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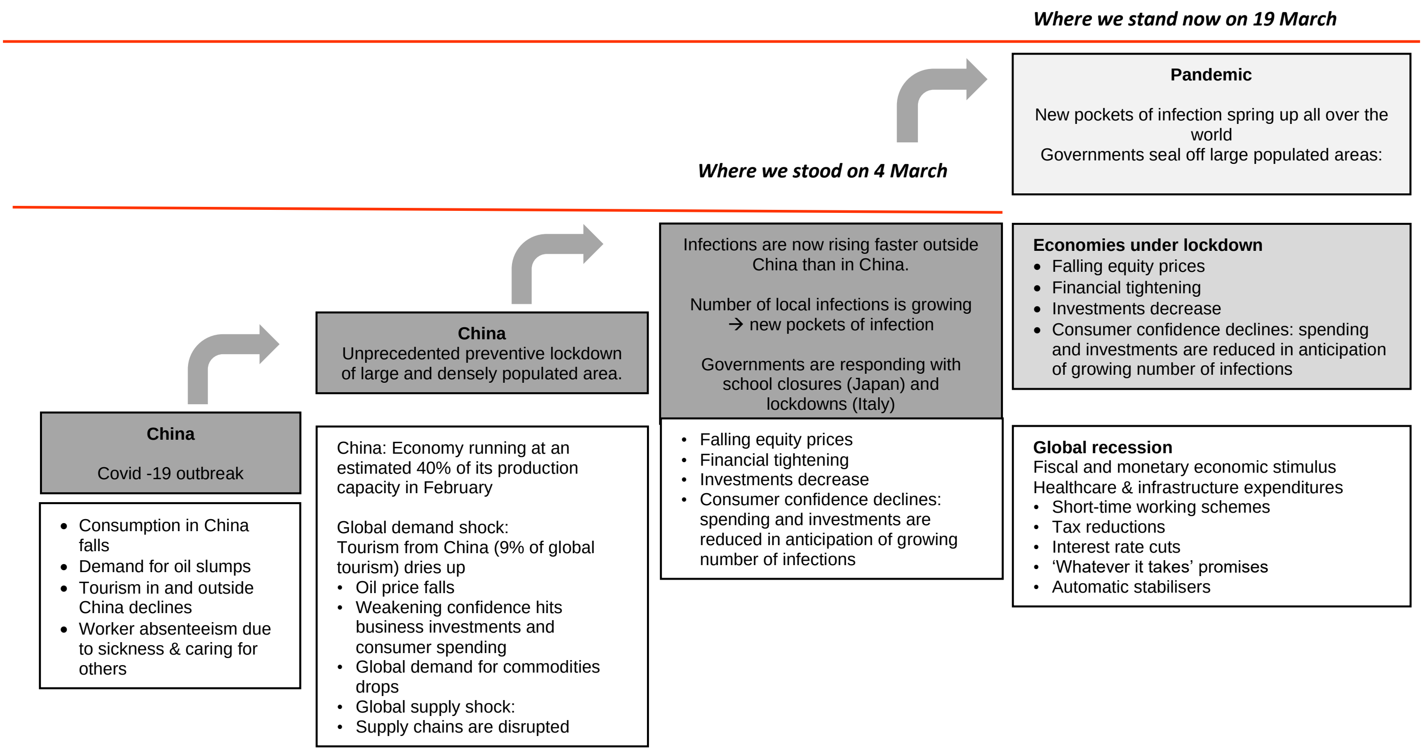
Global Monthly – Post-crisis recovery not until 2021

Sandra Phlippen, Chief Economist
Tel. +31 (0)20 628 1368 / sandra.phlippen@nl.abnamro.com

Since the coronavirus made landfall outside China and escalated at breakneck speed into a pandemic, draconian government measures to halt social (and hence economic) life and to stem the spread of the disease have followed in rapid succession. The 'recession territory' we referred to as a possibility on 4 March has meanwhile worsened into a deeper worldwide recession with a less favourable recovery outlook. We have thus reached the next phase in the escalation diagram sketched below.

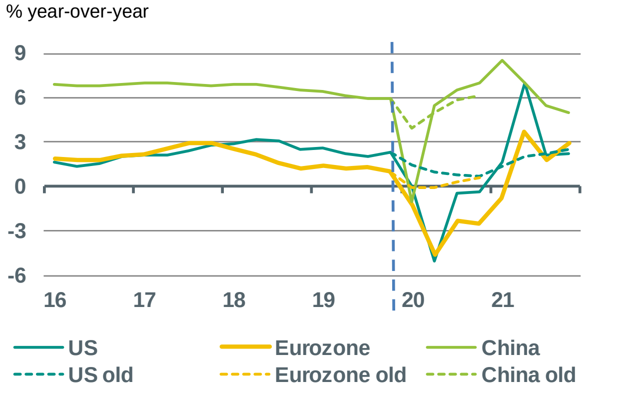
Figure 1 – Diagrammatic representation[1] of the step-by-step economic consequences of the virus outbreak



Due to this escalation, we have revised down our growth outlook for the biggest economies (see also table at back).

[1] This diagram is only a hypothetical framework. It does not indicate causal relationships.

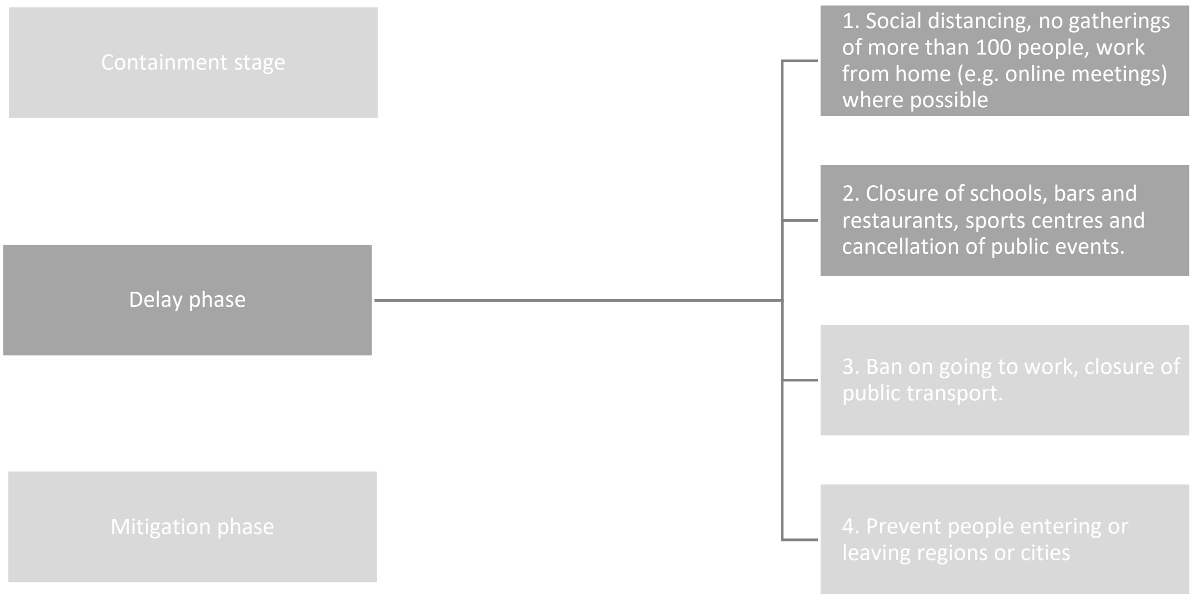
Economic growth



Source: Bloomberg, Group Economics estimates

Economic impact

Governments in the eurozone and the US will scale up their measures to a similar extent as the virus continues to spread. The nature and timing of the measures will differ from country to country, but all will put an unprecedented drag on economic activity. The varying degrees of lockdown are shown in the figure below. Regarding the Dutch economy, we can make more specific assumptions based on the following government strategies to stem the virus and their respective impacts on the various sectors. These will be published next week.

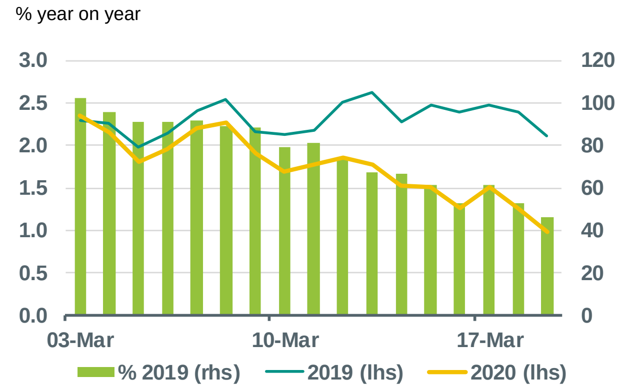


To calculate the economic implications for the global economy as a whole and the largest economies individually, we have made several simplified assumptions. Our assumption for the eurozone is that the freezing of economic activity (including the closure of bars & restaurants and schools) will last a month in large parts of the region. For the US, we assume a number of states on the east and west coast, where the virus outbreak is concentrated, will go into lockdown for one month, starting in the final week of March. These coastal states jointly represent 25% of US GDP. But ‘social distancing’ policies – already widespread – are also likely to be rolled out in the remainder of the US.

These measures will trigger a sharp contraction of the affected economies throughout the first two quarters of this year.

Primarily, this is due to an expected 90% decline in all non-essential consumption (comprising about 30% of total consumption) during the economic shutdown. Even in places where public life has not ground to a halt, we expect a certain shrinkage in (one-off) discretionary purchases. Examples of economic sectors that have seen an instant collapse in revenue include tourism, hospitality and aviation.

Aviation activity in the United States



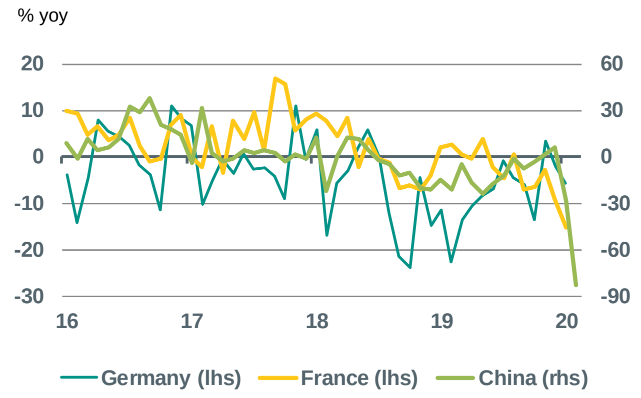
Source: Bloomberg

Supply shock and the Chinese boomerang

The supply side of these economies has also been hit hard. In fact, the supply side of the global economy is in for a double battering. First of all, the supply shock from China where the virus started. Although the Chinese economy is clearly starting to recover and get back into its stride, the supply chains from China to markets elsewhere in the world remains disrupted. Added to this, China must now brace itself for an additional economic blow from shrinking worldwide demand for products that are directly or indirectly sourced from China. In other words, we are seeing a reverse of the situation in February, when the coronavirus outbreak started in China, affecting growth elsewhere. In March, the global outbreak is 'boomeranging' back on China. As a result, we have again revised down our growth estimate for China in the first quarter of 2020. We continue to foresee a sharp recovery in the second and third quarters, although at a reduced pace now that the rest of the world is in recession.

The second blow for the supply side of the global economy comes from the supply of labour in the regions that have virtually ground to a halt due to government intervention. A large group of people are not working due to illness or to provide care to others. Others have been laid off or are working from home as best they can. All in all, this is putting a drag on labour productivity. For the automotive industry, for instance, the combination of supply chain disruptions, loss of labour and deflated demand has created a perfect storm. Production has plummeted dramatically worldwide. In France, for instance, almost all car manufacturing plants are closed.

Car production



Source: Bloomberg

Recovery impeded by interaction between disruptions

Although the lockdown measures are expected to be temporary, with the economy likely to rebound as soon as they are lifted, certain factors will significantly constrain the recovery. The expectation is that – after a brief revival spurred by pent-up demand in the third quarter – these factors will again cause tentative economic growth to stall before the end of the year. As a result, the eurozone may even see a double dip recession at the end of the year. In our view, a vigorous recovery – with growth accelerating to persistently above-trend levels on the back of pent-up demand – will therefore only materialise in the course of 2021. Another reason for the delayed resurgence is the time lag between government and central bank stimulus and the positive effects on the real economy.

The disruptions with longer-term consequences consist of the following four factors:

- First, there has been a huge tightening of financing conditions.
- Added to this, enormous production cutbacks will lead to job losses. The combination of financial tightening and higher unemployment means that non-essential consumption will not fully rebound after the lifting of lockdown measures, but remain stuck at about 90% of its former level for a time.
- Companies will struggle to meet their payment obligations and capital expenditures will fall back.
- The disruptions in the supply chain will take longer to resolve.

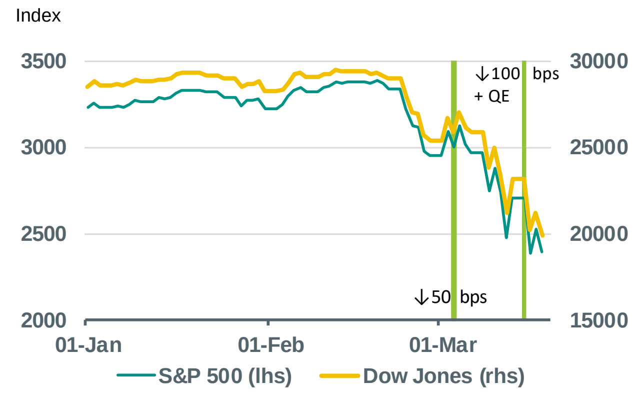
These factors will conspire together to cause a decline in economic growth in the last quarter, and potentially even a contraction (we forsee this for instance in the eurozone).

Policy measures unable to remove all disruptions

Monetary and fiscal authorities are rushing through a raft of new measures to prop up economic growth. These measures will no doubt dampen the downward slide, but not entirely.

Substantial stimulus measures by the major central banks have helped to stem the tightening of financial conditions. After the aggressive policy easing by the Federal Reserve, the European Central Bank has followed suit with its own extensive package of emergency measures. This has restored a measure of calm to the equity markets. Our expectation is that central banks have now quelled the worst of the blaze, but may loosen policy even further at a later stage.

US: indices 2020 with Fed actions



Source: Bloomberg

Fiscal policy

Fiscal policy consists of three types of measures: **Firstly**, the automatic stabilisers. In times of recession, the automatic stabilisers allow public deficits to rise as a result of lower tax revenues alongside higher expenditures in the form of benefit payments and e.g. short-time working grants. **Secondly**, discretionary fiscal measures. At this stage, we foresee discretionary fiscal investments worth 1.2% of GDP in the eurozone and 2.5% of GDP in the United States. **Thirdly**, the largest amounts in the government's fiscal armoury concern state guarantees for bank credit. Although essential to limit the number of bankruptcies, these credit measures are not a form of fiscal stimulus, and so will not boost growth in the same way.

The Chinese government, for its part, is mainly pinning its hopes on a spate of targeted policy measures. Tax postponement has been granted to specific economic activities and certain sectors such as aviation are receiving government support. On the macroprudential front, the Chinese central bank is allowing banks to take a lenient approach to distressed loans of crisis-hit SMEs. Finally, the Chinese state is bringing forward the issuance of local government bonds in order to finance large infrastructure projects.

A final word

The economic impact of the coronavirus crisis is unprecedented and the effects will not have disappeared after the second quarter. We foresee an initial revival in the third quarter, followed by a pullback in the fourth quarter due to second-order effects. All in all, a strong recovery of the global economy is not on the cards until 2021

GDP growth estimates for major economies

	Year				Quarter							
	2019	2020	2021		20Q1	20Q2	20Q3	20Q4	21Q1	21Q2	21Q3	21Q4
US	2.3	-1.4	3.2	% qoq **annualised**	-6.0	-17.0	23.3	2.5	1.9	1.8	2.4	2.7
Old		*1.0*	*2.0*		*0.0*	*-0.1*	*1.4*	*1.7*				
Eurozone	1.2	-2.7	1.9	% qoq	-1.8	-3.2	2.8	-0.1	-0.1	1.1	0.9	1.0
Old		*0.4*	*1.6*		*-0.1*	*-0.1*	*0.3*	*0.6*				
China	6.1	4.5	6.5	% yoy	-1.0	5.5	6.5	7.0	8.5	7.0	5.5	5.0
Old		*5.3*	*6.0*		*4.0*	*5.0*	*5.9*	*6.2*				