

THEIR VIEW

MINT CURATOR

# How economic management and outcomes differ across the G20

Stimulus-injected rich countries suffered low output loss amid high covid mortality while India and others have fared worse



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Although the rapid spread of covid led it to be regarded as a pandemic, covid-related mortality, equalized to deaths per million, varies sharply across countries. On average, covid mortality in the Transatlantic-Mediterranean region (comprising the Americas, Europe, Middle East, North Africa and Central Asia) is about 10 times than in more populous South and East Asia. Covid mortality has been selected as a proxy for the relative virulence of covid, rather than the number of infections, as testing rates and protocols vary greatly across nations.

The policy response, comprising lockdowns, wearing a mask, restrictions on movement and gatherings, has however been largely undifferentiated across countries. The Global Financial Crisis (GFC) a decade ago was also largely a Transatlantic phenomenon. While there was monetary and fiscal easing across the globe, the policy response in Emerging Markets and Developing Economies (EMDEs) was muted and tailored to their circumstances. Their financial systems also held up. EMDEs continued to grow relatively strongly, cushioning the decline in global growth. This time around, in sharp contradistinction to the GFC, the decline in growth and output loss is largely similar. It is, therefore, unsurprising that global growth has suffered far more during the covid pandemic than during the GFC.

Economic growth varies from year-to-year around an average trend, sometimes growing above this line, and sometimes below. This trend growth is indicative of a country's potential gross domestic product (GDP). Economic recessions are steep declines in growth relative to the trend line. Recessions that are a natural part of a business cycle incline to a strong V-shaped recovery, where an economy grows sharply, but briefly, above its trend line to recoup lost output before reverting to its trend. When a recession is caused by an underlying structural crisis, the economy might lose some output permanently before returning to its former trend line once the underlying problem is resolved. If the crisis is severe and protracted, the trend line itself might shift lower through a process of hysteresis, as the growth potential or productive capacity of the economy declines.

The covid-related steep fall in economic activity was not part of a natural business cycle. International Monetary Fund (IMF) projections indicate that there would be permanent losses in output going forward. Ordinarily, we should expect that higher the mortality, the greater the economic disruption and larger the loss of output. That having been said, countries may fare better or worse than what one would expect on the above assumption. A relatively large output loss with relatively low mortality can be assumed to

## The corona effect

Advanced countries managed to keep output better shielded thanks to aggressive stimulus efforts and lighter pandemic restrictions while emerging economies like India did relatively well on covid mortality but worse on GDP.

G-20 countries	Growth figures in %								
	Actual 2019	Projection 2020*	Trend Growth#	Estimate 2020**	Projection 2021	Projection 2022	Gain/loss###	Deaths/mn 29 Jan 2021	Mgt grade
Argentina	-2.1	-1.3	-1.7	-10.4	4.5	2.7	1.9	1,048	
Australia	1.9	2.3	2.1	-2.9	3.5	2.9	-2.8	35	B--
Brazil	1.4	2.2	1.8	-4.5	3.6	2.6	-3.7	1,039	B--
Canada	1.9	1.8	1.9	-5.5	3.6	4.1	-3.5	518	B--
China	6.0	6.0	6.0	2.3	8.1	5.6	-2.0	3	B
France	1.5	1.3	1.4	-9.0	5.5	4.1	-3.6	1,144	B--
Germany	0.6	1.1	0.9	-5.4	3.5	3.1	-1.5	670	A
India	4.2	5.8	5.0	-8.0	11.5	6.8	-4.7	111	C
Indonesia	5.0	5.1	5.1	-1.9	4.8	6.0	-6.4	107	C
Italy	0.3	0.5	0.4	-9.2	3.0	3.6	-3.8	1,446	B--
Japan	0.3	0.7	0.5	-5.1	3.1	2.4	-1.1	42	B
Korea	2.0	2.2	2.1	-1.1	3.1	2.9	-1.4	27	B
Mexico	-0.1	1.0	0.5	-8.5	4.3	2.5	-3.2	1,196	B--
Russia	1.3	1.9	1.6	-3.6	3.0	3.9	-1.5	495	B+
Saudi Arabia	0.3	1.9	1.1	-3.9	2.6	4.0	-0.6	181	B+
South Africa	0.2	0.8	0.5	-7.5	2.8	1.4	-4.8	722	B--
Turkey	0.9	3.0	2.0	1.2	6.0	3.5	4.9	302	
United Kingdom	1.4	1.4	1.4	-10.0	4.5	5.0	-4.7	1,515	B--
United States	2.2	2.0	2.1	-3.4	5.1	2.5	-2.1	1,336	A

\*Projections before covid; \*\*Estimates after covid outbreak; #Average of 2019 and Projection for 2020; ###Cumulative output loss/gain in 2020-22 over trend growth

Source: IMF, Worldometer

indicate poor management of covid's economic fallout. Conversely, a relatively low output loss despite high covid mortality suggests good economic management.

The accompanying table, based on IMF and Worldometers.info/coronavirus/data, attempts an assessment of the management and impact of covid on the economies of G20 countries. This grouping includes the world's largest economies that together account for over three-fourths of global output, trade and population.

The trend growth base taken to calculate the output loss/gain each year is the average of actual growth in 2019 and the growth projected for 2020 by the IMF's *World Economic Outlook* (its October 2019/January 2020 updates, i.e., just before the pandemic). The output gain/loss is calculated by aggregating the difference between the estimated/projected and trend growth for the years 2020-2022. On average, the output loss estimations are lower than those obtained by the methodology used by IMF chief economist Gita Gopinath, as outlined in some interviews, which takes IMF's pre-covid projections for 2020 as its base.

As is to be expected, economic performance varies sharply across countries and groupings. Their relative performance has been graded between A (best), B and C (worst). The US and Germany have been graded A on account of a relatively low covid-related output loss (less than about 2% of GDP) and high (above 600 per million) covid-related mortality. At the other end, India and Indonesia with relatively high (exceeding 4.5%) output loss and low (less than 150 per million) mortality are graded C. The rest of the G20 countries are placed in the B category, further differentiated into B+, B and B-, based on relative

combinations of their mortality and output data.

Output loss is notional, based on unobserved data. It is very sensitive to the estimation of trend growth. Trend growth, and consequently output loss, might be underestimated in countries where growth was unstable in the pre-covid period. This is particularly the case in Argentina and Turkey, where there is an usually large difference between 2019's growth and 2020's estimated growth. Pre-covid instability in Argentina was too great to make an assessment of economic management.

The average output loss in G7 countries is 2.86% of GDP, while it is 3.34% in the BRICS countries of Brazil, Russia, India, China and South Africa, despite mortality being twice as high (953 versus 474) in G7 countries. This indicates that while G7 countries lost more lives to covid, they have managed its economic fallout better on the whole. This could be on account of a combination of better health care systems and a more aggressive fiscal and monetary policy stance.

According to the IMF's *Fiscal Monitor* (January 2021 update), G7 countries have on average put in place stimulus of around 33.4% of GDP (12.4% fiscal with liquidity support accounting for the rest), compared to 8.6% (4.9% fiscal and the rest liquidity support) by BRICS. The US (19.2% of GDP) and Germany (38.9% of GDP), both rated A, have some of the most aggressive fiscal and monetary stimulus. On the other hand, countries with far lower mortality may have overdone the lockdown of their economies. China's performance assessment of B and Indonesia's C might come as a surprise, since neither country had a big contraction of its economy. However, their trend growth is high, and so too the notional output loss relative to their low covid mortality.

THEIR VIEW

# The world has its eyes set on how Biden takes on China

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Days after Chinese President Xi Jinping addressed this year's virtual World Economic Forum, emphasizing the importance of global cooperation in fighting the covid pandemic and saving the world economy, Beijing declared its intent of conducting military exercises in the South China Sea in the Gulf of Tonkin, just east of Vietnam. This is the new Chinese style of diplomacy, wherein the world is supposed to take the rhetoric of cooperation more seriously than the country's aggressive actions. The Communist Party of China would have the world believe that even its malevolent actions against weaker, smaller states are actually about the greater global good.

At the World Economic Forum's virtual event, The Davos Agenda, Xi Jinping wanted the world to focus on multilateral cooperation, even as he targeted the US and its allies for "ideological prejudice". In some ways, Xi was once again trying to do what he did in 2017 when he delivered the keynote address at Davos—positioning China as guarantor of

the world economic order by signalling a willingness to take on a bigger role in global leadership at a time of growing American isolationism. But in 2017, it was Donald Trump at the helm of the US, while now President Joe Biden wants to make America globalist again.

So, calling for a rejection of isolationism and "ideological prejudice", the message from the Chinese leader was one of engagement on Chinese terms. And sure enough, his speech was followed by actions in the South China Sea, after a US carrier group led by the *USS Theodore Roosevelt* entered those waters on Saturday to promote freedom of sea navigation. Xi's message was aimed primarily at the Biden administration, which is still trying to settle in, and the contours of its China policy are only just about beginning to emerge. Given the Trump administration's explicit posturing vis-à-vis China on issues ranging from trade, the Indo-Pacific, Hong Kong, Xinjiang and Taiwan to the South China Sea, it is important for Beijing to lay down a clear marker for the new US administration. Beijing seems unsure about how relations between the two countries will shape up under President Biden.

Xi, therefore, made his preferences clear when he suggested that "we should respect

and accommodate differences, avoid meddling in other countries' internal affairs and resolve disagreements through consultation and dialogue." Referring to the last few years, the Chinese leader also said that "history and reality have made it clear time and again that the misguided approach of antagonism and confrontation—be it in the form of a cold war, hot war, trade war or tech war—will eventually hurt all countries' interest and undermine everyone's well-being."

While Biden has suggested that he would like his country to "engage with the world once more", there is every likelihood that his China policy will take its cues from his predecessor. And that's what China remains worried about. Terming Trump's approach to China a "strategic misjudgement", China's top diplomat Yang Jiechi recently urged the Biden administration to "rise above the outdated mentality of zero-sum, major-power rivalry and work with China to keep the relationship on the right track." Jiechi reminded the

US that Beijing expects Washington "to honour its commitment under the three Sino-US joint communiques" and abide by the 'One China' principle, as "these issues concern China's core interests, national dignity as well as the sentiments of its 1.4 billion people", thereby constituting "a red line that must not be crossed."

**America's leader has signalled the continuity of its China policy but Indo-Pacific countries aren't yet sure of it**

While the Biden administration might be keen on working with Beijing on big issues such as covid response, economic recovery and climate change, the tech and trade rivalry with China that sharpened under Trump is not going anywhere in a hurry. In his first foreign policy speech after taking office, Biden made it clear that America will confront Beijing's economic abuses, counter its aggressive, coercive action to push back on China's attack on human rights, intellectual property, and global governance." In the Indo-Pacific, new secretary of state Antony Blinken has re-committed the US to the defence of the Philippines, reaffirmed the strength of the United States-Thailand

defence alliance, rejected China's maritime claims in the South China Sea, and pledged to stand with Southeast Asian claimants in the face of Beijing's pressure. This followed the Biden administration's assurances to Japan over the defence of the Japanese-administered Senkaku Islands in the East China Sea, which China claims and calls the Diaoyu. Blinken has also underlined the importance of cooperation, including through multilateral organizations and mechanisms like the Quad, to tackle shared challenges in his outreach to regional US partners like Australia, Japan and India.

The stage is set for continuity in America's China policy, despite there being serious concerns in the Indo-Pacific about America's future posture towards China and the region. Biden and his team may need some more time to fully make up their mind about China, but regional powers are clear about the challenge they face. If the US won't respond adequately and in time, then regional players will have to marshal their own resources to manage the consequences of China's rise. It was Barack Obama's eight years in the White House that allowed China to emerge the menacing power it is today. For the Indo-Pacific, giving Biden any more time is a luxury the region can't afford.

# Ultra-long US Treasury bonds are an ultra-long shot, frankly

Low interest rates can be locked in but the idea is bad for taxpayers



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Janet Yellen once said she'd examine the idea of 50- and 100-year T-bills

It didn't take long for Wall Street to start talking about the prospect of the Biden administration issuing 50- or 100-year bonds. One of the first debt management topics studied by the prior Trump administration in 2017, new Treasury Secretary Janet Yellen stated in her confirmation hearing three weeks ago that she would look at the idea again. Although a few years have passed and the fiscal outlook has worsened with significant additional covid relief spending on the horizon, the answer likely remains the same: ultra-long debt is not in the best interest of US taxpayers.

In the context of 25% interest rates on personal credit cards and the double-digit rates of inflation seen in the 1970s, many believe it ludicrous that the government would not borrow money at historically low, single-digit interest rates for a length of time that few of us will outlive. Rather than incompetence, the Treasury's decision to not issue ultra-long bonds reflects both the savvy of its debt management office and the sound advice of the Treasury Borrowing Advisory Committee.

The primary goal for the Treasury's debt management office is to fund the government at the lowest expected cost over time. With \$27.7 trillion of debt outstanding, annual interest expenses of about \$375 billion and trillions of dollars in additional fiscal stimulus still needed to combat the pandemic, it is critical that the Treasury not waver from its main mandate.

The interest rates demanded for longer-dated bonds are almost always higher than those of their shorter-dated equivalents, for obvious reasons. Yields on 30-year bonds are currently about 1.82 percentage points more than those on two-year notes. That difference, or spread, is above the median of 1.22 percentage points since 1980. The spread between 10-year notes and 30-year bonds is about 0.79 percentage point, above the median of 0.35 percentage point over the long term. As such, in today's environment, it is still more cost effective for the Treasury to issue and refinance shorter-dated debt than to issue longer-dated debt.

Nevertheless, with longer-term interest rates near historic lows on an absolute basis, many suggest the Treasury should act more opportunistically. Decisions to issue (or stop issuing) certain securities based upon a political appointee's assessment of the level of interest rates is certain to open a Pandora's box. If that were to happen, the significant liquidity premium earned over the years through the Treasury's "regular and predictable" approach

to debt management would evaporate, leading to higher relative borrowing costs across all Treasury debt issuances.

What of the risk of inflation eventually driving short-term interest rates higher? Would the government then have surely wished that it had locked in the current low rates? If the Treasury's debt managers were confident that a significant acceleration in inflation was coming, then issuing ultra-long bonds could make sense. However, the very fact that interest rates are so low largely reflects the broader market's belief that it won't happen.

Markets can be wrong. Investors make (and lose) huge sums of money trying to divine the message being sent by markets. The Treasury's debt managers are different in that they are stewards of both taxpayer money and the risk-free benchmark upon which nearly all financial assets are priced; it would be irresponsible of them to gamble on future interest rates and inflation.

Reducing the volume of debt coming due each week and the risk that an insufficient number of investors show up at the Treasury's debt auctions is the final argument put forth by advocates of ultra-long bonds.

Refinancing or rollover risk is better mitigated by holding a prudent level of cash than by extending the maturity of the debt. With an average of about \$350 billion coming due each week, the Treasury would need to issue an astronomical volume of ultra-long bonds to meaningfully reduce this risk. And, as highlighted by the Treasury Borrowing Advisory Committee, investor demand for ultra-long debt is much too limited and uncertain.

All this is not to say that there are no legitimate reasons to issue 50- or 100-year bonds. Ultra-long issuance would support both price discovery and liquidity in the corporate debt market. By providing this public good, the Treasury would support greater issuance of longer-dated corporate debt, thereby improving the capital structure and financial stability of the private sector. Pension plans and insurance companies would also benefit, with a larger investable universe to hedge their long-duration liabilities. These benefits, though, currently remain amorphous and small relative to the additional expense of issuing ultra-long debt.

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