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Economic Insights:
Economic Resilience in Action Now

Key takeaways

- In the face of a global recession, the framework of economic resilience allows us to understand the ability of countries to absorb shocks
- With none of the Eurozone G7 countries in the top ten most resilient economies, the Euro Area is more exposed to shocks than the US. Global policy coordination is now vital in reinforcing global resilience
- Policy makers will need to resort to unorthodox measures, with the subsequent recovery likely prolonged due to weaker structural economic factors to begin with
- Resilience, among other things, stems from monetary and fiscal space. Countries with weaker balance sheets experience deeper and longer recessions, followed by more protracted recoveries

About Economic Insights
Analysis of key economic developments and their implications for the global re/insurance industry.

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In a nutshell

COVID-19 is putting economic activity and resilience under pressure around the world, raising a key question: where do policy makers and the economy go from here? We believe that now more than ever, a coordinated policy response is essential given the weaker global economic resilience to begin with, combined with the uncertainty surrounding today's economic shock.

The coronavirus outbreak represents a sudden shock to the global economy, affecting supply, demand and financial conditions. Global growth was already weakened going into 2020, and we expect a global recession as a result of the shock[1]. The recession is still expected to be mild in a historical context, but the extent of it is highly dependent on the evolution of the outbreak, the subsequent containment measures and vigour in taking a coordinated policy response.

The coronavirus outbreak is a global test of macro economic resilience. Our SRI – LSE Macroeconomic Resilience Index[2] outlines an economy's ability to absorb shocks. As previously noted, we believe the global economy is less resilient to shocks than in 2007[3]. This is largely due to virtually exhausted monetary policy and often constrained fiscal space in advanced economies. This matters because countries with weaker balance sheets – such as several of the Eurozone countries[4] – experience recessions that are roughly twice as deep and two times as long, with the recoveries about a third as strong as is the case for countries with stronger balance sheets. Understanding the composition of buffers available to an economy is key to comprehend how best to address shocks. While the Eurozone is economically less resilient than the US, European countries are currently more exposed to the spread of the coronavirus. We believe global policy coordination is now vital in reinforcing country level resilience in the face of the ongoing shock – something that is being considered for the first time since the Global Financial Crisis.

In the context of our resilience index, relaxing monetary and fiscal policies results in a lower ability to stimulate economies in potential subsequent downturns. We therefore think that policy coordination needs to be strengthened, which should happen on two levels at this point in time: across G7 countries, and between monetary and fiscal policy makers. New growth recipes are needed to reach higher sustainable growth rates, and these should cease to rely solely on monetary policy. Fiscal policy can be a

[1] See Economic and financial risk insights – Global recession is testing economic resilience, Swiss Re Institute.
[2] See *sigma* 5/2019 – Indexing resilience: a primer for insurance markets and economies, Swiss Re Institute.
[3] See *sigma* 6/2019 – Sustaining resilience amid slowing growth: global economic and insurance outlook 2020/21, Swiss Re Institute.
[4] *Public Sector Balance Sheet Strength and the Macro Economy*, IMF Working Paper, 2019.

substantial driver of economic growth, particularly when backed by cooperating central banks. In a benign case, the cooperation could enhance the fiscal multiplier 2-3x relative to normal times. Key is that the delivered stimulus increases the productive capacity of an economy[5]. This would provide the additional benefit of strengthening future economic resilience through higher and more sustainable growth rates.

Beyond the real economy, concerns surrounding COVID-19 have also translated into a substantial flight to quality in the financial markets with stock prices falling and corporate spreads widening, while government yields declined. The lack of market response to the Fed's decision to ease monetary policy further emphasises the need for policy coordination. Monetary policy alone cannot prevent a negative feedback loop of the tightening in financial conditions onto the global economy.

Figure 1
The five most resilient countries in 2018

Country	Rank
Switzerland	1
Canada	2
USA	3
Finland	4
Norway	5

The SRI-LSE Macroeconomic Resilience Index
The index is composed of nine components categorized into two overarching dimensions:

1) *Macro buffer components* – considers an economy's room to use monetary and fiscal policy
2) *Structural components* – considers the fundamental framework of an economy, such as access to talent, the banking industry backdrop, economic diversification, etc

Source: Swiss Re Institute - London School of Economics Macroeconomic Resilience Index

Looking ahead and despite the expected global stimulus, we don't expect a "V"-shaped economic recovery. Instead, we expect a protracted growth path part due to the relatively low levels of available buffers to major economies. In fact, within the Eurozone, only Finland and the Netherlands are in the top ten most resilient economies and there is a substantial gap between "core" and "peripheral" economies' resilience levels. For the Asia Pacific region, only Japan is in the top 10 and the region's aggregate resilience score is roughly the same as for the Eurozone.

[5] For more information please refer to the *sigma* 6/2019

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