GLOBAL ECONOMICS CHART BOOK

Past the worst, but recovery to be uneven

- After falling by around 6% q/q in Q1, world GDP looks set for an equally sharp slump in the second quarter. As major advanced economies are following Asia’s lead in easing containment measures, global activity has hopefully passed its trough. Manufacturing and construction sectors are back to work and there are signs of life in high-frequency indicators such as US gasoline demand and passenger journeys throughout DMs, as suggested by Apple map route searches. (See Chart 1.) However, experience from China suggests that consumer demand is likely to be fragile for some time as people steer clear of shopping malls, restaurants and public transport. Lockdown measures may need to be re-imposed in some countries amid future outbreaks. And since unemployment has risen around the world, what may initially look like a V-shaped recovery seems set to lose steam, leaving activity below its pre-virus path for years to come.

- Coronavirus infections appear to have peaked in most DMs, but cases are ramping up in EMs outside Asia.

- Output and activity collapsed in March and April but may have reached a trough in most DM economies.

- Business surveys plunged to record lows in May, but even this probably understates how much output fell.

- Consumer spending faces strong headwinds even as containment measures are eased and shops reopen.

- External trade activity has fallen only moderately so far, but timely and leading indicators are down sharply.

- Labour markets are taking a big hit, but government job and benefit schemes are cushioning the blow.

- Inflation plunged in April due mainly to energy price effects but also falling core inflation.

- Monetary policymakers have averted a funding crisis. Attention has now turned to supporting businesses.

- Commodity prices have rallied, with oil up over 50% from a month ago and gold trading at over $1,700/oz.

- Financial markets have regained some poise after unprecedented provision of liquidity by central banks.

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**Chart 1: Apple Maps Driving Routing Requests (7-day moving average, 13th January = 100)**

- **US**
- **UK**
- **Germany**
- **France**
- **Italy**

Source: Apple Mobility
Coronavirus

- At the global level, the number of new coronavirus cases has continued to rise at a fairly consistent pace of between 65,000 and 100,000 each day over the past six weeks (2). However, that number has masked a divergence in trends at the country level.

- In most advanced economies, the peak appears to have passed. Admittedly, in terms of cases per million of the population, advanced economies are still faring badly. But across the euro-zone, the number of new daily infections has fallen steadily now since the start of April (3). And in the US, while the country still has the highest number of cases worldwide, the tide appears to be turning too (4). But the story is very different in EMs. In particular, Russia and Brazil are seeing a rapid increase in the total number of new cases, with the former now second to only the US (5).

- In those countries where the virus has seemingly been brought under control, governments are starting to slowly ease lockdown restrictions (6). In the euro-zone, some shops and restaurants are reopening, and children are starting to return to schools in some countries Elsewhere, the UK has recently moved to the “level 3” stage of lockdown and similar moves will start to occur in the coming weeks. But certain EMs are tightening restrictions, including in Chile while others, such as India, are extending their lockdowns (7).

Sources: Refinitiv, Oxford University, CEIC, John Hopkins, CE
Output and Activity

- So far, it looks like the world economy shrank by 5.9% q/q in Q1 – by far the weakest performance since at least 1980, and probably since WWII. Nascent signs of a recovery in several major economies won’t prevent an even bigger drop in global output in the second quarter.

- Out of those that have reported so far, GDP in China fell the furthest in Q1. This makes sense given that China is ahead of other countries in terms of the virus and economic impact. The euro-zone economy shrank by almost 4%, while other DMs shrank by 1-2%, with the damage coming towards the tail end of the quarter. Manufacturing output in DMs suffered the largest monthly drop since at least 1995 in March, with autos and textiles faring the worst, and food and pharmaceuticals the best. A lot worse is to come in April. Indeed, having fallen by 5.5% in March, output in the US fell by 13.7% last month.

- In most DMs, though, things may now be passing the worst as restrictions are eased and many firms reopen, albeit with diminished capacity due to social distancing. In the US, for instance, gasoline demand is up, and diners are slowly returning to restaurants. In Europe, transport use has now risen in major cities, which is where China was around the end of February. However, caution on the part of consumers, weak business balance sheets, and the lingering threat of a “second wave” will prevent a strong recovery. We don’t expect global GDP to make it back to its pre-virus path within our forecast horizon.
Business surveys

- With most economies in lockdown throughout the April survey period, it was no surprise that the PMIs went from bad to worse. The global composite PMI fell to 26.5, 13 points below the previous low. And the picture was just as bleak at the country level, with almost every major economy hitting all-time lows (14).

- The services sector has clearly borne the brunt of the economic collapse (15). But, at 39.8, the global manufacturing PMI is still consistent with sharp falls in industrial output. What’s more, that fall would have looked even worse if it weren’t for the perverse effect from the suppliers’ delivery times component (16). A lengthening in delivery times contributes positively to the headline number since it usually reflects strong demand. However, in this case the lengthening reflects severe supply chain disruption. Indeed, the output sub-index alone suggests that industrial output is set to fall by 12% y/y (17).

- On past form, the global composite PMI points to advanced economy GDP falling by 9% q/q annualised (18). Given the qualitative nature of the surveys, though, the PMIs may be understating the weakness. In fact, we expect GDP to decline by over two times that. But while the surveys may struggle to fully capture the downturn, they do provide a reliable gauge for any turning points once lockdown measures ease. In China, where lockdown measures were lifted in March, both the official and Caixin PMIs rebounded (19).

Sources: IHS Markit, Refinitiv, Capital Economics
Consumer Spending

- The consumer sector continues to face massive headwinds even as lockdowns begin to ease in several countries, with discretionary spending limited by low confidence and higher unemployment. Retail sales data in the US plunged by 16.4% in April, with grocery spending and online sales the only components to see gains (20). The 11.2% fall in euro-zone retail sales in March left sales at a level last seen in 2014.

- Restaurants and bars have begun to open in most DMs (21), but timely data shows that discretionary consumption remains significantly lower than pre-virus levels. For example, in the US, air travel and restaurant reservations are still down by over 90% compared to last year (22). City centre footfall in the UK may have reached a trough, but it is still depressed (23) and there is a considerable risk that high streets will continue to struggle as consumers remain cautious about going out shopping post-lockdown.

- Even putting virus concerns to one side, the massive hit to jobs, incomes and household wealth is dragging heavily on consumer confidence (24). Recent experience in China suggests that the consumer recovery will be gradual. Indeed, high-frequency passenger travel figures show that households are largely choosing to stay at home at weekends rather than travel and shop. And official data show that growth in retail sales and broader services activity remains deep in negative territory at -7.5% and -4.5% y/y respectively (25).

Sources: Refinitiv, TSA, IMDB, OpenTable, Springboard, CEIC, CE

Chart 20: Breakdown of US Retail Sales (% Change Between February & April)

Chart 21: Global Restaurant Bookings (% y/y)

Chart 22: US Discretionary Consumer Indicators (% y/y)

Chart 23: Footfall in UK City Centres (% y/y)

Chart 24: Standardised Consumer Confidence Indices

Chart 25: China Retail Sales & Services Prod. (% y/y)
External Trade

- February’s CPB Netherlands trade data showed a 1.5% monthly contraction in global trade (26). But given that the lockdowns did not come into effect until mid-March in most economies, these data are old news. Instead, more timely national data provide some insights into the impact of the coronavirus. Japanese exports slumped by 11.7% y/y in March, with a particularly sharp 26% fall to the EU (27). And more timely data from Korea showed that exports were down by a staggering 30% y/y in the first ten days of May (28).

- Business surveys also point to a sharp decline in world trade volumes in the months ahead. At the global level, the new export orders component of April’s manufacturing PMI is consistent with trade volumes falling by 15% y/y (29). And the picture may be bleaker than the surveys suggest since their qualitative nature means that they are not designed to capture large falls in new orders.

- On the face of it, our forecast of a 5.5% annual contraction in GDP is consistent with a much larger 40% plunge in world trade volumes. But with the services sector harder hit, world trade in goods will probably fall to a lesser extent relative to the decline in GDP than in the past. On balance, we expect goods trade to decline by around a fifth this year (30). Once lockdowns start to ease, though, evidence from China suggests trade volumes might recover to more normal levels quite quickly (31).
Labour Markets

- The virus has clearly hit labour markets hard, with the employment component of the developed market composite PMI pointing to a collapse in G7 employment (32). Indeed, the latest evidence from the US showed that the unemployment rate surged to 14.7% in April – the highest on record (33). While employment fell in every sector, unsurprisingly, job losses were concentrated in leisure & hospitality (34).

- Government job retention schemes should prevent the worst-case scenario. In the euro-zone, the jobless rate held broadly steady at 7.4% in March. While we expect the rate to surge, with over 32 million people now part of short working hours schemes, it is unlikely to reach the 15% figure which we had pencilled in (35). Meanwhile in the UK, given that the unemployment rate typically rises by about 0.3% for every 1% fall in GDP (36), we would expect the unemployment rate to rise to 12%. But with eight million people signed up to the government’s furlough scheme, that number will portably end up more like 9%.

- Unemployment rates should fall back fairly quickly once the lockdown measures ease. But with some businesses inevitably going bust, and others unlikely to be operating at full capacity when they do reopen, there will probably be some permanent scarring to the labour market. After all, our estimate of China’s composite employment PMI is still consistent with limited new job creation (37).

Sources: Refinitiv, National Labour Ministries, IHS Markit, Zhaopin, CE
Inflation

- Headline inflation in the OECD slumped to 0.5% in April and the core rate fell to its lowest level since early 2011, at 1.3% (38). With weak global demand keeping underlying inflation subdued, we expect a period of disinflation this year, even as oil prices begin to recover. Compared to our pre-virus oil forecast, energy prices look to have knocked about 1.5%-pts off headline inflation so far (39). But we suspect this drag from oil prices is more or less over now – energy prices should soon start to push up inflation rates.

- At the same time, though, the impact of weaker demand from the coronavirus is weighing on underlying price pressures. US core inflation fell to a nine-year low of 1.4% in April, albeit in large part due to extreme falls in the prices of goods and services in exposed sectors as opposed to the more general easing of price pressures witnessed after the financial crisis (40). Outside emerging Europe, core inflation in emerging markets has also fallen this year (41). With activity well below potential in all EMs, further falls are likely.

- Our forecast for GDP to contract by around 8.5% in DMs is, on the face of it, consistent with core inflation plunging to almost minus 2% (42). However, we instead expect core inflation to ease to below 1% on average. For one thing, the damage to the economy’s supply capacity should restrict how low core inflation can go; e.g. fewer seats restaurants may cause the prices of meals to rise. What’s more, the flatness of the Phillips curve suggests that the spike in unemployment will have a limited impact on wage growth (43).

![Chart 38: OECD Inflation (Excluding Turkey, %)](chart)

![Chart 39: Oil Price & Energy Contrib. to OECD Inflation](chart)

![Chart 40: Selected Components of US CPI (% y/y)](chart)

![Chart 41: Jan-Apr.* Change in EM Core Inflation (%-pts)](chart)

![Chart 42: Output Gap & Core Inflation in DMs](chart)

![Chart 43: G7 Phillips Curve](chart)

Sources: Refinitiv, OECD, CEIC, Capital Economics
**Monetary**

- Central banks have generally relied heavily on asset purchases and lending facilities to provide policy support to financial markets and the wider economy. Market strains were biggest in the US, so the Fed’s balance sheet expansion has been the largest of the “G4” major central banks. In contrast, there has been little stress in Japan, and the BoJ’s response has been much smaller accordingly (44).

- Having surged by $2tn between the middle of March and April, the Fed’s outright security holdings have only risen by $500bn since then now that liquidity problems have abated (45); its holdings of MMF assets and primary dealer credit have actually fallen (46). Liquidity concerns have shifted to the non-financial sector, and so have policymakers’ efforts. There has been a promising uptake of loans under the BoE’s Term Funding Scheme, and credit extended under the ECB’s LTROs has risen by over 50% since March.

- But the Fed’s Main Street Lending Program won’t be up and running for another few weeks. Strangely, US banks have reported that, in stark contrast to the UK, euro-zone and Japan, firms’ demand for bank loans is subdued (47). For firms wanting access to credit, US banks have apparently tightened lending standards drastically, again in contrast to lenders in other advanced economies (48).

- Meanwhile, after extensive policy easing in China, credit growth there hit a 22-month high in April (49). With more monetary stimulus on the way, credit growth is likely to pick up further and support the recovery.
Commodity Prices

- There have been early signs of a revival in commodities demand in recent weeks (50). China’s industrial production rebounded in April and weekly data from the US showed a pick-up in gasoline demand as restrictions there eased (51). But with the recovery in global demand likely to be slow, we expect only modest increases in commodity prices by the end of the year.

- In energy commodities, the biggest story over the past month was the extraordinary collapse in the US WTI price to -$38 per barrel in April (52). That was primarily due to fears that available storage capacity was running out (53). Since then, though, prices have started to claw their way back. China’s Bureau of statistics showed that daily crude usage had rebounded from 11.8m bpd in March to 13.1m bpd in April. And a prolonged bout of low prices has resulted in oil producers cutting drilling activity, which should weigh on supply. As a result, Brent crude has risen by 80% since April’s trough of $19pb, to about $35pb.

- Meanwhile, the price of gold has rallied, hitting its highest level since 2012. It has generally been supported by falling real yields in the US (54). But during the past week, it has taken another leg up to over $1,700/oz as US-China tensions re-surfaced. As for industrial metals, with activity returning in China prices have continued to rise after a bounce in late March. However, metals prices have underperformed other risky assets since March – a story that has plagued commodities prices more generally (55).

Sources: Refinitiv, IEA, Capital Economics
Financial Markets

- After central banks stepping in to provide liquidity to financial markets, roughly half of the tightening of financial conditions seen since the start of March has been reversed (56). Large-scale asset purchases have generally done the job of restoring calm to sovereign bond markets. However, yields have been higher again for the past month in the euro-periphery, and particularly in Italy (57), as European leaders failed to agree a joint fiscal package or debt mutualisation deal, raising concerns about high public debt burdens.

- Asset purchases through the Fed’s commercial paper funding facility have helped normalise conditions in the commercial paper market, although the BoE has more work to do to reverse the rise in corporate borrowing costs (58). Commitments by central banks to buy up corporate debt – including fallen angel securities – has given a lift to the corporate bond market (59), while optimism about the relaxation of lockdowns has fuelled a rally in global equities. The US stock market has been the star performer, while EM equities outside China, in contrast, remain over 25% below their level at the start of the year (60).

- Finally, capital outflows from many emerging markets have weighed heavily on exchange rates. The usual suspects – Brazil, Turkey and South Africa – have fared the worst since pandemic fears took hold (61). DM currencies have generally held up much better, with the yen up by over 6% against trade partners, buoyed by safe-haven demand and cuts in interest rates elsewhere in the world. Commodity currencies, including the Canadian loonie and especially the Norwegian krona, have been the worst performing DM currencies.
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