...Reformatics
Creating Your Successful Legacy

Corona Capitalism

Despite achieving a great progress in medicine, biotechnology, and genetics over the past decade, the world have been unprepared to meet the challenges associated with the Coronavirus pandemic. Today, the attention of governments and international organizations is fully focused on the problems of health and human life, which, of course, a natural reaction to the current situation. However, at the same time, the economic consequences of this pandemic have to be analyzed, and it is important to analyze what changes this process will bring to world geopolitics, economy, environment, or social relations.

What will the world be like in 2021, when we are faced with a new reality once the vaccine against the Coronavirus is created and available on the market? What can be done in the near future to ensure that countries (especially developing countries where economic problems are much larger than developed countries) are prepared to face the new reality in the post-Coronavirus period?

Over the past century several global events have been of the same magnitude as today's pandemic, the impact of which on the post-crisis economy can be compared with that of post-Coronavirus pandemic - the Great Depression of the 1930s, the post-World War II global economic crisis, economic recession in the post-Soviet Socialist Bloc caused by the collapse of this Block, and the global financial crisis of 2009-2010.

It is obvious that all of these crises have their own characteristics, and the post-pandemic year 2021 as well will be different from other crises, but we can draw some conclusions from the analysis of these crises and make some predictions for the next 1-2 years.

Of course, there is a high probability that the crisis will be short, that effective anti-coronavirus drugs will be produced in 1-2 months, and that normal economic life will be restored in the next 2-3 months. However, there is also the possibility that the condition of lockdown in the world will last longer and be extended even till the end of the year in different forms. In this case, most likely, we will witness a significant reshuffle of the world economic order. And even if it does not turn out to be a reshuffle of the same scale as in previous crises, this process, like all transformations, will still have its relative winners and losers. Of course, the whole world will suffer from the tragedy that the Coronavirus has brought to the humanity.

What will the global processes look like as a result of the pandemic?

To answer this question, I offer one of the possible scenarios for consideration:

Geopolitics

According to Bloomberg (www.bloomberg.com on April 1st), the most recent US intelligence reports claim that "China concealed extend of virus outbreak ..... and China's public reporting on cases and deaths is intentionally incomplete".

In other words, this means that once the lockdown mode is over and most immediate healthcare problem is under control (or even before), the US will start to more actively blame China for global economic meltdown, skyrocketing unemployment, bankrupt SMEs, disrupted tourist and airline sector and for initiating a record-breaking fall on the stock markets.

Well, to some extent China may be at fault here but, in addition to this, 2020 is the Presidential election year in the US and somebody needs to be made responsible for such an economic shock in pre-election period. This in turn could be translated into a great economic war against China a strategist of which will be the US and we might see many countries (especially the EU states) joining in gladly – as almost every country will suffer economically and politicians will be happy to blame this on China.

It is hard to predict exactly whether there are anti-China sanctions, trade restrictions, restrictions on access to international capital markets or other, but there is high probability we will witness a diplomatic and economic war between China and the West from the second half of 2020, which will result in a great economic and geopolitical reshuffle.

This process will not really bring down China's economy (its too big and adaptable to changes), but it will certainly reduce its growth rate, increase the confrontation between the West and China, which will have some impact on both developing countries and the private sector. This process will increase the risk of many companies investing in China, and this in turn will create additional opportunities for developing countries to attract investments that were previously destined to China.

As it seems today, one of the most unprepared players for this type of crisis is the European Union - not European countries (as we see Germany and other Northern European countries cope with the current crisis quite well), but the European Union as an organization. It has neither the relevant structures nor the relevant regulations to effectively deal with the crisis caused by coronavirus. The only European institution that is taking effective anti-crisis action is the European Central Bank, but as it turned out this is not sufficient at this stage.

Most likely, by the end of 2020-early 2021, EU member states will intensify discussions on the future of the organization - whether there is a need for the EU to have a unified ant-crises center, a unified army, a unified fiscal policy etc.

On the positive side, this crisis will accelerate such decisions, and by 2021 it will be clear whether the EU will finally become a true economic, political and military union or will remain an organization as it is today - with many positive policies (free movement, single economic space, single currency), but unfortunately ineffective during the crises.

Just like in the last scene of Sergio Leone's famous film, "The good, the bad, the ugly," there is a trilateral standoff between today's oil-producing countries (Saudi Arabia Russia and the US shale oil industry).

Unless the US government extends some support to the US shale oil industry it will be the first one to go down (because extracting oil with such a technology is much more expensive than its production by traditional way and is more costly, than the current prices on oil). However, there is a good chance that the US government will intervene in this situation making the US shale oil industry unbeatable in this "Texas shootout".

Also, an important question is whether the US government will only intervene in this process through some subsidies for its own oil industry, or will it play the role of mediator between Saudi Arabia and Russia to avoid falling of oil prices in the long run that could bankrupt the US shale oil industry.

It can be assumed that the initial attempt will be to reach a joint agreement, but if this does not work out, the US will look after its industry and Saudi Arabia and Russia will have to test each other's economic stability and reserves.

In such a case the major factors to consider will be: Russia already has an experience to function in a semi-isolation mode (due to past sanctions) and the Russian ruble devalues in parallel with the drop of oil prices, which does not reduce its revenues in Russian rubles by much, when the price of oil falls down. Of course, this has its negative consequences, both economically and socially, but the flexibility of the currency is an additional advantage during such an economic confrontation.

Saudi Arabia has a fixed exchange rate, which is likely to lead to a higher reserve spending (or a rejection of a fixed exchange rate - which will cause social dissatisfaction). However, Saudi Arabia's foreign exchange reserves (US$ 490 billion, a maximum of US$ 731 billion in 2014) per capita are 5 times higher than those of Russia (US$ 15,000 and US$ 3,000, respectively), and also higher in terms of import multiples - Saudi Arabia's foreign exchange reserves are 40 times monthly imports, whereas Russia's is - 27 monthly import value. Russia's foreign exchange reserves amount to US$ 440 billion (the maximum volume of these reserves - US$ 582 billion Russia had in July 2008) .

Of course, no country will allow these reserves to be reduced to the minimum, even though these figures will play a serious role in the confrontation (information on foreign exchange reserves are officially published, although both countries have additional sovereign funds exact data on which are not available).

Unless some type of agreement is reached within next few weeks (if this happens it will be initiated by the US to protect its shale oil industry) the country that will demonstrate that it outlasts the opposing side will win the battle, causing major economic meltdown and maybe even social unrest in another.

However, this will certainly take time and the results of today's confrontation will be visible in only 2-3 years. Both sides have very large reserves and the fall in oil prices is not enough to cause a serious economic damage. Additional factors will be crucial - the social background and internal socio-economic problems in these countries, economic reforms, which these countries implement in nearest future, prolongation/cancelation/postponing/tightening of sanctions against Russia, the consequences of various military conflicts in the region (Syria, Yemen) etc.

The speed of globalization will significantly slow down temporarily. This is unlikely to affect online services such as online education, online consulting, online shopping, etc. (which we'll talk about later), but at least in the first phase (3-5 years) the intensity of negotiations on free trade agreements will be reduced. Instead of deepening free trade agreements and reducing trade barriers, the governments will try to be more conservative. They will resort to various forms of protectionism declaring that it is in the country's interest to produce everything that it needs internally in order to be self-sufficient and not dependent on international trade (and here the justification will be: if we were not dependent on international trade, there would be less economic decline during this crisis). This will in turn increase corruption in developing countries - which industries to protect, which companies to make local champions will be determined in a different way, not through fair competition, slowing down economic growth of their economies.

State control will increase. Various types of control systems (face recognition software, mobile phone tracing software, etc.) the introduction of which has raised many questions in the past will stay as a norm using the argument that stricter measures of state control could have saved thousands of lives. It is also possible that annual testing of population for various viruses will become the norm.

As for defense strategies, most likely more focus will be made on biological warfare, sending countries into new Bioweapon race and channeling substantial state funding into biotech industry.

Economics

Some time ago relocating production to China was very efficient move, but due to current losses experienced by numerous firms as a result of breaking down these value and supply chains, the business will think twice before it decides if it is still worth to relocate production to China or expand already existing businesses in this country .

In addition, as suggested above, many governments may restrict trade with China to certain extend. For example - 80% of antibiotics that is consumed in the US is produced in China and after the current crises the US may decide that this is not acceptable any more, possibly imposing significant trade barriers on the China's import of antibiotics, in turn luring many companies to move back to the US or relocate their businesses to other, more predictable and reliable countries.

This crisis showed how easily value chains and supply chains (especially linked with China) broke down.

In addition to the geopolitical factor discussed above (China - West economic confrontation), due to these disrupted value and supply chains, trade restrictions (in the name of supply security) many companies will start to move their production from China back home or to safer, less risky countries.

This is where many developing countries in the Post-Soviet Union, the Balkans and Eastern Europe will have an amazing chance to participate in this global economic reshuffle and seize opportunities that they have not even dreamt of.

Of course, every crisis brings new great opportunities and this one as well will have its losers and winners. Winners will be those countries whose governments are efficient, effective, smart and adapt to new realities, look at this crisis as an opportunity to emerge as stronger players and that think creatively and out of box.

Debt of developing countries will increase significantly, but what is worse – the increased debt will be spent on social needs and saving companies from bankruptcies rather than on investments. It should be underlined that this measure must be definitely implemented by developing countries to save SMEs, the tourism and trade sectors, and to avoid serious social problems.

This will increase borrowing rates of the indebted countries and hinder growth during the next few years. However, there is another side of this coin – in 2021 many companies (mostly SMEs) will go bankrupt but big investors will accumulate huge amount of cash not knowing where to invest and which companies to trust – thus sitting on huge amount of USD-denominated cash with zero or negative interest rates. Due to this factor state bonds of the developing countries may still be attractive (despite the hike in the debt / GDP ratios) and some countries will definitely enjoy lower borrowing rates.

Also, governments will have great opportunities to attract new investors just providing minimum returns but offering other terms and conditions that will make investors more comfortable (e.g. PPPs with USD denominated offtakes at least for the first few years, international arbitration clauses in the investment contracts, etc.).

Global FDI will drop to its minimum and will depend only on USD, giving an ever bigger power to the US and the FED. Throughout the next 2-3 years, in developing countries investors will refuse to take risks associated with almost any other currencies then the USD. Most of the developing countries will depend only on IFIs and will be forced to ensure currency risks for FDI, meaning provision of USD-backed guarantees. The US dollar will gain more value, thus effecting almost all currencies in the developing world.

The issuance of additional money by the US Reserve Bank will weaken the dollar to some extent in the next phase, but it will still not increase the demand for currencies of developing countries (the US dollar may depreciate more against the Euro, the Pound, the Yuan and the Yen – in case of more quantitative easing measures).

IFIs will become ever more important for the developing world. However, they will need to change their modus operandi as well.

It is expected that there will be lack of equity, not lack of debt in the developing courtiers and those IFIs which come up with the best tools to inject equity into developing and emerging economies will matter the most (through PPP, through local Private Equities or other). It is also expected that international financial institutions will consider the possibility of partial write-off and / or restructuring of debt for developing and poor countries.

More investment will go into IT and AI (specially for security reasons), in medical equipment, healthcare and biotech industries as well as agriculture – under the slogan "Whatever our country needs for internal consumption we need to produce ourselves". Of course, internet providers and communication companies will also see huge capital inflows as many have already got used to video conferencing and distant learning rather than face to face meetings, lectures, etc.

New distress asset funds and cash rich Private Equity Funds will take over most of local businesses in developing countries creating new monopolies and oligopolies or new internationally competitive large companies, depending on government regulations. The first will hinder economic growth of countries, the second on the opposite – will ensure new jobs, new exports and new global or regional players.

"Green economy" will suffer a big hit – with such a low price on petrol electric cars and renewables will face a stronger than ever competition.

Environment

"In China and Italy the air is strikingly clean. Venice's Grand Canal … is running clear. In Seattle, New York, Los Angeles, Chicago and Atlanta, the fog of pollution has lifted. Even global carbon emissions has fallen" (nytimes.com March 17).

Many environmentalists have claimed that the humans are affecting the environment on such a scale that it may take decades or even centuries to clean it up. However, the Coronavirus "shutdown" of the world showed that it took only a few days for the environment in many super polluted cities to improve significantly.

This should result in rethinking the answers to the question – exactly how big is humankind's negative impact on the environment? Is it as big as it was assumed?

Would the Earth clean up so fast (from big cities pollution point of view only) if the impact was as devastating as some scientist have assumed?

Yes, the Earth is getting warmer but maybe not due to human intervention, but rather due to its natural circle. The Earth got colder during the Ice Age (as part of its natural life-cycle and maybe now it is getting warm due to the same reason).

Maybe all we need to do is to announce a "lockdown" for a week (let's start with one week first) all over the world once a year for environmental protection and against pollution, especially in large cities, even if there is no threat of any virus. This would help the Earth to "breathe" better and would make us healthier as well.

Social Interaction

Social interaction will also be affected significantly. The recent month showed that distance learning is possible and very effective.

Even after the lockdowns will be eased, most educational institutions (schools and universities) will apply different than before approach– big part of the process becoming online. Creating amazing opportunities for everyone in the world to get the best of the best education through more widely used online courses, online lectures of the best professors, etc., which will take a global scale, providing the new generation with the opportunity to get the best education.

Private sector has seen that many topics can be discussed online and there is no need to travel as much as it used to be. Online consulting, online legal services, online financial advisory etc., will save time of many but will significantly affect airline industry, bringing down business passengers.

People are getting to online shopping even more than before. It will become a norm increasing online shopping industry and bringing down real estate prices in commercial areas. Real estate prices in business districts will also be negatively affected by businesses requiring less commercial space as they transform more and more into online businesses.

And finally, our transportation means will also be affected by the current crisis. New types of rules and regulations will be put in place to keep social distancing in public transportation. Demand will increase on bicycles, scooters, especially electric scooters, as well as on cars. Airlines will also need to make some adjustments – especially for inside the plane air circulation and protocols for boarding the plane – maybe even require to take quick tests before getting on a plane. This protocol will also help with next possible epidemics from spreading internationally.

Winners & Losers

So which countries may emerge as winners and which countries may lose out the most in corona capitalism (post-corona) world?

The winners will be those countries that most effectively manage elaboration and implementation of anti-crisis programs to mitigate the impact of economic downturn, those countries that introduce new anti-crisis approaches faster than others and will be the first to adapt to new realities; countries that will project what should be offered to investors in order to be attractive after 12-18 months, when the euphoria of the virus is slowed down and the world economy is significantly shrunk, many companies have gone bankrupt and many investors with available financial resources, but under the conditions of the negative interest rates.

In addition, many enterprises will be shut down in many countries, that have broken the supply chain, or simply have not been able to withstand the current financial crisis. Consequently, some developing countries will have a chance to attract new investments (due to low interest rates) and or have a chance to relocate already operating enterprises to their markets. Respectively, more attention will be attached to business environment of developing countries – simple regulations, tax regimes etc.

As a result of the crisis, countries may have a stronger, more important role to play. To do this, a new reality requires a new vision, new initiatives, and appropriate implementation of those.

As for Georgia ...

If the processes develop as described here (of course this is just one option and a lot may change in the coming months), then we will really be witnessing a great economic reshuffle.

If until now China and similar countries were considered to be less politically risky (due to political stability) and therefore their attractiveness for investors was high, the new Coronavirus crisis showed that these types of countries easily hide information, are not transparent, may not report the threats they already know of, and because of political reasons may pose additional risks to investors as well as to the international community. Countries that will introduce special regulations during this crisis for capital outflow, repatriation of profits, etc., will inevitably worsen the investment attractiveness after this crisis (for example, the Russian government has already introduced an additional 15% tax on capital outflow in order to reduce the capital flight).

Consequently, the risk factor for such countries is likely to increase and the attractiveness of open, transparent and democratic countries will increase, both for investors and for international donors. In this case, Georgia is given a chance to appear more competitive than many other countries if we meet certain standards of an open and democratic state.

Only 7 countries in the world have free trade agreements with China and the European Union at the same time. These countries are Iceland, Chile, Singapore, South Korea, Switzerland, Peru and Georgia. Among these countries, Georgia looks quite competitive in terms of both geographical location and the cost of doing business (labor costs, costs for construction, taxes, etc.).

In addition, Georgia has free trade agreements with Turkey, Hong Kong, EFTA countries and the former Soviet Union countries. If investors withdraw from China and China and Russia are unacceptable for new investments, the chances of attracting such investments to Georgia are quite real.

Of course, we will not be alone on this market. Much of the investment will go to the European Union and the United States, but small volumes will still be invested in other countries (and in this case, "small" is relative and may mean tens of billions of dollars).

In this situation, Georgia's main competitors will be other post-Soviet countries (for example, Ukraine, Kazakhstan), as well as Turkey, Eastern European and Balkan countries. The competition will be big, but with the right reforms and good positioning, we may have a chance to develop completely new industries - bringing new technologies and creating many new jobs.

A good case in point here is the example of the hazelnut production in Georgia when the "non transparency " of the Turkish hazelnut market and the risks associated with it gave Georgia a chance to become a "sudden" exporter of hazelnuts 13 years ago, and farmers started to earn a living on this.

As mentioned above, in 2021, many companies and potential investors will likely accumulate large sums of cash, the interest rate on which will be close to zero. The US Federal Reserve, the Bank of England, and the European Central Bank have reduced interest rates to such a low level and / or started quantitative that the process will be maintained for some time to come. Most likely this will cause reduction of interest rates on governmental bonds and deposits almost to zero (maybe even to negative interest rate as it was a few years ago after the 2009 crisis).

Against this background, even a small but positive interest rate for investors will be enough to invest some of their money in developing countries - bank deposits and other types of securities. In this situation, the countries whose economic climate, regulations and potential growth rate is most acceptable for investors will benefit more. In 2010-2011, this type of investment turned out to be important for the rapid transformation of the Georgian economy (in the 2nd quarter of 2009 we had a -9 percent decline, and in 2010 and 2011 we ended up with +6.4 and +7.2 percent economic growth, respectively).

In 2010 and 2011 the also role of international financial institutions (World Bank, European Bank for Reconstruction and Development, Asian Development Bank, etc.) was very important. Most likely, these organizations will play one of the most important roles in our region now as well.

However, this time around, in addition to credit allocation, we may need to offer other formulas to financial organizations, such as investment in equities, guarantees for PPP projects (which will reduce the risk for private investors and thus increase the number of interested investors).

It will also be important to involve international financial institutions in issuing private sector securities. This tool should exist not only for banks, that are already making such transactions, but also for other types of companies, such as construction, energy, trading or tourism companies so that these companies can issue commercial paper - high demand and low interest will be on portfolio investments in 2021, and not on Foreign Direct Investments (FDI).

As for FDI, Georgia will probably have to introduce a temporary partial dollarization formula for FDI, where part of investment is insured in dollars under various PPP formulas, which will be co-financed or co-guaranteed by the international financial institutions.

And finally, in 2021, as soon as the new Coronavirus vaccine is created and is already available, there will definitely be an instant change in stock markets.

Today, Georgia's sovereign Eurobonds are traded at 7-8%, and it is probably not advisable to issue any additional Eurobonds in this situation. However, after the vaccine is released on the market, international markets will change completely, and against the background of low-interest loans in developed countries, Georgia's 2-3% loan should be attractive to investors. In this way, it will be possible to attract $ 1 billion, but preparations for this should start now and 2020 has to be overcome decently.

To summarize, we have 2 years ahead of us with great challenges and great opportunities. How we get out of this reshuffle - with a prolonged economic crisis, or with the status of a new economic leader in the region - depends only on us (currently no one has time for us to interfere badly or make provocations). We will not be given such opportunities many times again and I would like to wish for Georgia to come out victorious from this very challenging situation.

Cheers to Georgia - those of you have read this long article to the end, let's pour a glass of wine and drink to Georgia ☺