Managing SARS economic fallout

MIERSCOPE

By Mohamed Ariff

As is often said, when bad luck strikes, it tends to come in quick succession, one after another. This indeed seems to be case for some East Asian economies. Although the 1997-98 financial crisis itself cannot be dismissed simply as “bad luck” as if these economies were innocent victims, subsequent happenings may aptly be described as mere “bad luck”. The post-crisis recovery efforts have been torpedoed by a number of exogenous factors beyond the controls of the afflicted economies. The recovery process was bedeviled first by the sudden demise of the electronics boom in the United States in 2001, followed by the insane war in Iraq and now by the Severe Acute Respiratory Syndrome (SARS). Of all these, SARS appears to be the most dangerous and the least manageable.

What makes SARS so awesome and so awful is that it is spreading with no respite. At first no one viewed it seriously, as it was believed to be contagious only through physical contact. Now that it is clear that the deadly virus is airborne, people are understandably nervous. Worse still, we are now told that the virus is mutating, attacking not only the lungs but also the intestines. As of end-April, the number of SARS cases has climbed to 5,481 with death toll rising to 356 the world over. China, the epicentre of the epidemic, tops the list with 3,303 reported cases and 148 deaths. The China figures do not include Hong Kong where the numbers have increased to 1,572 cases and 150 deaths. Singapore ranks third with 201 cases and 24 deaths. And, the numbers keep rising day by day.

Fortunately, in this regard, Malaysia pales in comparison, as the number of known cases are only six with just two deaths. Nonetheless, the nature of the killer disease is such that there is absolutely no room for any complacency. The borders of Malaysia are so porous that the country is very vulnerable to transmissions from outside, even though the authorities at home are doing every thing possible to contain the bug. So long as the virus is on the loose, no country is safe.

The shadow of fear is beginning to have a crippling effect on the economies affected by SARS. Hong Kong and Singapore, in particular, are very badly hit. Even the high-flier China is not spared. The toll on the Malaysian economy, despite the smaller magnitude of the SARS problem, is severe enough to warrant deep concerns. The services industries are particularly affected, as consumers tend to shun crowded places such as shopping malls, eateries and entertainment outlets. All this is likely to spill over to the manufacturing sector after a while, as lower consumption would translate into lower production. Already the manufactures are complaining about logistic problems and cancellation of orders.

Should the SARS menace continue to dampen consumption, the danger of deflation would become a distinct possibility. The fact that consumer price index (CPI) dropped to 0.7 per cent in March may not have much to do with SARS, but this disinfationary trend is a cause for concern under the present circumstances.

Tourism has been hit the hardest. Occupancy rates of the hotels in the country have fallen sharply to 30-35 per cent and in some cases to as low as 15 per cent. Airlines are reporting 50-60 per cent cancellations of bookings. Malaysia Airlines has reportedly suffered a revenue loss of RM131 million due to the cancellation of over 700 flights to SARS-affected destinations. It is also reported that the national carrier’s load factor to SARS-hit areas fell to 53 per cent in April. The number of airline passengers arriving in the country has also plummeted by over 40 per cent in recent times. Anecdotal evidence shows that SARS is beginning to curb international business as well, as the headquarters of several multinational corporations have banned travelling to SARS-affected countries.

In terms of economic impact, SARS is far more damaging than the war in Iraq. Many research outfits are busy revising the growth forecasts for the regional economies. Malaysia is no exception. The current year revised GDP (gross domestic product) growth projections for Malaysia range from 3.0 per cent to 4.5 per cent. MIER, for example, has recently slashed its earlier 2003 GDP growth forecast of 5.7 per cent down to 3.7 per cent, based on a number of assumptions, which include a credible stimulus package from the government.

However, upon closer scrutiny, it is uncertain what difference the stimulus package will really make. Arguably, much would depend on "how soon" and "how much": if it is too little or too late, the impact is likely to be insignificant. Experience has shown that stimulus packages everywhere take time to work themselves out. Seen in these terms, there is a sense of urgency, as one-third of the year has gone already. Conventional wisdom would likewise suggest that the "size" of the package also matters: the smaller the package, the weaker the impact.

Singapore has recently put in place a stimulus package worthUS$130 million, which include a levy reduction for foreign workers, property tax cut for hotels, restaurants and shops, and rebates on airport landing fees. Hong Kong has followed suit with a much bigger package, twelve time bigger, to the tune of US$1.5 billion, which include a reduction in landing fees for airlines, rent relief for private sector property companies, funds for medical research and increased allocations for health care. Malaysia is expected to unveil its stimulus package shortly.

As alluded to above, it is not certain what difference the stimulus package, no matter how big or how soon, will make under the present circumstances. Fiscal stimulus usually works well as a counter-cyclical measure. Increased government spending and tax cuts would put more money in the pockets of consumers to spend, ratcheting up the growth momentum. Undeniably, consumption expenditure plays a critical role in the growth process. Stimulus packages can fuel consumption, which in turn will rekindle investment, one reinforcing the other. But, SARS is by no means a cyclical phenomenon. Consumers are not spending now, not because they have no money to spend, but because they dare not venture out of their homes. Under conditions of fear, placing more money in the wallets and purses of consumers may not lead to increased consumer spending.

Indeed, this is not an argument against stimulus packages per se. The point driven home is that the impact of the intended stimulus package, under conditions of fear, will be limited. However, it is also important to bear in mind that the fiscal stimulus in question is not just about SARS only. The economy has been showing signs of weariness from the beginning of the year and the economy is undoubtedly under-performing, way below its potentials. It is in this sense that fiscal stimulus is appropriate.

The private sector, understandably, would want to take advantage of the SARS scare to extract as much concessions from the government as possible. These may include tax reductions, lower interest rates and higher subsidies. To be sure, there is no insinuation that these are bad for the economy or that the private sector demands are unreasonable. The point made here is that such requests represent a long-term agenda and any concession given now may well confer long-term benefits for the economy, but they cannot really do much to undo the short-term damage inflicted by SARS.

The fact remains that there is only so much that any government can do effectively at times like this. In any case, not to do anything is not an option either. For inaction will only erode investor sentiments and consumer confidence further. It is in this sense that a stimulus package is very much in order. It must, however, be clearly understood that the SARS-related economic woes cannot be resolved by simply throwing more money at them.

The main thrust of the package should be aimed at easing the pain the virus has caused to the economy at large. Thus, assistance given to the affected industries or sectors, such as airlines, hotels and shops in the form of reduced taxes, tariffs and rates would enable them to go on without having to retrench workers. The stimulus need not necessarily be in monetary terms only. It may come in the form of reduced red tapes, easier rules, softer terms, faster processing of papers, etc. Any liberalisation that would reduce the cost of doing business will certainly be helpful. Increased allocations for medical research, health worker protection, and health care in general and SARS control in particular, will go a long way in allaying fears and boosting consumer confidence.

The overriding objective of the package should be to alleviate the economic pain. This can be accomplished by (a) allocating more funds for the prevention, detection and treatment of SARS (b) easing the burden of sectors negatively impacted by the SARS outbreak, and (c) rebuilding consumer confidence. Admittedly, the restoring consumer confidence is no easy task. Most importantly, the government must convince the public that it is on top of the problem. This calls for measures not only to arrest internal transmissions of the disease but also to plug all the holes at the borders to prevent transmissions from external sources. The perception out there is that we are inadvertently "importing" the deadly virus. It will be impossible to contain the problem without the cooperation of neighbouring countries. No efforts should therefore be spared to seek and secure such cooperation. It is encouraging to note that countries affected by the SARS crisis, including China, are discussing such possibilities.

The public perception that the borders are too porous and measures taken to screen the travelers are too inadequate has to be dispelled. If consumers are convinced that the probability of contracting SARS is no more than that of being hit by a truck, they will be more forthcoming. All indications are that the bug is not going to disappear any time soon. Like it or not, we have to learn to live with it for some time by making sure that the problem is not blown out of proportions. A glimmer of hope is already in sight, with the World Health Organisation (WHO) declaring that the epidemic had peaked outside of China.

While there is every reason to remain vigilant, it is important not to resort to micromanaging the economy through the SARS crisis so as not to undermine the working of the market. Hopefully, SARS is a passing phenomenon, and it will be a folly to over-react to it at the expense of long-term interests.

The writer is the Executive Director of the Malaysian Institute of Economic Research (MIER).