

# Australia and the economic impacts of the COVID-19 outbreak

James Laurenceson

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## Introduction

The rampant spread of the COVID-19 virus has caused alarm not only in terms of the health consequences but potential economic impact. This UTS:ACRI brief investigates these developments to date.

## The time profile of the COVID-19 shock

The SARS virus from 2003 is commonly referenced to understand how the COVID-19 shock is likely to unfold over time. This episode suggests that the negative impact will be sharp but short-lived. Two percentage points were shaved from China's 11.1 percent year-on-year growth in the first quarter of 2003 to 9.1 percent in the second: so around a 20 percent fall in the rate of growth. It rebounded to 10 percent in the third quarter.

There are reasons to think that the time profile of COVID-19 shock will be 'sharp but short' too. In the case of SARS, it took three months for the Chinese authorities to notify the World Health Organization (WHO). This compares with one month for COVID-19. China has also enacted unprecedented restrictions on domestic movement in a bid to contain the spread. The city of Wuhan, the epicentre of the outbreak, was locked down on January 23. Now the number of people in cities across China facing varying restrictions stands at around 500 million according to *Reuters*.<sup>1</sup> *The New York Times* puts the number at 760 million, or more than half of China's entire population.<sup>2</sup>

The impact of such measures, combined with measures taken overseas, is seen in that while as of February 16 there were 51,866 laboratory-confirmed cases world-wide, 38,839 are in a single Chinese province (Hubei) and less than one percent are overseas.<sup>3</sup> In Australia, there have only been 15 confirmed cases, zero deaths and six people have already recovered.

Most economic forecasters were quick to knock off around 0.3 percentage points (pp) to 0.5 pp from China's 2020 growth forecast, placing it in the 5's, with nearly all of this hit being concentrated in the first quarter.<sup>4</sup> In late January China's central government extended the usual new year break by one week, delaying the restart of normal economic activity, and the latest available high frequency indicators such as passenger traffic,

1 *Reuters*, 'Under China's coronavirus lockdown, millions have nowhere to go', February 14 2020 <<https://www.reuters.com/article/us-china-health-scale/under-chinas-coronavirus-lockdown-millions-have-nowhere-to-go-idUSKBN2081DB>>.

2 Raymond Zhong, Paul Mozur, 'To tame coronavirus, Mao-style social control blankets China', *The New York Times*, February 15 2020 <<https://www.nytimes.com/2020/02/15/business/china-coronavirus-lockdown.html>>.

3 World Health Organisation, 'Novel coronavirus (COVID-19) situation', February 17 2020 <<http://who.maps.arcgis.com/apps/opsdashboard/index.html#/c88e37cfc43b4ed3baf977d77e4a0667>>.

4 Phillip Inman, 'Will the coronavirus outbreak derail the global economy?', *The Guardian*, February 10 2020 <<https://www.theguardian.com/news/2020/feb/10/will-the-coronavirus-outbreak-derail-the-global-economy>>.

coal consumption and property sales have still not recovered.<sup>5</sup> It was hoped the prominence of e-commerce in China might keep consumption moving forward even as shoppers avoided malls, but Alibaba, the largest platform, has just assessed the revenue impact in the first quarter will be negative, potentially 'significantly'.<sup>6</sup> Alibaba noted that 'while demand for goods and services is there' – suggesting a quick rebound is possible once the virus spread is contained – the problem now is that increasingly production supply chains are also breaking down. In the first quarter of 2019, China's GDP grew by a seasonally-adjusted 1.4 percent. When China's first quarter results are released in April, expect the quarter-on-quarter growth rate to be in the zeros at best, with a contraction entirely possible.

A survey by the Australian Chamber of Commerce in Shanghai shows more than half of the 100 members who responded said they were expecting a 20 percent drop or more in first quarter revenues. Just over one quarter forecast a drop of 20 percent or more over the full year.<sup>7</sup>

Still, forward looking financial markets are not yet panicking. When Wuhan was locked down, the Shanghai Composite Index fell by 10 percent in two days. But it has since recovered about half the ground lost.

### The risk profile of COVID-19 for Australia

Philip Lowe, the governor of the Reserve Bank of Australia (RBA) noted on February 7 that the risk profile of COVID-19 for Australia is almost certainly worse than SARS. The size of China's economy and its international connectedness has increased dramatically. In 2003, China accounted for 8.7 percent of world GDP. Now it is worth 19.7 percent.<sup>8</sup> In 2001, less than 20 percent of countries traded more with China than the US. But by 2018, two-thirds of countries traded more with China. What this means is that economic contagion from China doesn't just spill over to Australia directly but also through third markets.<sup>9</sup>

In the case of Australia, the latest data shows China buys 38 percent of Australia's goods exports, up from 8.4 percent in 2003. China is also Australia's number one goods import source, accounting for 24 percent of the total. This means not only will demand for final goods and services like beef, wine, education and tourism be affected but supply chains for products such as building materials and components for manufactured goods as well. And China is number one for Australia's services exports too, accounting for 19 percent of the total, nearly double that of the US in second place.

Still, at a macroeconomic level the impact should not be exaggerated. Cushioning the blow as it has done many times previously is the Australian dollar, having depreciated four percent since January 1. The RBA puts the likely growth cost at around 0.2 pp in the first quarter.<sup>10</sup> Some private forecasters have the impact a good deal higher at 0.5 pp, which would put the Australian economy on the cusp of shrinking from January to March.

At a more disaggregated level, there are a plethora of businesses exposed to Chinese demand and are feeling immediate impact.

The restaurant trade in China is taking a battering as people elect to stay at home and this quickly has an impact on agricultural producers in Australia. For example, agricultural economist Ben Lyons from the University of South Queensland notes that two-thirds of the red meat that Australia exports to China is used in food service at a restaurant.<sup>11</sup>

5 Mark Williams, 'The COVID-19 coronavirus and its economic impact', Capital Economics, February 3 2020 <<https://www.capitaleconomics.com/the-economic-effects-of-the-coronavirus/>>.

6 Lulu Yilun Chen, Kari Soo Lindberg, Zheping Huang, 'Alibaba warns virus having broad impact on Chinese economy', *Bloomberg*, February 13 2020 <<https://www.bloomberg.com/news/articles/2020-02-13/alibaba-s-revenue-beats-after-singles-day-offsets-china-slowdown>>.

7 Michael Smith, 'Australian companies in China brace for first-quarter revenue hit', *The Australian Financial Review*, February 14 2020 <<https://www.afr.com/world/asia/australian-companies-in-china-brace-for-first-quarter-revenue-hit-20200213-p540me>>.

8 International Monetary Fund, 'GDP based on PPP, share of world', October 2019 <<https://www.imf.org/external/datamapper/PPPSH@WEO/OEMDC/ADVEC/WEOORLD/CHN>>.

9 Alyssa Leng, Roland Rajah, 'Chart of the week: global trade through a US-China lens', *The Interpreter*, December 18 2019 <<https://www.lowyinstitute.org/the-interpreter/chart-week-global-trade-through-us-china-lens>>.

10 Patrick Commins, 'Reserve Bank chief Philip Lowe remains buoyant but says economy has significant issues', *The Australian*, February 7 2020 <<https://www.theaustralian.com.au/business/economics/reserve-bank-chief-philip-low-remains-buoyant-about-economy/news-story/f48b19fdc1397ccea4d5af7ad114fc6a>>.

11 Jessica Strutt, 'What kind of hit will the economy take from the coronavirus outbreak?', ABC Radio Perth, February 10 2020 <<https://www.abc.net.au/radio/perth/programs/focus/viruseconomy/11950740>>.

The tourism sector is also reeling from the travel bans put in the place by the Australian government, which have now been extended for a third week until February 22.<sup>12</sup> And these were straight off the back of Australia's disastrous bushfires in December and January. Comparing the two, the Australian Tourism Industry Council is clear in its expectation that the impact of COVID-19 will exceed that of the bushfires.<sup>13</sup> Over the past year Chinese holiday makers and those visiting friends and relatives (that is, excluding Chinese visitors for education and business purposes) totalled 948,000, spending \$4.3 billion.<sup>14</sup> This suggests the direct cost to the tourism industry is running at more than \$80 million a week. But the true number is almost certainly significantly higher. Now is peak season for Chinese visitors, coinciding with the Chinese New Year holiday and the start of the academic year. Total Chinese visitor arrivals in February is typically double that of the average month. And then there are multiplied effects on the broader economy as tourism operators cut staff and other expenditure in response to the collapse in demand. A multiplier of two is standard, implying that the total cost to the Australia economy stemming from the tourism sector alone could easily exceed \$300 million a week.

The tourism industry will also face challenges bouncing back to normal operations once the virus spread in China is contained and the travel bans in Australia are removed. This is because the infrastructure that supports tourism links between Australia and China is being dismantled. Previously, there were 164 direct flights a week. This has now been reduced to just 20. One industry expert expects that even by August only 58 inbound flights would be operating and many from second tier cities are unlikely to return.<sup>15</sup>

Education is another sector acutely feeling the effects. Chinese visitors for education purposes over the past year totalled 260,000, spending \$7.1 billion. For some leading universities fees from Chinese students account for one-quarter of total revenues. Just as tourism operators have begun cutting staff and other expenditure, there are already reports of universities doing likewise.<sup>16</sup> Accordingly to federal government data, 56 percent of Chinese students with a valid visa are currently outside Australia, the overwhelming majority in China and so are affected by the travel ban.<sup>17</sup> There are anecdotal reports that some of these may be able to enter Australia via spending a 14-day quarantine period in a third country. Still, universities are scrambling to put in place flexible learning arrangements, including online delivery and flexible semester start times.<sup>18</sup> They are also frustrated by the Australian government, which in addition to travel bans, has stopped processing visas for students applying from China.<sup>19</sup> A survey of Chinese students in China found nearly one-third would enrol in another country if they were prevented from studying in Australia in the first semester of this year.<sup>20</sup> Australia's two biggest education competitors, the UK and Canada, have not put in place travel bans. Other countries, like Singapore, have a travel ban but exempt Chinese holders of a student visa.<sup>21</sup>

## Over the near-term horizon

What is being experienced is a classic, albeit extreme, negative demand shock. The economic complementarities between Australia and China remain as they were before the COVID-19 outbreak. China's stock of wealth and purchasing power also hasn't disappeared, even if it's being temporarily held back. This reinforces the conclusion that while the outlook for Australia in the first quarter from COVID-19 is sharply

- 12 ABC News, 'Coronavirus travel ban extended to 'keep Australians safe', Peter Dutton insists amid Chinese 'dissatisfaction', February 14 2020 <<https://www.abc.net.au/news/2020-02-14/peter-dutton-defends-government-extending-china-travel-ban/11964916>>.
- 13 Robyn Ironside, 'Coronavirus: Beijing goes early on plane ban extension', *The Australian*, February 13 2020 <<https://www.theaustralian.com.au/business/aviation/coronavirus-beijing-goes-early-on-plane-ban-extension/news-story/8b0b72ae26b531f1da9db32bacf57fda>>.
- 14 Tourism Research Australia, 'Latest international visitor survey (IVS) results', <<https://www.ra.gov.au/International/International-tourism-results/overview>>.
- 15 Robyn Ironside, 'Coronavirus: Beijing goes early on plane ban extension', *The Australian*, February 13 2020 <<https://www.theaustralian.com.au/business/aviation/coronavirus-beijing-goes-early-on-plane-ban-extension/news-story/8b0b72ae26b531f1da9db32bacf57fda>>.
- 16 Alison Xiao, 'University of Wollongong clamps down on spending after coronavirus damages enrolment', ABC News, February 14 2020 <<https://www.abc.net.au/news/2020-02-14/coronavirus-causes-sydney-uni-spending-reduction/11962812>>.
- 17 Australian Government Department of Education, Skills and Employment, 'Novel coronavirus (2019-nCoV)', February 14 2020 <<https://internationaleducation.gov.au/News/Latest-News/Pages/Novel-coronavirus-update-for-international-students.aspx>>.
- 18 Jason Fang, Iris Zhao, 'Coronavirus ban sees students head for third countries to see out quarantine period', ABC News, February 12 2020 <<https://www.abc.net.au/news/2020-02-12/coronavirus-international-students-travel-through-third-country/11954618>>.
- 19 Tim Dodd, 'Home Affairs halts new visas for Chinese students', *The Australian*, February 11 2020 <<https://www.theaustralian.com.au/higher-education/home-affairs-halts-new-visas-for-chinese-students/news-story/f21fc6672beef8e7268a4dfa46c38bf0>>.
- 20 Tim Dodd, 'Coronavirus: travel ban risks exodus of Chinese students', *The Australian*, February 13 <<https://www.theaustralian.com.au/nation/coronavirus-pm-likely-to-extend-china-travel-ban-after-national-security-committee-of-cabinet-meeting/news-story/492f4f6c593856e6a9889f4ad3cd9dba>>.
- 21 Sher Asaf, 'Countries ban recent travellers from China over coronavirus fears', *Business Traveller*, February 4 2020 <<https://www.businesstraveller.com/business-travel/2020/02/04/countries-ban-recent-travellers-from-china-over-coronavirus-fears/>>.

negative, a rebound can be expected in the second half of the year as the fundamentals of the economic relationship reassert themselves.

In fact, it's even possible to see a silver lining. The COVID-19 outbreak will once again raise doubts amongst China's rapidly growing middle class over food safety issues and the effectiveness of the country's health and broader governance system. Australia's high living standards and 'clean and green' reputation positions it nicely to capitalise.

*Professor James Laurenceson is Director of the Australia-China Relations Institute at the University of Technology Sydney.*