The Telegraph

IMF forecasts pour doubt on wisdom of furlough

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April 8, 2021

A comparison of two countries' economic forecasts is a shaky basis from which to evaluate Covid-19 relief policy. But IMF projections this week were nevertheless striking for their divergent assessments of the economic prospects for the UK and US.

Off the back of a more modest pandemic downturn than here, and with rapid growth forecast for 2021 and 2022, the IMF projects US GDP will be 6.2pc above its 2019 level by the end of 2022. That would leave the American economy larger than forecast before the pandemic hit. The UK's predicted 5pc-plus GDP growth rate for each of 2021 and 2022, in contrast, wouldn't even make up for last year's Covid-19 shock: UK output would be smaller in 2022 than 2019.

Remember how the UK furlough scheme was heralded for averting US-style unemployment? Last spring the official American jobless rate jumped to 14.8pc as Congress prioritised relief to households rather than supporting payrolls. Well, despite that volatility, the IMF now believes the UK's direct approach of "saving jobs" won't endure. UK unemployment is forecast to rise to 6.1pc and stick there in 2022, while US unemployment is predicted to fall sharply to a rate of just 4.2pc.

Policy differences between the two countries extend beyond how relief was dished out, of course. The US, with state governors leading public health efforts, is reopening already, despite a tardier vaccine rollout. Restrictions have been lifted entirely in major states such as Florida and Texas. No doubt the IMF's Keynesian models are biased towards the idea that more government spending "boosts growth" too, so Joe Biden's recent additional 10pc of GDP fiscal "stimulus" undergirds these extraordinary predictions.

But while the idea the US economy has been strengthened by Covid-19 is fanciful, and the difficulties of American workers reallocating to new jobs means the IMF could be over-optimistic about the country's near-term growth, the advantages and disadvantages of the different relief approaches can be seen already.

US cheques to households and hugely expanded unemployment benefits protected incomes and supported consumption, but at the cost of more short-term layoffs. In the UK, official unemployment remained low but activity plunged – there was less reorientation of economic life during the pandemic. The US lent more heavily on adjustment, in others words; the UK favoured job security.

The Conservative Government's approach was ultimately predicated on the idea that Covid-19 was a temporary aberration. Standing by and allowing the loss of firm-specific work relationships would severely scar workers' prospects, it was thought, causing unnecessary harm given things would ultimately return to normal. The implicit bet was that consumer demands would revert to their pre-pandemic patterns after the crisis passed and those working from home would, by and large, return to the office.

A year in, does anyone think the contours of the February 2020 economy will return intact? Survey research from Stanford University's Nicholas Bloom suggests that British employees currently working at home want to continue to do so for about two days a week and that, on average, people are slightly more productive at home than in the office. Although these averages hide a diversity in preferences, there will inevitably be a lot of stickiness in these pandemic work arrangements. An entrenched shift in where work occurs though will change the spatial demand for service industries, causing job losses.

While official UK unemployment numbers were masked by furlough, the number of payrolled employees already fell by 872,000 from March to November last year, while redundancy rates topped out higher than those seen in the financial crisis. The IMF's forecasts reflect job pain being delayed. A reallocation of workers and capital will wind its way through both economies, but the UK's policy-enshrined stasis leaves it with a standing start.

Polling of international investors by FTI Consulting supports the belief the US has been the most "economically resilient" major economy worldwide, reflective of a degree of North American parochialism.

But while the Democratic Party's desire to reregulate labour markets could entrench higher long-term unemployment after this crisis, the US economy is showing a remarkable adaptiveness in the face of last year's shock.

If the end of this nightmare does bring rising UK unemployment, with workers having to move or retrain, it will raise an interesting political dilemma for Boris Johnson's administration. Having "saved jobs" for over a year, will the Chancellor, Rishi Sunak, really be willing to let market-led creative destruction rip?

Last autumn, the Government tried to coax us back to our old spending and work habits even as the risks of Covid-19 remained, first through Eat Out to Help Out and then urging us all to return to the office to save sandwich shops. Those actions strongly imply that the Government won't let the high and rising £58bn in furlough costs (to date) lie, but will be keen to protect their investment in existing employment relationships.

Furlough has already been extended until Sept 30, albeit with the Government tapering its support from 80pc of pay for hours not worked, down to 60pc in August and September. Yet with rapid progress on vaccines, the economy should open up long before this. As of the most recent figures, 4.65m workers are currently enrolled in the government scheme, many of whom will face an uncertain work future.

The Government is keen to give existing jobs a fighting chance as the reopening commences. But the IMF is just the latest body to suggest that supporting payrolls may not be the best approach for ensuring economic dynamism as the pandemic ends.