Research
Macquarie Wealth Management

Global Economic Outlook

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In the near term, Macquarie expect the recovery to continue at a modestly faster pace than seen after the GFC. However, the rapid snapback phase looks to have already come to an end as the major non-China economies deal with rolling new waves of COVID-19.	In their central scenario, Macquarie assume that a vaccine is approved towards the end of Q1. The relatively flexible nature of many of the affected small- and medium-sized businesses should allow services to recover relatively quickly once the virus is controlled.	Macquarie has lifted their GDP growth forecasts for Australia as incoming high-frequency spending data has suggested household consumption, and GDP, is likely to rebound in Q3 by more than they previously thought.

Macquarie's Global Economics team have updated their outlook and forecasts post the recent gains seen in global GDP as restrictions eased and activity resumed "Global Economic Outlook – Depression averted, mountain still to climb …". The following is a summary of their views.

After the rapid snapback – recovery to slow

Global economic activity began to recover in May after collapsing in March and April. The initial snapback was the fastest ever recorded – global GDP growth appears likely to be at ~7% in Q320 (after ~10% fall in H120).

Global Economic Forecasts

	2019	2020	2021	2022
US	2.3	-3.8	4.1	2.9
China	6.1	2.0	8.5	5.0
Eurozone	1.3	-7.8	6.4	1.9
Japan	0.7	-5.3	3.6	1.4
India	4.7	-6.2	16.4	6.4
UK	1.5	-10.2	8.0	2.7
Canada	1.7	-6.3	4.2	2.8
Australia	1.8	-3.1	2.8	3.4
New Zealand	2.3	-5.5	5.4	2.6
Global (MER)	2.5	-4.2	6.2	3.2
Global (PPP)	2.8	-3.9	7.1	3.5

Source: Macquarie Macro Strategy, September 2020

While the combination of unprecedented macro stimulus with easing in social-distancing restrictions has seen the global economy avoid a repeat of the 1930s Depression, challenges to the recovery remain.

Record rebound expected in Q3 GDP

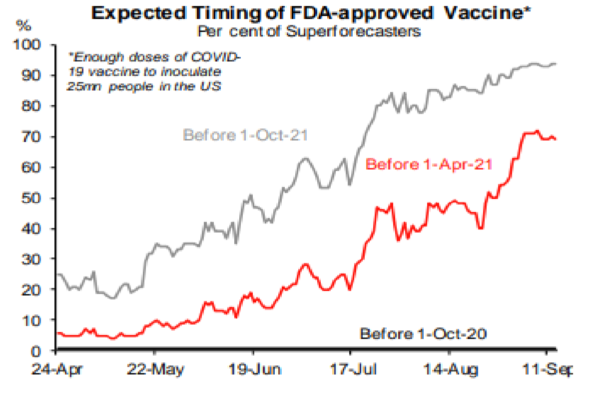
Source: Macquarie Macro Strategy, September 2020

Much of the rebound has occurred in the goods sector, where fiscal stimulus and substitution away from services has driven a boom – remarkably, global industrial production is back at pre-COVID levels. In contrast, the normally resilient services sector remains very weak, as high-income earners either can't (due to ongoing social-distancing restrictions) or choose not to (caution) engage in activities involving social interaction.

Despite the initial pace of the recovery exceeding most expectations, activity levels remain very low (still down 4% from pre-COVID levels). Recent partial data suggest that the rapid snapback looks to be coming to an end – growth is likely to slow materially in Q4 particularly as the non-China economies continue to deal with rolling waves of the infection. Notwithstanding expectations that the pace of the recovery will slow – Macquarie expects that it will be faster than seen post-GFC given this recession was not driven by structural imbalances or excesses.

The team's central scenario is predicated on the view that a COVID-19 vaccine is approved by Q121 and is progressively rolled out over the subsequent six months. The team expects that the recovery in the small and medium sized businesses should see services recover relatively quickly once social distancing restrictions are further eased. Along with the ongoing fiscal support, global GDP is anticipated to reach its previous peak by mid-2021.

Macquarie assumes a vaccine is approved by end-Q1



Source: The Good Judgment Project, Macquarie Macro Strategy, September 2020

United States: Resilient recovery

After reaching a trough in April, US activity rebounded rapidly in May and June. Since that time, the economy has proven resilient to two shocks:

- In July, COVID cases surged and many state governments re-imposed social restrictions; and
- In August, the level of unemployment benefits fell as Congress failed to agree a new fiscal package.

Despite these two material headwinds, both employment and consumption have continued to grow through to September.

Growth in 3Q is likely to be amongst the strongest quarters on record. Macquarie now foresees a firmer magnitude in this phase than previously. This reflects the longer than anticipated momentum from re-opening and the team's assumption of a vaccine in 2021. According to their baseline view, the 4Q19 level of real GDP is not surpassed until late 2021.

Macquarie assumes faster than consensus recovery

Source: Macquarie Macro Strategy, September 2020

US policy and rates outlook

Macquarie believes the Federal Funds rate is likely to remain at the zero 'lower bound' for several years. In a late August speech at Jackson Hole, Chair Powell outlined revisions to the Statement on Longer-Run Goals and Monetary Policy Strategy, suggesting a greater tolerance for above 2% inflation, and by extension a more accommodative monetary stance.

China: Strong recovery paves the way for policy normalization

China's economy had a strong rebound in 2Q20, with GDP growing 11.5% q/q. As a result, output has already exceeded the pre-COVID level. The strong recovery paved the way for policy normalization after the July Politburo meeting. Macquarie's China Economist views further policy easing is not necessary at the stage, but it's still too early for policy tightening, with the economy still running below its trend level. On the monetary policy, the PBoC has refrained from cutting interest rate or RRR since April.

In the meantime, Beijing is spending more time on curbing financial risks, especially in the property sector. The latest news is that Beijing laid out three "red lines" for developers: 70% for the liability to asset ratio, 100% for the net debt to equity ratio, 100% for the cash to short-term debt ratio. In the next few months, sales and new starts are expected to continue to recover, but property investment should slow soon.

Eurozone: Worse than the GFC, but recovery from Q3

Eurozone GDP fell more heavily than in the US. However, recovery is now well underway, with the mechanical rebound likely to see GDP increase by something like 8½% in Q3,

Unfortunately, Europe is now experiencing a major COVID second wave, with the near-term outlook in large part driven by the response (both policy and by individuals) to the resurgence. Macquarie's economists expect that the Europeans will follow the US model, with new restrictions localised and less severe than those seen during March, implying that the recovery should continue. However, were more stringent lockdowns implemented – as seen in the Australian state of Victoria – output could fall again, with services growth already slowing

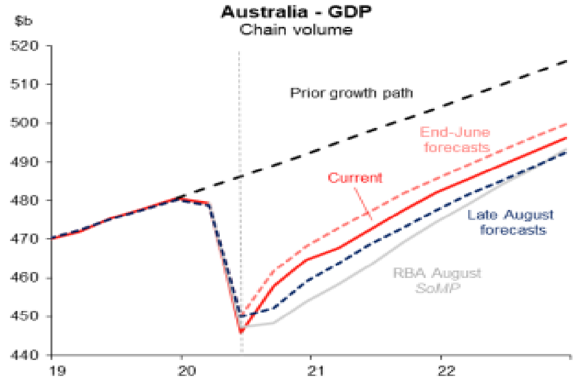
Australia: Upgrade to near-term profile

The 7.2% fall in Australia's GDP over H1 2020 was noticeably smaller than the median decline of 11.7% across 43 other economies. This means that the initial recovery in growth in Australia's GDP is also likely to be smaller than elsewhere. However, Macquarie expects the fall in GDP over 2020 as a whole to be relatively modest in Australia compared with other economies.

The second wave of coronavirus cases in Victoria has held back the recovery in the broader economy and made forecasting the near-term trajectory of the economy very difficult. As mobility restrictions tightened months ago in Victoria – one-quarter of the economy – Macquarie downwardly revised the broader growth outlook.

However, incoming high-frequency spending data has more recently convinced Macquarie that household consumption, and thus GDP, is likely to rebound in Q3 by more than they previously thought. Secondly, the team's explicit assumption that a somewhat effective COVID-19 vaccine becomes available before end-March 2021 has led Macquarie to modestly lift the activity outlook further out.

Macquarie have upgraded GDP forecast for Australia



Source: Macquarie Macro Strategy, September 2020

RBA: fiscal stimulus firmly in its sights

The RBA effectively eased monetary policy further by deciding at the September Board meeting to extend and ramp up the Term Funding Facility (which provides very cheap 3-year funding to banks at 0.25%). This will help to ensure that the cost of credit for the private sector is hardly an issue.

Macquarie's central view is that the RBA should keep its story very simple: the cost of credit is already at all-time lows and credit remains readily available for most potential borrowers, particularly given the recessionary conditions. For the time being, the most effective macro policy arm is fiscal policy, and Australia has ample room to borrow and spend a lot more to support activity.

Australian Economic Forecasts

		2019	2020	2021	2022
GDP	y/y	1.8	-3.1	2.8	3.4
CPI	y/y	1.6	0.8	1.5	1.6
Core CPI	y/y	1.4	1.2	1.1	1.6
A$/US$		0.70	0.73	0.75	0.75
RBA cash rate	%	0.75	0.25	0.25	0.25
3-yr yield	%	0.90	0.26	0.26	0.26
10-yr yield	%	1.37	0.90	1.10	1.40

Source: Macquarie Macro Strategy, September 2020

Jason and the Investment Strategy Team

The report was finalised on 16 September 2020

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