World crisis: paradoxes of analysis and scenario options for development

Sergey A. Afontsev¹

¹ Lomonosov Moscow State University, Moscow, 199911, Russia; IMEMO RAS, Moscow, 117997, Russia

Received 24 April 2020 • Accepted 11 May 2020 • Published 1 June 2020


Abstract

During the period of global crises, economists often form the belief that the current shocks are unique and after them “the world economy will no longer be the same”. At first glance, the current crisis gives every reason for similar generalizations. However, the analysis shows that both the crisis deployment mechanisms and the factors of its exacerbation demonstrate a high degree of continuity with previous episodes of crisis dynamics. This means that getting out of crisis will also be not a unique challenge, but a task closely linked to previous global experience of anti-crisis policy. Calculations show that the depth of the economic recession in the Russian Federation can be about one and a half times higher than the expected rate of decline in the global economy, and real population income in 2020 under a negative scenario can decrease by more than 10%. This means that the income support should become one of the top priorities of the anti-crisis policy in Russia. Ignoring it can not only make the crisis deeper but also bring give to problems in the socio-political sphere.

Keywords

world economy, global crisis, coronavirus, GDP, protectionism, oil prices, Russia, population income

JEL codes: E32, F01, F13, F44

Human psychology is framed in a very strange way, and the psychology of professional economists is no exception here. Every time the global economy goes through any long period of sustained growth, most analysts are clearly divided into “optimist” and “pessimist” groups. The former state that “this time things will be different”, so that the period of high growth rates will continue for an unlimited period of time, though the entire previous experience suggests otherwise. The latter predict a crisis daily, and when it finally occurs, try to convince the entire world that it was they who had warned everyone from the beginning, but ignorant listeners neglected their prophecies. On what both optimists and pessimists invariably converge sooner or later is that “after the crisis the world economy will no longer be the same”, and then certainly “everything will be different”.

Copyright Afontsev SA. This is an open access article distributed under the terms of the Creative Commons Attribution License (CC-BY 4.0), which permits unrestricted use, distribution, and reproduction in any medium, provided the original author and source are credited.
At first glance, the current crisis gives every reason for similar generalizations. On the one hand, it was preceded by a very long period of growth of the global economy, marking its recovery from the crisis turmoil of 2008–2009. If one takes June 2009 as the first month of the post-crisis recovery of the US economy (NBER 2012), then in July 2019 its previous record of continuous growth (120 months from March 1991 to March 2001) was broken, and by January 2020 the duration of the new record was 126 months. Although the dynamics of US GDP have been significantly more sluggish than during previous periods of growth (The Economist 2019; Marotta 2020), and crisis impulses have occasionally hit various regions have been felt occasionally (the most important having been the 2010–2013 Eurozone crisis and the 2015 stock market crisis in the PRC), the prolonged growth of the world economy was evident, and its drivers were remarkably different from those characteristic of the pre-2008 growth period (Afontsev 2014; Afontsev 2019a). Although concerns about the growth sustainability been periodically expressed, in the first half of the last year the potential “leading indicators” of the crisis gave no reason for concern.

On the other hand, the coronavirus pandemic which has become the trigger of the current crisis with all its consequences for the world economy (still not fully understood in view of the uncertainty about the duration of the pandemic and the restrictive measures imposed because of it) may seem a perfect illustration of the notion that market corrections that can develop into a global crisis are usually caused by exogenous factors that are either difficult or impossible to predict. It is one thing to note the overheating of markets and expect them to decline, but quite another to point out a specific trigger for the crisis. As recently as a year ago, experts could ironize over a bickering between two former Unites States Federal Reserve Chairmen – J. Yellen (“I don’t think expansions just die of old age”) and B. Bernanke (“I like to say they get murdered”) (Coy 2019). Now we can see that both were right, however, under circumstances that everyone would like to avoid.

Meanwhile, the situation is not so simple. Even if the coronavirus has become the direct driver of the crisis, it cannot be said that it has brought down the long-growing world economy without any fundamental reasons. First, already in the second half of 2019, the “negative” for the world economy began to grow rapidly. The volume of international trade subject to newly introduced protectionist measures has continued to grow. After jumping from $79 billion (calculated from mid-October 2016 to mid-October 2017) to $588 billion (October 2017–October 2018), it showed further increase to $747 billion between October 2018 and October 2019 (WTO 2019). More importantly, the monthly growth of industrial production in the leading economically developed countries has gone in the negative zone. While in the United States this happened only in September 2019, and the pace of the recession did not exceed 1%, Germany experienced a year-round recession, with decline rates exceeding 4.5% in June and October and reaching 5.2% in December. In Italy and the United Kingdom, industrial production in 2019 had been falling for 11 months, in the Netherlands and Japan for 10 months (in Japan, decline rates exceeded 8% in October and November). In this sense, it is impossible to say that the current crisis has arisen “out of nothing” and the coronavirus is its only reason.

Secondly, an important factor in the crisis dynamics was the collapse of oil prices following the disintegration of the previous agreement to limit oil production in the OPEC+ format. Thus, the actual decline in oil prices has already begun in the end of February, and the increase of inter-country contradictions, which led to the collapse of the previous version of the OPEC+ agreement, was the result of the growing imbalance between oil supply and demand in the context of the spread of the coronavirus. Similarly, the new OPEC+ agreement,
concluded on April 10, 2020, could potentially remove about 10 million barrels of oil per
day from the world market in May-June 2020, while according to cautious OPEC estimates
the drop in oil demand in the second quarter of 2020 will amount to 11.86 million barrels
per day in comparison with the same period last year (OPEC 2020). In addition, the new
OPEC+ agreement affects only oil production but not its exports, which does not prevent
the leading OPEC countries (primarily Saudi Arabia) from exporting previously produced
oil, using a flexible price discount mechanism. Oil prices fell the main victim of the crisis,
dropping twice as fast as the prices of natural gas supplies to Asian and EU countries, and
more than 3 times faster than the market prices for aluminum and iron ore (IMF 2020a: 17).
As a result, countries dependent on oil production and exports will be the main candidates
for the status of principal victims of the crisis this year, and the situation – at least for the
Russian economy – is likely to be largely similar to the realities of the 2008–2009 crisis. In
this sense, we will not see anything new either.

Finally, forecasts that “after the crisis everything will be totally different” are also highly
speculative today. In particular, this applies to popular forecasts regarding the growth of
digital services markets in the post-crisis period. Indeed, in the context of restrictions im-
posed on personal movement and contacts, the markets for the relevant services appear to
be extremely dynamic. But what about the fundamental factors of their development? Es-
timates made in the pre-crisis period did not induce much optimism (UNCTAD 2019). In
the context of scenarios calculated for the world economy within the framework developed
by the Russian Foreign Trade Academy (VAVT 2017), the assessments of the contribution
of digital industries to developed and emerging economies in 2019–2025 did not exceed
0.1–0.35 percentage points per year (Afontsev 2019b). According to preliminary estimates,
the respective indicators in the period immediately after the crisis may increase by 1.3–1.6
times to 0.13–0.56 percentage points. But in any case, these are not the figures that can have
a decisive impact on the development of the world economy. Of course, on the wave of quar-
tines there is a great temptation to declare that the increased demand for digital services
will remain even after the end of the crisis. This hypothesis, however, is by no means uncon-
troversial, and it takes time to verify it. However, now it is obvious that in many cases the
replacement of traditional services with online ones was an ‘emergency option’, and higher
labour intensity of online services combined with the obvious problems of quality control
(particularly in education) make super-optimistic predictions concerning the development
of digital industries after the crisis rather premature.

As for the estimates of the impact of the current crisis on the global economy, they prin-
cipally depend on the scenario of future crisis dynamics. Three main options are available
here.

1. The V-scenario suggests that a sharp decline for several quarters will be followed by an
equally rapid upturn. Before the collapse of the previous OPEC+ agreement and the
sharp fall in global oil prices, the V-scenario was seen as quite possible (OECD 2020),
but today its probability is rather low, and most forecasts mention it just to make the
set of available options complete (e.g., S&P Global 2020).
2. The U-scenario, in which a sharp downturn is followed by a period of stagnation
transforming into recovery, is now by far the most likely. The main intrigue is how
long the stagnation phase will prove to be. The range of forecasts is from two quarters
to two years, with the date of the ‘ultimate turning point’ being beyond the knowledge
of economists as everything depends on whether the coronavirus pandemic will end
after the current wave of its spread or will be followed by new ones. According to IMF
calculations, the U-scenario could cost the world economy from 4 to 9 percentage points of lost GDP growth in 2020–2021, and the negative impact of the crisis on growth rates could be felt even in 2024. (IMF 2020a: 7, 9, 15–16).

3. The L-scenario (a sharp downturn with prolonged stagnation and uncertain prospects for recovery) is the most painful for the global economy, but fortunately not too likely, as it requires a combination of a long coronavirus pandemic with the inability of regulators to find adequate anti-crisis responses. However, for some countries, this scenario may prove quite real. This primarily refers to commodity-exporting countries affected by commodity price shocks, intensive capital flight from emerging markets and, as a consequence, high instability of national currencies (IMF 2020b: 11–13).

The Russian Federation is among the countries under the highest risk. As with the 2008–2009 crisis, the decline of Russian economy is likely to be much deeper than the decline in global GDP. According to IMEMO RAS estimates, in case of the U-scenario, Russian GDP can drop by 3.3 to 4.6% in 2020, which is about one and a half times more than the expected decline rates of the world economy. In case of the L-scenario, Russian GDP can fall by 5.5% in 2020 with prospects of further decline by 0.6–1.4% in 2021. Given that the most realistic estimate of the drop in disposable population income under the U-scenario in 2020is 6.5% (calculations of the VEB RF Institute of Research and Expertise for a decline of GDP by 3.8%; VEB RF Institute of Research and Expertise 2020), the “drift” of the Russian economy toward the L-scenario can be associated with a cumulative fall in income by no less than 10% in 2020–2021, with a wide range of potential challenges for Russian economy as well as social and political stability. This, in turn, means that income support should become one of the top priorities of the anti-crisis policy in Russia. Unfortunately, this priority was paid due attention to neither during the 2008–2009 crisis nor during the 2014–2015 “sanctions shock” period. It is to be hoped that, at least in this regard, “everything will be different” during the current crisis.

**Reference list**


VAVT (2017) Analysis of conditions for implementation of the strategy of social and economic development of the Russian Federation. Final report on topic P115-01-17. VAVT, Moscow. (in Russian)


Information about the author

- Sergey Alexandrovich Afontsev, Corresponding Member of the Russian Academy of Sciences, Doctor of Economics, Head of the Department of World Economics of Lomonosov Moscow State University, Deputy Director of E.M.Prismakov National Research Institute of World Economy and International Relations of RAS. E-mail: afontsev@gmail.com