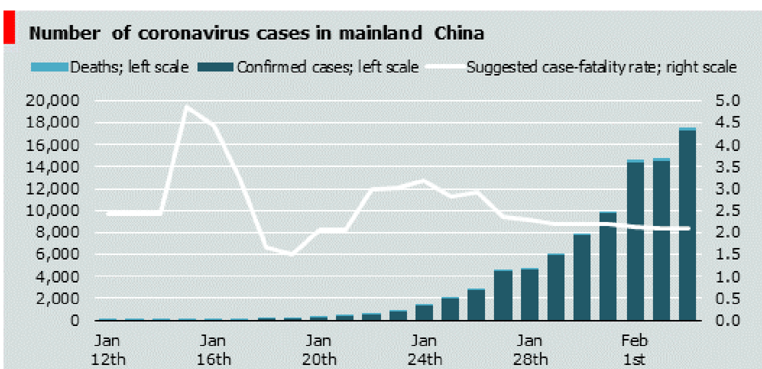
China

February 3rd 2020

Coronavirus: four scenarios for China’s economy

- Data are still insufficient to fully understand the nature of the novel coronavirus, but The Economist Intelligence Unit is planning to revise its economic forecasts on the assumption that the public health emergency within China will come under control by end-March. We assign a 50% probability to this outcome.
- Under this core scenario, we provisionally plan to lower our forecast for China's real GDP growth in 2020 to 5.4%, from 5.9% currently. Stimulus policies will cushion some of the economic disruption caused by the virus outbreak and the second half of the year should see a recovery in activity.
- Companies should prepare contingency plans for a range of scenarios, including the possibility that the virus will take longer to be brought under control or will even prove uncontainable. Such eventualities would have a long-term economic impact.

A novel coronavirus (2019-nCoV) originating from Wuhan, a city of 11.3m people in central Hubei province, has spread to all provinces in mainland China and overseas. The Chinese authorities are taking unprecedented quarantine measures to halt the spread of the pathogen, which appears to be highly contagious.



Note. As of noon China Standard Time on February 3rd.
Source: National Health Commission.

The pathogen does not appear to be as deadly as first assumed, however, with the suggested case-fatality rate stabilising at 2.2% as of February 1st. Nevertheless, the risk of the virus mutating, heightened transmission risks during the post-Chinese New Year travel period, and strains on the Chinese public healthcare system are grounds for concern.

Comparable global health precedents

Pandemic	Year	Virus type	Number of people infected (approximate)	Estimated deaths worldwide	Case-fatality rate

Spanish flu	1918-1919	A/H1N1	500m	50-100m	2-3%
Asian flu	1956-1958	A/H2N2	?	1-4m	n/a
Hong Kong flu	1968-1969	A/H3N2	?	1-4m	n/a
SARS	2002-2003	SARS-CoV	8,098	774	9.6%
Swine flu	2009-2010	Pandemic H1N1/09	10-200m	18,500 (lab-confirmed; WHO) to 203,000 (est. Lancet)	0.03%
MERS	2012 to date	MERS-CoV	1,917 lab-identified in 27 countries (WHO)	677.0	36%
Ebola	2013-16	Ebola haemorrhagic fever	28,616	11,310	39.50%
Seasonal flu	Every year	mainly A/H3N2, A/H1N1, and B	340m-1bn	250,000-500,000 per year	Variable

Sources: WHO; European Centre for Disease Prevention and Control; The Economist Intelligence Unit.

Four scenarios for China's economy

Below, we offer four scenarios for China's economy in 2020 based on when the public health emergency (defined by the Chinese government and the WHO) will be brought under control, although infections may continue after this time. At this point the government will lift quarantine measures and economic activity will normalise. To achieve this, the authorities will need to bring down sharply the number of new infections.

Our baseline scenario is that the public health emergency within China will be under control by end-March. This is based on the latest scientific studies and comparisons with the outbreak of a similar coronavirus, severe acute respiratory syndrome (SARS), in 2002-03. There is a range of opinions on when the virus is likely to be under control, with some experts affiliated with the Chinese authorities suggesting that the situation may substantially improve by mid-February. However, most calculations point to a much longer period.

The impact on the economy of this coronavirus outbreak is set to be substantive and deeper than that of SARS. Assuming that we hold to our baseline scenario that the virus will be under control by end-March, we plan to cut our real GDP forecast for China in 2020 to 5.4%, from 5.9% currently. This drop is consistent with our initial estimated range. The slowdown will be concentrated in the first quarter of the year, when economic expansion could drop to as low as 4.1% year on year (from 6.1% in full-year 2019), and will still be strongly felt in the second quarter. The second half of the year, during which China typically produces most of its GDP, will see a recovery in economic growth.

A drop in the growth of the world's largest emerging market will clearly have a direct impact on the global economy, as has already been indicated by recent volatility across international financial markets. Taking into account the impact of weaker demand in China on other countries, as well potential economic disruption in other countries should the coronavirus outbreak spread further globally, our forecast for global real GDP growth (at market exchange rates) could dip below 2%, from 2.3% at present.

Projected economic impact of coronavirus (2019-nCoV)

Scenario	Date by which the coronavirus outbreak comes under control within China	Probability	China's revised real GDP growth, 2020 (%)
Optimistic	End-February	25%	5.7
Baseline	End-March	50%	5.4
Pessimistic	End-June	20%	4.5

Nightmare	The outbreak is not contained in 2020.	5%	<4.5

Source: The Economist Intelligence Unit.

We encourage planning for scenarios other than our baseline scenario. These include the possibility that the outbreak will not be under control until end-June (20% probability)—thereby disrupting second-quarter economic activity as well as that of the first quarter—and that the outbreak may even prove to be uncontainable (5% probability). The latter could be a risk if the virus proves itself able to mutate and become more virulent or contagious.

The sectoral impact

In terms of the sectoral impact, we expect private consumption spending to soften as households become more precautionary and store and facility closures limit consumer options. Surging food prices, exacerbated by disrupted logistics chains, will curtail household spending on non-food items even further. The second half of the year will see a release of pent-up consumer spending as virus concerns dissipate, but a full recovery is unlikely until 2021. Under our core scenario, we plan to trim our forecast for private consumption growth in 2020 by around one percentage point (in real terms) from 6.5% at present.

Investment will also be affected, with businesses facing a fresh period of uncertainty having struggled through the US-China trade war over the past two years. The costs associated with the Chinese New Year holiday extension—including ongoing wage payments and loss of production—will use up capital that would otherwise have been used for investment. Property development investment will soften, with market demand for homes set to cool, while government-led investment into infrastructure could be affected by staffing challenges and the need to divert budgets into healthcare. Our investment forecast will be lowered by around 0.5 percentage points, from 4.2% currently, under our core scenario.

Public consumption is likely to be the one area of the economy that will not slow. Government spending on healthcare and medical supplies and facilities will surge in the coming months. As a result, we are likely to boost our government consumption forecast by around two percentage points under our core scenario, from 9.3% at present.

The virus risks damaging important regional supply chains: Hubei is home to significant automotive, steel and biopharmaceutical manufacturing industries. It could also become increasingly difficult to transport goods between the country's coast and interior, owing to Wuhan's status as an important regional transport hub. Of additional concern are the coastal Guangdong and Zhejiang provinces, both major export manufacturing hubs, which have confirmed the highest number of infections after Hubei. These challenges mean that we are likely to trim our goods and services export forecast from 1.7%, while softer domestic demand will also result in a lowering of forecast import growth from 2.4% at present.

Stimulus options

Differing levels of stimulus will be applied under the various scenarios we set out. Our working baseline forecast of 5.4% economic expansion in 2020 assumes relatively assertive stimulus actions (without them, annual growth would be substantially lower). Already, the authorities have moved to extend deadlines for tax and social security payments for firms.

The government's priority in its stimulus approach will be to ensure labour market and income stability; we do not think that it will implement measures for the sake of hitting the assumed real GDP growth target of "around 6%" in 2020. For most of our scenarios, this would imply an embrace of the sort of extremely loose monetary and fiscal policies that the authorities have disavowed in recent years. Citing the national emergency, the assumed growth target may be adjusted lower by the time it is announced publicly during the annual session of the National People's Congress in March (assuming the event goes ahead).

An initial policy priority will be to support companies that are struggling with cash flow issues caused by the effect of quarantine policies on businesses. This likely means liquidity injections by the People's Bank of China (the central bank) to give banks space to extend corporate debt repayment schedules. The authorities may also call upon state-owned enterprises to buy back stockmarket shares to further boost private firms' liquidity levels. Under our core scenario, we believe that the authorities will look to push the benchmark one-year loan prime rate downwards, to under 4% this year (from 4.15% currently).

In terms of fiscal policy, in 2020 the authorities are likely to abandon their traditional official budget deficit floor of the equivalent of 3% of GDP. Tax and fee cuts will likely be forthcoming for firms, while the authorities will look to stabilise household consumption through the provision of subsidies for selected goods. A loosening in property market restrictions will probably also be considered on a city-by-city basis, in a partial reversal of the existing tight policy stance.