

# BARRON'S

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- 
- [ECONOMY AND POLICY](#)
- [Q&A](#)

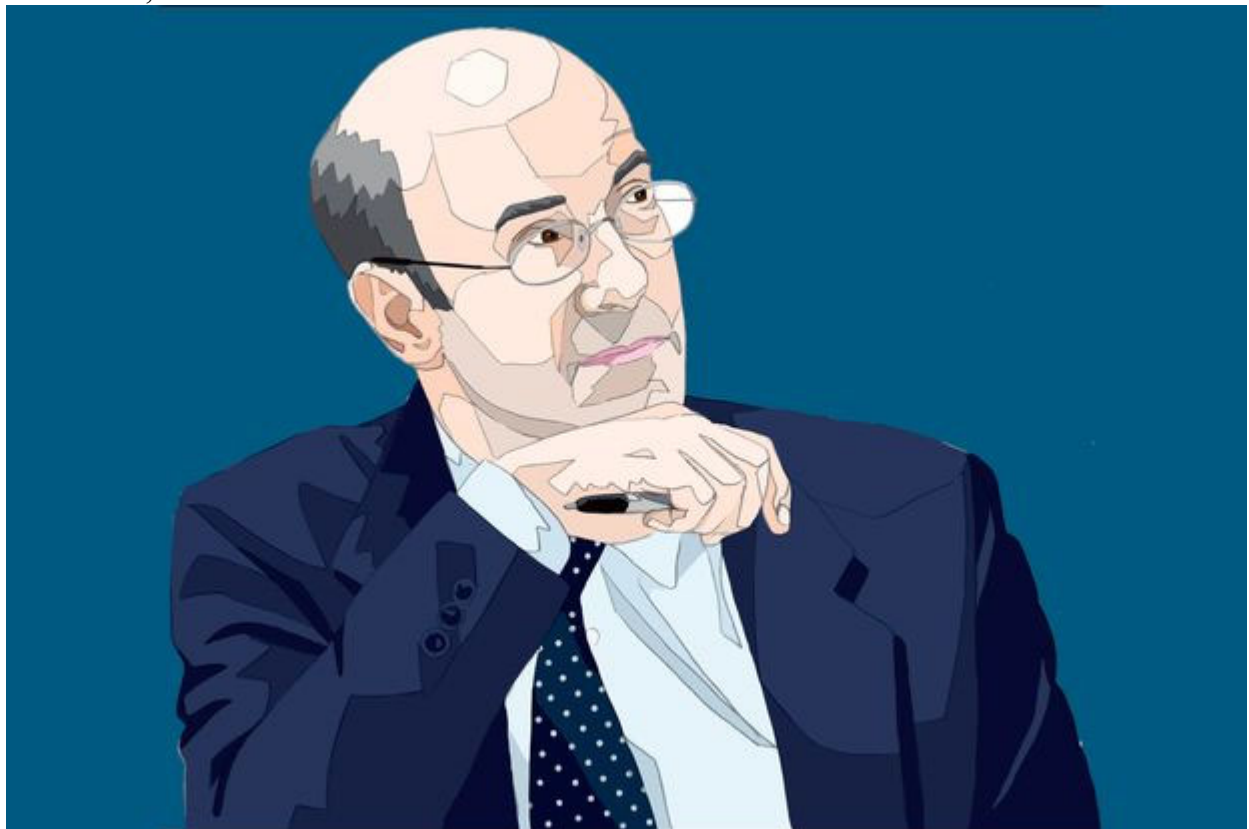
## Global Economy Could Take a Depression-Like Hit From Coronavirus, Says Harvard's Rogoff, Who Has Studied 800 Years of Crises

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By

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Kenneth Rogoff

Illustration by Danilo Agutoli

Harvard economist Kenneth Rogoff knows what a financial crisis looks like. He studied 800 years of crises with fellow economist Carmen Reinhart. In this pandemic, Rogoff sees the global economy possibly headed for a Depression-era like hit, with emerging markets, corporate debt and an election year making the situation more precarious.

Barron's spoke with Rogoff—who co-wrote *This Time Is Different: Eight Centuries of Financial Folly* with Reinhart in 2009—about how this coronavirus crisis compares with the Great Depression, how it could morph into a financial crisis, and what election years and crises have in common. This is an edited version of the discussion.

**Barron's:** How does the fallout from this pandemic compare with the Great Depression?

**Rogoff:** The real big question is how far we'll come back. All the things being done are extremely important and this will be won or lost on the health front. People have compared this to the Spanish influenza. But the world grew during that period because there was no option of pausing the global economy. I'm not criticizing [moves by governments to shut down economies]. On the peak-trough, the U.S. probably won't hit Great Depression levels. But if you look at the world [economy]—on the depth of this downturn—there is a good chance it will look as bad as anything over the last century and half. If we are back to 95% of normal in two years, it will be a lot better than the Depression.

**Bulls are looking for a v-shaped economic recovery in the fall. What do you think?**

I'm skeptical. There's too much lasting damage to small businesses—to airlines, hotels, the financial sector. If you are locking people in their houses for two months and thereafter three weeks for periods of time [when there are re-infections or flare-ups]... Demand-side stimulus is important to stop the panic, but this isn't just that. It is also a supply shock.

**What needs to be done to address a supply shock?**

We get a C- or worse on that. Where is testing—and hazmat suits? We were ill-prepared and we may give great stimulus. If we aren't solving the health problem, we are still going to suffer mightily. Europe has similar issues.

**How does Europe's situation compare to past crises?**

A big question [to the scope of the recovery] is what happens in Europe because the scale of this is bigger than the euro crisis. You can't impose

austerity on Italy, for example. GDP has collapsed, apart from the humanitarian impact. Should they be making debt payments when dealing with a health crisis? Germany may let the European Central Bank issue what is a de facto Eurobond, making some of the risk joint. But I've seen nothing in terms of progress of intra-European relations to suggest they will resolve this.

### **Could this morph into a financial crisis?**

A lot depends on how fast we pull out of the pause safely. One month of [the U.S. economy being shut] is roughly \$2 trillion of GDP. I can't imagine we are operating at more than 70%—generously. Chinese employment seemed to have fallen 30% at one point. That's a massive loss of output, which will never come back. We can handle it for a while but if it lasts too long, it gets harder.

### **What are some of the weakest spots investors should be watching?**

Capital is racing out of emerging markets at a faster rate than in the Asian currency crisis. The graphs are off the chart. And dollar-denominated debt for emerging markets was soaring and growth was falling. Frontier states are already falling on the cusp. We will see one after another emerging market restructure debt.

### **What else is vulnerable?**

Corporate debt, especially in the U.S. The Fed has gone some ways to prevent panic. And the magnitude of the stimulus was fine; we may end up needing to do the same again, at least once, before this is over if it lasts. In 2008, the Fed made money on its interventions. I'm not so sure this time. If the economy stays at pause long enough, there are still going to be massive corporate defaults.

### **The banks have buffers. Should we still be concerned?**

Stress tests built in severe shocks but not this severe. I don't think there will be panic because we saw what the Fed did in 2008. We're not going to let our banking system collapse. But we could be in a situation in a worst-case scenario like Europe where the banking system was moribund [postcrisis]; it is a lot of the reason why Europe has stagnated.

### **What is the political risk that emerges from this crisis?**

That's been studied. Very consistently when you have a big shock like this, it makes polarization worse in the long-run. The perfect storm for bad financial crisis is in part borrowing, part is real shocks in the economy but almost often it is a lack of political cohesiveness. You'd be amazed at how many happen during an election year. Markets can smell that you can't respond as aggressively because of politicking. If it happened after an election, the macro response would have been better.

### **Is there any silver lining?**

We are lucky this isn't worse and we are getting a whiff of what can happen in a highly urbanized and globalized world. We will figure it out in a constructive way. Hopefully this will be a wake-up call.

We need to throw more at the health sector, do wartime measures way sooner and treat this like a national emergency nationwide. It would calm people. Spend \$500 billion on that and it would save trillions on the economy. I would give the U.S. response a 3. It is really abysmal and we should be ashamed.