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ECONOTE No 90: Epidemic controls, climate change policies and some lessons for Asia and the world 8/3/2020

Summary	Investment Conclusions
A morbid definition of epidemics is that “they are the perfect capitalist weapon-they kill people but leave physical capital undamaged”. There is the added issue that the duration and extent of infection is very difficult to forecast and, hence, forecasts of the expected damage will be unreliable. The cost of epidemics can be divided to: (A) Domestic : direct disruption costs plus human losses in countries with strong infection focuses and (B) Collateral damage in countries with little domestic infection but affected by local and global economic and financial disruptions. likely N.B. There are links between climate and epidemic control policies with important lessons.	China and Hong Kong, and to a lesser degree, S.Korea will be impacted <u>domestically</u> , with most other Asian economies suffering likely modest, <u>collateral</u> damage. The China-related supply chain disruptions could recover faster than the purely domestic disruptions, such as drop in retail sales. Asian economies with low export dependency, such as India, will suffer less while economies with tourist sectors, such as Thailand will feel more the <u>collateral</u> damage. There is reason to believe that the decline and upturn V- shaped GDP movements could be relatively short lasting.

The evidence so far

Given the warning that forecasting GDP movements on the basis of epidemic dynamics is a fool's game, we employ here instead three simple criteria to help judge the likely extent of the domestic and collateral damage. **FIRST**: Economies with pre-existing cyclical downturns could be hit harder than those in the cusp of, or on an actual upturn. This group contains predominantly Hong Kong, India, Malaysia, and to a lesser extent, China whose growth deceleration has been slow but persistent. The second group with accelerating economies contains Taiwan, S.Korea and Philippines, with the Singapore, Indonesia and possibly Thailand classified as “neutral” (Fig. 1). **SECOND**: The extent to which these economies are integrated in the supply chain originating in China, the latter being, for now, one the most affected of all the Asian economies. So, for example, based on 2015 data (Bloomberg) in S.Korea 38.0% of all its imports of intermediate products came from China followed by Thailand with 31.0% all the way to the Philippines with 26.0%. The higher the percentage the stronger the likely impact of the disruption from

China. The **THIRD** criterion includes a variety of country-specific characteristics such as the importance of tourism where in Thailand it accounts for 20.0% of GDP with 25.0% of tourists coming from China. In Hong Kong the percent is about 4.0 with nearly 70.0% of all tourists coming from China. Criteria Two and Three are supposed to modify and recalibrate the GDP cyclical measurements (Fig.1) but the cyclical ranking seem reasonable for now.

Fig 1: Asia GDP growth yoy % 2019

	1Q.19	2Q.19	3Q.19	4Q.19	1Q.20
PRC	6.4	6.2	6.0	6.0	-
HK	0.7	0.4	-2.8	-2.9	-
Taiwan	1.8	2.6	3.0	3.3	-
S.Korea	1.7	2.0	2.0	2.3	-
Sing.	1.0	0.2	0.7	1.0	-
India	5.8	5.6	5.1	4.7	-
Thailand	2.9	2.4	2.6	1.6	-
Malaysia	4.5	4.9	4.4	3.6	-
Indo.	5.1	5.1	5.0	5.0	-
Phil.	5.6	5.5	6.0	6.4	-

Green:bottoming,accelerating,Red:decelerating ,Black neutral.(Bloomberg)

Climate crisis and epidemics: Mirror images ?

In the last two weeks two important climate control events passed unnoticed under the avalanche of the Covid-19 threat. (a) President Trump dismissed the likely economic costs to the US economy contained in the 4th National Climate Assessment and (b) The EU tabled legislation to make the EU economies, bar Poland, carbon neutral by 2050. These events give an opportunity to focus to the similarities between the policies controlling epidemics and those controlling climate changes. In Economics a “public good” is not a good whose use cannot be excluded to anyone in the economy nor its availability drops if more than one person uses it, and whose benefits can be enjoyed without paying for it. Equally a “public bad” refers to a good whose use generates costs that the user does not pay for, and which cannot be avoided by non-users. The links between controlling pollution and climate change and controlling the spread of infection can now

FACTBOX: The cost of SARS (2003) to HK and China

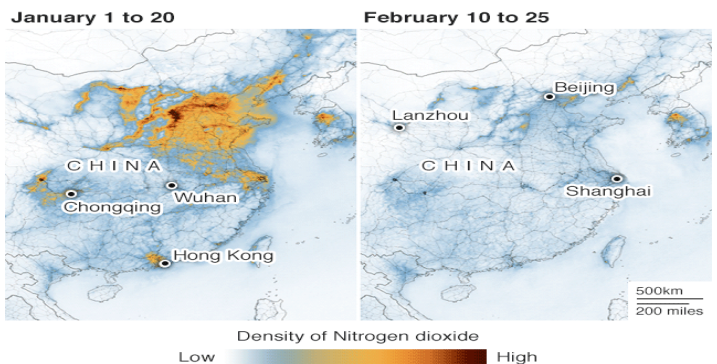
The 2003 SARS impact on **Hong Kong** was almost imperceptible with quarterly yoy% GDP growth as follows: 1Q.03 3.9%, **2Q.03 -0.6%**, 3Q.03 4.0% and 4Q.03 4.7%. The annual GDP growth rates were even more impressive: 2002 4.1%, 2003 4.7% and 2004 8.3%. The data for **China** are equally surprising. The GDP growth, yoy, for 2003 was: 1Q 11.1%, **2Q 9.1%**, 3Q 10.0% and 4Q 10.0%. The annual rates were for 2002 9.1%, 2003 10.0% and 2004 10.1%. **Important caveat.** The very mild impact of the 2003 SARS on the economies of China and of Hong Kong is by no means a guide as to what will be the 2020 impact of Covid-19 as the size and spread of the infection was much larger in China as well as the extent of the disruption. Covid-19 hit Hong Kong after 6 months of unprecedented political disruption as well as an economy, which was already decelerating since the start of 2018.
Source: Bloomberg

be placed on a parallel basis. The rapid expansion of Covid-19 resulted to rapid reactions by state authorities in quarantining suspected or actual cases of infection, controlling movements within national frontiers and restricting or stopping altogether activities such education, sports and entertainment. State action was taken with no public discussion or approval. All this is in sharp contrast to policies limiting pollution and climate change that frequently meet strong opposition. In the case of epidemics, using “public goods” to spread the benefits of limiting infection are easily and, mostly, immediately acceptable. Vaccination prevents infection to the person receiving it but also stops infection spreading to other unrelated people who have not contributed to the cost or even know of the vaccination. The difference in the degree of resistance to policy measures controlling infection and controlling climate change reflects the size of the expected personal benefits or costs and difference in their time dimension. .

Fig.2 Cruel but true, epidemics as an effective instrument of climate control

Satellite images show pollution clear amid slowdown

Nitrogen dioxide levels in the lower atmosphere



Source: BBC

The time dimension premium or cost can be crudely summarized as “Stay alive and healthy now, enjoy better climate by 2050”!

Conclusions: Nothing new under the sun in Asia

(1)The spread and duration of the Covid-19 is unpredictable but its impact is understood and partially measurable but dependent on its unpredictable duration. (2) As the main impact is disruptive than destructive, the recovery pattern may well be “V shaped” that is sharp and fast.(3) Asian economies which were on the upturn of their cycle, such as Taiwan and Philippines may experience lower costs than economies such as Hong Kong which were hit three times by a cyclical downturn, political turmoil and an epidemic .(4) Much more obvious conclusions will include that the less export dependent is an economy the lesser the impact (India) and the more supply-chain-connected (S.Korea) the worse the impact. (5) The SARS impact experience (overall very mild) is not a guide as the Covid-19 is now global and far more disruptive (6) The intervention by central banks by cutting rates could help the financial markets but will have little impact on GDP growth as that will depend on the elimination of the supply disruption and on consumers resuming their spending.(7) Fiscal policies in terms of additional government spending will be far more effective.In that respect the HK government has given a lead with direct cash handouts to all HK citizens and to targetted businesses. (8) Draconian measure when it comes to climate control can work, as is shown in Fig.2. Slow down the economy and pollution disappears ! Lastly, the epidemic has shown the extent of global links and the fact that **individual** action by states to limit infection can work.This sets a hugely important example for the coordination of climate change policies **where individual action can be as important as joint action.**“America or XX country first” clearly does not work in epidemic control and does not work either in climate change control.