Perspectives
Economics

Swiss Life Asset Managers

November/December 2020

Key messages

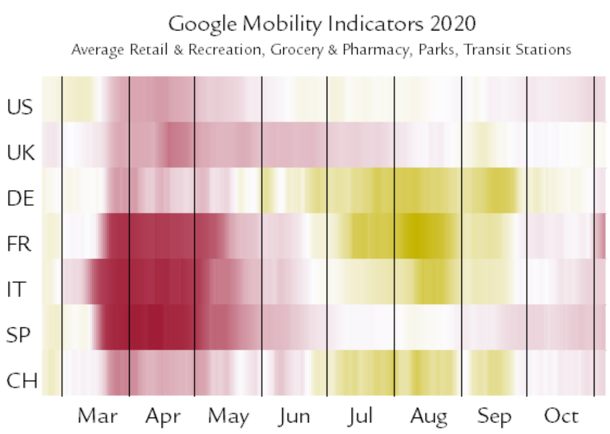
- New containment measures to break the second wave trigger downward revisions to our growth forecasts
- The US elections do not alter our economic outlook; the latter is clouded due to the resurging pandemic
- Fast and widespread availability of a vaccine would be a major game changer next year

Comparison of forecasts

	2020 GDP growth		2021 GDP growth		2020 inflation rate		2021 inflation rate	
	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus
USA	-3.6% ↓	-3.7% ↑	2.4% ↓	3.8% ↑	1.2%	1.2%	1.9%	2.0%
Eurozone	-6.8% ↓	-7.3% ↑	3.2% ↓	4.7% ↓	0.3% ↓	0.3%	1.0% ↓	0.9%
Germany	-5.5% ↓	-5.5%	2.2% ↓	3.8% ↓	0.5% ↓	0.5%	1.5% ↓	1.5%
France	-8.7% ↓	-9.5%	4.7% ↓	5.9% ↓	0.5% ↓	0.5%	1.1% ↓	0.8% ↓
UK	-10.5% ↓	-11.0% ↓	3.9% ↓	4.7% ↓	0.8%	0.9%	1.5%	1.5%
Switzerland	-3.8%	-4.3% ↑	2.9% ↓	3.4% ↓	-0.7% ↓	-0.7% ↑	0.5% ↓	0.2%
Japan	-4.8%	-5.5% ↑	2.6%	2.5%	0.1%	0.0%	0.0% ↓	0.0%
China	2.0% ↓	2.0% ↓	8.2% ↑	7.9%	2.7%	2.7% ↓	1.9%	1.9% ↓

Arrows indicate difference from previous month
Source: Consensus Economics Inc. London, 9 November 2020

Chart of the month



Europe is implementing new nationwide containment measures after the second COVID-19 wave took it by surprise. These measures will leave a mark not only on mobility indicators but on overall economic activity in the fourth quarter. The northern hemisphere will have to go through this first “corona winter” without a vaccine, despite the recent positive news. The impact will be larger in the UK and in France compared to Germany and Switzerland. The former two countries are almost back in a spring-style lockdown, with the important difference that schools, factories and construction sites remain open. Germany opted for a less strict entertainment lockdown, while Switzerland is still mostly leaving strict measures up to the cantons.

US
Focus back on the pandemic

GDP growth

Swiss Life Asset Managers	Consensus
2020: -3.6 %	2020: -3.7 %
2021: 2.4 %	2021: 3.8 %

Financial markets reacted positively to the outcome of the US elections. First, while President-elect Joe Biden will certainly keep a tough stance on China, his policy approach will likely be more predictable and be less centred around harmful tariff threats. Second, the elections were accompanied by the expected noise from President Trump but were conducted in a peaceful and fair manner that renders an extended, potentially violent dispute about the outcome unlikely. Third, the Democratic landslide that most pollsters expected did not happen. If Congress remains divided between both parties, this will significantly limit the room for manoeuvre for the Biden government, notably on the fiscal front where a partial reversal of the Trump tax cuts was planned. Nevertheless, a Democratic-controlled Senate remains possible as the two Senate seats for Georgia will face a runoff election on 5 January. Overall, the US elections do not change our economic outlook. The downward revision of our US growth forecasts is the result of the significant resurgence of the pandemic. Few restrictions have been imposed so far, as mostly conservative rural states are affected currently. However, we expect the pandemic to reach the populous and economically more relevant coastal areas again as we move towards the cold winter months. On the positive side for 2021, the US will likely be the first country to benefit from a potential vaccine.

Inflation

Swiss Life Asset Managers	Consensus
2020: 1.2 %	2020: 1.2 %
2021: 1.9 %	2021: 2.0 %

As expected, US core inflation stabilised at 1.7% in August and September, after a significant crisis-induced decline in the previous months. We expect core inflation to remain around that level until March 2021. Meanwhile, headline inflation is set to fluctuate strongly due to significant swings of energy prices and the related base effects. We expect headline inflation to hit a low of 1.0% in December, before temporarily shooting above the 2%-target in the second quarter of 2021.

Eurozone
On a less damaging second wave

GDP growth

Swiss Life Asset Managers	Consensus
2020: -6.8 %	2020: -7.3 %
2021: 3.2 %	2021: 4.7 %

A new set of high frequency data is helpful to accurately assess economic dynamics in these times of a pandemic. For the third quarter, we expected GDP in the Eurozone to have recovered by 11.6% from the previous quarter, which by far exceeded the consensus of 9.6% reported by Bloomberg. At 12.7% quarterly growth, the official data revealed an even faster pace of the recovery. Everything else left unchanged, the past data thus would force us to lift the forecast for 2020 considerably. Yet, fast rising new infection cases and the authorities' response in the form of a renewed tightening of containment measures have a negative impact on economic dynamics. Current containment regimes range from comparably soft in Estonia and Finland to almost identical measures like those seen in spring in Ireland, Austria, Spain and France. We now expect GDP to decline by 0.7% in the last quarter 2020, which is substantially less than during the second quarter. The differences to the highly uncertain situation in March are manifold: We have better visibility of the potential length of a renewed lockdown. Individual mobility is far less restricted than in April according to information from Google. Global supply chains are restored, and exporters report firm demand from Asia and the US. Additionally, fears of a financial crisis are gone and a breakthrough in the search for a vaccine has moved within reach recently.

Inflation

Swiss Life Asset Managers	Consensus
2020: 0.3 %	2020: 0.3 %
2021: 1.0 %	2021: 0.9 %

Official data reveal that inflation remained in negative territory as we entered the last quarter 2020. The preliminary estimate published by Eurostat showed that consumer prices dropped by 0.3% in the year until October. We project inflation to stay negative until January next year. Apparently, the broader public's perception of price developments is completely different from this statistical information: in a survey published by the EU commission, the mean response to the question of actual inflation in the Eurozone was 7.5%.

Germany
The show must not go on

GDP growth

Swiss Life Asset Managers	Consensus
2020: -5.5 %	2020: -5.5 %
2021: 2.2 %	2021: 3.8 %

Starting 2 November, Germany entered an "entertainment lockdown" for at least one month, restricting contacts to two households and closing restaurants, bars and other leisure venues. These measures against the COVID-19 surge are less strict than the spring-lockdown but stricter than what we had anticipated, leading us to revise our GDP forecast down. The impact of the new restrictions should first be visible in the Google mobility indicators (see chart of the month) and hopefully soon after in a peaking number of new COVID-19 cases. Business closures in the most affected services sectors will likely rise, despite the generous fiscal support measures for revenue compensations recently announced. Likewise, we project the unemployment rate to increase again, after it declined from 6.4% in summer to 6.2% in October. In the manufacturing sector, however, we see further recovery potential with positive impulses from China and the US. Industrial production increased by 1.6% in September, undershooting consensus expectations, but the October manufacturing Purchasing Managers' Index increased further to 58.2 points, clearly staying in growth territory. Yet, we now think that growth overall will stagnate in the final quarter of 2020 and recover only slowly throughout winter. The better-than-expected third-quarter GDP print (8.2% quarterly growth vs. 7.7% expected) cushions the 2020 downward revision, but statistical carry over, leads to a 2021 GDP growth revision to 2.2%, down from 4.1%.

Inflation

Swiss Life Asset Managers	Consensus
2020: 0.5 %	2020: 0.5 %
2021: 1.5 %	2021: 1.5 %

Harmonised consumer price inflation remained in negative territory in September and October (-0.4% and -0.5% year-on-year). Base effects from low energy prices and the summer VAT cut are still the driving forces. October inflation details will be released after this text goes to print. It is, however, clear, that this recession has been disinflationary so far.

France
Big jump in unemployment

GDP growth

Swiss Life Asset Managers	Consensus
2020: -8.7 %	2020: -9.5 %
2021: 4.7 %	2021: 5.9 %

The impact of COVID-19 on the French economy was already comparably high in the first wave and is expected to again be more significant in the current quarter as the French authorities were forced to implement comparably restrictive new containment measures. In contrast to the first lockdown, manufacturing sectors will be less affected this time, as global supply chains are functioning again and demand from Asia and the US is hardly affected by the current developments of the pandemic in Europe. Accordingly, business surveys out of the manufacturing sectors are coming in higher than feared by analysts so far this quarter. The final data for the October manufacturing Purchasing Managers' Index (PMI) was even slightly higher than the preliminary number, suggesting that the worsening medical situation in the final days of October only had a limited impact on industrial activity and incoming orders. Things look different in the services industries, where the short-term outlook has clearly worsened: The services sector PMI was stuck below the 50-points expansion line for two consecutive months and the rise in the unemployment rate to 8.8% from 7.0% in the third quarter weighs on consumer sentiment. In contrast to other regions in Europe, the second lockdown has already had a material impact on individual time spent in retail and leisure places. Considering these worsening domestic conditions, we cut our GDP growth forecast for this year from -8.0% to -8.7%.

Inflation

Swiss Life Asset Managers	Consensus
2020: 0.5 %	2020: 0.5 %
2021: 1.1 %	2021: 0.8 %

Annual headline inflation fell from 1.7% in January to zero last month. From month to month, inflation numbers were extremely volatile, a major driver being the different timing of seasonal factors compared to normal years. While we expect less volatility in the months ahead, price setting power in the domestic service sectors is likely to remain subdued, keeping inflation pressure low during the first quarter 2021.

UK
Feebly into the second wave

GDP growth

Swiss Life Asset Managers	Consensus
2020: -10.5 %	2020: -11.0 %
2021: 3.9 %	2021: 4.7 %

The second wave hit the UK at a time when the economy had only modestly recovered from the first wave. According to our estimates, UK GDP only stood at around 94% of pre-crisis levels in September, far lower than in Germany, France (both estimated at 97%) or even Italy (96%). The stop-and-go approach witnessed elsewhere in Europe was taken to the next level in the UK, where the government's "eat out to help out" scheme fiscally encouraged Britons to spend money in restaurants during August, only to close all bars and restaurants again in the second lockdown imposed for the month of November. Non-essential shops also remain shut, but surging online retail sales and the fact that schools and factories are open will likely limit the economic damage this time. Also, the starting point in terms of capacity utilisation is so much lower than in spring that we expect the second lockdown to induce a monthly GDP decline of 5.4% in November, roughly a quarter of the plunge witnessed in April. Regarding Brexit, we still expect a benign outcome, as Joe Biden's election as US President has ironically increased the pressure on the UK government to strike a trade deal with the EU. The UK's internal market bill, intended to push the EU to a compromise, was denounced by US Democrats to threaten the peace process in Northern Ireland. Hence, the bill, which is still stuck in parliament, has now become an empty threat as it would likely block the path for a transatlantic trade deal.

Inflation

Swiss Life Asset Managers	Consensus
2020: 0.8 %	2020: 0.9 %
2021: 1.5 %	2021: 1.5 %

The "eat out to help out" programme led to lower August inflation numbers and a technical rebound in September, to 0.5% for the headline and 1.3% for the core inflation print. Headline inflation will remain below core inflation over the next months due to depresses energy prices, but the unwinding of the temporary VAT should bring headline inflation back above the 1%-mark at the beginning of 2021.

Switzerland
An island in Europe

GDP growth

Swiss Life Asset Managers	Consensus
2020: -3.8 %	2020: -4.3 %
2021: 2.9 %	2021: 3.4 %

When it comes to breaking the second wave of the pandemic, Switzerland chose a comparably mild toolkit of containment measures. Consequently, high frequency data suggest that the current impact on economic activity is far less severe than during the lockdown earlier this year. As per early November, mobility indicators provided by Google suggest a 28% lower duration of stay in retail and leisure related areas compared to February. At its trough in the first week of April, this measure stood at a fifth of its February level. Debit card usage data and October car sales numbers hint at robust private consumption until recently. Global supply chains in manufacturing are restored and kept intact even in regions which have implemented more restrictive containment regimes than the Swiss authorities. We have lowered our assumptions for the final quarter 2020 for which we currently expect a mild temporary decline by just 0.5%. While this is a comparably mild drop in activity, we are not neglecting long-term effects of the recession: Another set of high frequency data suggests that a growing number of people is actively looking for a job as they fear to lose their current employment. We expect the unemployment rate to climb above 4% during the first quarter 2021 and are also anticipating a rise in corporate bankruptcies. The widespread and fast availability of vaccines would be a game changer and could result in stronger growth in the second half of 2021 already.

Inflation

Swiss Life Asset Managers	Consensus
2020: -0.7 %	2020: -0.7 %
2021: 0.5 %	2021: 0.2 %

Annual consumer price inflation is set to stay negative until early 2021, when base effects from very low energy prices will fade. As the inflation print for October came in slightly below our estimates, we had to revise the full year forecast slightly to the downside this month. Details in the consumer confidence survey published by SECO show that inflation expectations remain well anchored among Swiss households.

Japan
Foreign demand on the rise

GDP growth	
Swiss Life Asset Managers	Consensus
2020: -4.8 %	2020: -5.5 %
2021: 2.6 %	2021: 2.5 %

The recent surge of infections in Europe and current regional dynamics in the US, where we see a close correlation between temperatures and infection rates, suggest that COVID-19 follows a seasonal pattern that will inevitably hit Japan as well during the winter months. Indeed, new cases have already started to reaccelerate, notably in the northernmost island of Hokkaido. This brings some downside risks for the ongoing slow recovery, especially in the services sector, but is unlikely to trigger any economically punitive measures as the government has so far successfully relied on the population to voluntary reduce social interaction. Meanwhile, "fiscal incontinence" continues seamlessly under the new government of Yoshihide Suga, which has just announced yet another supplementary budget to support the recovery. What should also keep the Japan economy on track over the next months is foreign demand, as the two main trading partners China and the US enjoy a healthy economic recovery. Indeed, the export orders subcomponents of the manufacturing Purchasing Managers' Index recently moved into expansion territory for the first time in two years. Industrial production has steadily moved up since May to around 92% of pre-crisis levels in September, driven by a strong recovery of the Japanese auto sector that had especially suffered from the COVID-19 crisis.

Inflation	
Swiss Life Asset Managers	Consensus
2020: 0.1 %	2020: 0.0 %
2021: 0.0 %	2021: 0.0 %

In October, annual headline inflation dropped into negative territory for the first time in four years, to -0.3%. The reason is that positive base effects from last year's consumption tax hike drop out of the calculation. As the tax hike was only gradually passed on to consumers last year, inflation is set to decline further, reaching a trough of -0.8% in January 2021.

China
Technology at the forefront

GDP growth	
Swiss Life Asset Managers	Consensus
2020: 2.0 %	2020: 2.0 %
2021: 8.2 %	2021: 7.9 %

China's economy grew by 4.9% in the third quarter compared to a year ago, which has however, been below our and consensus estimates, leading us to revise down our full-year GDP growth projection for this year to 2.0% from 2.5% previously. Nevertheless, despite this slower-than-anticipated pickup, China's monthly activity indicators show that the country's recovery remains intact. Particularly, the acceleration in September retail sales, which expanded by 3.3% compared to a year ago, confirms that private demand is substantially improving and that China's initially uneven recovery, that has been driven by the industrial sector, is broadening out. Moreover, China unveiled a first glimpse of its economic plan for the next five years. While details of the latest five-year plan will only be revealed in spring at the National People's Congress, one of the key messages has been that technological advance is at the forefront. In particular, technological self-reliance has been elevated, in response to imminent oversees restrictions on imports from abroad, and especially from the US. This will likely translate into substantially greater research and development spending in fields such as semiconductors, biotech and new energy vehicles. A potential Biden presidency would most likely be a shift away from unilateral tariffs as the main US policy tool to deal with China, but a hawkish China stance will persist, and US-China tensions are here to stay.

Inflation	
Swiss Life Asset Managers	Consensus
2020: 2.7 %	2020: 2.7 %
2021: 1.9 %	2021: 1.9 %

Easing pork prices led to a notable slowdown in China's September headline inflation that reached 1.7% compared to 2.4% in August. As pork prices will continue to moderate, we expect inflation to continue its downward trend. Meanwhile, although core inflation remained subdued at 0.5%, recreation prices rebounded for the first time since May, reflecting an ongoing recovery in China's services sector.

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