INSIGHT

Labor Policies Key to Securing Post-Pandemic Economic Recovery

Policies must reduce gray areas in employment safety and facilitate the reentry into the workforce of those who lost their jobs due to COVID-19. Photo credit: Korea Institute of Finance.

Policy makers must improve labor market conditions and reduce employment uncertainties as part of their economic stimulus plans.

Published: 17 February 2021

Introduction

It took years for pandemic-hit countries in the past to restore their economies to pre-pandemic level. Compared to other crises, a pandemic might further delay economic recovery as it hurts both demand and supply in the labor market. Countries must watch closely the impact of labor market conditions on economic recovery efforts and design policies that can help mitigate labor market anxieties. The Republic of Korea (ROK) is no exception in this regard.

Analysis

Looking at the past pandemics can help project how long the current economic shock would continue or how the economies would recover from the effects of the coronavirus disease (COVID-19). Though the 14th century plague and the 1918 Spanish flu led to more deaths, the current pandemic affected the economies of the world more with restrictions to a greater volume of cross-border movements.

Researchers at the University of California, Davis tracked major epidemics that broke out since the 14th century. They found out that, on average, the neutral rate?a hypothetical rate to achieve potential growth rate without either inflationary or deflationary pressure?only recovered to pre-epidemic level after about 40 years from an outbreak. In comparison, in the aftermath of a financial crisis, it took about 5 to 10 years to recover the neutral rate. Another study claimed that during the Spanish flu in 1918 through 1920, the gross domestic product (GDP) of the 48 surveyed countries fell by an average 6% in a short time and did not recover for years. During this period, the correlation coefficient between cumulative fatality rate and GDP growth rate stood at -0.42, indicating that the stronger the contagious power of the flu, the worse the recession was.

Another study examined six contagious diseases that had worldwide impact since the 1960s?Hong Kong flu (1968), SARS (2003), H1N1 (2009), MERS (2012), Ebola (2014), and Zika (2016)?and found out that epidemic-hit countries had a real GDP growth rate lower than unaffected countries by an average of 3 percentage points, and also took longer to recover.

Instability in both the supply and demand in labor markets due to various factors obstructs a swift economic recovery. Typically, a contagious disease lowers both labor demand as corporate revenues dwindle and labor supply with workers' fears over safety. For this reason, the impact of a pandemic-triggered job market shock on the economy could be greater than during a war when labor demand surges, or a financial crisis where labor demand falls but not labor supply. Unemployment and job market instability could weaken economic activities for a considerable time even after the contagion subsides. Studies conducted in the United States and the Republic of Korea showed that about half of workers who lost their jobs due to the pandemic were concerned over the possibility of a permanent state of unemployment. Furthermore, anxiety over the second wave of COVID-19 could magnify the vicious cycle.

Implication

The impact of labor market conditions on efforts to reboot the economy needs to be watched closely. Policies that focus on mitigating labor-related anxieties must be designed and implemented.

In major economies including the Republic of Korea, the share of workers who lost their jobs or were furloughed since the outbreak was relatively higher for low-income workers, self-employed workers, young workers, and female workers. This is also true for jobs that are hard to be done remotely or at home. Furthermore, the share of labor market participants vulnerable to the pandemic is relatively higher in the country given its fast-aging population and many self-employed workers. The pace of decline in working-age population is steepest in the country compared to other countries, and the share of self-employed workers is 24.6%—the eighth highest among the 38 Organization for Economic Co-operation and Development (OECD) member states as of 2019.

More studies must be conducted to estimate how the makeup of the country's labor market and the outlook for a further income divide stemming from the pandemic might affect the economy.

Policy-wise, a diversified analysis must be conducted on the population particularly vulnerable to COVID-19 to reduce gray areas in the employment safety network and to facilitate their reentry into the workforce. Efforts to minimize policy uncertainties surrounding the government's disease-fighting measures and financial support must be continued. Otherwise, economic recovery may be slow even if the pandemic calms down as people remain wary of the situation.

Resources

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