Global Pandemics and the Small Business Economy:

Regional Implications of the Economic Meltdown

Professor Mark Hart
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with special thanks to Joanne Turner and Temitope Akinremi (2020) “The business effects of pandemics – a rapid literature review”, ERC Insight Paper, April 2020
Looking Back – Taking Stock

• What can we learn from previous pandemics?

• Early assessments on emerging evidence on business impacts of COVID-19 pandemic on Chinese firms – especially SMEs and also supply chains

• COVID-19 and Business Dynamism in the UK

• Developing scenarios - lessons from the Global Financial Crisis (GFC) - global trends in entrepreneurial attitudes and activity – Global Entrepreneurship Monitor (GEM) data

• But – an economic crisis resulting from a public health emergency is uncharted territory!!
Covid-19 and business dynamism

• All businesses will be impacted by the COVID-19 pandemic, most negatively, some positively – contingent on size, sector and location.

• Some generalities:
  – larger firms with more significant financial resources may be better able to survive shocks than SMEs – but sector specific – global airlines and hotel chains!!
  – SMEs more exposed to existential shocks or extreme events
  – Failure of micro and small businesses will impact the normal functioning of daily life
  – Young small firms drive job creation and crucial to recovery – how many survive?
1918 ‘Spanish Flu’ Pandemic

- Killed 40 million people worldwide from the early spring 1918 through to late spring 1919.

- In the US, the health impact of the 1918 pandemic was not uniform across states.
  - Although some states were able to take precautions, such as closing schools and churches to limit the spread of infection, there was a positive correlation between population density and deaths – a statistic supported by cities within US states registering higher mortality rates than rural areas (Garrett, 2007, 2008).

- Average business losses were more than $100,000 per day (2006 prices). Many businesses, especially those in the service and entertainment industries, suffered double-digit losses in revenue. Other businesses that specialised in health-care products experienced an increase in revenues.

- Those US states that experienced a higher number of deaths per capita experienced higher rates of growth in per capita income following the pandemic. After the pandemic, the increase in capital per worker resulted in higher output per worker and higher incomes (Brainerd and Siegler, 2003).
Recent Pandemics/Epidemics?

• H1N1 influenza pandemic (‘Swine Flu’) on the Mexican tourist and pork industries during Spring 2009 - economic consequences were short-term.

• Similar short-term economic effects experienced by South-east Asian nations following the SARS outbreak in 2003 or by the UK after foot and mouth disease (FMD) in 2001 and the bovine spongiform encephalopathy (BSE) outbreak during the early 1990s (Rassy and Smith, 2013).

• Social and economic impact of the Avian flu in East Asia – a human pandemic similar to the 1918 influenza pandemic:
  – direct economic costs on the poultry sector due to losses from the disease and control measures put in place.
  – Poultry losses meant financial losses to farmers and impacts the poultry supply chain and the sector as a whole with a 15% economic loss in poultry output in Vietnam.
  – Also, distributional effects from the loss of livelihood by poultry dependent rural communities and loss of profits and capability by industrial and commercial poultry producers represent potential impacts of the pandemic.
Potential Covid-19 Impact?

• Findings on the potential impact of an influenza pandemic suggest a concurrent **decline in global aggregate demand and international trade** leading to a further decline in national income and output.

• In addition, uncoordinated control measures to avoid infection may result in a **severe demand shock** especially for service sectors like tourism, retail sales, hospitality and mass transportation.

• Also, the potential effect of workplace absenteeism, disruption in business activities and production processes and a change from business as usual to more costly procedures may lead to **supply shocks which may impact supply chains at the national and global level.**

• Emergency measures such as quarantines and restrictions on travel and trade imposed by governing authorities to slow or mitigate the pandemic may also lead to **supply chain disruptions** and a temporary **breakdown of local and international trade and logistic services.**
COVID-19 Pandemic

- COVID-19 pandemic which originated in Wuhan, China, in December 2019 has so far as of 13th May resulted in 291,519 deaths
COVID-19 – Effects

- The spread of COVID-19 has seen economies struck by a simultaneous demand and supply shock, with there being no correlation between economic impact and mortality rates (Fernandes, 2020).
- COVID-19 will be felt disproportionately across an economy. Some sectors may benefit financially, while others will suffer huge losses. Those countries with more service-oriented economies will be more negatively affected, and suffer larger negative employment effects.
- Hospitality-related sectors have been hit hard – tourist destinations are deserted, airlines have grounded fleets, holidays have been cancelled and hotels have closed.
- The world stock market has also suffered since the outbreak of COVID-19.
- The oil gas and coal businesses have seen huge losses (50 per cent below the start-of-year prices, on average), driven by a fall in the price of oil and a reduction in consumption (Fernandes, 2020).
COVID-19 and China

• By the end of January 2020, the COVID-19 outbreak, mass quarantine, and international travel ban had begun to severely affect China’s economy (Bouey, 2020).

• Lost revenue in both retail and food services during the Chinese New Year week is reported to be RMB 1 trillion ($142 billion) (The Star, 2020), with service-sector losses during the same period expected to be 1 per cent of lost GDP growth in the first quarter (Luohan Academy, 2020).

• Businesses relying on physical space and shops, such as supermarkets, traditional food markets, restaurants, car dealers, theatres, gyms and bars, suffered losses, whereas local convenience stores and online businesses and health-related businesses experienced an upsurge in demand (hand sanitizer and personal protection equipment, for example).
COVID-19 and Chinese SMEs

• A survey of 995 Chinese SMEs in February 2020 indicates that:
  – 30% of firms have seen their income fall by more than 50%, with almost a third reporting a 20%-50% reduction (Bouey, 2020).
  – More than one-third of firms reported that they could stay open for one month with their current cash flow, one-third could sustain two months, and less than 10% could stay open for more than six months. Firms indicted that they felt financial pressure from salary, rent and loan payment demands.

• A recent study by Dai et al. (2020) identifies the firm-specific impact of the COVID-19 pandemic in China:
  – Findings indicate that 80% of surveyed firms were yet to resume production at the time of the survey while 40% were unable to determine a definitive timeframe for production resumption.
  – Economic stagnation emanating from measures imposed to control the spread of the pandemic and mitigate its impact means that firms are unable to resume business activities.
  – Such firms may be pushed towards bankruptcy as they run out of cash and are unable to run the business. Thus, an extended duration of the pandemic may lead to a surge in SME bankruptcies.
COVID-19 and Chinese Supply Chains

• Prior to the COVID-19 outbreak, China produced
  – 33%-53% of global electrical equipment and motor vehicle parts,
  – 52% of basic metals, 58% of mineral products, 58% of textiles, apparel, and leather, 40% of wood and wood products, and 35% of pharmaceuticals.

• Many of these sectors incorporate intricate supply chains that in some cases include a multi-country dimension, in particular the electrical equipment, electronics, automotive, and textile sectors (McKinsey Global Institute, 2019b).

• A supply-chain network is an important channel through which the COVID-19 pandemic may negatively impact both the domestic and global economy. Goods and services reach final destinations via complex supply chains.

• Supply chains become severely disrupted during a pandemic, and governments may need to direct support towards particular firms that are essential for meeting demand in a crisis.
COVID-19 and Chinese Supply Chains

- As firms closed in China and transportation links collapse, it became increasingly difficult for some firms to produce in other continents, nations and regions.

- Global car manufacturers have ceased production due to a lack of parts, and Swiss watch manufacturers have faced disruption to their supply of components.
COVID-19 AND UK
MARCH 2020 – COVID-19 Impacts

**Incorporations Q1 2019 and 2020**

- 70% increase in the number of company dissolutions in March 2020 compared to March 2019.

- Fall in incorporations in March 2020 compared to March 2019 – especially after UK lockdown on 23rd March

**Dissolutions Q1 2019 and 2020**

Source: FAME
Dissolutions by UK Region

Source: FAME
Dissolutions by Sector

Source: FAME
ERC Scenarios for British Business Bank

• **Scenario 1**: same as downturn in Great Recession – by end of 2020:
  – 208,114 firms close
  – 3.32 million jobs lost

• **Scenario 2**: what’s happened to date by start of Q3 2020:
  – 84,597 firms close
  – 1.3 million jobs lost

• **Scenario 3**: more severe shock in line with OBR and BCC surveys – by end of 2020:
  – 831,868 firms close
  – 11.4 million jobs lost
# COVID-19 UK Regional Scenarios

<table>
<thead>
<tr>
<th>REGION</th>
<th>No. of Firms lost/at risk</th>
<th>No. of Jobs lost/at risk</th>
<th>Percentage loss of total jobs in region</th>
<th>Percentage loss of firms in the UK</th>
<th>Percentage loss of jobs in the UK</th>
</tr>
</thead>
<tbody>
<tr>
<td>North East</td>
<td>2,448</td>
<td>37,558</td>
<td>6.0%</td>
<td>2.9%</td>
<td>3.0%</td>
</tr>
<tr>
<td>North West</td>
<td>8,529</td>
<td>131,944</td>
<td>6.1%</td>
<td>10.1%</td>
<td>10.6%</td>
</tr>
<tr>
<td>Yorkshire and Humber</td>
<td>6,192</td>
<td>96,398</td>
<td>5.5%</td>
<td>7.3%</td>
<td>7.7%</td>
</tr>
<tr>
<td>East Midlands</td>
<td>5,752</td>
<td>88,348</td>
<td>5.0%</td>
<td>6.8%</td>
<td>7.1%</td>
</tr>
<tr>
<td>West Midlands</td>
<td>7,052</td>
<td>103,120</td>
<td>5.3%</td>
<td>8.3%</td>
<td>8.3%</td>
</tr>
<tr>
<td>East of England</td>
<td>8,594</td>
<td>119,682</td>
<td>4.8%</td>
<td>10.2%</td>
<td>9.6%</td>
</tr>
<tr>
<td>London</td>
<td>14,607</td>
<td>210,447</td>
<td>4.6%</td>
<td>17.3%</td>
<td>16.9%</td>
</tr>
<tr>
<td>South East</td>
<td>12,623</td>
<td>179,773</td>
<td>5.7%</td>
<td>14.9%</td>
<td>14.4%</td>
</tr>
<tr>
<td>South West</td>
<td>7,472</td>
<td>109,103</td>
<td>6.8%</td>
<td>8.8%</td>
<td>8.8%</td>
</tr>
<tr>
<td>Wales</td>
<td>3,401</td>
<td>48,575</td>
<td>7.1%</td>
<td>4.0%</td>
<td>3.9%</td>
</tr>
<tr>
<td>Scotland</td>
<td>5,811</td>
<td>87,168</td>
<td>6.1%</td>
<td>6.9%</td>
<td>7.0%</td>
</tr>
<tr>
<td>Northern Ireland</td>
<td>2,116</td>
<td>34,467</td>
<td>7.9%</td>
<td>2.5%</td>
<td>2.8%</td>
</tr>
<tr>
<td>England</td>
<td>73,269</td>
<td>1,076,372</td>
<td>5.4%</td>
<td>86.6%</td>
<td>86.3%</td>
</tr>
<tr>
<td><strong>UK</strong></td>
<td><strong>84,597</strong></td>
<td><strong>1,246,582</strong></td>
<td><strong>5.5%</strong></td>
<td><strong>100.0%</strong></td>
<td><strong>100.0%</strong></td>
</tr>
</tbody>
</table>
Low income regions face the biggest challenges — UK suffered from persistent and significant regional income disparities – made worse by COVID-19 related furloughs and lay-offs - McKinsey & Co (11th May 2020)
COVID-19

“London apart, the darkly shaded areas are looking increasingly like a map of the old industrial regions of England”

John Tomaney
12th May 2020

Population data are the latest ONS mid-year estimates.
LESSONS FROM GLOBAL FINANCIAL CRISIS (GFC)
Lessons from Global Financial Crisis (GFC) – GEM (Opps)

Contrasting trends in GFC – UK & Spain – sharp decline in % seeing good opportunities in GFC; Netherlands – no change and USA – increase of over 10%
Lessons from Global Financial Crisis (GFC) – GEM (Intention)

**Start-up Intention:** contrasting trends in GFC – UK & USA – sharp decline in % intending to set up a business – but bounced back sharply; Spain & Netherlands a slight increase – reflecting lack of safety net??
Lessons from Global Financial Crisis (GFC) – GEM (Necessity)

Necessity entrepreneurship – all countries experienced a rise – slight in case of UK and the Netherlands and very steep in case of USA and Spain – but while Spain remained high USA fell back to pre-GFC levels
Young Start-ups & GFC

Start-ups: Dramatic “collapse” in start-ups after 2008 signalling the start of the GFC period the lower level persists for the next two years the pattern of change in jobs per start-up is considerably less volatile and flat over GFC period.

Exits: “surge” in deaths around the GFC period. By 2011 deaths were back within their pre-GFC range, however, during the three “surge” years deaths were about 25% above the pre- and post-GFC average. Again, as with start-ups, average size of exits seems to have been little affected by the GFC.
What have we Learned from GFC?

- Intention to start a business collapsed in GFC but bounced back quickly – why important? – strongly correlated with actual future start-ups

- Actual start-ups fell sharply but bounced back – evidence that this has been driven by necessity entrepreneurship – especially USA

- Young firms (<5 years) are job creators; suffered more from GFC – but recovered more quickly

- Regional effects? – the ‘bounce-back’ will be more pronounced in those cities and regions where there is a preponderance of innovation driven enterprises – these in turn are associated with populations of highly-educated individuals many of whom are immigrants and migrants.
Conclusion – Regional Effects

• Business base in all regions will shrink as businesses close and new entrants fall – related to national/regional lockdown policies – i.e., reach and time-scale

• Large metropolitan areas will suffer most from higher mortality – knock-on effects in terms of longer lockdown and increased business closure or at best hibernation of many businesses

• Sector:
  – Regions with key sectors tied into global supply chains will be impacted disproportionately – e.g., the Automotive sector or Asian garment manufacturers - factory closures, supply chain disruption, and a collapse in demand. Just-in-time manufacturing processes have propagated the impact across the globe. SMEs are among those hardest hit and millions of jobs are at risk.
  – Regions with an over-reliance on travel/tourism/hospitality sector will experience a more severe contraction of the business base – e.g., Asia-Pacific regions
  – In areas at higher risk of job losses, there is a greater proportion of elementary and skilled trades occupations, and a smaller proportion of professional occupations.
Contact us:

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