

**The economic
consequences of
re-containment on the
French economy**

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The economic consequences of re-containment

The second wave of the COVID-19 epidemic which has affected, since the end of October 2020, a large part of Europe as well as the decision taken by the French government, following many other European governments, to re-confine the country from of October 30th, will have significant economic consequences. Even if the rules for this new lockdown are a little less strict than during the former one which lasted from March to May 2020, the economic impact will nonetheless be significant. It will add to the difficulties facing the French economy today. This impact will not be limited to lockdown immediate effects. It will translate into a sharp rise in uncertainty among households and businesses, an uncertainty that is expected to persist until the epidemic is effectively controlled. This uncertainty will profoundly affect the recovery trajectory of the economy until 2024.

0. How to assess the economic consequences of confinement

The question of how these economic consequences can be understood is a complex one. In October 2020 in France there was a debate on the consequences of the first confinement between the evaluations done by the government, which estimated the cost for growth at 9%, and the IMF, which evaluated this cost at around 10%¹. The difference may seem small, but it represents nevertheless a disagreement of around 10% on the economic consequences. The author of the study presented on the IMF blog also specified: "*The divergence in income prospects between advanced economies and emerging and developing economies (excluding China) triggered by this pandemic is projected to worsen. We are upgrading our forecast for advanced economies for 2020 to -5.8 percent, followed by a rebound in growth to 3.9 percent in 2021.*"² She also signaled that the pandemic would leave significant traces in the economies of countries that had been affected, traces whose effect would be felt for many years to come: "*This crisis will likely leave scars well into the medium term as labor markets take time to heal, investment is held back by uncertainty and balance sheet problems, and lost schooling impairs human capital. After the rebound in 2021, global growth is expected to gradually slow to about 3.5 percent into the medium term. The cumulative loss in output relative to the pre-pandemic projected path is projected to grow from 11 trillion over 2020–21 to 28 trillion over 2020–25. This represents a severe setback to the improvement in average living standards across all country groups.*"³

This shows that the economic consequences will not end with the immediate consequences. It is therefore necessary here to specify the nature of these economic consequences.

- First of all we have the immediate consequences, which stem from the administrative measures concerning the closure of economic activities, which are taken by the government. In the case of France, these measures stem from "*Decree n ° 2020-1310 of October 29, 2020 prescribing the general measures necessary to deal with the epidemic of covid-19 within the framework of the state of health emergency*"⁴. This

¹ Gopinath G., « A long uneven and uncertain ascent », in *IMF Blog*, Washington D.C., 13 octobre 2020, <https://blogs.imf.org/2020/10/13/a-long-uneven-and-uncertain-ascent/>

² Gopinath G., « A long uneven and uncertain ascent », op.cit..

³ Idem.

⁴ <https://www.legifrance.gouv.fr/jorf/id/JORFTEXT000042475143>

decree specifies, in its articles 37, 38, 39, 40 and 41, the authorized and prohibited economic and commercial activities. Thus, nearly 200,000 businesses considered "non-essential" were closed by this decree. The immediate consequences are therefore easily measurable, and they are proportional to the duration of the confinement. At the moment, the lockdown is only scheduled for 4 weeks, but it could be extended for 6 or even 8 weeks.

- These immediate consequences do not exhaust the question of economic consequences. So we also have the indirect consequences, which stem from the effects induced by the epidemic. Thus, when a company is authorized to work but its activity is durably affected by the implementation of health protocols, or its activity is compromised because that of its subcontractors is affected or made impossible by the epidemic, we are in the presence of indirect consequences. Observation of what happened during the first containment suggests that the indirect consequences are often underestimated.

- Finally, there are the consequences of confinement. The latter then include the effects of the uncertainty linked to the evolution of the epidemic, which weighs on businesses and households, as G. Gopinath says, but also the impact of the restructuring of consumption due to the loss of income induced by confinement. Other factors are also weighting like the effects linked to irreversible situations caused by confinement (business bankruptcies), cumulative losses in the education sector, and finally the impact of the general disorganization of society induced by this epidemic. These consequences will affect the rate of recovery of the economy after the lockdown episode. If the latter has been compared to Snow White falling asleep after biting the poisoned apple, economy's awakening lasts for a much longer period of time. The International Monetary Fund estimated that the French economy would not have recovered from the shock of the first confinement, that is to say would have regained its level of GDP in 2019, only after 2022. Thus, while the direct and indirect consequences of the containment were estimated by the IMF at 9.8% of 2019 GDP, the total losses until 2022 were assumed to amount to 14.4% of 2019 GDP, indicating that the induced losses could represent up to 47 % of direct and indirect losses.

These figures indicate the potential magnitude of the consequences of a containment of the economy. They require to not focusing on to the year in which this event took place, but to consider, on the contrary, all the effects induced over several years. The analysis of the economic consequences of containment must therefore necessarily take into account the recovery trajectory of the economy after this episode. It is in this trajectory that the induced consequences are felt, which makes it possible to distinguish them from the direct and indirect consequences.

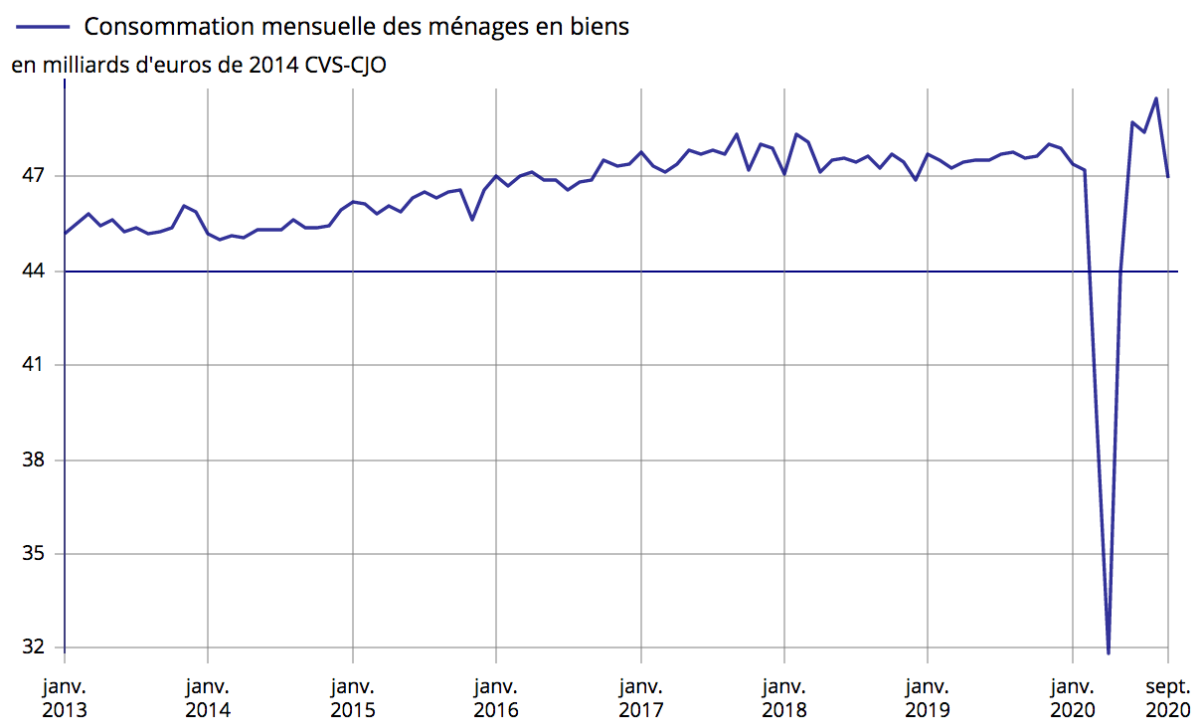
This distinction between direct, indirect and induced consequences can then make it possible to deal with the problem of the economic consequences of containment. It then explains the fact that the first estimates tend to be overly optimistic.

I. State of the situation as of October 30

Mr Bruno Le Maire, the French Minister of the Economy and Finance, therefore declared on October 30 that, following the first confinement, and as part of the effects of the

second, the French economy would experience a decline in its GDP of 11%⁵. He said, in the first days of September, and under the probably false feeling of safety coming from a relatively strong recovery in activity from June, that he estimated the decline at -9%. It should be noted that this forecast is slightly more optimistic than the one we made, and which placed this decline between -10% and -12%⁶. It should also be noted that the IMF estimated at the beginning of October the magnitude of this decline in GDP at -9.8%⁷. However, from the end of October, and based on the figures for September 2020, INSEE warned that the recovery would be significantly less dynamic than the figures observed immediately after the end of the first lockdown.

Graph 1
Monthly goods consumption in euros Billion, 2014 prices



Source: INSEE

Several economic indicators, however, showed that economic activity, after the rebound in June and July, was showing signs of a slowdown. This slowdown only reflected the progressive impact of the consequences of the first confinement.

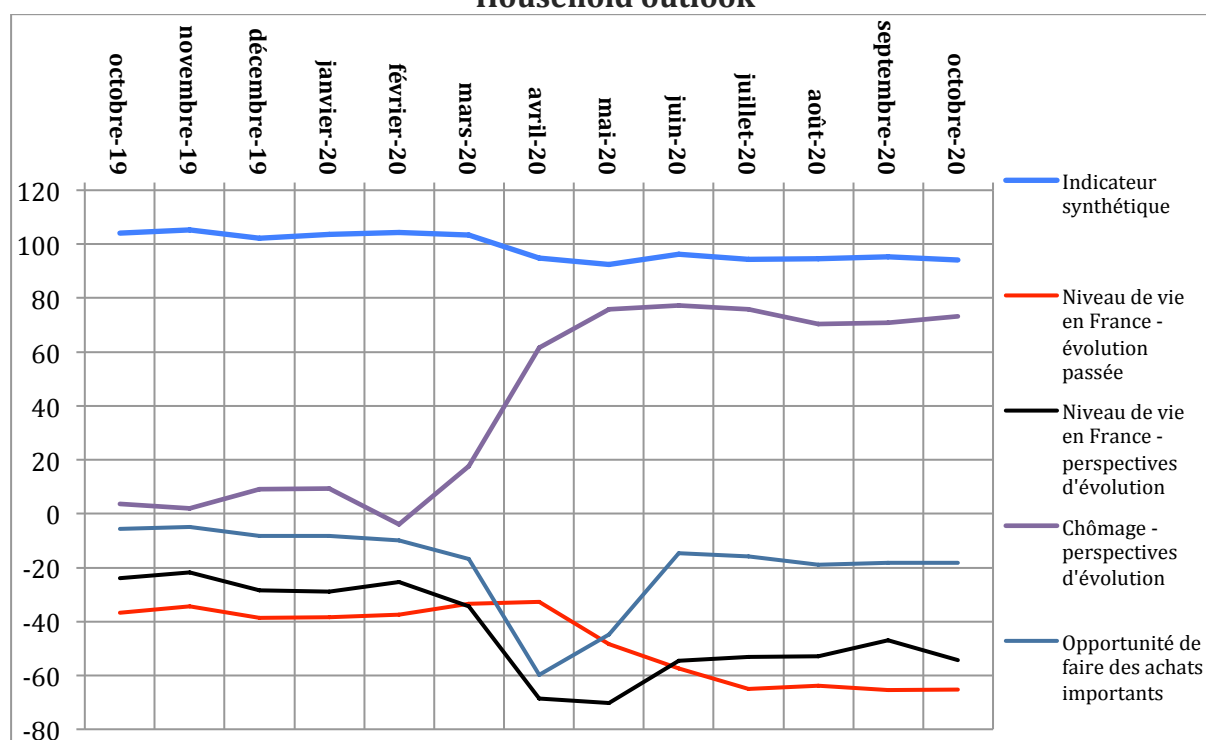
At the beginning of October, household confidence in the economic situation fell slightly again: the indicator that synthesizes it then lost one point when compared to September. At 94, it was back to its July and August level and remained significantly below its long run average.

⁵ <https://www.lopinion.fr/edition/economie/pib-francais-devrait-se-contracter-11-en-2020-227896>

⁶ Sapir J., « Would the lock-down induced economic contraction be a prelude to a major depression? » in *Ekonomika i Matematicheskiye Metody* [Economic and Mathematical Methods], 56 (3), pp. 5-25.

⁷ IMF, *World Economic Outlook*, Washington DC, October 2020.

Graph 2
Household outlook



Source: INSEE

The slowdown, however, mainly affected the service sector. In October 2020, the balance of opinion on the general outlook for the sector's activity fell again and therefore remained well below its average level. Business leaders were much more pessimistic than the previous month about their own outlook for the next three months: balances on expected activity and expected demand falling and further deviating from their average.

Overall, however, business leaders reported that their turnover has increased over the past three months: the balance of opinion on past activity continues to rebound and exceeds its long-run average. This was proof that consumption had resumed strongly in the weeks immediately following the 1st lockdown. But these same business leaders reported in the INSEE survey that demand expectations were falling⁸. This confirmed that the rebound after the 1st containment was already running out of steam for various reasons but which can generally be classified in the category of the consequences induced by the containment. Such sectoral study as done by the French statistics institution is of some use as it enables to see undercurrents running behind the surface of rough data.

Regarding employment, the balance of opinion on the workforce over the past three months increased slightly but remained below its average. The one on the planned numbers fell back, well below its previous number. All this then combined to lead to a negative outlook for the service sector. Here again we get the distinct feeling that after two or three months of fast improvements coming after the end of the 1st lockdown, the economic was again degrading, well before to have reached it 2019 level.

Table 1

⁸ <https://www.insee.fr/fr/statistiques/4808217>

Latest World Economic Outlook Growth Projections

(real GDP, annual percent change)	PROJECTIONS		
	2019	2020	2021
World Output	2.8	-4.4	5.2
Advanced Economies	1.7	-5.8	3.9
United States	2.2	-4.3	3.1
Euro Area	1.3	-8.3	5.2
Germany	0.6	-6.0	4.2
France	1.5	-9.8	6.0
Italy	0.3	-10.6	5.2
Spain	2.0	-12.8	7.2
Japan	0.7	-5.3	2.3
United Kingdom	1.5	-9.8	5.9
Canada	1.7	-7.1	5.2
Other Advanced Economies	1.7	-3.8	3.6
Emerging Markets and Developing Economies	3.7	-3.3	6.0
Emerging and Developing Asia	5.5	-1.7	8.0
China	6.1	1.9	8.2
India	4.2	-10.3	8.8
ASEAN-5	4.9	-3.4	6.2
Emerging and Developing Europe	2.1	-4.6	3.9
Russia	1.3	-4.1	2.8
Latin America and the Caribbean	0.0	-8.1	3.6
Brazil	1.1	-5.8	2.8
Mexico	-0.3	-9.0	3.5
Middle East and Central Asia	1.4	-4.1	3.0
Saudi Arabia	0.3	-5.4	3.1
Sub-Saharan Africa	3.2	-3.0	3.1
Nigeria	2.2	-4.3	1.7
South Africa	0.2	-8.0	3.0
Low-Income Developing Countries	5.3	-1.2	4.9

Source: IMF, *World Economic Outlook*, October 2020

For India, data and forecasts are presented on a fiscal year basis, with FY 2020/21 starting in April 2020. India's growth is -8.6 percent in 2020 and 6.8 percent in 2021 based on the calendar year.

However, these services excluded those related to tourism (hotel / catering), a sector that had particularly suffered from the impact of the epidemic and where the return to normal, despite the peak of seasonal activity for the month August was chaotic.

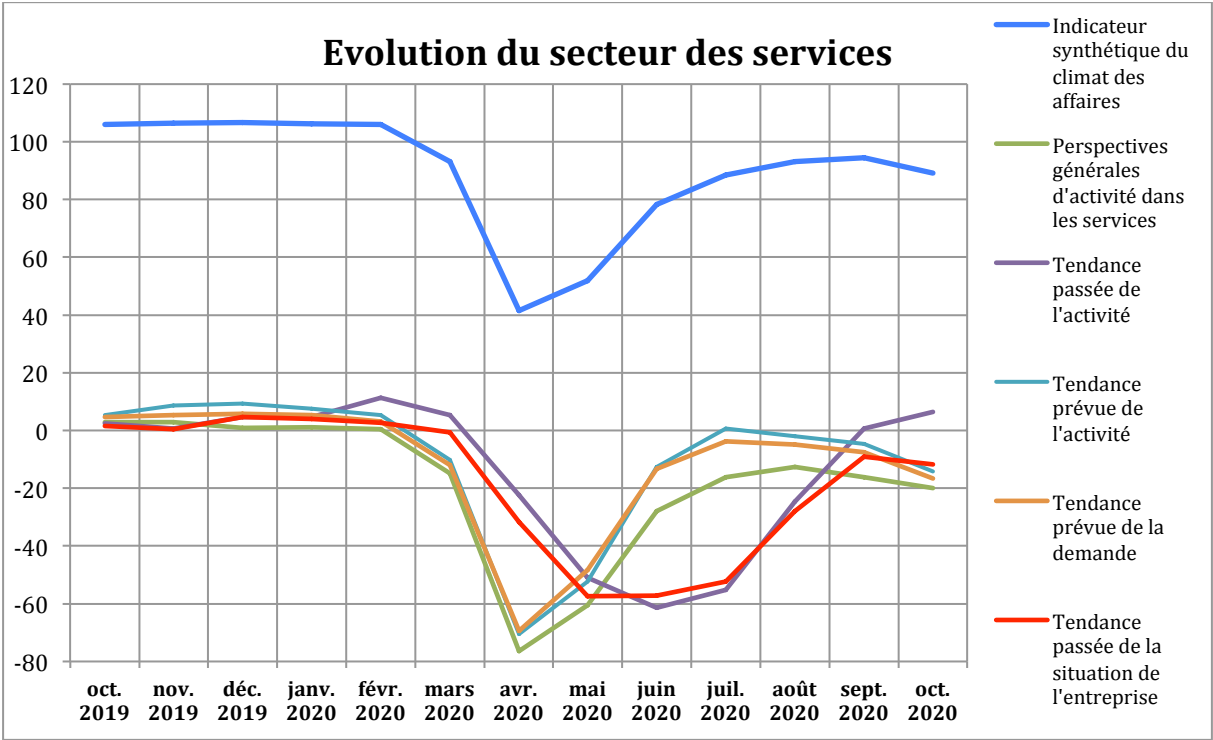
Table 2
Composition of the service sector

4941A	Interurban freight transport by road
4941B	Local freight transport by road
4941C	Truck rental with driver
5229A	Courier, express freight
5320Z	Other post and courier activities

(Source: INSEE)

The combination of data on services and data on households actually painted a relatively bleak picture of the French economy (graph 3) on the eve of being hit by the second wave of the epidemic. Very clearly, the French economy had not returned to the situation of 2019 and the resumption of activity was taking place at a slower pace than expected and hoped for from the month of August 2020.

Graph 3
Services sector evolution



Source: INSEE

This general situation already made the official forecasts, at the beginning of October 2020, not very credible. The forecasts made by the IMF in October 2020 therefore reflected this concern that one might have about the pace of the return to normal. The 4th quarter could be expected to be - at best - disappointing. It is therefore in this context that the 2nd confinement occurred, imposed by the very strong upsurge in the COVID-19 epidemic.

II - What new confinement for what impact?

The new containment is therefore not an exact replica of the first, far from it. It is currently scheduled for a month. But, it is highly likely that it will be extended for 6 weeks or even two months.

Schools, colleges and high schools should remain open, although the conditions for receiving students may vary⁹, and many businesses too. The most immediately binding measures concern catering, events, sports-related activities, small shops that are not "essential". In terms of direct activity, the impact should therefore be weaker, even if the months of November and December concentrate a large part of the purchases. However, the French had not resumed their usual volume of consumption after the 1st confinement. The volume of purchases that will again be delayed or even cancelled, will be significant. This naturally will translate into a drop in production when it comes to goods, and a loss of activity when it comes to services. To the direct impact, linked to the drop in turnover of businesses and businesses closed by administrative decision, it will therefore be necessary to add products that will not be manufactured due to lack of demand. In the newspaper *Les Echos*¹⁰, economists estimated the cost of this new confinement, if it was limited to 4 weeks, at 5% of the GDP produced in the 4th quarter of 2020. Overall, this should amount to just fewer than 2% of annual GDP (given the size of Q4 GDP).

But, this does not take into account the medium-term effects generated by this new confinement, whether it is indirect effects and induced effects. Indeed, this new confinement adds to the effects of the first the effect of generalized uncertainty. Economic actors, and a large part of the population, might have thought that the first confinement, as painful as it was, would be unique. The second lockdown implicitly poses the threat of more such episodes. The uncertainty generated by this 2nd wave, of which no one can say if it will not be followed by a 3rd next spring, will put a halt to the main investment projects of companies, and push households to suspend their investments projects. Private investment, whether by businesses or households, will be the first victim of this uncertainty. However, without investment, there will be no real recovery in 2021 and 2022. We must therefore, to consider the trajectory of the French economy in the coming years, formulate several hypotheses.

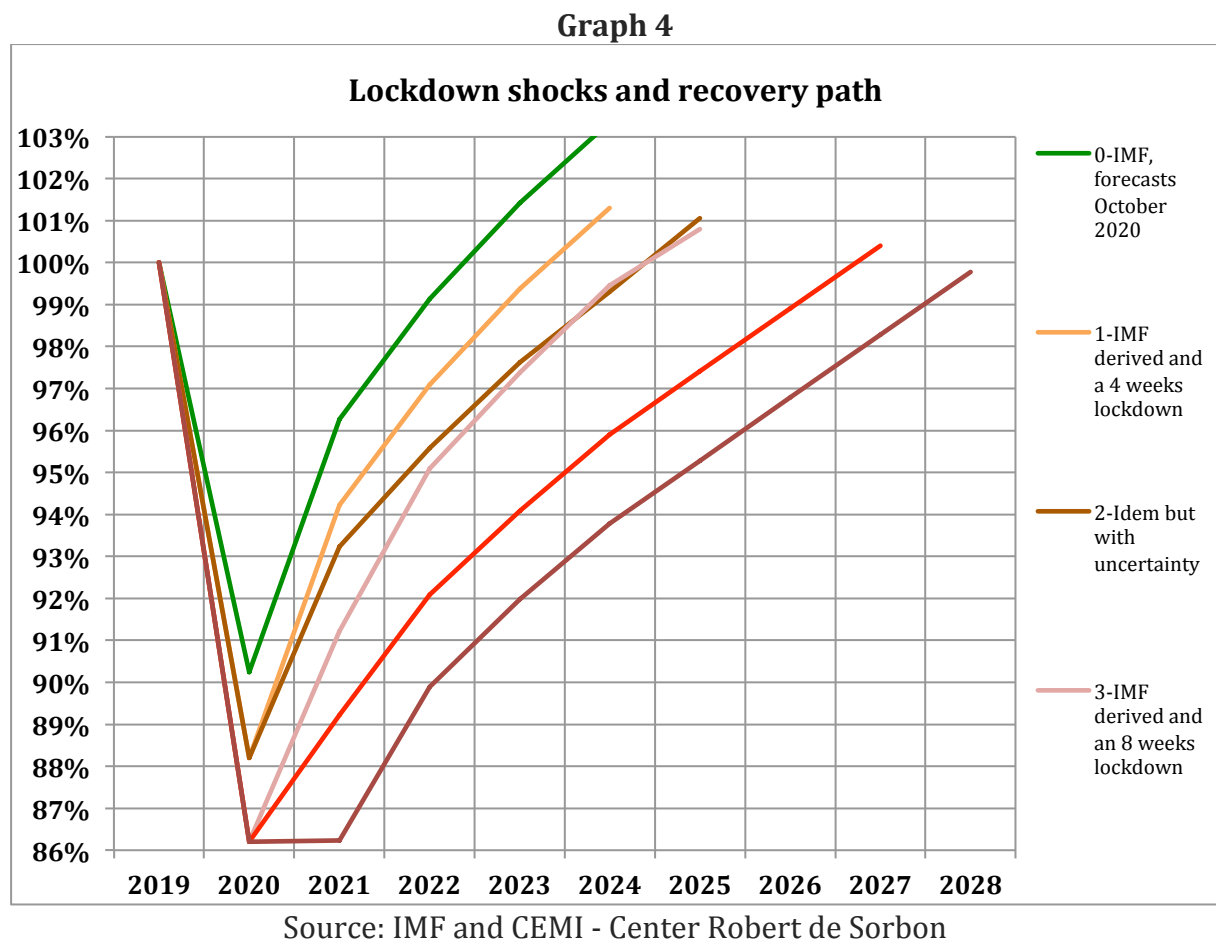
1. An "optimistic" hypothesis where the IMF's forecasts would simply be delayed by 2% due to the 2nd containment, and where the recovery would follow the trajectory estimated in October 2020.
2. An assumption retaining a moderate estimate of the impact of the 2nd confinement, but including the effect of the uncertainty generated by this 2nd confinement on the rate of return to normal.

⁹ <https://www.europe1.fr/societe/covid-19-blancq-annonce-un-protocole-sanitaire-renforce-au-lycee-4003679>

¹⁰ https://www.lesechos.fr/economie-france/conjoncture/covid-la-reprise-de-lepidemie-pourrait-faire-chuter-lactivite-de-5-en-fin-dannee-1260509#utm_source=newsletter&utm_medium=email&utm_campaign=re_8h&utm_content=20201030&utm_source=newsletter&utm_medium=email&utm_campaign=re_8h&utm_content=20201030

3. A "pessimistic" hypothesis where the IMF forecasts would this time be shifted by 4% due to a second longer confinement, and where the recovery would follow the trajectory estimated in October 2020.
4. An assumption with this estimate of the impact of the 2nd confinement at 4%, and also including the effect of the uncertainty generated by this 2nd confinement on the rate of return to normal.
5. A very pessimistic assumption including the effect of a possible 3rd lockdown and stagnation of the economy in 2021, then adding the effects of great uncertainty on the rate of return to normal.

These different assumptions are shown in graph 4, where the IMF's initial forecast (qualified as "0" assumption) is then used as a basis for measuring the additional effect of the 2nd containment.



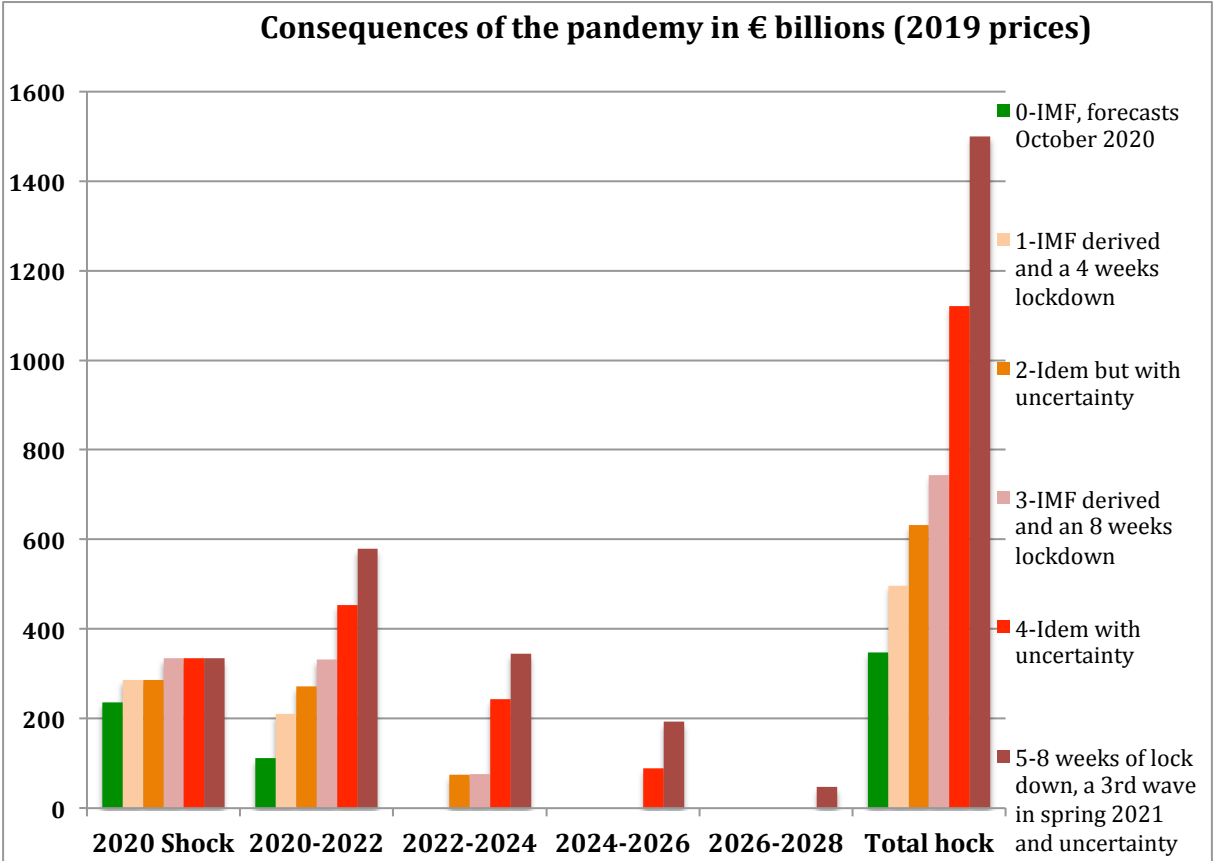
The first hypothesis can be called the optimistic one. It is implicitly grounded on the idea that the 2nd confinement would last only one month and that an effective and safe vaccine (or a treatment unanimously accepted) would appear towards the end of spring 2021. It appears today as weakly realistic. The second hypothesis, which includes the impact of uncertainty due to very moderately effective medical responses, leads to the same result as the third hypothesis, which differs only from the first in the duration of confinement. The French economy would not have returned to its 2019 level in 2024.

The 4th hypothesis, which also includes the impact of uncertainty, worsens the previous result. The French economy, in 2024, is far from returning to the level of 2019, and is between that of 2017 and 2018.

The 5th hypothesis, it includes a hypothetical 3rd wave which plunges the French economy more or less to the level where it was at the beginning of the years 2010. The Franc would not return to the level of production of 2019 until 2028. It is therefore, at the present time, the hypothesis of the "worst" that can occur. The economic impact can be measured by considering that, economically, in 2024 we would be at least 6 years back.

These assumptions imply different costs or economic consequences. The magnitude of the "induced consequences" varies greatly depending on the different hypotheses.

Graph 5



IMF and CEMI, Center Robert de Sorbon

The relationship between direct and indirect consequences and induced consequences appears to be strongly linked to the hypotheses formulated. The latter are also characterized by very different recovery times from the activity level of 2019. Thus, for the first 4 hypotheses, the French economy would have returned to its 2019 level in 2024 at the latest and even before for the most optimistic hypothesis. The impact on the ratio between direct and indirect consequences and induced consequences therefore fluctuates considerably depending on the total duration of the effects of confinements.

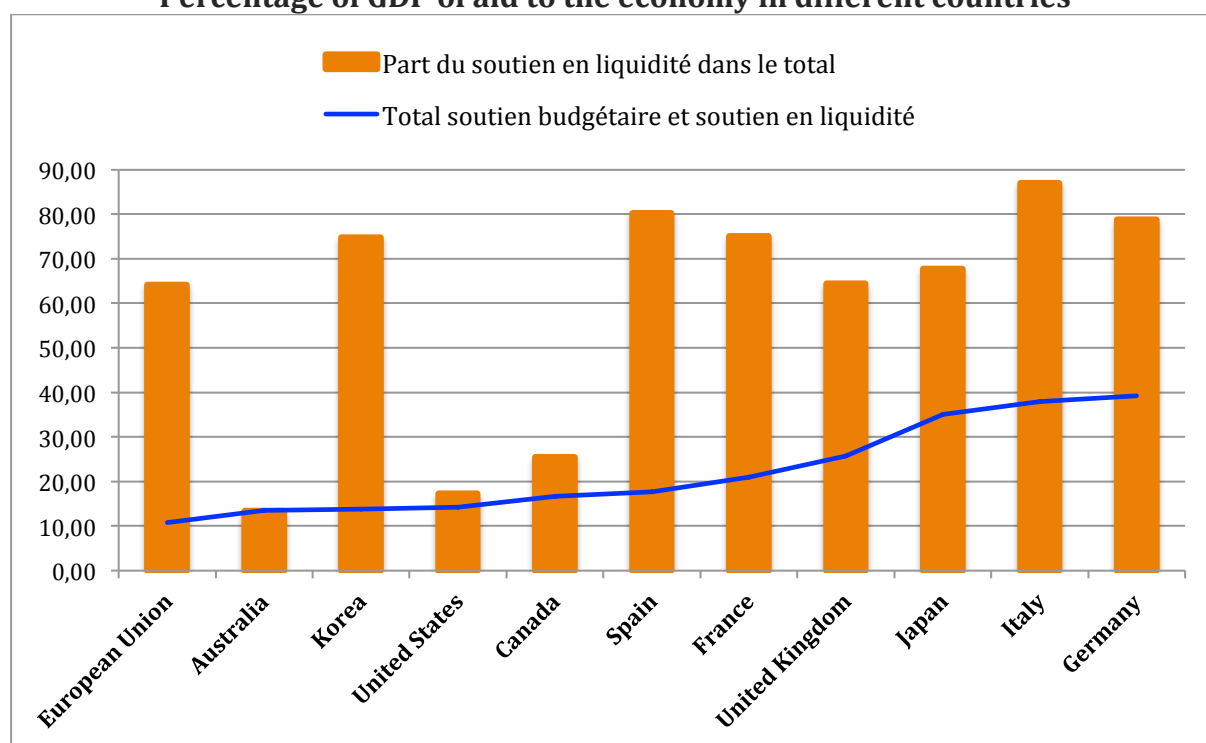
Table 3
Economic consequences of lockdowns in billions of euros at 2019 prices

	Direct and indirect consequences	Induced consequences	Induced consequences / direct and indirect consequences
IMF Forecast in October 2020	236,682	111,583	47,1%
IMF and Forecasts for 4-week containment	286,234	210,686	73,6%
Forecasts for a 4-week confinement and effect of uncertainty	286,234	345,681	120,8%
IMF and Forecast for 8-week containment	334,748	408,749	122,1%
Forecasts for an 8 week confinement and uncertainty	334,748	785,712	234,7%
Containment of 8 weeks and 3rd wave in spring	334,748	1164,473	347,9%

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In addition, the last three assumptions must also include a significant impact of confinements on banks. In fact, the policy of supporting the state economy in France mainly involves credit mechanisms. However, part of the loans guaranteed by the State will not be repaid in the situation that will develop following the 2nd lockdown. The situation of French banks will become difficult due to the massive rise in bad debts on their balance sheets.

Graph 6
Percentage of GDP of aid to the economy in different countries



Source: IMF, September 2020

However, France, like Italy, Germany or Spain, has supported its economy massively with guaranteed loans, the latter representing 75% of total support to the economy. Conversely, countries like the United States and Canada have mostly focused on budget support.

III. A significant impoverishment for France?

In terms of loss of wealth compared to the situation in mid-October, the 2nd confinement could have, depending on the hypotheses adopted, an impact that would go from the reasonable to the dramatic.

Table 4
Wealth losses (in% of 2019 GDP) additional to IMF assumptions

H	Assumption	Losses (2020)	Total losses
1	IMF transposed 4 weeks	2,0%	6,1%
2	IMF transposed 4 weeks and uncertainty effect	2,0%	11,7%
3	IMF transposed 8 weeks	4,0%	16,3%
4	IMF transposed 8 weeks and uncertainty	4,0%	31,8%
5	IMF transposed 8 weeks uncertainty and 3rd wave	4,0%	47,4%

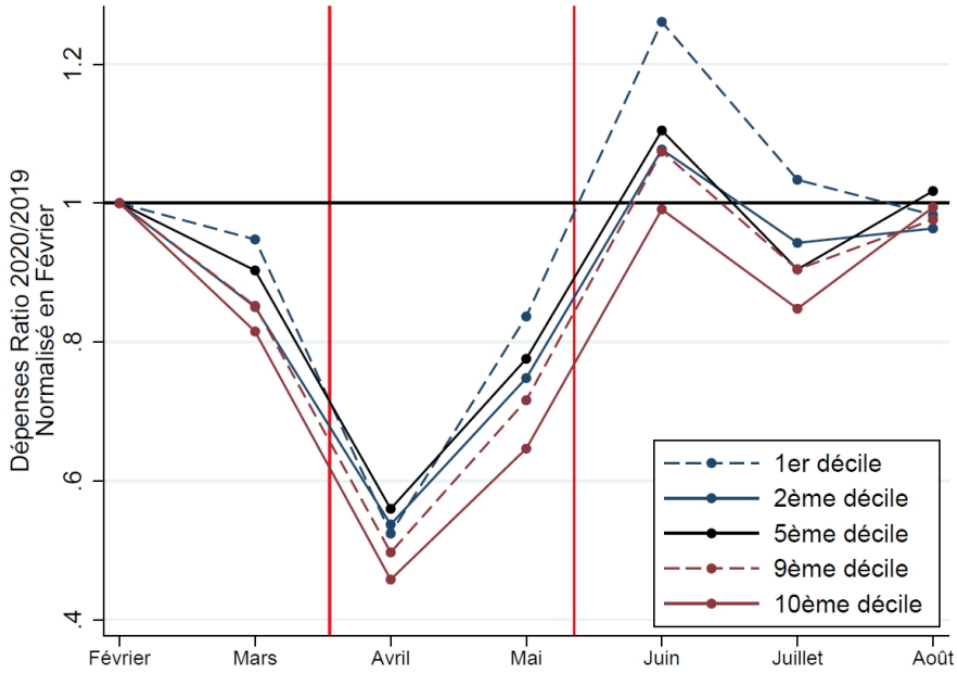
Two observations stand out. The first is that the introduction of uncertainty in an "optimistic" assumption (1 month of confinement) adds only a few additional losses compared to the basic assumption, which had been formulated by the IMF at the beginning of the month. October 2020. On the other hand, the losses of wealth rise rapidly in the "pessimistic" assumptions, and because of the losses induced by the duration of the confinement and because of the uncertainty. These additional losses obviously reach their maximum with hypothesis (5), and would then amount to 47.4% of GDP in 2019.

To these overall losses should then be added the additional expenses induced by the treatment of the probable banking crisis and those generated by all the pathologies associated with the sharp rise in unemployment which will inevitably occur.

On this last point, we must fear the cumulative effect on the cash flow of very small businesses (and many small businesses because it is expected that 200,000 of them will be the subject of an administrative closure) of this 2nd containment. In fact, in small businesses, the products sold finance their own purchase, with suppliers granting payment terms or drafts ranging from 30 to 90 days. The fact that businesses can no longer sell (except food businesses) and, moreover, in a period of strong anticipated sales, will cause a cash flow crisis in a very large number of micro-businesses and businesses, a crisis that the government seeks to avoid it through specific measures. These include support up to € 10,000 per month for the loss of turnover of VSEs / SMEs that have been administratively closed, cash flow measures for charges and rents to be paid in this period, a special plan for the self-employed, traders and very small and medium-sized enterprises, a plan on which, at the present time, very little is known, support for VSEs / SMEs as well as craftsmen who will undertake digitization initiatives and the maintenance of exceptional partial unemployment. However, the government has neither addressed the subject of operating losses, nor detailed the "special plan" for VSEs / SMEs that it intends to implement.

Let us add, and this was already observed during the 1st confinement, that the inequalities would increase significantly. This can be seen in the consumption and savings behaviour of households (Chart 6), as shown in the CAE study published on October 12. The authors of this study, carried out on the basis of the exploitation of bank data, write: “The accumulation of savings during the recent period has therefore been very uneven. While overall household savings during the period were massive (nearly 50 billion euros more than what the continuation of the pre-Covid trend would have predicted), it was very strongly concentrated in the last two deciles . The additional savings of the two wealthiest deciles amount to 32 billion euros. Almost 70% of the additional savings were therefore made by 20% of households. On the other hand, the first two deciles were able to save much less over this period ”.

Graph 7
Dynamics of consumption by expenditure deciles



Source: CAE Dynamics of consumption in the crisis: real-time lessons from banking data, October 2020, p. 7.

They conclude: “This analysis confirms the high sensitivity of low-income households with low savings to variations in income. Indeed, the marginal propensity to consume is, for example, higher among households with less liquid savings. It suggests that much more frank support for the most modest households, more exposed to the economic consequences of health measures, will very quickly become necessary ”. The new phase of confinement that France is experiencing will therefore not only lead to a repetition of what happened last spring, but there is a strong risk of adding a cumulative element to it which risks causing part of the population to fall into the background. very great poverty. It is therefore clear that inequalities have increased. A note from the Directorate General of the Treasury also lists this phenomenon linked to confinement.

In 2024, the risk is therefore not only that we will be in a poorer France, but also much more unequal than that of 2010.

Conclusion

The 2nd lockdown will therefore, despite the planned reductions compared to the 1st lockdown (March-May 2020), have negative effects on the French economy. These effects will be linked both to its actual duration (now one month, but potentially 6 to 8 weeks) and to the degree of uncertainty about the future that it will introduce for economic players. Its impact on growing inequalities is more than likely, although it cannot be accurately estimated at this time.

The most worrying remains, however, that, in hypotheses (4) and (5), the level of 2019 would not be found before 2026-2028. In other words, the French economy would experience, because of the COVID-19 epidemic, the equivalent of a "lost decade". The cost of this "lost decade" would then be considerable. This cost would then consist less of the direct and indirect consequences of the epidemic than of the consequences induced by the latter. It would have important consequences both on the level of unemployment and on public finances and investments. As a result, the "growth potential" of the French economy would then be low until 2030, and its capacity to regain, if not full employment but quite simply the level of employment of 2019, while remaining within the current frameworks of the euro and the EU, would remain very limited. Only a very expansive public investment policy, replacing failing private investment, accompanied by a substantial modification of the European institutional framework in which the French economy is part, would be likely to prevent this "lost decade".