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The economic impact of Covid-19 lockdowns

Summary

A Westminster Hall debate has been scheduled for 29th November 2022 on the economic impact of covid-19 lockdowns. The debate will be opened by Esther McVey MP.

1 Introduction

The pandemic caused a severe recession, with an unprecedented drop in GDP during the first national lockdown in 2020. As businesses and consumers adapted, subsequent lockdowns in autumn 2020 and winter 2020/21 did not lead to as severe a decline in economic activity.

Numerous policies were introduced by the government and the Bank of England in order to support businesses and workers and mitigate at least some of the negative economic impacts from the pandemic and lockdowns.

These measures were designed to keep businesses afloat and as many people as possible employed. The measures financially supported businesses, workers and the wider public during the pandemic, as well as attempting to reduce economic uncertainty.

Many of the costs of the pandemic were associated with reduced economic activity, but we also cannot estimate precisely how much of this reduction was caused by the lockdowns and how much would have been caused anyway by people voluntarily reducing their social contact.[1]

The Library briefing papers Coronavirus: Economic impact (published December 2021), Public spending during the Covid-19 pandemic (March 2022) and Coronavirus: Impact on the labour market (August 2022) contain more detail.

1 For example, see IMF, COVID's Impact in Real Time: Finding Balance Amid the Crisis, Oct 2020

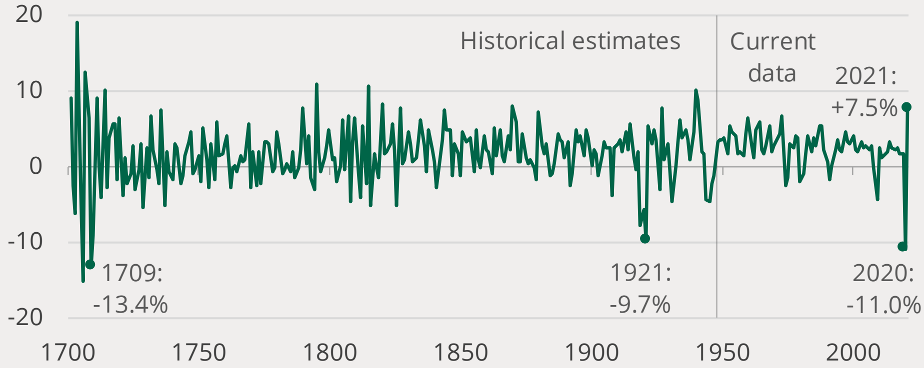
2 Economic developments in pandemic

2.1 GDP growth

The magnitude of the recession caused by the pandemic is unprecedented in modern times. GDP declined by 11.0% in 2020, the steepest drop since consistent records began in 1948. Based on less precise estimates of GDP going further back, the decline in 2020 was the largest since 1709.[2]

2020 saw a historically large decline in GDP

Annual % change in GDP



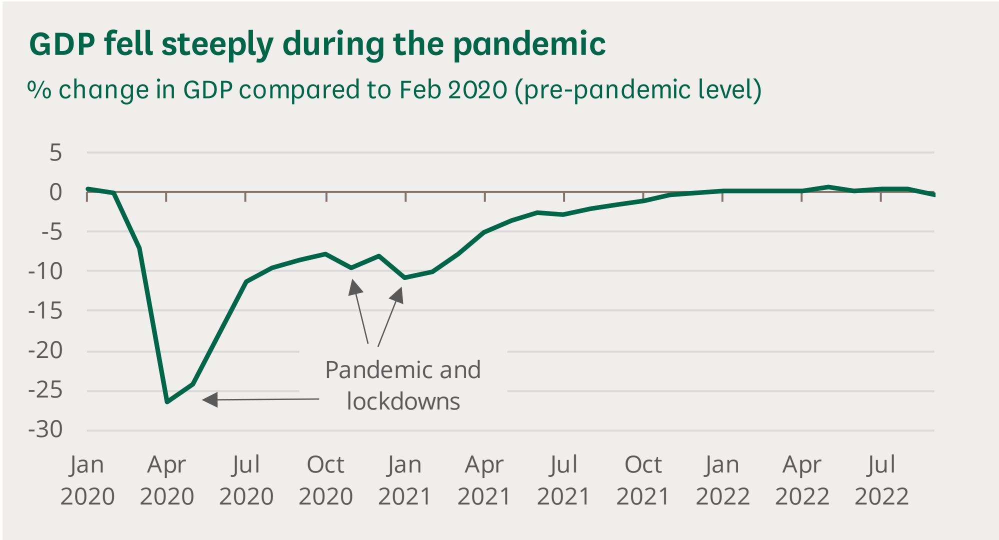
Sources: Bank of England, Millennium of macroeconomic data; ONS, Annual GDP growth

During the first lockdown, UK GDP was 26% lower in April 2020 than it was only two months earlier in February.[3] Economic activity picked up over the spring and summer of 2020, reflecting the opening up of the economy. This was followed by a rise in Covid-19 cases and further lockdowns during the autumn and winter 2020/21, leading to economic activity falling again.

The decline was, however, much less severe than during the first lockdown, as consumers and businesses had adapted over the previous year. Growth recovered over the rest of 2021.

With GDP stagnating over the course of 2022, largely due to inflation rising sharply[4], GDP was still 0.2% lower in September 2022 than it was before the pandemic in February 2020.[5]

2 Bank of England, Millennium of macroeconomic data; ONS, Annual GDP growth
3 ONS, GDP monthly estimate, UK: September 2022, 11 November 2022
4 For more see Library briefing, Background to Autumn Statement 2022
5 ONS, GDP monthly estimate, UK: September 2022, 11 November 2022



Source: ONS, Monthly GDP

The pandemic affected different sectors of the economy to different degrees. Sectors reliant on social contact, including hospitality and entertainment, have been especially badly hit. Some sectors, such as financial services, have fared relatively better.

More detail on the evolution of economic activity during the pandemic and the lockdowns is available in Library briefing Coronavirus: Economic impact (published December 2021). Some of the specific figures for economic data in that briefing have subsequently been revised, but the overall trends remain the same.

2.2 Labour market

The official unemployment and employment figures did not show the dramatic negative impact that one might expect given the scale of the recession. This is likely due to the many government support schemes, such as the Coronavirus Job Retention Scheme (the 'furlough scheme'), introduced in order to support businesses and workers during the pandemic. [6]

The **number of furloughed workers** was over 8 million during April and May 2020, during the first lockdown. It peaked at 8.9 million, approximately one-third of all employees, on 8 May 2020. This number then declined steadily to 2.4 million on 31 October, before rising again in subsequent months to 5.1 million by mid-January 2021 during the early 2021 lockdown.

Numbers have declined over 2021 as the economy reopened. According to preliminary HMRC estimates, 1.2 million jobs were furloughed on

[6] Furloughed workers are classed as employed in official statistics

30 September 2021 (roughly 5% of eligible jobs), the last day of the scheme before it ended.[7] The Library Insight Examining the end of the furlough scheme provides analysis.

Overall, 11.7 million jobs were furloughed in total on the furlough scheme. Further information and detail are available in Library briefing, Coronavirus: Impact on the labour market.

2.3 Monetary policy

In response to the coronavirus pandemic and its impact on the economy, the Bank of England and its Monetary Policy Committee (MPC) implemented a series of measures.

Prior to the pandemic, interest rates were at 0.75%. The MPC's quantitative easing (QE) programme – where the Bank of England creates additional money and uses it to buy financial assets (almost entirely UK government bonds)– stood at £445 billion. The QE programme had been unchanged since the aftermath of the EU referendum in summer 2016.

In response to the pandemic, the Bank cut interest rates to 0.1% and more than doubled its QE programme (by £450 billion), taking the total value of assets it owned to a peak of £895 billion by December 2021.

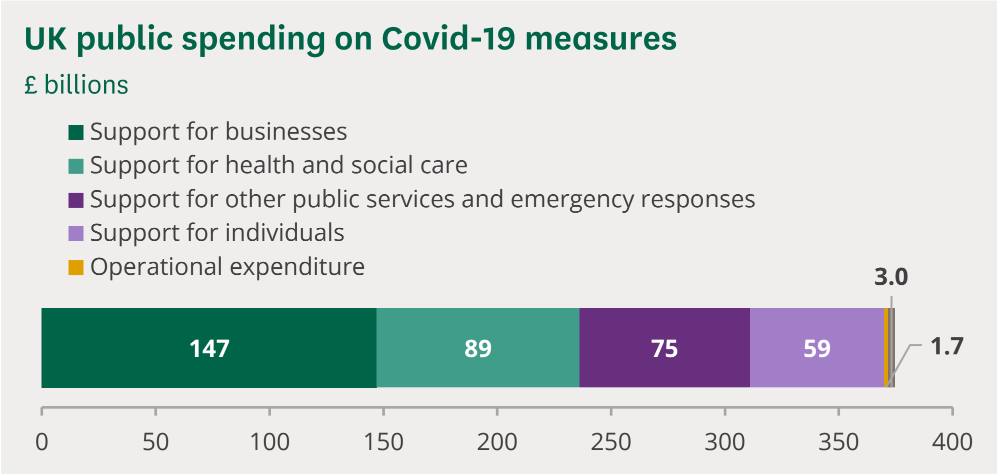
For more on monetary policy during the pandemic see section 5.2 of the Library briefing, Coronavirus: Economic impact (published December 2021). More recent developments in monetary policy are covered in the Library briefing, Background to Autumn Statement 2022.

7 HMRC, Coronavirus Job Retention Scheme statistics, 4 November 2021

3 Public spending on lockdown measures

The total amount of public money spent on tackling the pandemic has been variously estimated at around £311 billion (by the Office for Budget Responsibility in March 2022),[8] £376 billion (by the National Audit Office in June 2022),[9] and £407 billion (by the International Monetary Fund in September 2021).[10]

The most detailed functional breakdown of this spending is provided by the National Audit Office (NAO). The main costs (using the NAO's own categorisation) were as shown in the chart below.



Source: National Audit Office, COVID-19 Cost Tracker, retrieved 25 November 2022

This shows that the largest contributor to Covid-19 spending was support for businesses, with an estimated total cost of around £147 billion. Within this category, the largest individual programmes were the Coronavirus Job Retention Scheme (CJRS, also known as the furlough scheme), at an estimated £69 billion, followed by the business rates holidays for the retail, hospitality and leisure sectors (£18 billion) and the Bounce Back Loan Scheme (£14 billion).

Large proportions of the overall amount of spending went on supporting health and social care or on increasing benefits, neither of which are specifically linked to lockdowns. The Library estimates that of the main Covid-19 spending measures, roughly 40% of the money went on measures that were not lockdown-related.

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8 Office for Budget Responsibility, Economic and fiscal outlook – March 2022, 23 March 2021, table A.7

9 National Audit Office, COVID-19 Cost Tracker, retrieved 25 November 2022

10 International Monetary Fund, Fiscal Monitor Database of Country Fiscal Measures in Response to the COVID-19 Pandemic, September 2021

It is difficult to say how much of the remaining 60% as directly linked to lockdowns. For example, the CJRS ran from March 2020 to September 2021, despite full lockdown restrictions applying nationally for much less time than this.[11]

Many of the costs of the pandemic were associated with reduced economic activity, but we also cannot estimate how much of this reduction was caused by the lockdowns and how much would have been caused anyway by people voluntarily reducing their social contact.[12]

Arguments could also be made the other way. For example, we have not counted the £840 million spent on the Eat Out to Help Out scheme as lockdown-related, because it took place only in August 2020, when no national lockdowns were in force. However, the scheme was introduced in the context of trying to encourage customers back into hospitality business following the initial lockdown,[13] and could therefore be seen as related to that lockdown.

More details on the costs associated with the pandemic can be found in the Library's briefing Public spending during the Covid-19 pandemic (last updated in March 2022).

11 See the Library's briefing Coronavirus: A history of English lockdown laws for more detail on what restrictions were in force at which times.
12 For example, see IMF, COVID's Impact in Real Time: Finding Balance Amid the Crisis, Oct 2020
13 Commons Library briefing, Eat Out to Help Out Scheme

4 Public finances

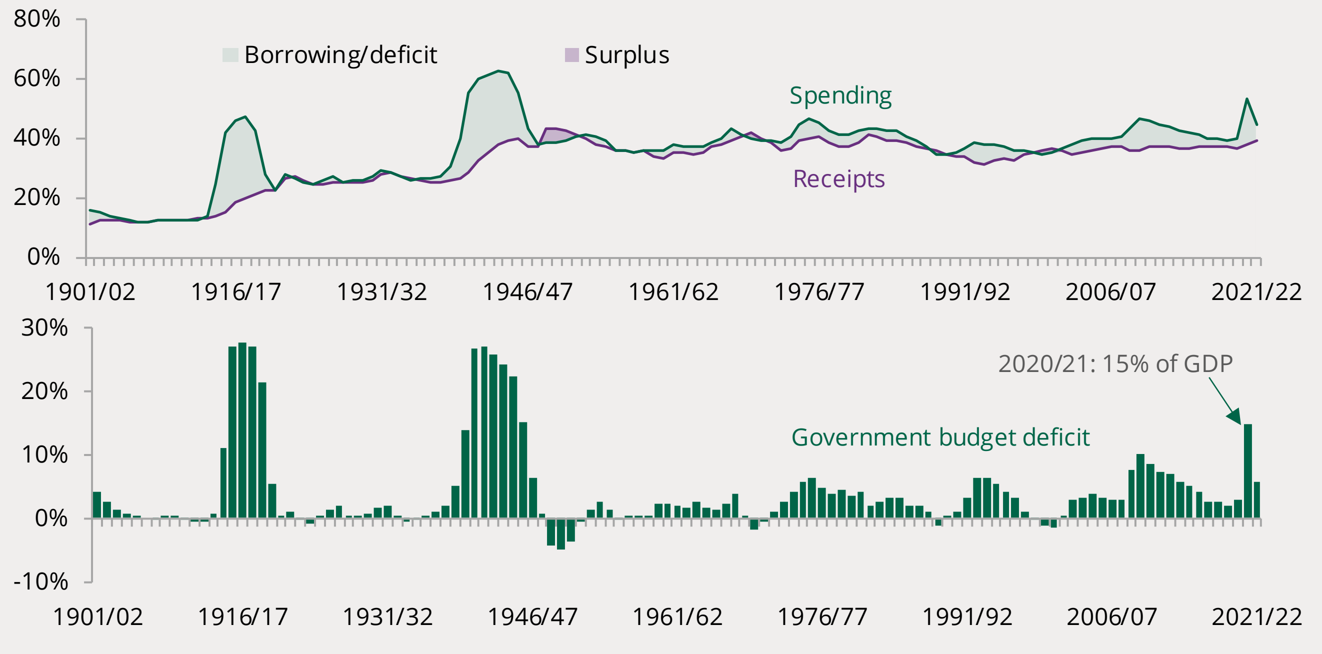
4.1 Overview

The UK's public finances were hugely affected by the economic shock of the coronavirus pandemic. It isn't possible to quantify the extent to which this was due to lockdowns. As discussed earlier, while reduced economic activity played a role, it isn't clear how much people would have voluntarily reduced their social contact in the absence of lockdowns. Nor can we say how the virus would have evolved if the Government had not introduced lockdowns.

The Government's budget deficit reached a peacetime record of 15% of GDP in 2020/21, as government spending increased and – to a lesser extent – tax revenues fell.[14] Most significantly, the Government spent around £230 billion, through measures such as the furlough scheme, to tackle the virus, support households and businesses, and limit permanent economic damage.[15]

When spending is higher than receipts, government has a budget deficit

Government spending, receipts and deficit, % of GDP



Source: OBR. Public finances databank

The public health emergency was less acute during 2021/22 and the Government was able to reduce the amount of support it provided. The Government provided around £78 billion of support to businesses, households

14 ONS. Public sector finances, UK: October 2022

15 OBR. Economic and fiscal outlook – November 2022, Table 3.28

and public services in 2021/22.[16] The budget deficit fell to 5.7% of GDP, which is the eleventh highest level since the late 1940s.[17]

The Government borrows to covers its budget deficit. This borrowing adds to the Government's debt. Government debt – the stock of its past borrowing – inevitably increased. Going into the pandemic, government debt was equivalent to around 80% of GDP; it was 97% of GDP at the end of 2021/22.[18]

4.2 The budget deficit

2020/21

In 2020/21, government had an income of £794 billion (from tax receipts and other revenues) and spent £1,107 billion (£1.1 trillion). The budget deficit was, therefore, £312 billion, or 15.0% of GDP – a peacetime record.

The deficit last exceeded 10% of GDP following the 2008-2009 financial crisis. We need to look back to World War II for the previous time it happened.

Higher spending on subsidies and goods & services

Pre-pandemic (in early March 2020) the OBR forecast that the 2020/21 budget deficit would be £55 billion. The actual deficit was around £258 billion higher at £312 billion. Public spending was £179 billion higher than forecast, while government income was £79 billion lower. Government's day-to-day spending (known as current spending) increased substantially in 2020/21, particularly on subsidies and goods and services.

Around £78 billion was provided through the Coronavirus Job Retention Scheme (the furlough scheme) and its sister programme for the self-employed (the SEISS).[19]

Day-to-day spending on goods and services in 2020/21 was £44 billion higher than forecast pre-pandemic. This was partly due to spending by government departments and devolved administrations responding to the coronavirus, including Test and Trace and the cost of vaccines. The total includes government's procurement costs.

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16 OBR. Economic and fiscal outlook – November 2022, Table 3.28

17 ONS. Public sector finances, UK: October 2022

18 ONS. Series, HF6X. Comparisons here are made with August 2019. This is because the denominator (GDP) is measured over 12 months centred around the month in question. August 2019 is the first month in which the GDP denominator isn't affected by the pandemic, as the centred GDP data extends until February 2022

19 These figures differ from those in section 5.4 because those figures are net figures which include the tax and NICs raised from the CJRS and SEISS payments.

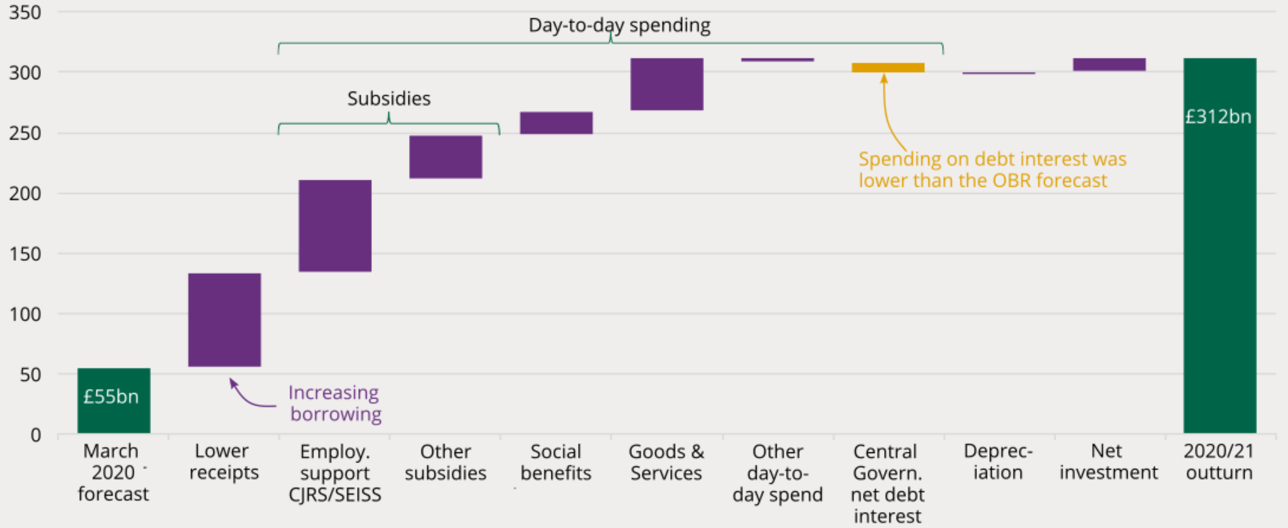
Lower spending on debt interest

The Government spent £25 billion on net debt interest in 2020/21, which is £9 billion lower than forecast pre-pandemic. Spending on debt interest was lower because of three factors: lower inflation (the interest paid on over 20% of government debt is linked to inflation); lower interest rates; and the Bank of England holding around 30% of government debt (see Box 10).

The effective interest rate paid by government on the debt held by the Bank of England is the UK's official interest rate (known as the bank rate), which reached a record low during the pandemic.

Government borrowing was £258 billion higher in 2020/21 than forecast pre-pandemic

Sources of change in public sector net borrowing between March 2020 forecast and outturn



Source: OBR. Public finances databank and ONS. Public sector finances - October 2022

Government's income

Government raised £794 billion in 2020/21 from taxes and other sources of revenue, £79 billion less than forecast pre-pandemic by the OBR.

In cash terms, the hardest hit tax was VAT, where receipts were £23 billion below the pre-pandemic forecast. Consumers were less able to go out and spend, and Government policies, such as cutting VAT from 20% to 5% for the 'hospitality, accommodation and attractions' sector, also affected VAT receipts.

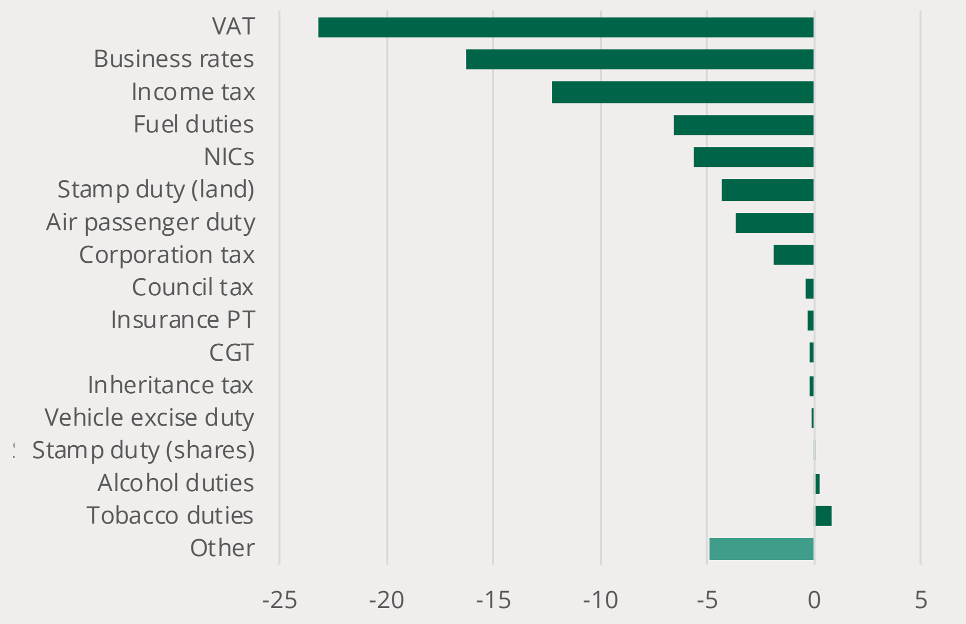
The UK's two largest sources of government income are income tax and National Insurance contributions (NICs). While receipts from both in 2020/21 were lower than forecast, they would have fallen further were it not for the furlough scheme for employees and the grants going to the self-employed.

These schemes have supported household incomes and kept workers attached to their employer. Income tax and NICs are levied on the payments.

Largely due to public health restrictions, air passenger duty receipts were 92% lower than forecast. Business rates receipts were £16 billion lower than forecast, as the Government gave a business rates holiday to sectors affected by restrictions. Alcohol duty receipts were higher than forecast, as higher sales in shops made up for lower sales in pubs and restaurants.

Tax receipts were £79bn lower in 2020/21 than forecast

Difference between 2020/21 receipts and March 2020 forecast, £ billion



Source: OBR. Public finances databank and ONS. Public sector finances - October 2022

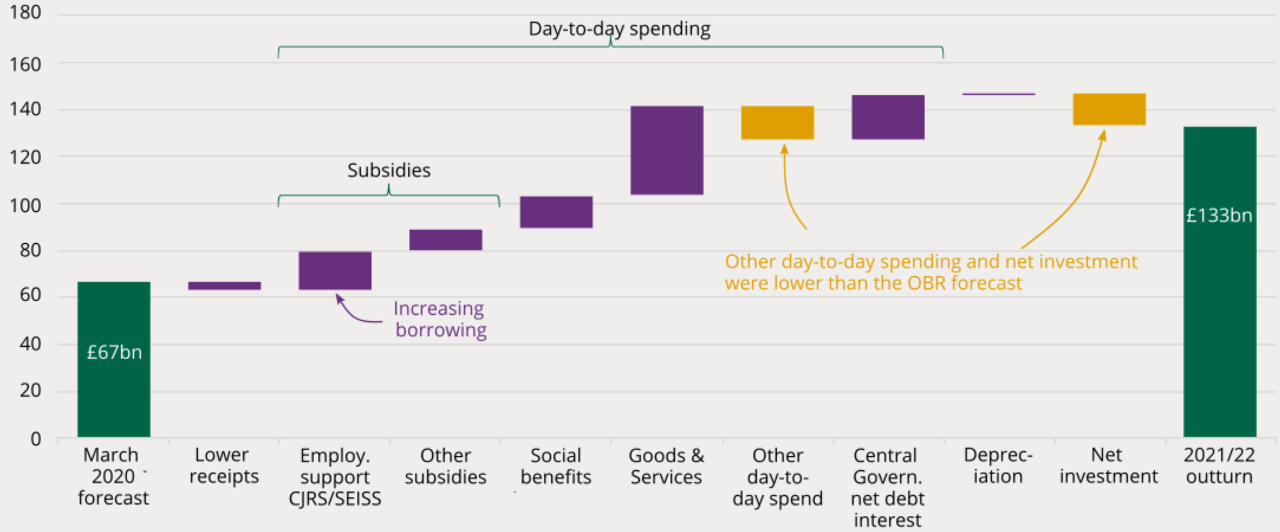
2021/22

The public health emergency was less acute during 2021/22 and the Government was able to reduce its support for public services, households and businesses. The deficit fell to £133 billion. This is equivalent to 5.7% of GDP, which is the eleventh highest level since the late 1940s. Pre-pandemic the OBR forecast that the 2021/22 budget deficit would be £67 billion, or 2.8% of GDP.

In 2021/22 Government spent around £17 billion through the CJRS and SEISS – £61 billion less than during 2020/21. Government spending on goods and services was £39 billion higher than the OBR forecast pre-pandemic. This includes additional spending on health. Debt interest spending was £19 billion higher than forecast pre-pandemic while government income was around £4 billion lower than forecast. Debt interest spending was higher due to the interest being paid on index-linked gilts rising with higher than forecast inflation.[20]

Government borrowing was £66 billion higher in 2021/22 than forecast pre-pandemic

Sources of change in public sector net borrowing between March 2020 forecast and outturn



Source: OBR. Public finances databank and ONS. Public sector finances - October 2022

[20] The interest paid on around one quarter of the Government's debt is linked to the Retail Prices Index (RPI) measure of inflation.

4.3 Government debt

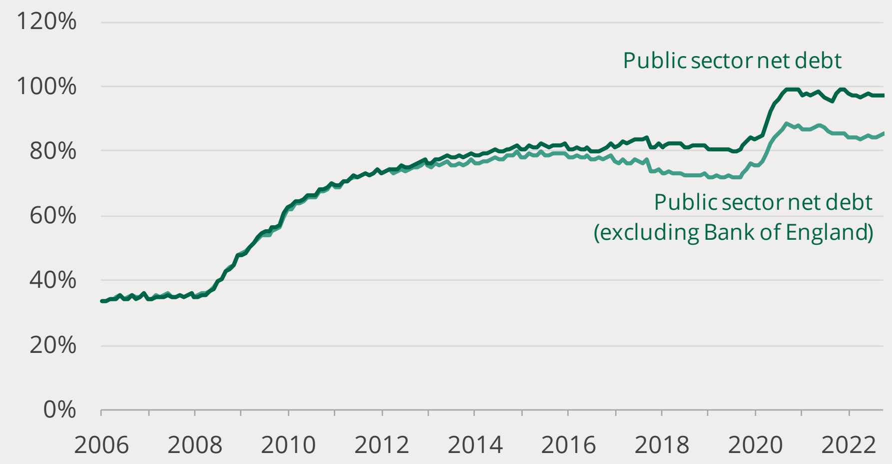
Government debt is the overall level of government indebtedness, built up over many years. Broadly speaking, it is the stock of borrowing arising from past budget deficits.

Government debt increased as the Government borrowed extensively during the pandemic. In addition, some of the Bank of England's policy measures – such as the new Term Funding Scheme – added to government debt.[21]

Going into the pandemic, government debt was equivalent to around 80% of GDP; it was 97% of GDP at the end of 2021/22. Once some largely temporary measures taken by the Bank of England are removed, the underlying debt-to-GDP ratio was 84% at the end of 2021/22, having been around 72% prior to the pandemic. [22]

Government debt is higher than pre-pandemic

Public sector net debt, including and excluding BoE % GDP



Source: ONS. Series HF6X, CPOA

[21] The Term Funding Scheme was designed to ensure banks pass on interest rate cuts to businesses and consumers by giving them access to cheap loans from the Bank of England. The scheme is formally called the Term Funding Scheme with additional incentives for lending to SMEs (TFSME)

[22] ONS. Series. HF6X. Comparisons here are made with August 2019. This is because the denominator (GDP) is measured over 12 months centred around the month in question. August 2019 is the first month in which the GDP denominator isn't affected by the pandemic, as the centred GDP data extends until February 2022

4.4 Further information

The Library's Coronavirus: Economic impact includes a more detailed discussion of the public finances. It was last updated in December 2021 and some of the data has since been revised.

The Institute for Fiscal Studies How did COVID affect government revenues, spending, borrowing and debt? focuses largely on 2020/21. It was last updated in June 2021.

5 Press articles

We are all paying the terrible price for lockdown: A historic failure of government during the pandemic set a ticking time bomb not just under the economy, but also in health and education

Jonathan Sumption

Daily Telegraph, 19 November 2022

Only now are the crippling costs of lockdown becoming fully apparent: The economic harm these policies have caused may be even worse than the financial crisis

Jeremy Warner

Daily Telegraph, 20 August 2022

Long Covid to leave lasting mark on UK economy, says IFS: Workers losing total of £1.5bn a month as a result of chronic illness, think-tank finds

Delphine Strauss

Financial Times, 27 July 2022

How has the UK economy fared in the two tumultuous years since Covid? Analysis: the country suffered its worst recession in a century and inflation made an unwelcome return

Richard Partington

The Guardian, 23 March 2022

UK high streets bounce back from Covid curbs as London falters: Britain's suburbs and small towns benefit from pandemic shift towards local shopping

Chris Cook

Financial Times, 27 February 2022

How the UK high street was hit by the pandemic: Although 'levelling up' focuses on the north and Midlands, the worst affected areas have been elsewhere

Chris Cook, Dan Clark, Alexandra Heal, Ella Hollowood, Oli Elliott, Sam Joiner and Caroline Nevitt

Financial Times, 19 January 2022

How to assess the costs and benefits of lockdowns: The policy will stay in governments' toolkits. A growing body of research will guide its use

The Economist, 1 July 2021

UK economy: one year on from the start of the first Covid lockdown: A sharp rebound in 2021 will not make up for the worst fall in output in 300 years

Valentina Romei

Financial Times, 23 March 2021

A year of Covid lockdowns has cost the UK economy £251bn, study says: Some of the poorest areas will suffer disproportionate burden for longer if government does not act, warns CEBR

Larry Elliot

The Guardian, 22 March 2021

What is the economic impact of the latest round of lockdowns?

The Economist, 13 January 2021

With every lockdown we lose some more of our economy

David Smith

Sunday Times, 10 January 2021

6 Parliamentary material

6.1 Written questions

Economic Situation: Coronavirus: Question for Treasury: UIN 128228

Asked by Mr Virendra Sharma

Asked on 23 February 2022

To ask the Chancellor of the Exchequer, what estimate his Department had made of the cost per day of covid-19 lockdowns to the economy.

Answered by John Glen

Answered on 28 February 2022

The pandemic and associated non-pharmaceutical interventions (NPIs) created significant economic disruption and drove the largest recession on record, with the UK economy contracting by 9.4% in 2020.

The government has outlined the impact of restrictions and lockdowns on the economy in the following publications: Analysis of the health, economic and social effects of Covid-19 and the approach to tiering (30 November 2020), Budget 2021 (3 March 2021) and Living with Covid (21 February 2022). These documents can be found below:

https://www.gov.uk/government/publications/the-health-economic-and-social-effects-of-covid-19-and-the-tiered-approach

https://www.gov.uk/government/publications/budget-2021-documents

https://www.gov.uk/government/publications/covid-19-response-living-with-covid-19

Any attempt to estimate the specific economic impacts of precise changes to individual restrictions for a defined period of time would be subject to very wide uncertainty. HM Treasury, as part of its normal activities, carefully monitors the UK economy, and any risks to it, and remains ready to respond to challenges.

Business: Coronavirus: Question for Treasury: UIN 93800

Asked by Rachael Maskell

Asked on 15 December 2021

To ask the Chancellor of the Exchequer, what additional support he will make available to businesses if further covid-19 lockdown restrictions are introduced.

Answered by Helen Whately

Answered on 11 January 2022

In response to the Omicron variant, the government has recently announced £1 billion of new grant support for the hospitality, leisure and cultural sectors to protect jobs and businesses through this period of uncertainty.

This builds on the comprehensive economic response the government has provided over the course of the pandemic, providing around £400 billion of direct support for the economy to date, which has helped to safeguard jobs, businesses and public services in every region and nation of the UK.

As we have done throughout the pandemic, we are closely monitoring the impact of COVID-19 on the economy. We will continue to respond appropriately and proportionately to the changing path of the virus.

6.2 Oral questions

Covid-19: Lockdowns

HL Deb 9 February 2022, c 1641-44

Covid-19: Economy Update

HC Deb 22 October 2020, c 1249-73

6.3 Debates

Economy: The Growth Plan 2022

HL Deb 10 October 2022, c 557-618

Long Covid: Impact on the Workforce

HC Deb 31 March 2022, c 1039-60

Covid-19: Economic Recovery

HL Deb 20 April 2021, c 264GC-310GC

Covid-19

HC Deb 22 February 2021, c 663-731

6.4 Library briefings

Coronavirus: Impact on the labour market

House of Commons Library, August 2022

Coronavirus: Support for businesses

House of Commons Library, July 2022

Hospitality industry and Covid-19

House of Commons Library, May 2022

Public spending during the Covid-19 pandemic

House of Commons Library, March 2022

General Debate on the impact of Long Covid on the UK Workforce

House of Commons Library, March 2022

Coronavirus: Economic impact

House of Commons Library, December 2021

7 Further reading

How did Treasury policy-makers approach the economic response to Covid-19?

Economic Observatory, November 2022

Rishi Sunak's covid record—and what it tells us about his views on health, wealth, and the value of science

British Medical Journal, November 2022

The economic impact of COVID in the UK depended on where you live

The Conversation, November 2022

Covid and the UK Economy

Speech by Clare Lombardelli, Chief Economic Advisor, HM Treasury, June 2022

Right Where You Left Me? Analysis of the Covid-19 pandemic's impact on local economies in the UK

Resolution Foundation, June 2022

A Literature Review and Meta-Analysis of the Effects of Lockdowns on COVID-19 Mortality

Johns Hopkins Institute for Applied Economics, Global Health and the Study of Business Enterprise, January 2022

The impact of COVID-19 restrictions on UK growth and the benefits of full inoculation

LSE, July 2021

Long COVID and the labour market

Institute for Fiscal Studies, June 2021

How did COVID affect government revenues, spending, borrowing and debt?

Institute for Fiscal Studies, June 2021

The Great Lockdown: Dissecting the Economic Effects

IMF, October 2020

Easing does it: Economic policy beyond the lockdown

Resolution Foundation, July 2020

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