolved and changed as the extent and severity, as well as government responses to it, have evolved. In this section we will look at three main groups of impacts.

First, we'll examine the direct shock to activity in China, followed by the supply chain and tourism impacts felt most immediately as China took measures to control the outbreak. We will then examine the impacts on domestic demand felt by economies undergoing lockdown, as the virus became prevalent in more countries. Finally, with the pandemic becoming truly global, and more widespread restrictions to international and domestic movement pushing the world economy towards crisis, we will examine the potential impact on growth around APAC from the slide into world recession.

### 2.1 INITIAL IMPACTS – CHINA'S EXTENDED SHUTDOWN

The first economic impacts from the outbreak of COVID-19 were felt most immediately in the Hubei province, the first part of China where personal movement was restricted. However, given the breadth of cross-China supply chains, the impact of factory shutdowns in Hubei was soon felt across China's industrial sector. Overall Chinese goods exports (in US\$ terms) fell more than 17% in January-February 2020 combined versus a year earlier. Key metrics such as the output of Chinese power stations demonstrate the scale of lost output, with energy usage down around a third versus normal levels at the end of February.

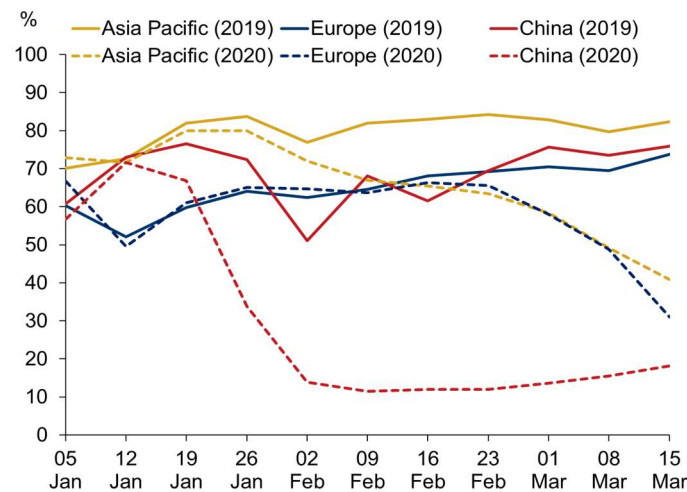
**FIGURE 4 – COAL CONSUMPTION AT 6 CHINESE POWER PRODUCERS**



## 2.2 IMPACTS FELT IN ASIA – TOURISM AND SUPPLY CHAIN

Restrictions on movement by Chinese citizens (imposed by both the Chinese government and others), dealt a major blow to tourism destinations across Asia. The number of outbound trips made by Chinese citizens has grown from 10m in 2000 to almost 150m in 2018, and Chinese travellers now make up 20% or more of total inbound visitors in eight Asian economies. The impact of travel restrictions was felt immediately, with total inbound visitors to Thailand down 42% on-year-ago in February. Hotel occupancy rates give a clear indication of the impact on the sector across Asia through February and into March, with occupancy down to just 40% or less.

**FIGURE 5 – HOTEL OCCUPANCY RATES BY WORLD REGION**



Source : Oxford Economics/STR

Additionally, the outage to Chinese production rippled across Asian supply chains. Official data on value-added in industry is only available with a lag across much of Asia, but countries relying upon China to supply a high proportion of their manufacturing inputs (Figure 6) saw a corresponding slump in the value of their own goods exports. In Vietnam, where goods exports had previously been rising at double-digit rates, part in thanks to trade diversion (due to higher US tariffs on direct Chinese exports), export growth slowed to just 2% on-year-ago in January-February 2020. In Thailand, industrial production was down close to 4% over the same period. Taiwan has seen trade data hold up reasonably well through the first few months of the year given greater reliance on the US and Europe as destination markets. But there are clear signs of major slowdown to come, with export orders falling in March as lockdown measures started to take hold, and the likelihood of much worse to come as the full impact of lockdown in Taiwan's key markets are felt.

Even for those economies not reliant on supply-chain imports from China, the interruption to Chinese industrial output posed a challenge to business continuity. China's emerging role as a key supplier of capital goods and machinery means it now supplies a third or more of all capital goods imports into several major advanced and emerging economies.



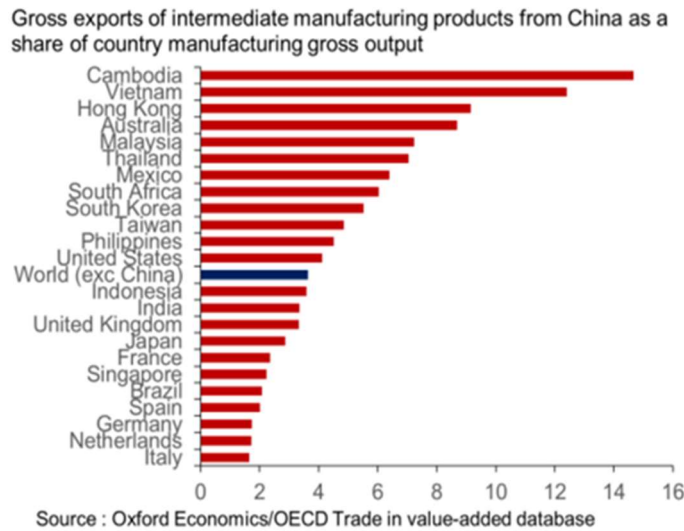
China's importance as a tourism market for several Asian economies meant the impact from the outbreak was felt immediately across Asia.



Cross-Asia supply chains were another key channel for COVID-19 economic impact through the first quarter of 2020, with economies across ASEAN feeling the impact of factory shutdowns in China.



**FIGURE 6 – SUPPLY CHAIN RELIANCE ON CHINA**



### 2.3 APAC LOCKDOWN

These shocks were a meaningful enough blow to the economic outlook at the Asian and global level. Oxford Economics' forecast for global GDP growth in 2020 was revised from 2.5% in our December 2019 forecast to 2.3% in our February 2020 forecast, with the Asia-Pacific region being revised from 4.3% to 3.8% over the same period.

But the evolution of the pandemic from an Asian outbreak to a truly global phenomenon has elevated these impacts on to another level. One key metric showing the potential loss of production capacity around the world is the number of children affected by school closures (as parents would be required to stay home to care for children rather than go out to work). This metric rose from just shy of 400 million in the first week of March to over 1.2 billion during the week of 16-22 March. In Asia, the number of students out of class nearly-doubled over the same period, rising from 300m to 575m, with economies accounting for 37% of APAC GDP under lockdown as of 10 April.

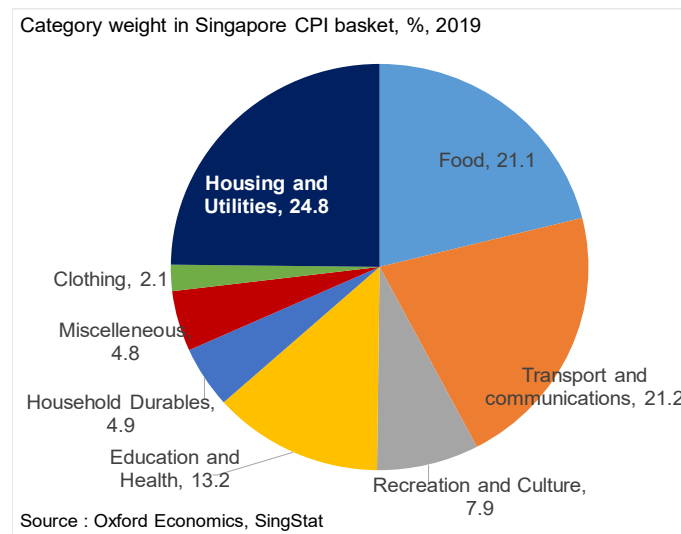
However, the loss of production capacity is perhaps less relevant now that outright curbs to movement are in force in around 100 economies around the world. What is more important from an economic perspective is the loss of spending activity, as households are simply prevented from going about their normal daily business. The scale of this impact is difficult to anticipate, but since consumer spending typically accounts for 50% or more of total economic activity in most major economies, it will be very significant.



Measures implemented through March and April mean around 37% of Asia Pacific GDP is currently under some form of lockdown.



**FIGURE 7 – COMPOSITION OF SINGAPORE’S CONSUMER BASKET**



Some sectors of consumer spending have clearly collapsed – global restaurant bookings made through the OpenTable app were down 90% on year ago as of mid-March. In Japan, passenger volumes on high-speed trains were down more than 50% in 2020Q1 versus a year earlier. But other parts of the consumer basket will be more resilient. Figure 7 shows the composition of Singapore’s consumer basket, and although a large portion of spending is clearly going to have been massively impacted by the recent lockdown measures (e.g. culture and recreation, transport, and clothing – all sectors reliant on consumers leaving home), other sectors such as food, household services and housing, will all be more resilient.

As such the blow from lockdown measures to consumer spending depends on the duration of restrictions, and the proportion of spending postponed or not spent during this period. For example, in an economy where lockdown was imposed for 6 weeks, and 50% of spending was not possible, the loss to consumer spending in that quarter would be 9%. For an economy where consumer spending accounted for 50% of total output, the GDP loss in that quarter would be 4.5%. This is on a par with the shrinkage of the world economy during the depth of the Global Financial Crisis.

The crisis has also had powerful impacts on economies across Asia-Pacific through the volatility and spike in risk aversion seen in global financial markets through the first quarter of the year. Equity markets lost a third of their value or more from their pre-COVID-19 peaks, as capital flowed out of not only directly-impacted economies, but also emerging markets more generally, with investors preferring so-called “safe-haven” assets. This has particularly impacted economies in emerging Asian, with spikes in government borrowing costs, increasing the cost of servicing public debt, and sharp currency depreciations.

## 2.4 PANDEMIC PUSHES WORLD INTO RECESSION

These impacts are serious enough on the level of an individual economy. We estimate for example that China’s economy will have contracted 8.5% on-year-ago during 2020Q1. In Hong Kong (also one of the first-affected by COVID) the economy is estimated to have contracted 10% on year ago in 2020 Q1. For



Lockdown measures mean a large portion of normal economic activity, including significant segments of consumer spending, cannot continue, driving steep falls in economic output.



economies where the spread of the outbreak (and corresponding lockdown measures) came later the impacts are being felt more severely in 2020 Q2 – e.g. in Thailand, where we forecast GDP to fall 10%, with the impacts of plummeting tourist arrivals compounded by the lockdown measures taken in March.

However, when such restrictions are being imposed across economies there is clearly a much more systemic impact at the global level, with both domestic and external demand both contracting sharply. We expect the world economy to have contracted 2.7% quarter-on-quarter in 2020Q1, and a further 3.6% contraction in 2020Q2. In turn, this weaker global outlook then compounds the impact to Asian economies through weaker trade flows, and demand for both goods produced in Asian factories, and tourism demand even after lockdown measures have eased.

## 3. A STRONG REBOUND IN 2021?

Based on our latest analysis of the impact of measures to contain the outbreak, Oxford Economics expects the world economy to contract by 5.2% on-year-ago in 2020Q2, the fastest quarterly pace of contraction on record. But we think that there is the scope for a rapid recovery late in 2020, and into 2021. In this section, we set out the conditions for such a recovery to take place, and its impact across the Asia-Pacific region.

### Key assumptions for our baseline economic forecast

Economic forecasting is subject to several sources of uncertainty at any time, but especially so when the factors buffeting households and businesses are not being driven by financial or economic factors. This is clearly such a time. Our forecasts therefore require us to make judgements on what a plausible path for the resolution of COVID-19 might be, and from that point map out the transmission from health and social measures to economic and business activity.

Our key baseline assumption is that lockdowns continue for 6-12 weeks, varying between countries, and that they affect most of the population in affected countries. Governments then start to relax these measures gradually through 2020H2, enabling households and businesses to start to return to normal.

### 3.1 HOW SHOULD ECONOMIC POLICY RESPOND TO COVID-19?

The immediate policy response to collapsing financial markets through 2020 Q1 was a major easing in monetary policy across most key economies. The Federal Reserve cut interest rates by a cumulative 150bp from February to March. In turn, this has given central banks across emerging markets, including in Asia, space to cut rates themselves.

But while lower interest rates will provide some respite to firms and households with floating rate debt, it will clearly do little to cushion the blow of precipitous falls in income (revenues for business, or employment income for workers) that arise from lockdown. If the temporary shock to economic activity is not to become a more destructive series of business failures and personal bankruptcies, with spill over impacts to the banking sector and government finances (triggering austerity measures that deepen the downturn), households and businesses need temporary - but urgent - financial support.

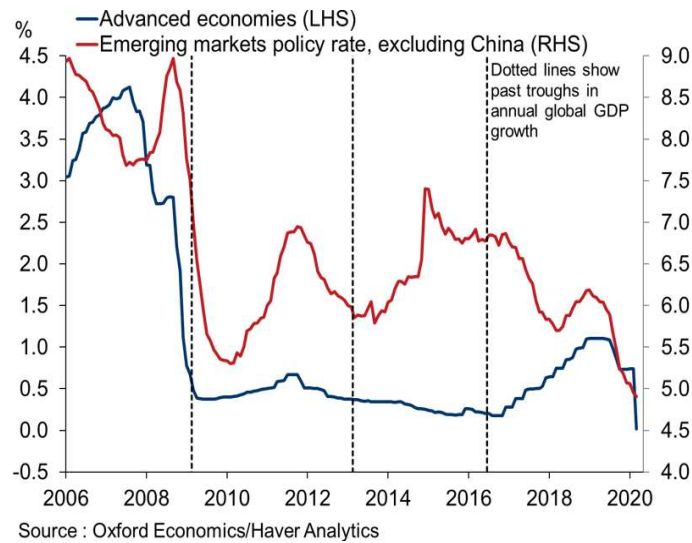
This could be delivered either through offering firms and households alternative sources of income, or ways to drastically reduce their outgoings. Targeted measures such loan guarantees to firms, as well as deferment or cutting of tax liabilities, can help firms ride out a temporary period of much lower cashflow, while wage subsidies can help them retain workers, protecting households. If firms are unable to keep workers on, again, targeted measures to support household income can help prevent households entering a damaging spiral of debt.



Immediate monetary policy response to COVID-19 is useful and important, but in itself would do little to protect households and firms from lasting economic damage.



**FIGURE 8 – GLOBAL MONETARY POLICY REACTIONS TO COVID**



**TABLE 2 – TARGETED MEASURES TAKEN ACROSS ASIAN ECONOMIES**

APAC Government Support Packages					
	Loans or loan guarantees	Tax/subsidies breaks for firms	Support for workers (particularly those on short hours)	More support for those that lose their job	Support vulnerable groups (e.g. self employed)
China	✓	✓			
Japan	✓	✓			✓
South Korea	✓				✓
Indonesia	✓	✓		✓	✓
Taiwan	✓	✓	✓	✓	✓
Singapore	✓		✓	✓	✓
Malaysia	✓	✓	✓		✓
Hong Kong	✓	✓			✓

Source: Oxford Economics

Such measures are being adopted around the world, and Asian economies are amongst the most ambitious in this respect. Singapore’s government has set out two separate stimulus packages, totalling around 12% of GDP and included wage subsidies, direct support to households, and aid for the food, aviation and tourism sectors. Hong Kong’s recent budget announced cash handouts of HK\$10,000 (US\$1,283) for each permanent resident adult, and a 100% write down of salary taxes for companies. A range of additional measures to lower the cost of living and the cost of business take the total stimulus to around 10% of GDP. Taiwan’s government announced measures to support the retention of around 2m vulnerable jobs, particularly in the manufacturing and tourism and transport sector, as well as protecting the income of quarantined workers, and extra support for the elderly. In total, Taiwan’s measures are estimated at 1.9% of GDP.

With some evidence the outbreak is stabilising in China (certainly compared to Europe and the Americas), the government’s focus has shifted towards supporting the rebound. This means enabling China to resume its key role in global supply chains as quickly as possible. Key measures in this respect include

**“** Governments across Asia are responding to the outbreak and lockdown with a range of targeted measures to support cashflow for firms, and income for households. **”**



lowering the cost of temporary exemption of port fees, and lower utility costs, to cut the cost of doing business and ensure production can be “caught up” where possible. The government has also set out a range of tax relief measures for affected firms, as well as interest rate cuts and loan extensions. Meanwhile the central government has further increased local government bond issuance quotas, in order to support local infrastructure spending.

**TABLE 3 – TOTAL SUPPORT MEASURES ACROSS ASIAN ECONOMIES**

	Fiscal package as % of GDP
China	1.3
Hong Kong	10
South Korea	7.4
Taiwan	1.9
Singapore	12
Malaysia	17.2
Indonesia	2.6
Thailand	11.4
Philippines	1.3

These measures clearly have a substantial fiscal cost – ranging from 1.3% of GDP to as much as 17%. But public debt levels across emerging Asia are substantially lower than in other emerging economies, giving governments ample space to provide support, and potentially increase spending further if need be. But it will be important for governments to quickly channel support to the households and firms that need it, in order to ensure temporary losses of income do not trigger more permanent damage to the economy through personal bankruptcies and business failure. Our baseline economic forecast is predicated on the judgement that governments in the region do this effectively – although in section 4 we examine an alternative scenario in which governments are unable to prevent the pandemic having more lasting economic damage.

### 3.2 WHAT WILL THE RECOVERY LOOK LIKE?

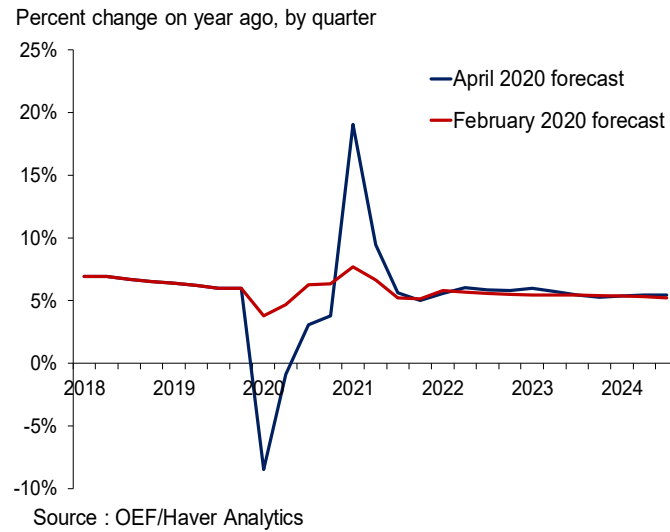
Based on these key assumptions over the containment of COVID-19, subsequent easing of measures implemented to contain its spread, and effective shielding of businesses and households from the most severe impacts of lose income, our baseline forecast is for a sharp recovery in the global economy through the second half of 2020. In China there is evidence that the recovery has already begun. We expect GDP growth to average 8% or so in the four quarters to mid-2021, and for GDP growth to accelerate from -0.2% in 2020 to 9% in 2021.



The measures being taken by governments across the region are in some cases on an unprecedented scale, but low public debt burdens provide scope to provide support.

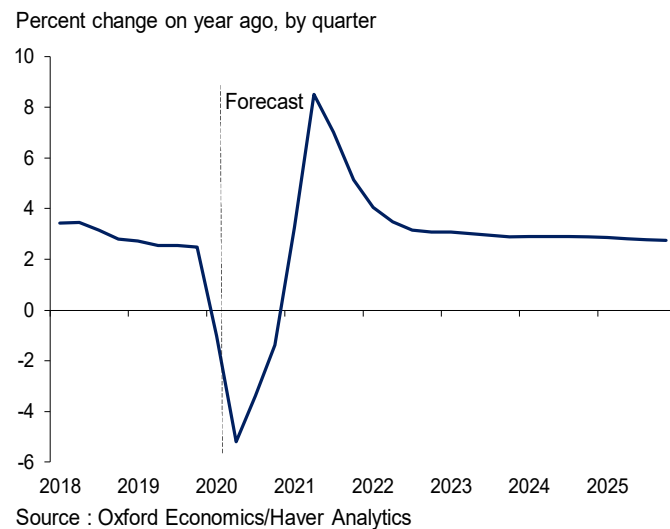


**FIGURE 9 – CHINA GDP GROWTH FORECAST COMPARISON**



The global recovery will lag a little, given the delay in experiencing and controlling the pandemic. After “bottoming out” in 2020Q2, we expect the global economy to rebound sharply from 2020Q3 onwards, as households and businesses are freed from constraints to normal activity and release “pent up” demand. Our latest forecast is for the world economy to contract 2.8% in 2020 (with very much a year of contrasting halves), followed by growth of 6% in 2021.

**FIGURE 10 – WORLD GDP GROWTH SET FOR SHARP RECOVERY**



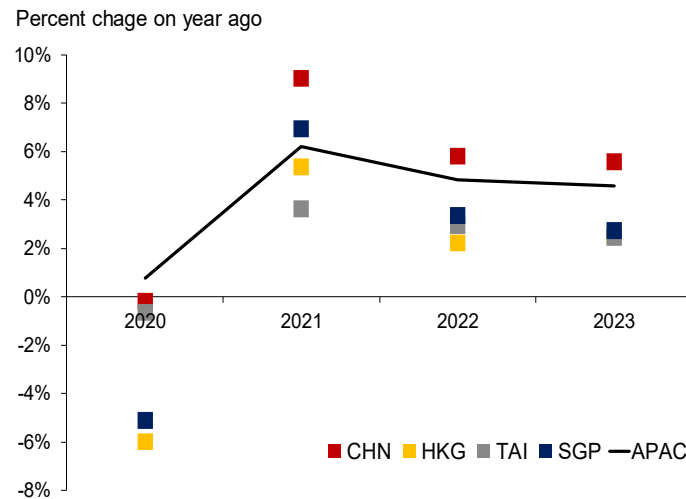
Around Asia Pacific the outlook, is also for a year of very weak growth overall in 2020. The impact of lockdown measures on domestic demand is being compounded by a corresponding collapse in world trade, as consumers in other economies are also locked down, and as businesses shelve investment plans due to the uncertainty over when the recovery might begin. Our forecast is for world trade to contract 15% in 2020, 5 percentage points more than in the Great Financial Crisis of 2009. This will impact key open trading economies such as Hong Kong, Singapore and Taiwan (not yet subject to lockdown measures), with GDP contractions of 6%, 5% and 0.6% forecast for 2020 respectively. The outlook in Taiwan is further clouded by the need to renew the Cross-Strait

Assuming governments can effectively shield households and businesses from the impact of lockdown, a sharp recovery can begin in the second half of 2020.

Economic Cooperation Framework Agreement (ECFA) with China by September – failure to ratify a renewal would deal a further blow to growth later this year.

Should the assumptions embedded in our baseline forecast (including the renewal of ECFA) prove correct though, we think sharp GDP contractions in 2020 can be followed by a sharp rebound in 2021. GDP growth of 5.4% in Hong Kong would be the fastest rate since 2010, while Singapore could accelerate to 7%, the fastest since 2010, and Taiwan reaches a six-year high at 3.6%. The global and domestic rebound would push growth in Indonesia, Vietnam and Philippines to 8% or above. Over the longer-term though, we would obviously expect growth to ease back towards more sustainable rates – around 5.5% or so in China, and 2-3% in key trading hubs such as Hong Kong, Singapore and Taiwan.

**FIGURE 11 – GDP GROWTH IN SELECTED APAC ECONOMIES**



But this forecast hinges on the key assumption governments can ease restrictions through the second half of the year, and in the meantime have effectively shielded them from the worst financial impacts of the severe slowdown. In our final section we explore an alternative scenario where we flex both these assumptions, with much longer-lasting and more damaging impacts for the global and Asian economies.

## 4. OR DEEPER DOWNTURN AND DELAYED RECOVERY?

### Key assumptions for deeper downturn and delayed recovery

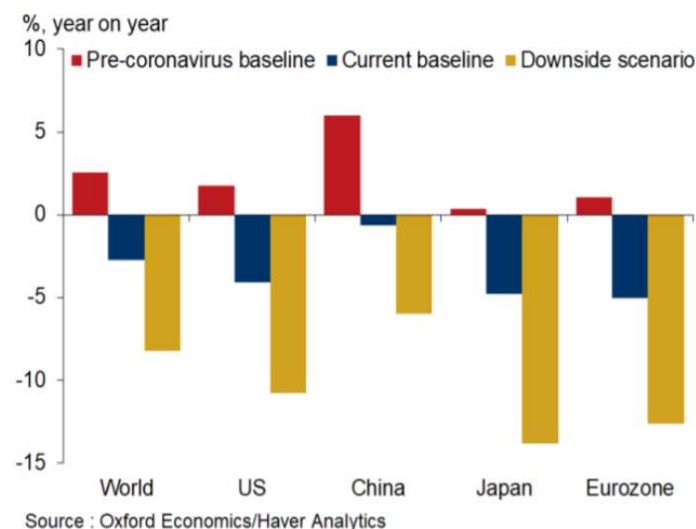
Our downside scenario, simulated using our Global Economic Model, explores an alternative set of assumptions. These include; a longer-than-expected outbreak of the current pandemic, meaning all countries impose severe lockdowns extending into 2020 Q3. The “slower-for-longer” rate of economic activity further undermines financial markets, causing spikes in borrowing costs for risky borrowers, and deeper financial distress.

In this scenario we still assume Governments can insulate households and firms from the worst impacts of the crisis. So once lockdown measures start to ease there is a recovery from 2021 onwards. But the scarring effects on households and firms are nevertheless greater than in our baseline scenario, meaning the recovery will be much less vigorous than in our baseline.

### 4.1 WORLD ECONOMY FACES BIGGEST CONTRACTION ON RECORD

The rate of collapse in economic activity and the depth of the eventual bottoming-out in our downside scenario are beyond any previous economic downturn measurable with comparable data. Our Global Economic Model finds that in this scenario, world economic output falls more than 15% year-on-year in 2020 Q4.

FIGURE 12 – WORLD GDP GROWTH IN 2020 IN DOWNSIDE SCENARIO



The downturn has massive impacts across the world, with the US economy contracting more than 10% in 2020, and China’s by close to 6%. Key economies for global manufacturing supply chains such as Taiwan and South Korea would contract by 8-10% in this scenario. Emerging Asian economies suffer both from

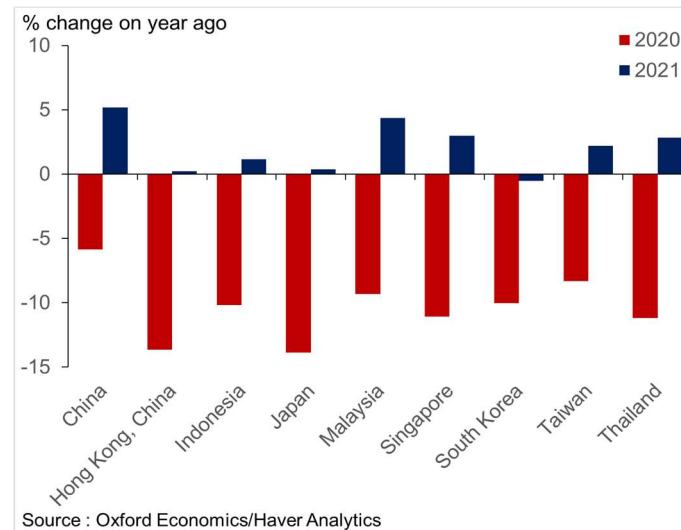
the direct impact of lockdown measures, but also the accelerating risk aversion in financial markets, as investors shift ever more of their portfolios into “safe” assets. GDP contractions of 8-15% would be felt in this scenario in Thailand, Indonesia, Malaysia and the Philippines. Asian trade hub economies such as Singapore and Hong Kong suffer less from risk aversion, but the collapse in world trade has a disproportionate effect on their economies, driving GDP contractions of 11% and 14% respectively.

#### 4.2 GREATER ECONOMIC SCARRING MEANS A SLOWER RECOVERY

The impacts of our downside scenario on economies across the Asia-Pacific region are without precedent in recent history. But our downside scenario does not assume a particularly rapid recovery, as we anticipate in the baseline forecast. The downside still assumes households and businesses are shielded from the worst financial impacts of the prolonged lockdown, but nevertheless there are important scarring effects.

Unemployment rates across the world remain substantially higher well into 2021 than in the baseline, meaning households remain much poorer, and less able to spend. Business investment rebounds only sluggishly, as firms struggle to deal with the cost to their balance sheets of additional debt taken on to remain afloat during the crisis. Meanwhile the prolonged shutdown means government debt burdens rise massively, meaning a slower pace of government spending growth going forward. At the global level GDP growth rebounds to just 2% in 2021.

**FIGURE 13 – GDP GROWTH IN DEEPER DOWNTURN AND DELAYED RECOVERY**



A scenario where lockdowns are extended globally and into 2020Q3 results in a global recession without precedent, and only a very tepid recovery in 2021.



## 5. CONCLUSIONS

The outbreak of COVID-19 is of course primarily a health and humanitarian emergency but understanding the potential economic implications of the pandemic is also crucial, for households, business and government. At the time of writing, the prevailing sense is one of uncertainty though, and so thinking about the economic outlook in terms of a range of possible assumptions or scenarios is even more important than ever.

That said, our latest assessment is that the impact of COVID-19 is primarily a short-term one. Measures taken to contain the outbreak look to have stabilised its spread in China, and the challenge is to replicate that achievement in other economies. At the same time, supporting households and businesses in a period of much lower income should position economies to rebound once the immediate threat to public health has passed. Based on these key assumptions, we expect a short, sharp recession, followed by a rebound through late 2020 and into 2021.

But the prevailing feeling is one of uncertainty. Over the months ahead, we will continue to monitor several key issues in order to better understand the potential short and longer-term implications of the outbreak. The rate of infection, and measures to contain the spread are key to understanding the short-term hit to business. The effectiveness of monetary and fiscal policy in supporting firms and households who face shortfalls in their income will tell us the extent to which a short-term recession will have longer-term financial costs. And once the pandemic is contained and normality returns, we may observe a range of changes to consumer and business behaviour with important economic impacts.



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