

Economic Recovery in 2022 – the Battle Between the Delta Variant & Vaccines

By Naoyuki Haraoka

This issue highlights the economic outlook for the global economy in 2022 and beyond. The more powerful Covid-19 Delta variant has complicated the economic recovery process from the pandemic and increased uncertainty. Without this variant, vaccines could have probably overcome the pandemic towards the end of 2022, but this is not certain anymore. Global economic recovery in 2022 is now critically dependent upon the outcome of the battle between the vaccines and the Delta variant, as well as other variants that could prove to be more infectious or fatal. In this regard, a public health policy that promotes vaccination will be a key to achieving a sustainable economy, as better health would lead to fewer restrictions on economic activity.

Fiscal and monetary policy has worked well so far towards the second half of 2021 and succeeded in producing a recovery from 2020 when global economic growth plummeted significantly and most major economies suffered from negative growth in the midst of the pandemic. Loose monetary policy and expansionary fiscal policy in 2020 and 2021 saved the world economy from falling into a disaster more serious than in the Financial Crisis of 2008. This can be attributed to the evolving macroeconomics of current times. However, this macropolicy mix has produced concerns as well.

First, excess demand possibly caused by this unprecedented stimulating macropolicy could lead the economy to inflation. Second, extremely low interest rates and large amounts of fiscal aid provided to the private sector could end up helping inefficient companies survive and thereby eventually causing overall economic inefficiency.

Meanwhile, under the pandemic we have increasingly seen inequality widening, as the income gap between sectors and individuals badly hit by the pandemic such

as restaurants, hotels and the tourism industry, or between non-permanent employees (mostly female) and white-collar workers. This could trigger political or social instability.

Digitalization, on the other hand, has been further encouraged by the pandemic because of the increase in teleworking, which could raise overall productivity in the economy. Our highlights are aimed at introducing readers to these wider perspectives of the pandemic and the macropolicies responding to it, and how we should think about the economy in 2022 and beyond.

We start by introducing views from international organizations – one from the OECD (Álvaro Santos Pereira, director of the Country Studies Branch at the Economics Department of the OECD) and another from ERIA (Dr. Lurong Chen, senior economist of the Economic Research Institute for ASEAN and East Asia, Indonesia). The first considers how the emergence of Covid-19 variants like Delta could destabilize the global economic recovery and concludes that it is too premature to say the hope of containing the pandemic is starting to be seen. The second focuses on the positive aspects of digitalization in Asia which could resolve the challenge faced by global supply chains (GSCs) during the pandemic and the US-China decoupling exacerbated by it.

We have articles on major regional economic outlooks such as in the United States, the European Union, Asia and Japan. Dr. Joseph Gagnon, senior fellow at the Peterson Institute for International Economics in Washington, D.C., and Dr. Stefan Kooths, director of the Business Cycles and Growth Research Center at the Kiel Institute, are confident in US and European macropolicy in pursuing economic recovery, though both note the uncertainty created by the Delta variant. Dr. Khuong Vu, associate professor at the Lee Kuan Yew School of Public



Policy, National University of Singapore, considers the role of digital technology in the Asian economy, both in the past and from now on, encouraging us to think the key to Asian economic recovery from the pandemic must be Information Technology.

On the Japanese economy, Dr. Keiichiro Kobayashi, a member of the governmental advisory committee on countermeasures against the coronavirus pandemic, is very cautious about the variant, but believes that 2022 will be a year of stable recovery given suitable public health policies to prevent the Delta variant or other variants from spreading explosively. Takuji Aida, chief economist at Okasan Securities, is optimistic about the future of the Japanese economy as long as stimulating fiscal and monetary policies continue. He believes with this policy mix that the Japanese economy will enjoy high and stable growth and soaring stock prices, and even its fiscal debt issue will be mitigated by increases in tax revenue with higher income growth.

Stephen Paudano, executive director of the London School of Economics' Economic Diplomacy Commission, presents his view on the possibility of price rises of certain strategically crucial goods not caused by a macropolicy mix but by malfunctioning GSCs due to the US-China decoupling. This is a concern about cost-push, not demand-pull, inflation. Finally, expansionary fiscal policy during the pandemic has exacerbated concerns about public debt, but the debt issue is not limited to governments but has expanded to the private sector, as many private companies have been borrowing excessively to try to restore their businesses. Adolfo Barajas, senior economist in the Global Financial Stability Analysis Division of the Monetary and Capital Markets Department at the IMF, contributes an IMF analysis on this issue.

(Brief Introductions)

COVER STORY 1

Interview with Álvaro Santos Pereira, Director of the Country Studies Branch at the Economics Department of the OECD

Long-Term Prospects for the OECD Economy Under the Risk of the Delta Variant

By Japan SPOTLIGHT

OECD economies' growth will be strong and stable probably at around 5.0% in 2022, unless the variants weaken the effects of vaccines significantly. As for inflation, it will spike a bit in some countries but is not likely to get out of control.

COVER STORY 2

Digital Asia: Responding to Challenges from GVCs Digitalization, US-China Decoupling & the Covid-19 Pandemic

By Lurong Chen

Asia could increase its weight in global value chains (GVCs) in the digital era with regional integration and digital transformation being mutually reinforcing. Thus the negative impacts of the US-China Cold War could be mitigated.

COVER STORY 3

Interview with Dr. Joseph Gagnon, Senior Fellow at the Peterson Institute for International Economics in Washington D.C.

Strong US Economy Could Turn Global Economic Outlook Positive as the Delta Virus Variant Increases Uncertainty

By Japan SPOTLIGHT

The US economy can still enjoy strong growth in 2022, such as 3-4% following a strong recovery in 2021 of 7-8%. Job security is an important goal for the US government and the Federal Reserve.



COVER STORY 4

Interview with Dr. Stefan Kooths, Director of the Business Cycles & Growth Research Center at the Kiel Institute, Germany

Free & Open Competition Would Play a Key Role in Maintaining Sustainable Growth in Europe

By Japan SPOTLIGHT

His estimate for growth of the euro area in 2022 is 4.4% following a forecast of 5.3% in 2021. This is a strong catching-up process to the level of the economy prior to the pandemic. The worry is not about a deflationary gap but inflation.

COVER STORY 5

Asia in the Global Dynamics of Embracing the Digital Revolution: Performance & Strategic Priorities for Policy Action

By Khuong Vu

Asia's efforts in embracing the digital revolution are significant. With strategic priorities for policy action to promote a digital economy, ICT development and digital transformation in Asia would advance faster even in the post-pandemic era and thus mitigate the negative impacts of the pandemic substantively.

COVER STORY 6

Interview with Dr. Keiichiro Kobayashi, a Member of the Governmental Advisory Committee on Countermeasures Against the Coronavirus Pandemic

Outlook for the Japanese Economy with the Delta Variant

By Japan SPOTLIGHT

The pandemic will continue in 2022 and probably even in 2023 and 2024. But with readiness to face it and necessary adjustments in people's daily activities restricted by public health policies, stable growth would be realized.

COVER STORY 7

Capital Investment Cycle to Lead Japan's Post-Coronavirus Economy in Overcoming Structural Deflation

By Takuji Aida

With fiscal austerity lifted by the pandemic, a V-shaped recovery on the back of an upswing in the capital investment cycle would be possible. Continued fiscal stimulus in 2022 and beyond would change the deflationary structure of the Japanese economy.

COVER STORY 8

Stress Test: Supply Chains, Inflation & a Future for G7 Economic Cooperation

By Stephen Paduano

As GSCs and global trends govern global prices, it will be critical to achieve global coordination around supply chain tests to avoid a significant rise of certain important product items' prices, such as semiconductors and critical pharmaceutical goods.

COVER STORY 9

Confronting the Hazards of Rising Private Sector Leverage

By Adolfo Barajas

Cuts in monetary policy rates in conjunction with quantitative easing to reduce private sector borrowing costs would result in easier financial conditions, which in turn spur a buildup in private sector leverage. This could have a contractionary impact on the economy. We will need appropriate macroprudential policies to fix it.

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