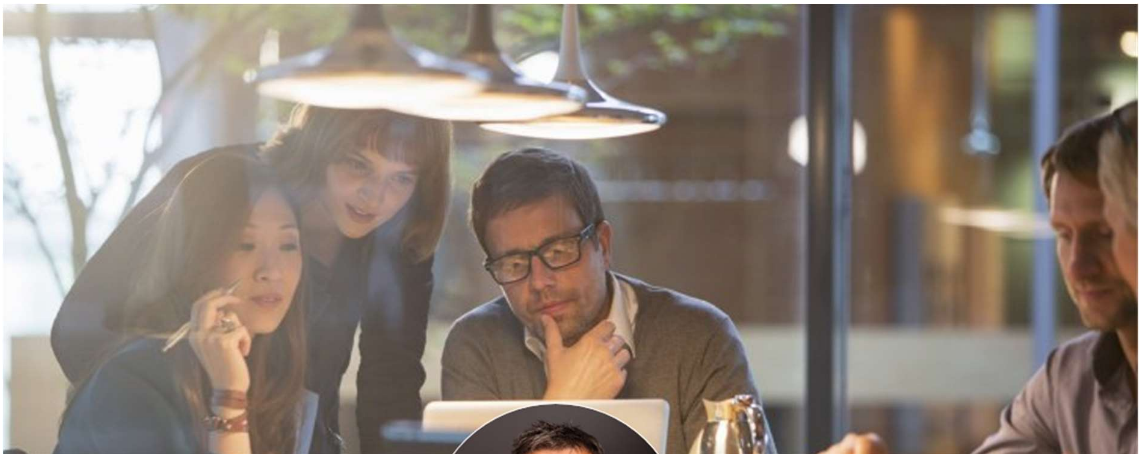
Global Economic Outlook 2020

13th of August 2020



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IN A NUTSHELL:

The covid-19 pandemic led to the world's worst recession since the Great Depression. Indeed, most of the countries imposed restrictive measures and social distancing, with a very negative impact on service-related sectors and global demand. Governments and central banks launched simultaneously huge stimulus policies to help maintain jobs, household income and access to liquidity. In spite of this strong intervention, economies fell sharply but are expected to rebound gradually later this year and especially in 2021. China should be the only major economy to record positive growth this year, benefitting from an earlier and stronger recovery compared to other countries. However, prevailing downside risks will linger. A second wave of the virus could weigh again on economic activity, but the risks are lower as governments should use targeted local lockdowns. The main short-term risk relates to renewed tensions between the US and China.

Economic forecast tables

GDP Growth %	BNP Paribas Forecasts 2019	2020	2021	Forecast Revisions (%) 2020	2021
United States	2,3	-4,9	4,8	1,7	-1
Japan	0,7	-4,8	2,1	0,2	0
United Kingdom	1.4	-9,1	5,3	-0,3	-0,1
Eurozone	**1.2**	**-9**	**5,8**	**0,2**	**0**
Germany	0,6	-5,6	5,3	0,4	0
France	1,3	-11,1	5,9	0	0
Italy	0.3	-12,1	6,1	0	0
Emerging					
China	6,1	2,5	8,1	0	0
India*	4.2	-4,7	9,5	-7,4	4,3
Brazil	1,1	-7	4	0	0
Russia	1,3	-6,5	3,5	0	0

* Fiscal year starting in April

Source: BNP Paribas

CPI Inflation %	BNP Paribas Forecasts 2019	2020	2021	Forecasts Revisions (%) 2020	2021
United States	1,8	0,8	1,5	-0,4	-0,7
Japan	0,5	-0,3	-0,7	-0,1	-0,5
United Kingdom	1,8	0,8	1,3	0,1	-0,4
Eurozone	**1,2**	**0,1**	**0,9**	**-0,1**	**-0,3**
Germany	1,4	0,4	1,5	-0,1	0,1
France	1,3	0,5	1	0,2	-0,3
Italy	0,6	-0,2	0,5	/	/
Emerging					
China	2.9	2,5	2,3	-0,6	0,3
India*	4,8	2,5	3,5	-1,3	0
Brazil	3.7	2,5	3	0	0
Russia	4,3	3	3,5	-0,3	0

* Fiscal year starting in April

Source: BNP Paribas

US: a troubled economic recovery

The US activity contracted by nearly 33% (annualised rate) on a quarterly basis over the second quarter. This is the worst recession since 1946. The covid-19 pandemic spread later in North America than in Europe and the country paid a heavy toll with more than 160k deaths. The US government reacted strongly, launching four consecutive stimulus packages (around 15% of GDP) to curb the impact on households and businesses and still expects an agreement on a fifth support plan. The Fed also quickly responded to prevent the economy from falling more by using conventional and unconventional tools. As the lender of last resort, the Fed injected massive liquidity. Equity markets promptly recovered, corporate bond spreads normalized, but the downturn deeply affected fundamentals. After an alarming recent surge of the virus in the Southern States, infection cases seemed to have peaked, but lockdown measures and social distancing prevented a quick reopening of the economy. Despite this, manufacturing sentiment showed signs of improvement, indeed latest surveys in the service sector showed a gradual recovery for the second consecutive months. Consumption rebounded in June especially in interest rate-sensitive sectors. With the absence of job retention schemes, the deterioration of the labour market was unprecedented but latest employment data were more encouraging. Inflation expectations dropped to historical lows, and short-term factors should cap a possible rise. We do not expect inflation to reach the central bank target next year since high unemployment will dampen wage growth. Given the latest more positive economic data (sharp rise of the so-called economic surprise index) and thanks to the massive government and central bank support, , we upgraded our growth forecast (compared to our previous expectations) by 1.7% for 2020 as we now see GDP contracting by 4.9% this year before firmly rebounding by 4.8% in 2021. US inflation will remain lower than expected in our previous global outlook. The latest headline Consumer Price Inflation (CPI) rebounded from almost zero in May to around 1% in July. Core CPI inflation rebounded to 1.6%. We revised down the figure for both this and next year to 0.8% and 1.5% respectively.

The main short-term risk is a worsening in US-China relations. A self-sustained recovery of the US economy also depends on the evolution of the virus. The country also faces a number of downside risks. Imbalances were already present before the crisis worsened. Corporate debt skyrocketed while the public deficit widened. US elections might bring more uncertainty.

Eurozone: encouraging first signs

Encouraging first signs were seen in euro area with leading economic indicators underscoring signs of an upturn. However, until a vaccine is found, some caution is recommended. There was a deep economic crisis and business losses will be difficult to absorb quickly. The logical rebound expected in the second half of 2020 following the end of the lockdown of the European population, will not erase the loss of activity recorded in the first half of the year. Thus, European growth should fall to -9% for the year 2020 and rebound in 2021 with an estimated growth of +5.8%. We also saw signs of a recovery in the Eurozone. Services PMI rebounded strongly in June, approaching 50 (figures above 50 suggest expansion), after bottoming out in April 2020 at its lowest level since the creation of the euro area (12). Despite the recent rebound, household consumption is expected to remain weak as suggested by consumer sentiment surveys. The household savings rate is expected to reach 19% of disposable income in 2020, significantly higher than the long-term average (13%). Companies still face uncertainties, and this could weigh on investments in the short-term. At the end of the year and especially in 2021, the effects of the massive stimulus program and central bank bond purchases should drive higher growth. Some upside could come from a virtuous circle with public investments leading to a significant recovery in consumer and business sentiment which would generate a boom in private sector investments. It is however too early to assume that.

Regarding inflation, headline inflation declined sharply (+0.1% in May, from 1.4% in January) under the impact of low energy prices, while core inflation is still mild. This was despite monetary expansion. There was a slight increase in June to 0.3%. Monetary expansion is not a risk for higher inflation as long as credit growth remains weak. We made some minor downward adjustments on our forecast and see inflation close to zero this year (0.1%) and close to 1% (0.9%) in 2021.

UK: two major risks

The country lifted containment measures much later than the rest of Europe, due to its late implementation of restriction measures. The UK GDP posted a much larger quarterly decline compared to other European countries (-20%). To curb the impact of the crisis, the Chancellor of the Exchequer promised companies GBP 330 bn in loan guarantees and announced a GBP 30 billion employment plan. The government also launched job support schemes for about GBP 80 bn. Nevertheless, we expect economic figures to improve in the coming months thanks to the reopening of the economy and the country should catch up with its European neighbours. But it will take a long time for the UK economy to return to its pre-crisis level. We slightly revised down our growth forecasts, and expect GDP to fall by 9.1% in 2020 before bouncing by 5.3% next year.

The failure of negotiations with the EU on a free trade agreement is another source of concern for the UK economy. This risk is particularly high as the United Kingdom has officially rejected the possibility of extending the transition period expiring at the end of the year. Talks over the last two months resumed and both sides expect an agreement on 31 October. If no agreement is reached, the rules of the World Trade Organization would apply, and this would be a much more constraining Brexit. The risk of having this type of agreement remains real, having serious consequences and causing major economic turmoil and financial market volatility. Inflation in the UK should follow a similar path compared to the US with 0.8% this year and 1.3% next year.

Japan: a slow recovery

Japan's economic momentum has already been weakened by the VAT increase in Q4 2019 and the typhoon. The country will also face a recession as a result of the covid-19 crisis. The government quickly imposed a state of emergency, which it lifted at the end of May. Leading economic indicators pointed to a recovery in activity but slower than in Europe, particularly in the manufacturing sector which remains in contraction in Japan. Domestic demand, which already weakened last year, is showing signs of recovery. Imports as well as household spending surprised to the upside in June, confirming the improvement in household sentiment. This rebound was supported by the government's fiscal stimulus, which amounts to nearly 20% of GDP. This fiscal package will add to the already very high public debt in the world. However, solvency risks are limited thanks in particular to the central bank's ultra-accommodative monetary policy. The BoJ left negative rates unchanged but stepped up its quantitative easing measures, notably through yield curve control, in order to avoid an increase in financing costs.

These expansionary policies are taking place in a context of low prices. We expect negative growth of around -4.8% in 2020 followed by a limited rebound of +2.1% in 2021.

Deflation remains a key concern for the country's future. We now expect -0.3% and -0.7% in 2020 and 2021 respectively.

Emerging market: China in the lead

Portfolio investments have gradually returned to emerging markets after strong outflows seen during the crisis. This leads to stabilization in exchange rates. Cumulative net inflows of non-resident portfolio investment in bonds and equities totalled USD 22 bn, thus overtaking cumulative net outflows of USD 100 bn between the end of February and mid-May. Even if China is the country with the most visible post-lockdown economic recovery, economic activity has rebounded across all emerging countries. Confidence also seems to be returning with PMIs increasing about 10-20 points from the April low.

Even if indicators are improving, the rebound in local stock markets remains fragile. In Brazil, India and Mexico, the pandemic is not under control and some countries are imposing new selective confinements. Moreover, the soaring budget deficits could generate a significant downside risk, even if we do not observe any difficulty in refinancing public debt for the moment.

China reopened its economy in March, while other continents were just entering a period of lockdown. Thus, the recovery came earlier and was more vigorous, although the rebound was differentiated by sector of activity. Leading economic indicators pointed to a significant V-shaped rebound in industrial production. Electricity demand saw a sharp recovery. Investment in public infrastructure and real estate also fueled this recovery supported by fiscal measures put in place by the authorities. Consumption remained weak due to household income losses and the deterioration of the labour market. The outlook for the export sectors remains dependent on the demand recovery from developed countries. A possible second wave would further weigh on domestic demand. There are also growing risk of renewed tensions with the United States. Although initially considered insufficient, the government's stimulus plan gained momentum and should enable the Chinese economy to avoid recession. By easing monetary and credit conditions, the central bank responded to higher demand for liquidities of the financial sector. We kept our forecast for Chinese GDP unchanged at +2.5% for this year followed by a sharp rebound to +8.1% next year. Inflation was revised down for this year and slightly up for next year with 2.5% and 2.3% respectively.

The forecasts for most other main emerging economies are unchanged except for India. Growth was revised down. The recent newsflow suggests that growth will be hardly hit this year due the lockdown policies, but it should witness a sharp rebound in 2021. Logically, inflation will also be lower than initially expected with 2.5% instead of 3.8% this year. Inflation in 2021 is still expected at 3.5%.

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