World economy to take biggest hit since Great Depression

By Nick Beams
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The International Monetary Fund has forecast that the world economy is entering its worst slump since the Great Depression of the 1930s and the loss of output will "dwarf" that suffered in the global financial crisis 12 years ago.

Even on the assumption that the second quarter records the sharpest downturn, followed by a recovery and then a rebound next year, the IMF said the world economy will lose $9 trillion in output over 2020 and 2021. This is an amount equivalent to the combined economies of Japan and Germany, the world's third and fourth largest respectively.

It said under the assumption that the pandemic and the required containment measures peak in the second quarter for most countries, global growth would fall to minus 3 percent this year, a 6.3 percentage fall from the forecast issued in January.

This "major revision over a very short period" made what the IMF has called the Great Lockdown the "worst recession since the Great Depression, and far worse that the global financial crisis," IMF chief economist Gita Gopinath wrote in a comment on its *World Economic Outlook* report issued yesterday.

Gopinath said the IMF forecasts were grounded in its "baseline scenario" in which it anticipated global growth would rebound to 5.8 percent next year. But even if that did take place, the recovery would only be "partial," with the level of economic activity below that projected for 2021, before the virus hit.

However, given the uncertainty surrounding the pandemic, the IMF has projected more adverse scenarios. The outbreak may not recede in the second half of the year, leading to longer periods of containment that would worsen financial conditions and a further breakdown of global supply chains.

Under these conditions, Gopinath wrote, "global GDP would fall even further: an additional 3 percent in 2020 if the pandemic is more protracted this year, while, if the pandemic continues into 2021, it may fall next year by an additional 8 percent compared to our baseline scenario."

The IMF has predicted a contraction of growth in the advanced economies of 6.1 percent with emerging and developing economies, excluding China, expected to experience negative growth rates of between 1 percent and 2 percent in 2020. Income per capita will fall in over 170 countries.

The actual falls could be steeper than estimated by the IMF at this point, with the forecasts of private sector organisations pointing to an even larger contraction. In recent years the IMF has had to revise down its forecasts amid the marked slowdown in the world economy that had developed well before the coronavirus shock.

An example of the possible depth of the collapse was highlighted in a report by the UK Office for Budget Responsibility, also issued yesterday. It said if the lockdown of the British economy proceeded for three months then it faced a 35 percent plunge in the second quarter.

It said this was not a forecast but should be taken as a "reference scenario" because it could not predict how long the restrictions on economic activity would need to be maintained.

However, if they stayed in place, education, accommodation and food services would be the hardest hit, with contractions of 90 percent and 85 percent respectively. Similar estimates have been made by government statisticians in France.

The IMF said multilateral cooperation was "vital" for the health of global recovery. But precisely the opposite is taking place.

In a comment on the IMF report, *Financial Times* economic columnist Martin Wolf wrote that the world was confronting the "biggest economic disaster since the Depression of the 1930s.

"The world has come into this moment with divisions among its great powers and incompetence as the highest levels of government of terrifying proportions."

He noted that the "negative-sum economic nationalism that has driven Donald Trump throughout his term as US president, and has even emerged within the EU, is a serious danger… If the world economy is broken apart, as happened in response to the Depression, the recovery will be blighted, if not slain."

Wolf cited the conclusion drawn by the Peterson Institute for International Economics in Washington which stated: "Put simply, in the COVID-19 pandemic, lack of international cooperation will mean that more people will die."

But just as the insatiable drive for profit via financialisation has undermined public health systems around the world, so the division of the global economy into rival nation-states and great powers is provoking a struggle of each against all. This is rapidly rendering any international collaboration a dead letter.

The IMF also issued a warning about the state of the global financial system saying it had already felt a "dramatic impact" and "further intensification of the crisis would affect global financial stability."

The massive injection of money by the world's central banks, amounting to at least $6 trillion, along with their indications of a readiness to do still more, has stabilised markets in recent weeks.

But signs of stress have emerged in major short-term funding markets, including the global market for US dollars. Less developed economies have been hardest hit experiencing an outflow of about $100 billion, the largest on record.

Major markets could also be impacted if the spread of the pandemic required further containment measures exacerbating the COVID-19 shock.

Asset managers facing large outflows could be forced to sell into falling markets, accelerating the decline. Leveraged investors may face further margin calls, aggravating selling pressures.

"As firms become distressed and default rates climb higher, credit markets may come to a sudden stop, especially in risky segments like high yield, leveraged loan and private debt markets. These markets have expanded rapidly since the global financial crisis, reaching $9 trillion globally, while borrowers' credit quality, underwriting standards, and investor protections have weakened," the IMF stated.

In other words, the consequences of the policies of central banks since the global financial crisis are coming home to roost. The continuous supply of ultra-cheap money to enable the continuation of the very same speculation and parasitism that produced the 2008 crash has created the conditions for an even bigger disaster.

The IMF noted that banks have more capital and liquidity than they did 12 years ago but they could be tested in the face of a "sharp slowdown that may turn out to be more severe and lengthy than currently anticipated."

Measures of bank capitalization based on market prices were now worse in many countries than in 2008, giving rise to a concern that "banks and other financial intermediaries may act as an amplifier should the crisis deepen further."