GLOBAL ECONOMICS CHART BOOK

Initial rebound at risk from renewed outbreaks

- Hard data for May generally revealed sharp improvements in activity, particularly retail spending, albeit not to pre-virus levels. This led us to revise our forecasts for several economies including the US, UK and euro-zone, where we now expect falls in Q2 GDP to be less steep than we initially envisaged. However, renewed coronavirus outbreaks in some parts of the world have added to reasons to expect the recovery to slow in the months ahead. Indeed, timely indicators including restaurant reservations suggest that increased consumer caution is already taking a toll. (See Chart 1.) The previous upward trend in the US seems to have stalled, due partly but not entirely to developments in the affected southern and western states. Meanwhile, even the relatively small and localised outbreak in Australia has seen bookings there nose-dive.

- Coronavirus infections have picked up pace in parts of the US and continue to rise in most EM economies.
- Output & activity has generally picked up faster than expected, but industry has so far been slow to recover.
- Business surveys continued to rebound in June and paint a more encouraging picture for manufacturing.
- Consumer spending has rebounded fairly sharply, but we expect the pace to slow in the months ahead.
- External trade collapsed in April, but the damage has been less severe than we initially feared.
- Labour market disruption has been limited by government support, but we expect further lay-offs.
- Inflation in OECD economies averaged just 0.3% in May, and EM inflation fell to a record low.
- Monetary indicators show that money and credit growth have accelerated, supported by loose policy.
- Commodity prices have had a mixed month, with metals rallying but energy commodities going sideways.
- Financial markets have taken a breather after a strong rally, though Chinese equities have begun to surge.

Chart 1: Restaurant Bookings (7d MA, % y/y)

Source: OpenTable

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Coronavirus

- At the global level, the number of new infections has continued to accelerate this past month reaching around 200,000 per day (2). Back in May when the number of new cases began to rise again, countries in the emerging world were the main drivers. But more recently, advanced economies have seen a renewed uptick (3), with the US, Australia, Spain, UK and Japan all hitting the headlines.

- But these new outbreaks differ dramatically in their severity and spread (4). In the US, for instance, the number of daily new cases has risen to about 50,000 per day, surpassing the previous peak (5). However, the number of new cases is currently running at around 800 in the UK, 400 in Spain and 100 or fewer in Japan and Australia – far below the previous worst.

- Meanwhile in EMs, case numbers have continued to rise, but lockdown measures have started to ease, nonetheless. Again, the picture is mixed (6). Parts of Emerging Europe, for instance, appear to have brought the virus under control. But elsewhere the picture is bleaker. While Brazil has failed to control the virus, lockdown measures have eased anyway. In India, cases remain on a sharp upward trajectory and limited testing means that the situation is almost certainly worse in reality (7). As a result, at the state level at least, many restrictions will need to remain in place for an extended period of time.

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

- In general, there is growing evidence that the world economy is picking itself up after a plunge in activity in March and April. In April, global industrial production fell by over 8% compared with March, as double-digit percentage drops in DMs, Asia and Latin America were mitigated by only a slight decline in emerging Europe and a continued rebound in China (8). The collapse in manufacturing in DMs was largest in transport goods and clothing, while foodstuffs, pharmaceuticals and electronics fared the least badly (9).

- Country data for May show that the global industrial recovery has been underwhelming. Output pulled off only relatively mild rebounds in economies that were hardest hit by lockdowns in April and continued to fall elsewhere (10), leaving output well below pre-virus levels. Taking account of a wider range of timely data, the OECD’s global leading indicator has bottomed out but remains in recession territory (11).

- Finally, our daily Covid Recovery Trackers suggest that activity continued to pick up around most of the world in June (12). Latin America is a notable exception, where the virus is still out of control. Recoveries also seem to have stalled in parts of the US, and not just in the virus hotspot states like California and Texas (13). Overall, though, the surprising strength of these indicators in recent months was one reason why we revised up several of our Q2 GDP growth forecasts. We had expected global GDP to contract by 8% last quarter, but now expect something closer to a still-record decline of 5 ½% q/q.
Business surveys

- While activity is still well below normal levels, the surprisingly large rebounds in the PMIs was one factor that convinced us to revise up some of our Q2 forecasts. The composite PMIs rose in all major economies in June, with most jumping by ten points or more (14).

- What the PMIs’ past relationship with GDP implies for growth rates in Q2 should not be taken literally. On the face of it, the DM composite PMI suggests that the drop in advanced-economy GDP in Q2 was a little smaller than the almost-2% fall experienced in the first quarter. But as we saw in 2009, and even in Q1 of this year, the PMIs will almost certainly understate the fall in GDP this quarter (15). The point is simply that it is encouraging that the PMIs have come back along way from their April lows so quickly.

- Having fallen further, the services activity indices have generally bounced back by more than those for manufacturing (16). And supplier delivery times have now shortened, which suggests that supply chain disruptions have begun to ease and bodes well for a continued recovery in production (17). Stripping out the effect of China on the headline EM manufacturing PMI, it seems that EM industry initially fared worse than that in DMs but has since bounced back further (18). At the global level, the manufacturing output PMI pointed to only a small year-on-year contraction in global output in June (19).
Consumer Spending

- While consumer spending has returned faster than we anticipated, we expect the recovery to slow further ahead. May’s retail sales data showed a sharp rebound in most DMs (20). Sales volumes were up by 17% m/m in the US, 17.8% in the euro-zone and 12% in the UK. But given the size of the collapse in March and April, retail sales are still far below their pre-virus levels in most major economies (21).

- The virus appears to have hastened the trend towards online shopping. In the UK, for instance, since February non-store sales have risen by 51.8% and now account for a third of all sales – up from a fifth before the crisis. And in China, this trend has continued even as brick and mortar stores have reopened. Timelier data suggest that the recovery has stalled. Having jumped when restaurants were reopened, bookings have since levelled off in the US and the euro-zone, and have actually slumped in Australia (22). What’s more, the uptick in air travel also seems to have slowed over the past few days (23).

- As a result, we doubt that the current speed of recovery will be maintained. After all, renewed fears about the virus and depressed consumer confidence will weigh on consumption in the months ahead (24). In the US, for instance, after rebounding steadily since mid-April, consumer footfall at retail stores has edged down recently as case numbers have started to pick up and some restrictions have been re-imposed in some states. However, footfall has also fallen in states relatively unaffected by the new rise in cases (25).
External Trade

- April’s 12.1% monthly fall in world trade volumes was by far the largest on record and left the three-month average annual growth rate at -7.9% (26). The euro-zone and the US were the worst hit, with exports falling by over 20% m/m (27). But while trade appeared to hold up slightly better in emerging economies, Latin American and Asian countries outside China also experienced large contractions in exports.

- With most countries in full lockdown, a very sharp fall was inevitable in April. In fact, the damage has been less severe than we might have expected given the scale of the economic collapse. On past form, our forecast for global GDP to decline by 5% this year looks consistent with a contraction of 40% y/y in world trade, but the falls have so far been far smaller (28). Boosted demand for some products, including medical equipment, has helped put a floor under trade flows. In China, for instance, without the support from these products, exports would have fallen by over 10% y/y in May, far greater than the actual 3.3% decline (29).

- There are signs of a tentative recovery. The new export orders component of June’s PMI suggests that the pace of decline in exports slowed (30). And timely data from Korea showed that exports fell by 18.5% y/y in June, a smidgen lower than the 23.6% drop in May. But with global demand weak, the recovery will be slow. Note that Chinese exports fell in May following the initial sharp rebound after lockdowns eased (31).

Sources: Refinitiv, IHS Markit, CPB Netherlands, Capital Economics
Labour Markets

- Loosening containment measures have allowed some people to return to work, but incomes are still depressed and we think that further redundancies are to come. While the DM composite PMI rose sharply in June, it remains far below its pre-virus level and consistent with falls in G7 employment (32).

- Job retention schemes have been effective at limiting the rise in unemployment in DMs outside the US. In Japan, the unemployment rate was just 2.9% in May, but 7.5% of workers are still furloughed and on reduced income (33). In the euro-zone, the unemployment rate edged up from 7.3% to 7.4% in May, as schemes continued to protect a large portion of workers (34). The unemployment rate even fell in France, Spain and Portugal, despite the economic slump (35). But these schemes won’t protect workers indefinitely and their generosity has been reduced in several cases. We forecast the euro-zone unemployment rate to peak at 9.5% in Q2 2021. Similarly, while the extension of the UK furlough scheme to October and the latest additional fiscal are helpful, we still see unemployment rising sharply in the months to come (36).

- In the US, the 4.8 million increase in non-farm payrolls in June offered further confirmation that the initial economic rebound had been far faster than anticipated (37). But employment remained 14.7 million below its February level and high-frequency data suggest that activity is stalling. On the back of this, the pace of job gains will be much weaker over the coming months, with the recovery likely to be bumpy.
Inflation

- Inflation continued to fall in May. At 1.2%, the OECD core inflation rate fell to its lowest level since 2011, which is consistent with weak demand outweighing supply constraints in driving prices. The headline rate plunged to 0.3% due mainly to the continued drag from energy prices, which has knocked over 1%-point off inflation this year (39). However, this drag from energy prices has now passed. With oil prices rebounding, higher energy prices will cause headline inflation to rise even as core rates remain subdued.

- Despite nascent recoveries, global demand is still well below pre-virus levels and is weighing on core price pressures. In Japan, surveys point to core inflation falling into negative territory. In other DMs, we think deflation is unlikely. Restrictions to productive capacity and huge policy stimulus should limit how low inflation can go, while the flatness of Phillips curves suggests that higher unemployment will have little negative impact on wage growth (41). Nonetheless, spare capacity in most sectors of the economy should still cause core inflation in DMs outside Japan to ease in the coming months. VAT cuts in the UK and the euro-zone is another reason to expect lower rates of core inflation in the second half of 2020 (40).

- Our measure of aggregate EM inflation fell to 3.1% in May – the lowest since our series began in 1996 – largely due to fuel deflation (42). Core inflation has fallen throughout Asia and Latin America but has risen in most of central and eastern Europe, where demand appears to be rebounding much more rapidly (43).
Monetary

- Money and credit growth have continued to accelerate, supported by central bank and government policy. Annual broad money growth has surged in the US, to 23% in May, while that in the euro-zone and UK has reached almost 10% (44). The increase has related partly to renewed central bank asset purchases. But in the US, these have slowed in the past two months as market conditions have improved (45).

- Another key factor has been a dramatic rise in corporate borrowing (46), stoked by central bank liquidity provision and government loan guarantees. The pick-up has been sharpest in the US, where corporate lending growth reached 29% y/y in May thanks to the Paycheck Protection Program. Firms have also been able to finance themselves via increased bond issuance, supported by continued falls in corporate bond yields (47). Lending to households has generally slowed given limited opportunities to spend (48).

- Our measure of aggregate EM credit growth held steady at around 10% y/y in April and May (49). As in DMs, a further slowdown in lending growth to households has been offset by accelerated lending to corporates. Credit growth has been supported by widespread loan guarantees and interest rate cuts. And, unlike in 2008-09, there has not been a pull-back in cross-border banking sector flows.

Sources: Refinitiv, CEIC, Capital Economics
Commodity Prices

- The performance of commodity prices has been mixed since the middle of June. Metals prices have rallied, but the prices of energy and agricultural commodities have generally moved sideways (50). Over recent months, though, the big picture is that energy commodities have pulled off a sharp rebound – at $43pb, the Brent oil price is more than double its April low (51). This rally has been driven by optimism about the recovery in demand, constrained global oil production – particularly by OPEC members (52) – and, until recently, by the revival in risk appetite which also boosted global equities (53).

- Although we expect demand to continue to recover in the coming months, oil prices will struggle to make further gains. After all, high stocks combined with the likelihood that drilling activity could pick up again on the back of higher prices means we expect Brent to end the year only a touch higher, at $45pb.

- Meanwhile, the price of most industrial metals has risen in recent weeks in large part due to the economic recovery in China (54). Supply concerns due to mine closures have also helped to boost prices. While base metals have begun to recover lost ground, the price of most precious metals fell in June. The exception was gold. Purchases of gold ETF shares and the fall in real bond yields have helped to lift the gold price over $1,800 per ounce (55). As investment demand peters out, though, we expect gold to edge down.
Financial Markets

- Financial markets have generally moved sideways during the past month, as concerns about renewed outbreaks of COVID-19 have restrained risk appetite even as the economic data have broadly surprised to the upside. While we remain upbeat about the outlook for equities and other risky assets, the rapid increase in new infections, especially in the US, poses a key downside risk to our optimistic forecasts (56).

- Financial conditions have stabilised in DMs and EMs (57). Corporate credit spreads have stopped narrowing (58), government bond yields in major markets have not changed from a month ago, and global equity prices have barely moved either. One major exception is the surge in China’s onshore equities during the past week (59), making it by far the best performer since the global market peak on 19th February (60). This rally has little obvious economic justification, in our view, and the fact that trading volumes have leapt to their 2015 highs suggests that the market could be due a correction further along the line.

- A small rise in the renminbi has accompanied the pile into Chinese equities, with the dollar exchange rate falling below RMB7/$ for the first time since March. There have been some selloffs in emerging market currencies recently, but in general there have been only small currency moves against the greenback (61). In trade-weighted terms, the US dollar has not changed over the past month.
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