THE HEALTH AND WEALTH OF NATIONS

In the last few weeks, the whole world has taken a giant leap through the looking glass. Between January and these last days of March, everything we thought about the global economic system and national politics has been completely upended. Health concerns for ourselves and families are the most pressing concern, but the deliberate crushing of economic activity to arrest and control the spread of the coronavirus is no small matter either.

Lots of people are asking the question - not least President Trump for self-evidently political reasons - whether we have the balance wrong between the health and the wealth of nations. This point sometimes features the idea that the economy is being sacrificed to save the lives of older and often infirm citizens. This, though, is a euthanasia discussion, and totally misses the macro point about a choice that no one thought they'd ever have to make. The central issue is the state of preparedness and capacity of our health systems, which would be crushed and unable to tend to both Covid and non-Covid patients in the event that 'normal' economic and social interactions were sustained.

The main lesson we should be already be taking on board, then, is that getting the health v wealth balance right, or acceptable, is all about having stronger and better resourced health systems that can bring a lot of capacity on stream quietly and efficiently if needs be. In one feels swoop then, the NHS has almost certainly been depoliticised. Past attitudes to public health and investment in the sector will be quite different in future.

WHAT ABOUT MARKETS AND THE ECONOMY?

For the moment, investors are understandably like rabbits in headlights. Liquidity in markets is poor, volatility is off the charts, you could sail an oil tanker through bid-offer spreads, credit spreads have blown up, and there is no confidence about what lies ahead. Following the bounce on the US government's decision to pass a record $2 trillion stimulus, do you look at a pause in this aggressive bear market as a chance to lick your wounds and liquidate? Or do you stick with it, close your eyes, and hope the market recovers its sea legs in the future?

History suggests the latter, but the Nikkei index in Japan, which has never revisited anywhere close to its 1989 peak, suggests the former. So, are we turning Japanese, or just going through an incredibly tough period?

It's hard to say, but for a couple of reasons, it's probably still fair to judge that eventually this crisis will ebb, and markets will leave the current bear behind. Sooner or later, the infection rate will peak and fall, the restrictions on economic activity will ease (even if they are reintroduced sporadically) and there will be a vaccine. The urgency of investment in health will mean that our health systems will be better prepared for future challenges, meaning hopefully that lockdowns will not be the norm, or are applied less forcefully.

The financial system seems in better shape than it was in 2008/09 when it was both insolvent and illiquid. I don't want to be complacent here. Credit markets are in bad shape, companies are in huge trouble, and pension fund solvency issues and non-performing loans loom large. But my sense is that the leverage in the financial system is not as dangerous. Note also that the Fed, Bank of England and ECB, for example, have been quick to wheel out huge liquidity and market support programmes to sustain functionality. They may have to do more, of course.

One of the big differences with 2008/09, though, is that this time, the economic slump is deeper and more difficult to address. In the GFC, boosting demand was a no-brainer. In the coronavirus crunch of 2020, governments are simultaneously shuttering the economy in order to get control over the pandemic and trying to boost it. That isn't going to work, yet. Right now, the priority is to maintain income and jobs for millions of people, keep viable firms afloat, and ensure that the

financial system can continue to function. Rishi Sunak's announcements in the last week or two in the UK certainly went a long way to meeting those goals, though it needs to be said that for now, the government can only do band-aid, rather than stimulus.

In time, though, and as people start to get back to work, the stimulus programmes should have a much greater effect. With austerity consigned to history, here on the other side of the looking glass, the British government has pledged initiatives which, together with the effect of economic contraction, will push the fiscal deficit to well over 10 per cent of GDP. The US government's fiscal package, comprising many similar measures, is the same order of magnitude. As in Germany, which has abandoned the balanced budget provision in its constitution. Other countries have followed suit. The EU has abandoned the Maastricht fiscal criteria and there might, repeat might, even be a joint bond issuance programme to fund higher fiscal spending in the Euro Area.

And don't think this will be the end of it. On top of large stimulus programmes, we may also see the start of what is colloquially called 'heli-money', or more formally, so-called Modern Monetary Theory (MMT). This is a highbrow term for what is in effect money-printing, in which central banks finance government spending programmes directly rather than buying bonds, for example under QE programmes. MMT is a contentious new policy area which will doubtless be the subject of considerable debate, but it will come as no surprise if some authorities, at least, venture into it as they seek to recalibrate stronger and remedial economic management again.

For all these policy-related reasons, then, my own view is that we won't face a drawn out and painful depression, that there will be an economic rebound consistent with greater public health confidence, and that financial markets will see these things coming, and behave better. I'm not saying soon, or that they'll reach earlier year peaks, or when they might, but at the moment, better behaved over the coming year would be a good outcome.

Many other topics will weigh on equity market and sector valuations, and economic performance during the covid crisis and after it fades. How much 'big government' will survive into the 2020s, and to the advantage and disadvantage of which sectors? What impact will the crisis and its management and consequences have on incumbent politicians, not least Donald Trump in November, or even Boris Johnson as the aftermath of covid and looming Brexit deadline collide?

More questions: Will the greater role of the state now lead to more determined policy initiatives on climate change, income and wealth inequalities, and who will pay? And what sort of legacy will the covid crisis leave for Sino-US and Sino-Western relations, and the temporarily forgotten 'trade war'?

Financial markets cannot answer these questions, and risk premiums are almost bound to remain elevated as a result. Cheap, as we know, can get cheaper. Right or wrong, I am going to sit this out and think about other things in the interim.

George Magnus | March 24th, 2020