Coronavirus pandemic could cause deepest recession on record, Bank warns

Economy projected to bounce back with 15 per cent growth in 2021

Philip Aldrick, Economics Editor
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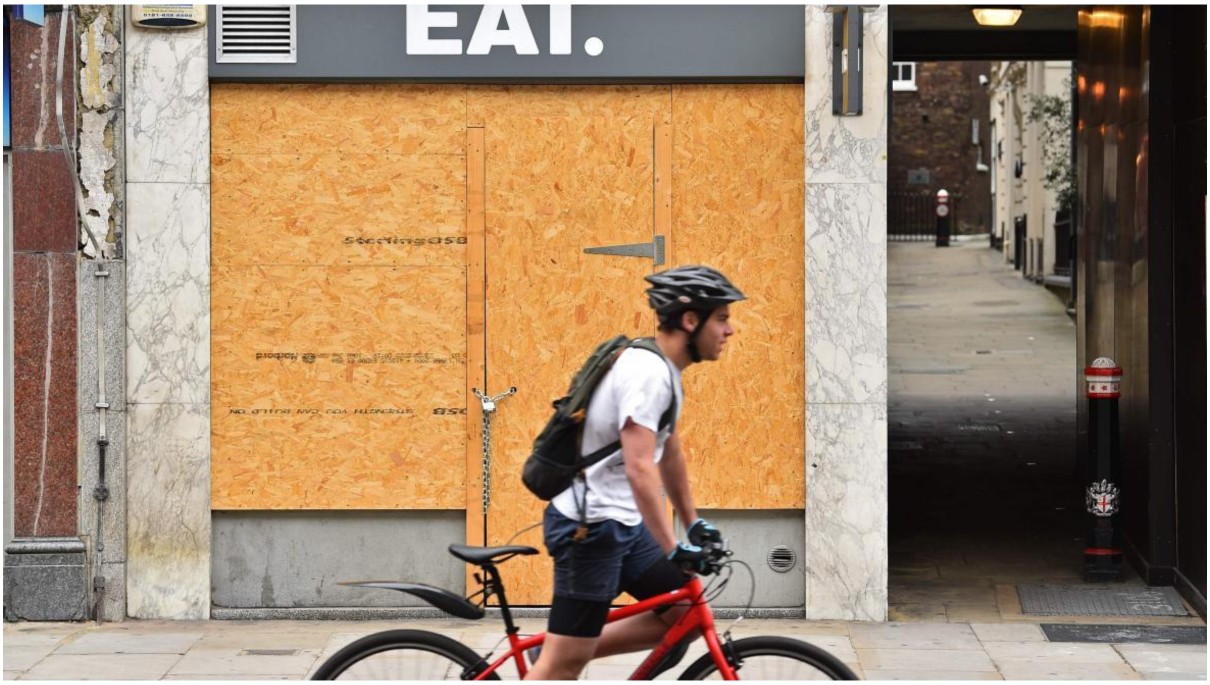
With six million workers furloughed and a further two million expected to lose their jobs, the Bank of England projection is gloomy in the short term but more optimistic in the longer term



The British economy will shrink by 14 per cent this year and two million people will lose their jobs, with a further six million people on the furlough scheme, the Bank of England has set out in the most disastrous projections it has ever published.

With the economy in lockdown GDP is on course to be 30 per cent smaller by June than it was in December and unemployment to have hit 9 per cent. The decline will be global as the pandemic strikes countries indiscriminately. World GDP is expected to shrink 12 per cent this year on a purchasing power parity basis, the Bank said.

This year’s recession will be the deepest since the Great Frost of 1709 and more than twice as bad as the 6 per cent crash in the financial crisis but the economy is projected to bounce back with 15 per cent growth in 2021.

However, the UK will not recover all the lost ground until the second half of next year, in a slower rebound than the Office for Budget Responsibility's official forecast for the government.

The Bank emphasised that the figures were a plausible illustrative scenario rather than a formal forecast because there are so many unknowables, including when and how lockdown would be lifted. It assumes that social restrictions, and the accompanying economic support schemes, will begin to be withdrawn in June and be fully removed in September.

The Bank has taken unprecedented action to shore up the financial system, markets and the economy since March. It has cut rates from 0.75 per cent to a record low 0.1 per cent and increased quantitative easing by £200 billion to £645 billion alongside cheap funding schemes for banks and businesses.

At its May meeting the monetary policy committee left the package unchanged but of the nine MPC members two voted for £100 billion more QE. The dissenters were the external members Michael Saunders and Jonathan Haskel.

The Bank's scenario is optimistic in the longer term. It foresees no lasting economic scarring from the pandemic and lockdown, productivity unaffected and unemployment back at current levels of 4 per cent by early 2022. It does not consider the possibility of a second spike in infections.

The long-term risk comes from the banking sector, as set out in its separate financial stability report. If banks fail to meet businesses cash flow needs the feedback loop into the real economy from insolvencies will be more lasting, it warned.

The banks have more than enough capital headroom to absorb losses and increase credit extension. It is in their own interests, as well as those of the wider economy, not to pull their horns in for fear of defaults, the Bank makes clear.

In a sign that Mr Saunders, Mr Haskel and others ratesetters remain concerned about the functioning of gilts markets, where the government raises the money to pay for its economic rescue package, the MPC signalled that it would look again at QE.

The minutes to the MPC meeting said: "The committee notes that the stock of asset purchases will reach £645 billion by the beginning of July, at the current pace of purchases. The committee continues to monitor closely a range of indicators of market functioning."

The government will raise £60 billion in gilts in July and more beyond that. So far the Bank has been buying the same amount of gilts in the markets as the government is issuing, keeping markets liquid and borrowing costs low, but under current projections it will stop doing so from July.