

lakyara vol.331

The economy's path to a post-pandemic future

Masaya Sasaki

10.November.2020

Executive Summary



Masaya Sasaki

Senior Economist
Strategy Planning Department

The economy is in a gradual recovery trend for now, bolstered by adaptive behavioral change and a growing cache of knowledge about COVID-19. Going forward, however, its trajectory could take the form of a series of wavelets that mirror the pandemic's waves.

Pandemic has impacted both demand and supply

Nearly a year has passed since the world first heard of the novel coronavirus subsequently named SARS-CoV-2. The pandemic that ensued has wrought widespread, severe economic damage globally.

Much of the damage is due to billions of people staying home more than usual, either voluntarily or compulsorily, to reduce infection risk. Such home confinement has weighed heavily on consumer spending. Although the initial sense of crisis has dissipated since peaking in late spring, consumption of nonessential goods and services remains below pre-pandemic levels to varying degrees across most countries. Spending on long-distance travel, tourism and entertainment has been especially hard-hit.

On the supply side as well, companies are beset by numerous challenges posed by pandemic containment measures. In service industries such as entertainment and food services in particular, businesses have been operating at drastically reduced capacity at the behest of the government or to accommodate social distancing. In the US, the country with the most COVID-19 cases, indoor service at restaurants and bars in New York City was banned until September 29¹⁾ and Disney announced it would have to lay off some 28,000 US theme park employees in response to deterioration in its earnings. Even businesses that are operating normally are burdened by the need to keep their premises thoroughly disinfected.

Faced with such pressures from both the supply and demand sides, many companies find themselves in a cash flow squeeze, unable to operate profitably. If this situation persists much longer, companies are likely to increasingly take on more debt, cut capex more deeply and/or start to shed workers to ensure their survival.

NOTE

1) On October 4, NYC Mayor Bill de Blasio announced that schools in nine Zip Codes in Brooklyn and Queens would close down again, largely in response to the test positivity rate's seven-day average exceeding the 3% threshold that triggers restrictions on economic activity. The school closures can be considered an example of a wave engendered by a flare-up in the pandemic as discussed below.

Adaptive behavioral change underpins economic recovery but...

Zooming out to a longer-term perspective, one could argue that because the pandemic is a transient (albeit lengthy) event that will end once a vaccine becomes available, it will ultimately be looked back upon as a fairly minor blip if we can somehow endure until a vaccine is ready.

Vaccine development, however, has become politicized despite being one of the most valuable international public goods at the moment. Not only was a COVID-19 vaccine a point of contention in the first US presidential debate, it is seen as a critically important geopolitical asset by a number of major nations.

Perhaps that is why US President Trump claimed at the September 29 debate that a vaccine would be available within weeks. Earlier in September, however, the CEO of the Serum Institute of India, the world's largest vaccine manufacturer, warned that vaccinating the global population against COVID-19 would take at least 4-5 years given the current dearth of vaccine production capacity globally²⁾. Additionally, many scientists have expressed caution about the prospects of rapidly developing an effective vaccine. If they are right, vaccination may not be a silver bullet.

On the bright side, the medical community is fast gaining expertise in treating COVID-19. The public also is adapting to the current adverse situation. For example, people's attitude toward prophylactic use of masks is now changing dramatically even in Western countries where mask-wearing was previously uncommon. With new habits such as mask-wearing helping to bring the pandemic under control, the real economy could gradually recover without suffering another major setback like this spring's downturn³⁾.

Economic recovery may unfold in series of wavelets mirroring pandemic's waves

However, even if the real economy does gradually recover, its recovery may not necessarily be linear.

New Zealand, widely regarded as one of the world's biggest COVID-19 success stories, temporarily eradicated community-acquired COVID-19 cases within its borders through a stringent nationwide lockdown from March to May. After 102

2) Findlay, Stephanie and Anna Gross, "Not enough Covid vaccine for all until 2024, says biggest producer," The Financial Times, Sep. 14, 2020. <https://www.ft.com/content/a832d5d7-4a7f-42cc-850d-8757f19c3b6b>

3) One potential impediment to this gradual recovery scenario is financial system jitters or a failed policy response thereto. As long as the pandemic persists, companies' financial strength will steadily erode. Capital markets and financial institutions are consequently likely to remain susceptible to stress for the time being. At the same time, continuation of accommodative/expansionary macroeconomic policies will be a key driver of recovery.

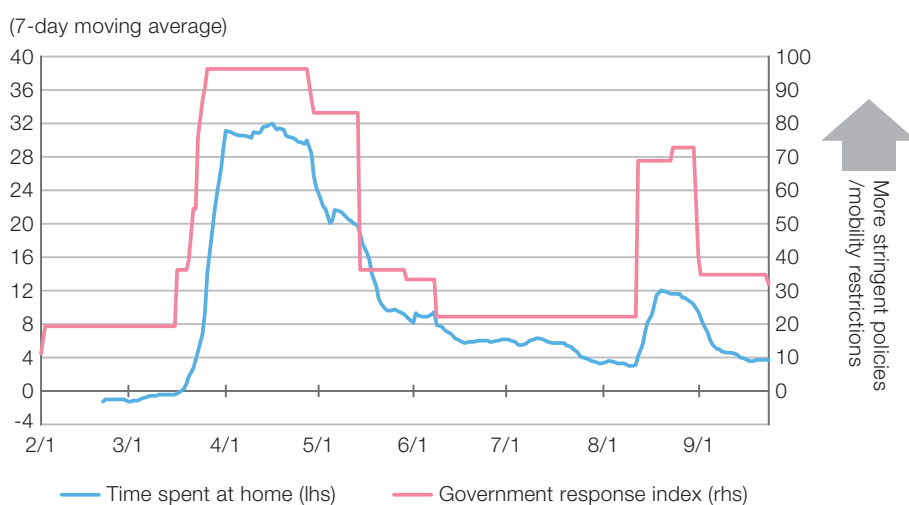
4) The second lockdown in Auckland was initially scheduled to last three days but it was extended in response to more new COVID-19 cases. On October 7, the New Zealand government lifted the Auckland lockdown after confirming that Auckland had no new cases for 10 consecutive days through October 5.

days with no reported cases, however, four cases of community transmission were reported on August 11 in Auckland, New Zealand's largest city. In response, lockdown restrictions were re-imposed in Auckland from noon on the 12th and the alert level was raised throughout the rest of the country⁴⁾.

The accompanying graph plots Oxford University's COVID-19 government response index for New Zealand against the average time spent at home by New Zealanders from February through September relative to a pre-pandemic baseline, per Google mobility data. The government response index quantifies how policy measures to curb the spread of COVID-19 have varied in stringency over the course of the pandemic. The graph shows that when the New Zealand government tightened mobility restrictions from March and again from August, New Zealanders spent more time than usual at home. However, in contrast to the initial nationwide lockdown, the second lockdown was mandatory only in Auckland and optional elsewhere in light of the location of the renewed outbreak. Consequently, average time spent at home on a nationwide basis did not increase as much during the second lockdown as during the first one.

It is reasonable to expect COVID-19 to continue to spread in waves of varying magnitude as we have already experienced. Meanwhile, the economy is currently

Policy measures to curb COVID-19's spread in New Zealand and New Zealanders' average time spent at home



Note: For Google Mobility Report data (time spent at home), 0 represents the median value on the same day of the week over the period from January 3 through February 6, 2020. The graph plots the seven-day moving average of percentage changes from this baseline.
 Source: NRI, based on Google COVID-19 Community Mobility Report data and Oxford COVID-19 Government Response Tracker data (both downloaded on October 5)

prone to both supply and demand fluctuations stemming from changes in the infection rate as mentioned earlier.

When the pandemic shows signs of flaring up or actually does flare up, economic recovery will tend to stall (or regress) in response to changes in people's behavior, like in New Zealand. Once the flare-up subsides, economic recovery should resume as mobility restrictions are eased. Until the pandemic is vanquished by a vaccine or cure, the economy's path forward is likely to basically be a slightly upwardly sloping series of wavelets arising from such fluctuations in the infection rate.

about NRI

Founded in 1965, Nomura Research Institute (NRI) is a leading global provider of system solutions and consulting services with annual sales above \$4.8 billion. NRI offers clients holistic support of all aspects of operations from back- to front-office, with NRI's research expertise and innovative solutions as well as understanding of operational challenges faced by financial services firms. The clients include broker-dealers, asset managers, banks and insurance providers. NRI has its offices globally including New York, London, Tokyo, Hong Kong and Singapore, and over 13,000 employees.

For more information, visit <https://www.nri.com/en>

.....

The entire content of this report is subject to copyright with all rights reserved.
The report is provided solely for informational purposes for our UK and USA readers and is not to be construed as providing advice, recommendations, endorsements, representations or warranties of any kind whatsoever.
Whilst every effort has been taken to ensure the accuracy of the information, NRI shall have no liability for any loss or damage arising directly or indirectly from the use of the information contained in this report.
Reproduction in whole or in part use for any public purpose is permitted only with the prior written approval of Nomura Research Institute, Ltd.

Inquiries to : Financial Market & Innovation Research Department
Nomura Research Institute, Ltd.
Otemachi Financial City Grand Cube,
1-9-2 Otemachi, Chiyoda-ku, Tokyo 100-0004, Japan
E-mail : kyara@nri.co.jp

<https://www.nri.com/en/knowledge/publication/fis/lakyara/>

.....