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Economic Growth versus Coronavirus Pandemic

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Abstract

The aim of this paper is to analyse the evolution of the Gross Domestic Product (GDP) and inflation within the European Union in the year 2020 and the economic projections for 2021. The Coronavirus pandemic triggered unexpected changes in the global economy as many sectors were severely affected by the lockdown. In this context, the impact of the Coronavirus pandemic on the economic growth in the EU-27 Member States will be outlined. In the process towards the economic recovery, economies should play strategically to avoid massive indebtedness and further inflation. Furthermore, alternative scenarios of economic policies to restart the economies shall be considered.

Keywords: Economic growth, GDP, inflation, Coronavirus pandemic, indebtedness.

JEL Classification: F43, E51, F63, O47

1. Introduction

The European Union works as a single market of 27 countries and represents a major world trade power. The economic policy of the European Union is aiming at creating jobs and boosting growth through smarter use of financial resources, removing barriers to investment and providing technical assistance to investment projects (Maza et al., 2012).

The European Union has ensured that it develops a single internal market through a standardised system of laws that apply in all Member States. EU policies aim to ensure the free movement of persons, goods, services and capital in the internal market and the adoption of legislation in the area of justice and home affairs and the perpetuation of common policies on trade, agriculture, fisheries and regional development.

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The effects of the Coronavirus pandemic are visible at European level and all Member States are trying to take the best measures to maintain economic activity at a pace as normal as possible, while respecting safeguards and preventing the spread of the virus.

The current economic forecast is uncertain during this period as it is linked on one hand to the duration and extent of the Covid-19 outbreak and, on the other hand, to the potential changes in consumer behaviour after the end of the Coronavirus crisis. It is also envisaged that generalised quarantine measures adopted so far to combat the outbreak of Coronavirus pandemic can lead to large losses in most economic sectors.

2. Problem Statement

The economy of the EU-27 Member States faced a strong recession in the first half of 2020 due to the Coronavirus pandemic across the globe. With an average fall of around 7.5% in world's Gross Domestic Product (GDP), the Coronavirus pandemic seems to push the global economy towards the deepest recession since *the Great Depression* and to the deepest output contraction since World War II (European Commission, 2020). Inflation is always and everywhere a monetary phenomenon in the sense that it is and can be produced only by a more rapid increase in the quantity of money than in output (Friedman, 1970). Inflation requires monetary growth to facilitate and enable it (Goodhart, 2020). In the first quarter of 2020 the household real consumption per capita dropped by 3.0% (Eurostat, 2020). This was mainly due to 2 types of savings: the *involuntary savings* and the *precautionary savings* (Goodhart, 2020). The involuntary savings are caused by the impossibility of people to purchase goods or services due to the lockdown measures. The precautionary savings are due to a change in the financial behaviour of people, who during pandemics learn the hard lesson to put aside money for unexpected events.

The current governmental strategies have as main objective the improvement of society's welfare. The economic development and the increase in the society's welfare result in a sustainable economic growth (Garin et al., 2016). The process of economic growth is perceived as the fundamental drive to increase the life standard, which is one of the most important events in people's life. For an effective development of the European Union, we strongly believe that focus should be oriented towards the achievement of economic growth in all sectors of the market economy. Moreover, this process should be aligned to the economic growth of the EU-27 Member States and their welfare increase (Anghelache et al., 2017).

Having as objective the economic growth in the EU Member States, one of the drivers of economic growth is consumption. From this perspective the Coronavirus pandemic represents a major shock for the economies with very serious socio-economic consequences. Despite the fast and comprehensive economic responses, the EU economy will have a deep recession in 2020 as the Coronavirus pandemic has severely affected consumer spending, industrial production, investment, trade, capital flows and supply chains. In addition, the gradual relaxation of the containment measures that are announced in the next period should pave the way for recovery. However, the losses incurred this year by the EU economy are not expected to be recovered before the end of 2021.

The management of the European Union's policies will be ingested to achieve a balance of effective policy measures at EU and national level in response to the crisis considered crucial to limit the economic damage and to facilitate a rapid and robust recovery so that economies can return to the path of sustainable and inclusive growth.

3. Research Questions/Aims of the research

The aim of this article is to analyse the evolution of the GDP in the first quarter of 2020 and possible projections for the future periods correlated with the annual inflation rates in the EU-27 Member States. Beside the statistical analysis of the mentioned macroeconomic indicators, we have also intended to analyse the major economic measures taken by the European institutions to boost the European economy and, especially those sectors severely affected by the Coronavirus pandemic.

4. Research Methods

The research methods applied in this study are descriptive statistics of the macroeconomic indicators of interest for us obtained from the Eurostat database. Also, we used qualitative methods of research to analyse the economic measures taken at EU-27 level to alleviate the Coronavirus global pandemic.

5. Findings

Figure 1 below indicates the GDP growth rates in the first quarter of 2020 highlighting in percentage the change over the previous quarter. In the EU-27 Member States, Ireland (+1.2%), Bulgaria (+0.3%) and Romania (+0.3%) registered positive growth rates compared to the previous quarter. At the opposite pole, registering negative growth, there are France (-5.3%) and Italy (-5.3%) followed closely by Spain (-5.2%) and Slovakia (-5.2%).

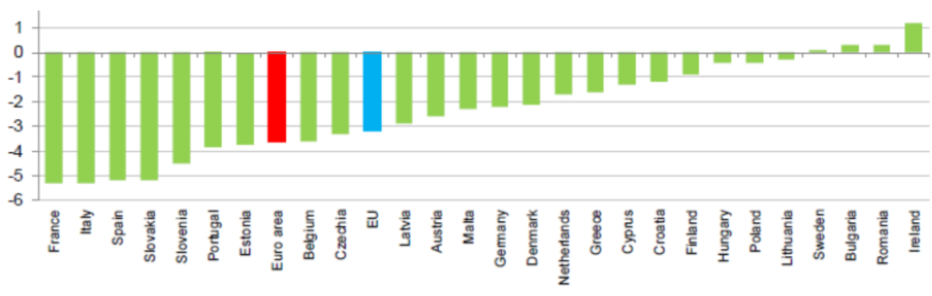

Figure 1. GDP growth rates in the first quarter of 2020
Source: Eurostat (2020)

The projections of the economic output for the second quarter of 2020 indicate a deeper curve compared to the first quarter of the year (European Commission, 2020), motivated by the prolongation of the confinement measures.

The impact of Coronavirus on inflation is still uncertain although in the first semester of 2020, despite the market closures, disinflation has dominated (La Caixa, 2020). Figure 2 below indicates that the lowest annual rates were registered in Cyprus (-2.2%),Greece (-1.9%) and Estonia (-1.6%), while the highest annual rates were recorded in Poland (3.8%) and Czechia (3.4%). The collapse in output increases downside the inflationary risks. One of the highest risks for inflation is the excess of monetary and fiscal stimulus that can bring back inflation. Some authors (Blanchard, 2020) speak about the 'wrong high inflation scenario', which requires the combination of a large increase in the debt-to-GDP ratio and a very large increase in the neutral interest rate of fiscal dominance over monetary policy.

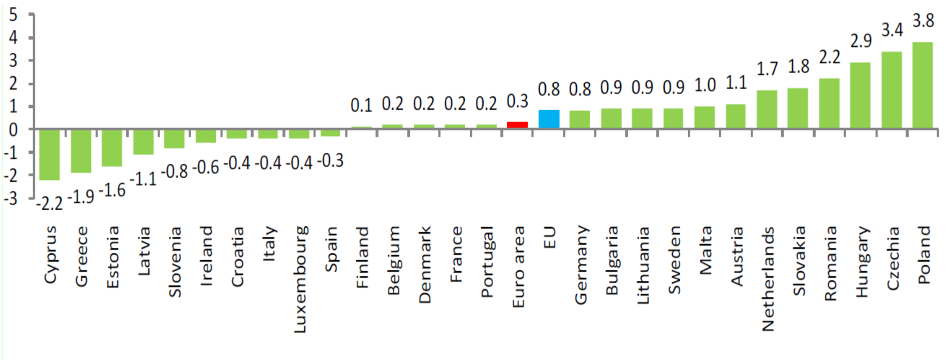

Figure 2. Annual inflation rates (%) in June 2020
Source: Eurostat (2020)

As the statistical analysis shows, the economic situation of the EU-27 Member States is highly affected by Coronavirus pandemic. It is important to highlight that the intensity of the impact is different from a region to another, depending on the specificities of each country. As GDP is strongly correlated with employment, in countries in which a larger share of population is employed in tourism and in the sectors related to it, GDP losses are bigger as compared to countries in which a larger share of population is employed in the public sector (Conte et al., 2020). The measures taken to alleviate the economic consequences of the crisis consider the magnitude of the impact in each country, offering loans to euro area Member States that constitute up to 2% of the country's GDP, but not exceeding EUR 240 billion (European Stability Mechanism, 2020). Another important measure is the introduction of temporary flexibility of EU funds, so as to allow transfers between funds, regions, focusing on the most affected members of society (European Council, 2020). The European Central Bank has managed the monetary policy during the Coronavirus pandemic crisis by introducing EUR 1 350 billion pandemic emergency purchase programme (European Central Bank, 2020).

6. Conclusions

All the responsible institutions have unified their forces and introduced the necessary measures to fight the Coronavirus pandemic, which has, along the irreversible human losses, negative economic consequences that will affect the quality of life of the majority of people. The popular solution proposed by President Bush after the terrorist attack in September 2001, namely to "go shopping" cannot be applied in this situation, because of the rapid spread of the virus and the fear generated by the Coronavirus pandemic across the globe. The consumer behaviour changed and most surely, it will be further affected in the following period, depending on how the pandemic will evolve. However, there is hope that the measures taken both at the European level and at national levels will help to recover the economy and to determine economic growth in the next year 2021.

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