

GLOBAL ECONOMIC OUTLOOK

VACCINATION AND POLICY SUPPORT ALLOW TO
LOOK AT THE OTHER SIDE OF THE VALLEY

WILLIAM DE VIJLDER

Group Chief Economist

Presentation Denmark, 29 January 2021



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Overview

1. Introduction
2. Recent market developments
3. Tracking the economic impact of health safety measures
4. Economy: recent data
5. Focus on the Nordics
6. Focus on France
7. Drivers of the recovery
8. Topics to monitor in 2021 (and beyond)
9. Forecasts
10. Financial markets in 2021: an economist's perspective
11. Longer-term consequences of the pandemic



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INTRODUCTION



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The narratives of 2020



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Outlook in summary

1. The new variants of the Covid-19 virus have rapidly become a major concern, forcing several countries –in particular in Europe- to tighten the health safety measures, more than expected at the start of the year.
2. This should weigh on activity levels in the first quarter –an impact on second quarter activity is possible as well-, leading to a double-dip recession in the eurozone, to be followed by a rebound thereafter with economies growing well above potential for several quarters
3. Policy support will remain significant, both fiscal and monetary. The ECB has eased further. The Fed continues its QE –no end date set- and is willing to do more if necessary. In the US a new fiscal stimulus has been voted in December and the Biden Administration is preparing another one
4. The vaccination campaigns and the monetary/fiscal policy action should support confidence but there is concern about the headwind caused by rising defaults and a temporary increase in unemployment.
5. Later on in the year, market attention will shift to 2022 with the risk of the Fed tapering its QE and the ECB stopping its PEPP
6. US Treasury yields should move higher on the back of fiscal stimulus and the economic recovery and because the Fed will accept and actually wants inflation to rise beyond 2%.
7. As usual, eurozone bond yields will be very much influenced by what happens to US yields. The prospect of a more lasting recovery as a vaccine will be deployed, should contribute to somewhat higher bond yields. Stopping PEPP should cause some spread widening versus Bunds
8. We expect the dollar to weaken further versus the euro towards 1.25 by year-end. A risk factor in this respect is a change in guidance of the Fed, but this is unlikely in the near-term



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RECENT MARKET DEVELOPMENTS: PRICING THE PROSPECT OF A LASTING ECONOMIC RECOVERY*

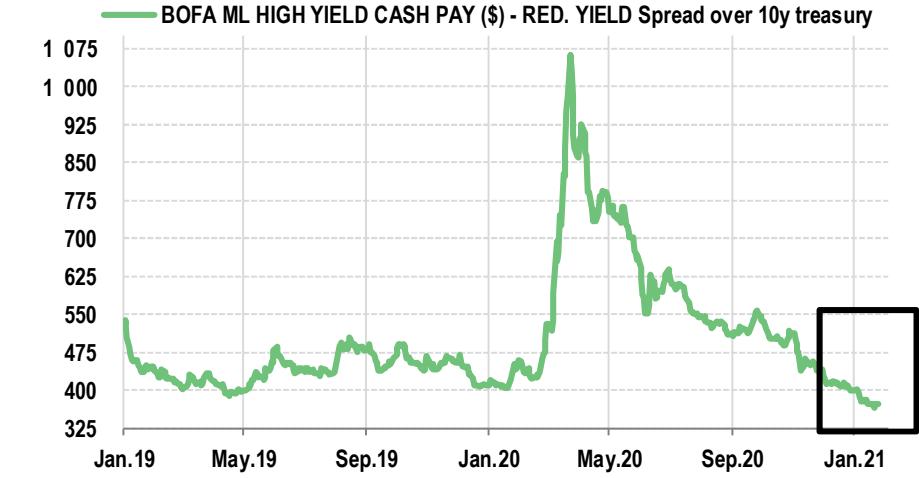
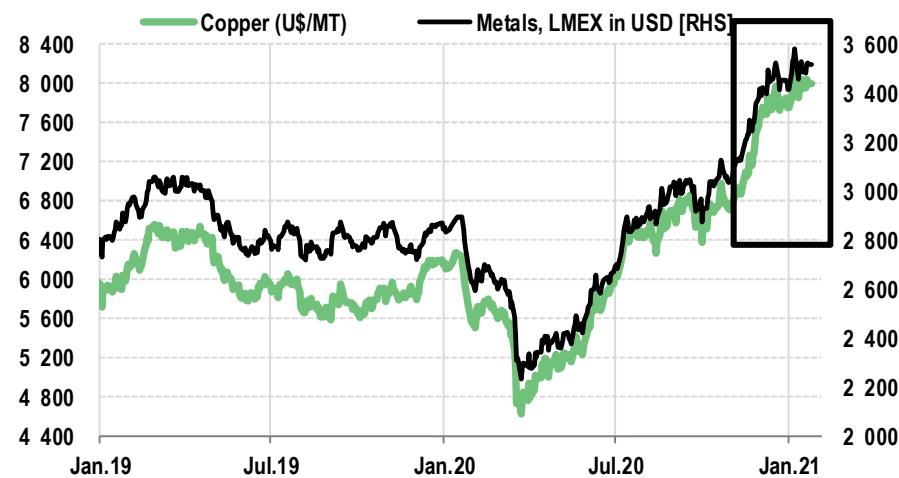
*CHARTS PRODUCED ON 25 JANUARY 2020



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Equities rally, US yield curve steepens, industrial metals rally, US high yield spread tightens further



Source: Refinitiv, BNP Paribas



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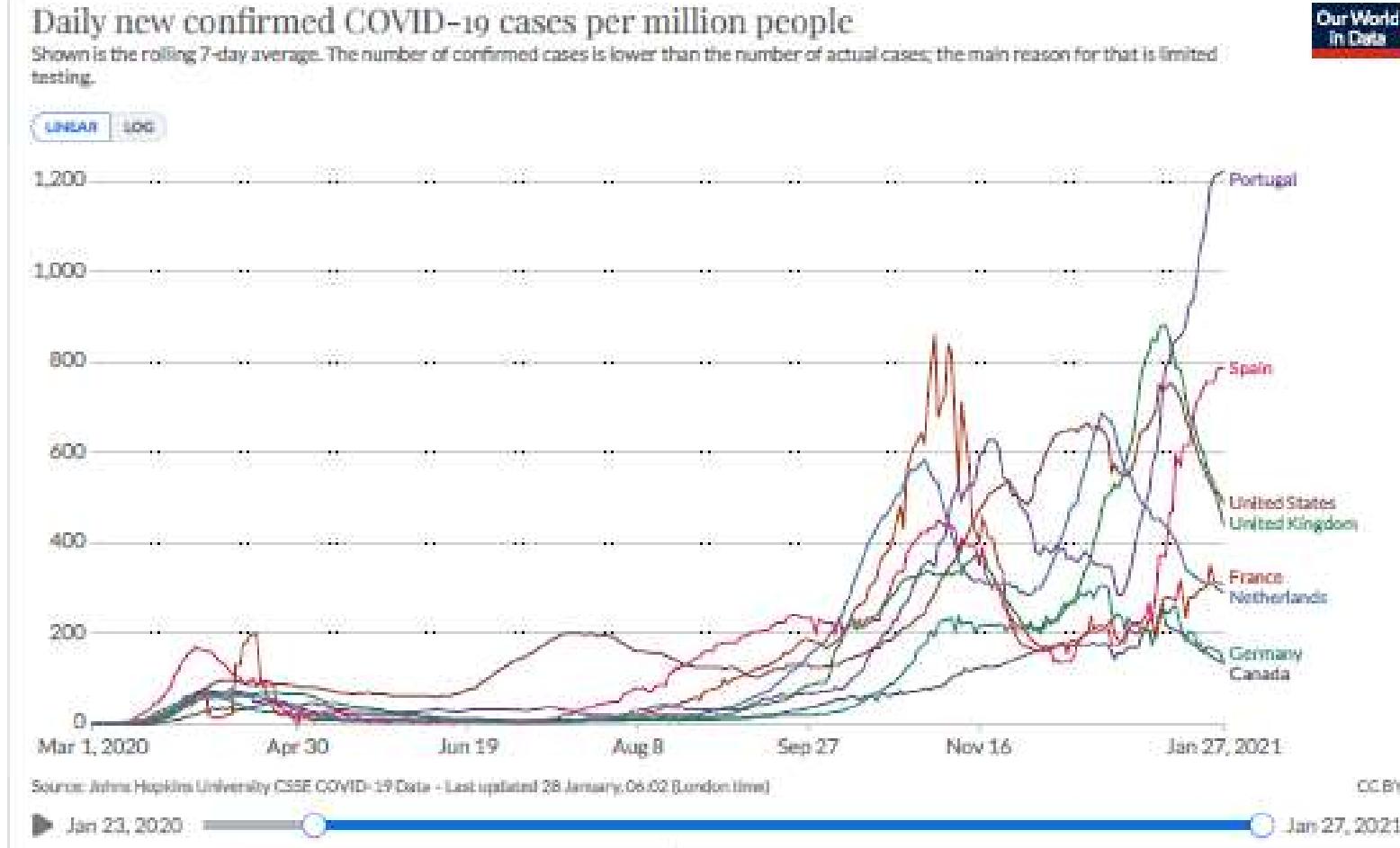
TRACKING THE ECONOMIC IMPACT OF HEALTH SAFETY MEASURES



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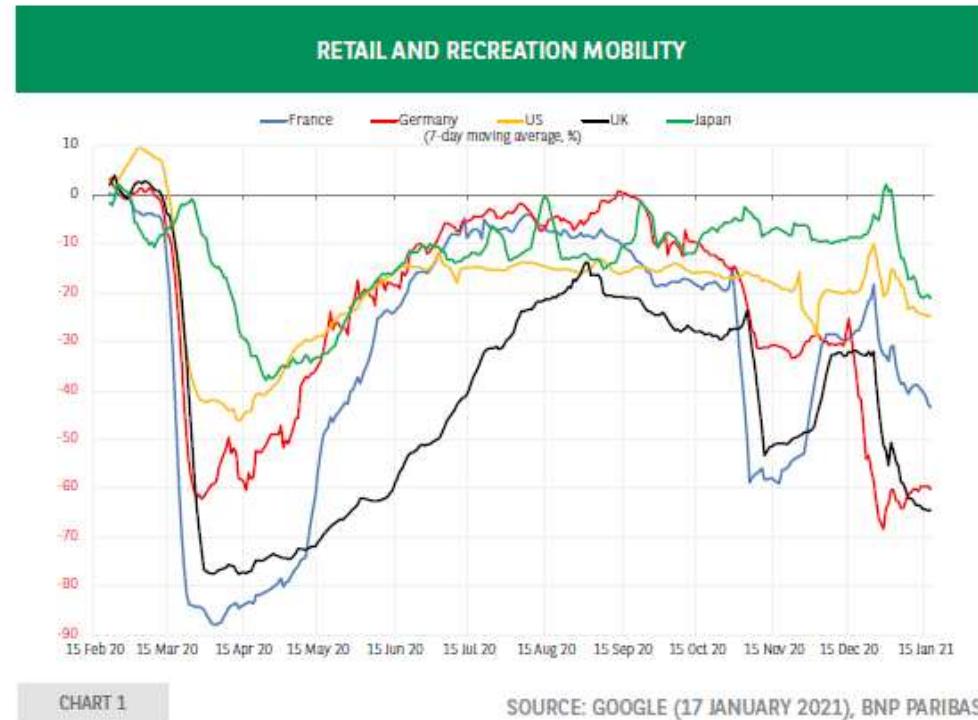
New infections down in most countries but real issue is new variants



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Google Mobility data show detrimental impact of recent infections



* Google Mobility Reports show how visits and length of stay at different places change compared to a baseline. The baseline is the median value, for the corresponding day of the week, during the 5-week period Jan 3–Feb 6, 2020. A figure of negative 30% indicates that traffic was down 30% compared to a baseline. The reports show trends over several weeks with the most recent data representing approximately 2-3 days ago—this is how long it takes to produce the reports. In order to smooth the series, we use a seven-day moving average of the raw data in the Google Mobility Reports. Source: Google.



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OECD weekly tracker of GDP growth

The OECD Weekly Tracker of GDP growth attempts to fill the gap in real-time high-frequency indicators of activity with a large country coverage. To the author's knowledge, the Tracker is the first weekly GDP proxy that can be compared across a large array of OECD and G20 countries. **The Tracker provides estimates of year-on-year growth rate in weekly GDP with a 5-day delay.** It applies a single machine learning algorithm on a panel of Google Trends data for 46 countries. The algorithm flexibly captures cross-country heterogeneity and provides comparable estimates across countries. It **exploits the full potential of Google Trends data by aggregating together information about search behaviour related to consumption, labour markets, housing, industrial activity and uncertainty.** The Tracker provides high frequency and real-time information about the COVID-19 crisis and subsequent rebound, as well as the impact of confinement measures.

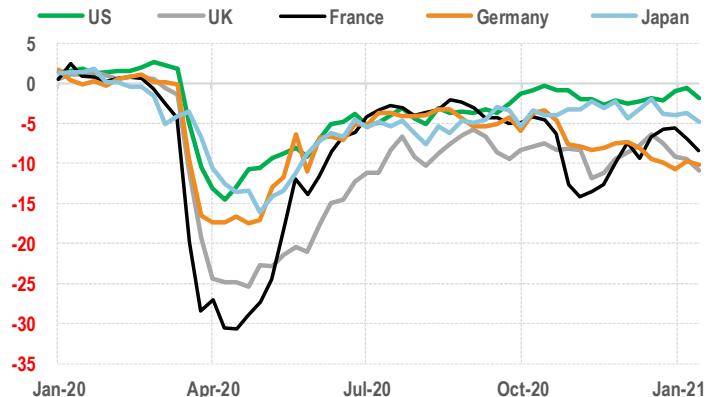
Source: OECD, TRACKING ACTIVITY IN REAL TIME WITH GOOGLE TRENDS, ECONOMICS DEPARTMENT
WORKING PAPERS No. 1634
By Nicolas Woloszko



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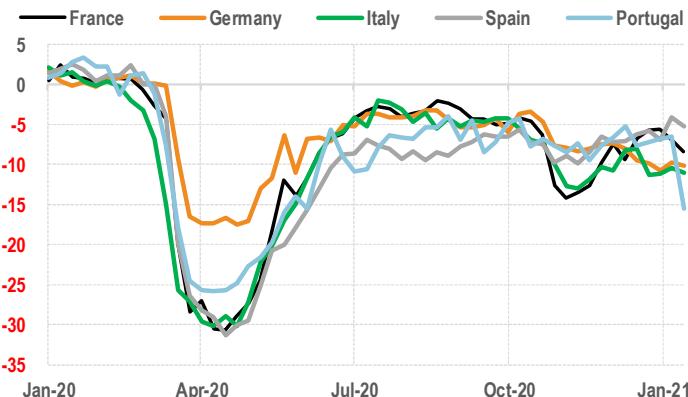
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OECD weekly tracker by country



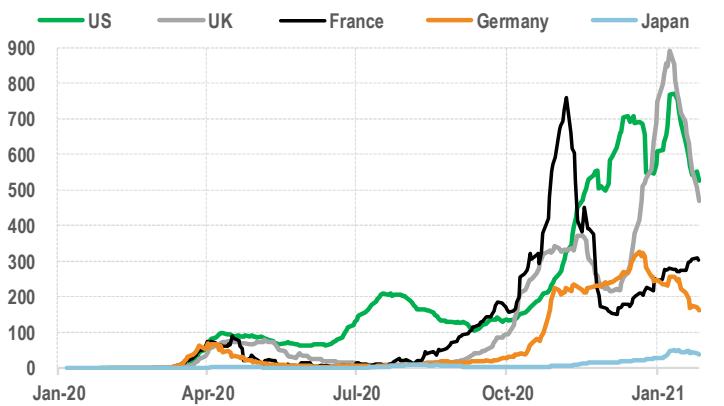
Source: OECD, BNP Paribas

OECD weekly tracker by country



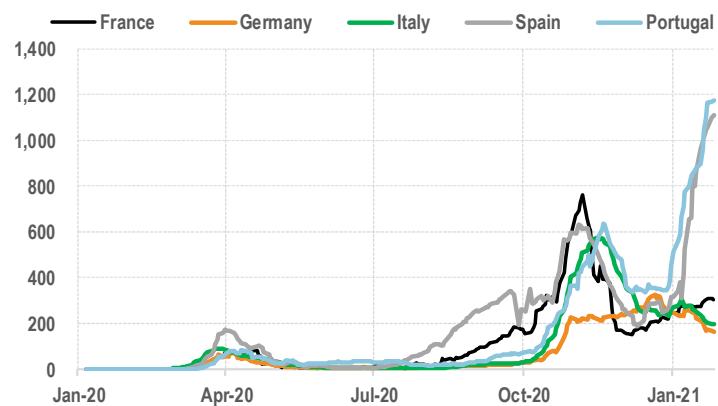
Source: OECD, BNP Paribas

Covid-19: new cases per million people (5-days average)



Source: Refinitiv, BNP Paribas

Covid-19: new cases per million people (5-days average)

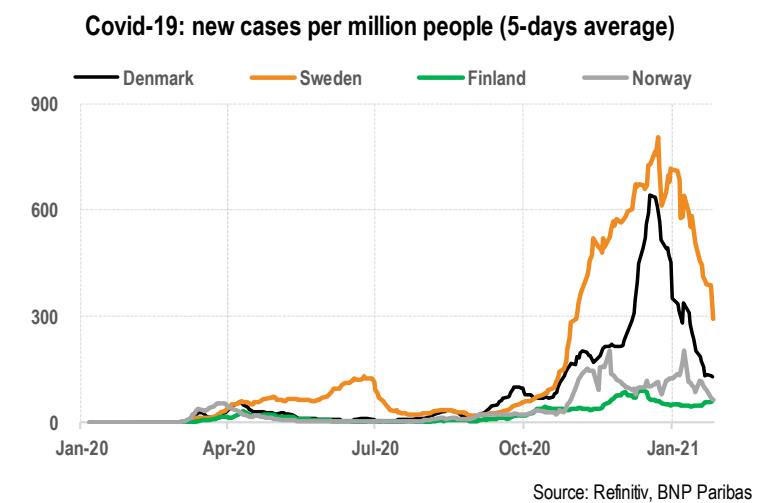
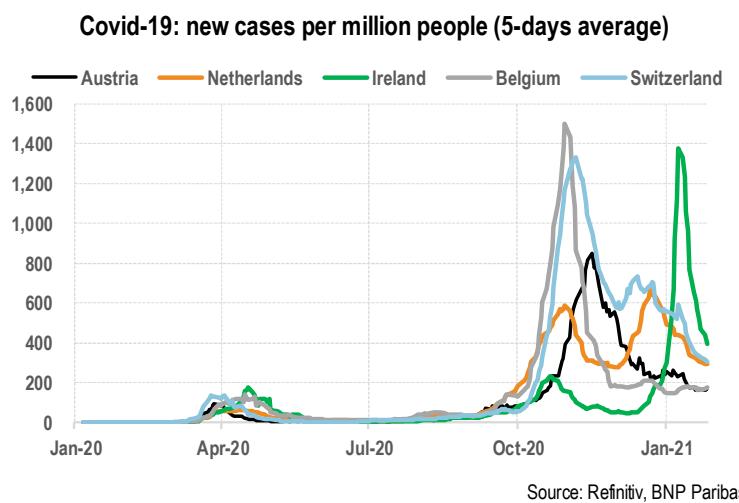
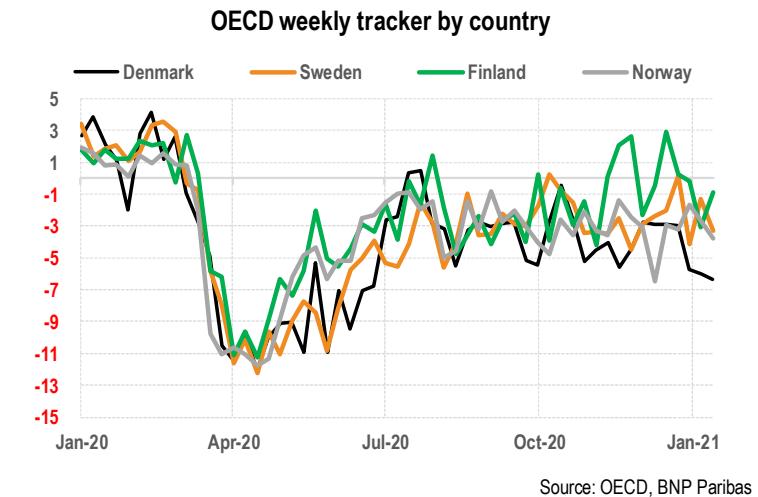
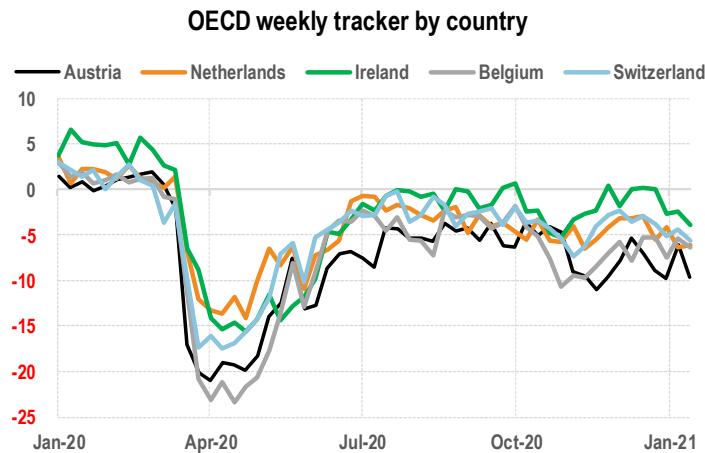


Source: Refinitiv, BNP Paribas



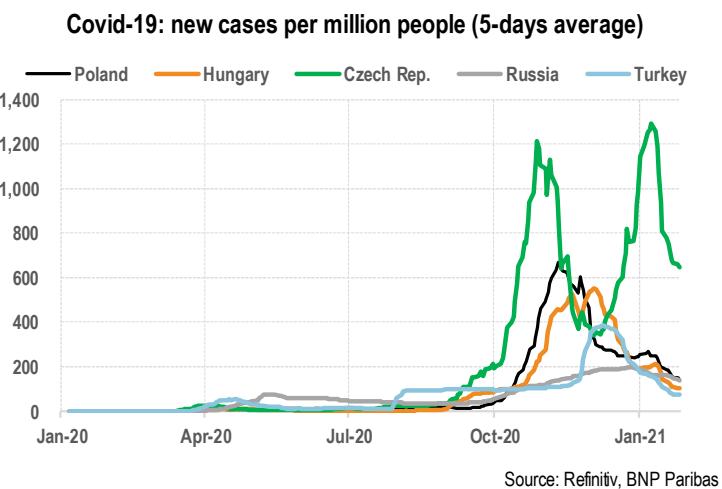
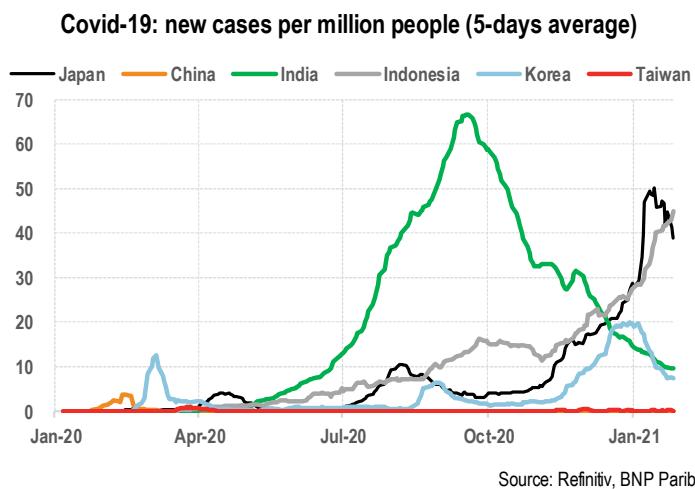
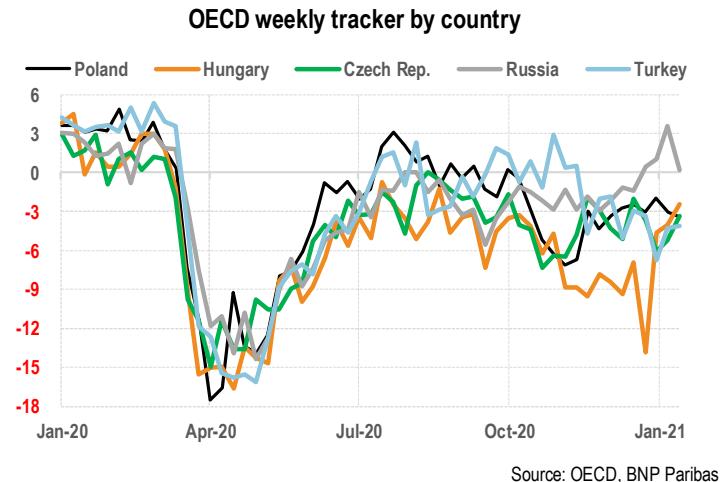
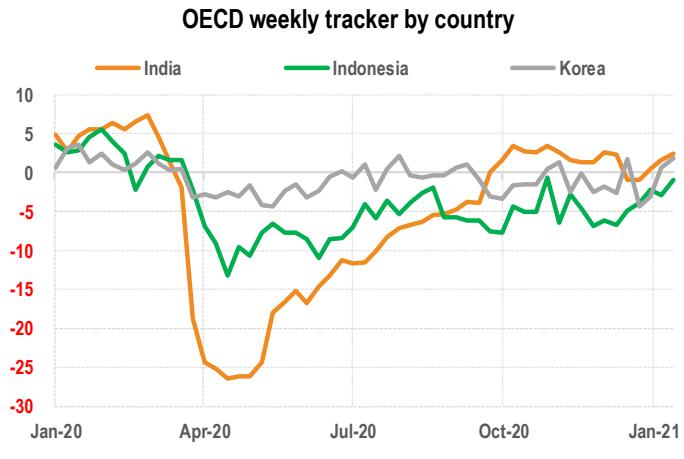
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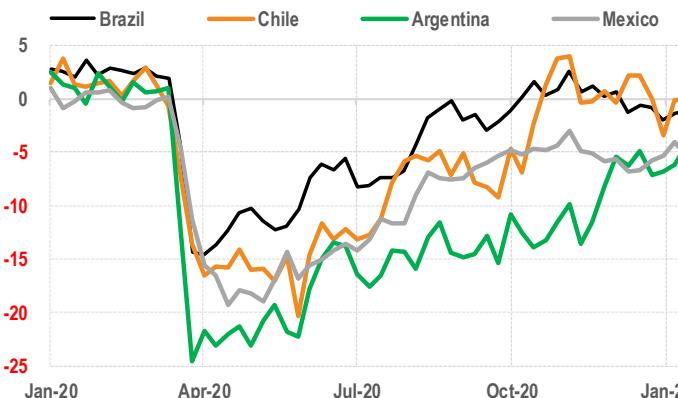
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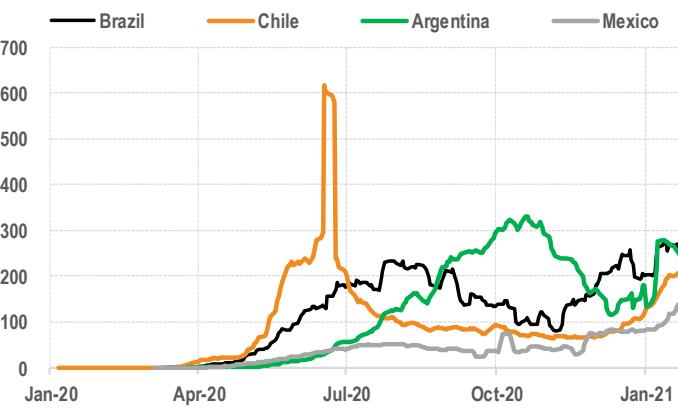
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OECD weekly tracker by country



Source: OECD, BNP Paribas

Covid-19: new cases per million people (5-days average)



Source: Refinitiv, BNP Paribas



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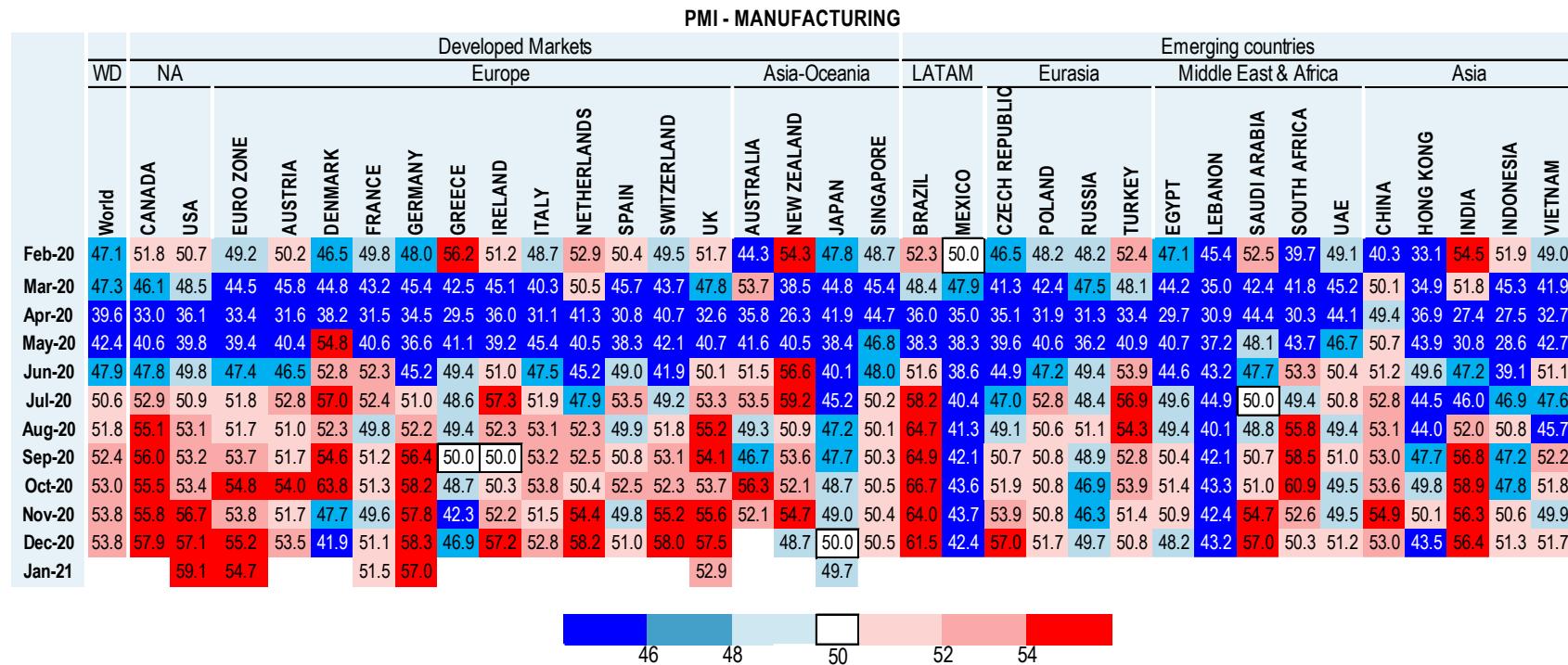
ECONOMY: RECENT DATA



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Purchasing managers' indices: manufacturing doing fine in most countries, despite rising number of infections in some

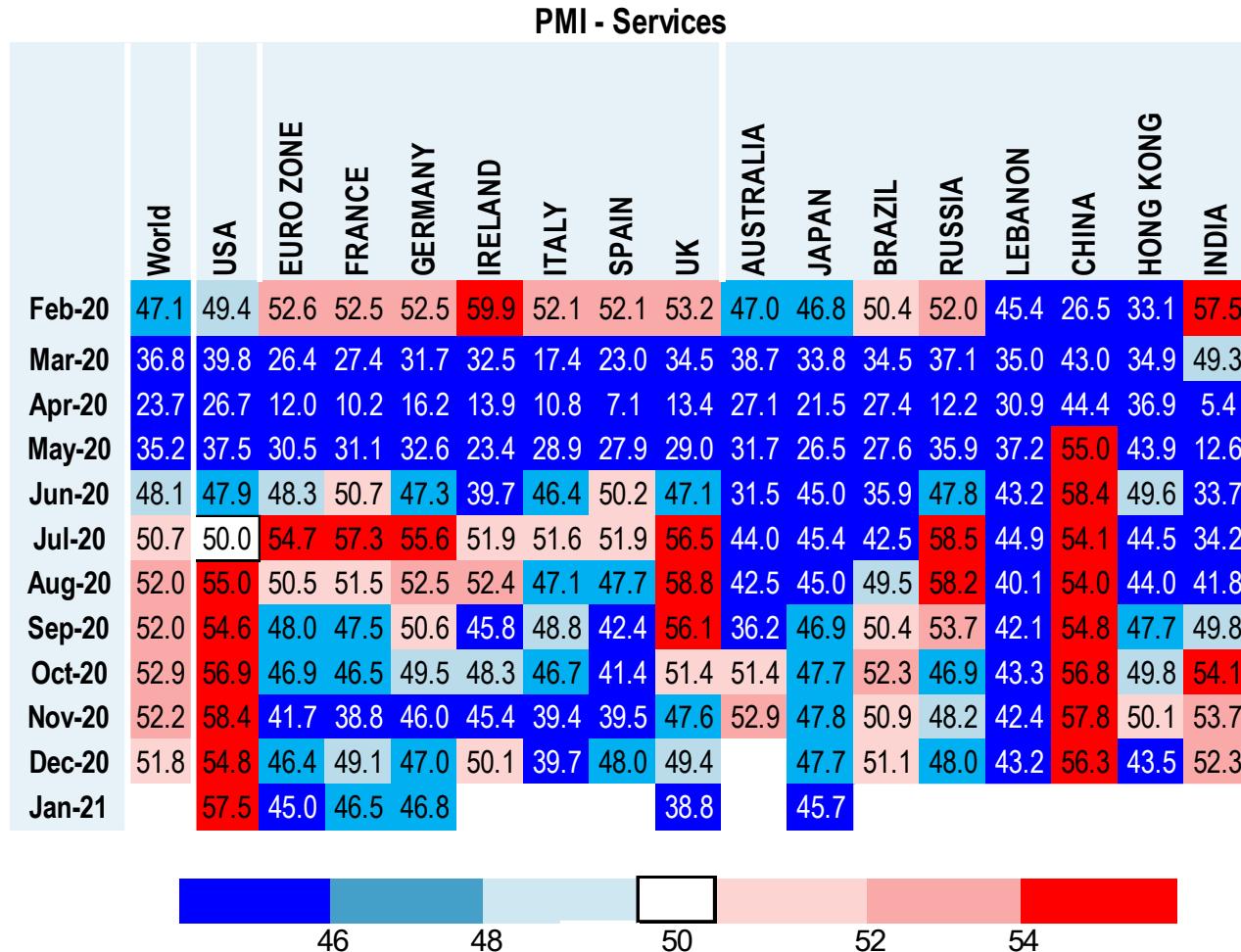


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Source: Markit, BNP Paribas

Purchasing managers' indices: services sector in Europe and Japan suffering from rising infections, but less than in Q1 2020

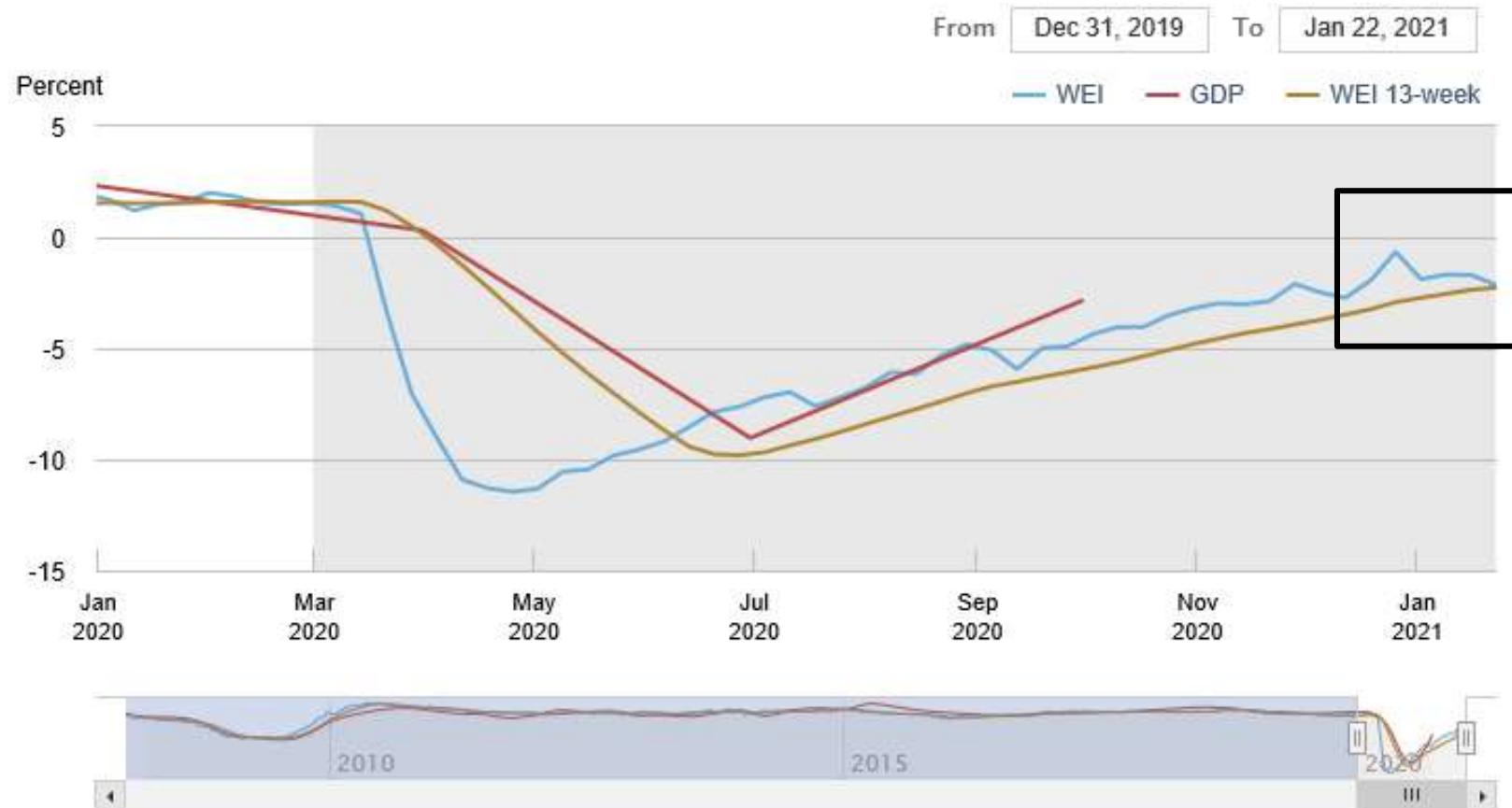


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Source: Markit, BNP Paribas

US: NY Fed's weekly economic index –a proxy for yoy real GDP growth- no longer increasing



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Source: Federal Reserve of New York

US: Federal Reserve Beige January 2021 points towards modest growth and specific types of wage and price pressure

Overall Economic Activity

- Economic activity increased modestly
- Business optimism about vaccines has been tempered by concern over the recent virus resurgence

Employment and Wages

- Employment rose, although the pace was slow
- Employers in some Districts reported raising wages or offering more generous benefits to limit employee turnover

Prices

- ... modest price increases with growth in input prices continuing to outpace that of finished goods and services.
- ... improved ability to raise final selling prices to consumers...
- Home prices continued to climb, driven by low inventories and rising construction costs.



US: the view from the CFOs

- “Corporate financial decision-makers are generally optimistic about U.S. economic prospects, but note downside risks for 2021”
- CFOs note several important risks and uncertainties, including a shift from concerns of low demand to issues such as labor quality, tax policy and increased automation.
- While hiring is expected to rebound in 2021, more than half of large firm CFOs say their companies are shifting away from labor towards automation.

Source: The CFO Survey, Federal Reserve Bank of Richmond. survey was fielded from November 30 to December 11, 2020

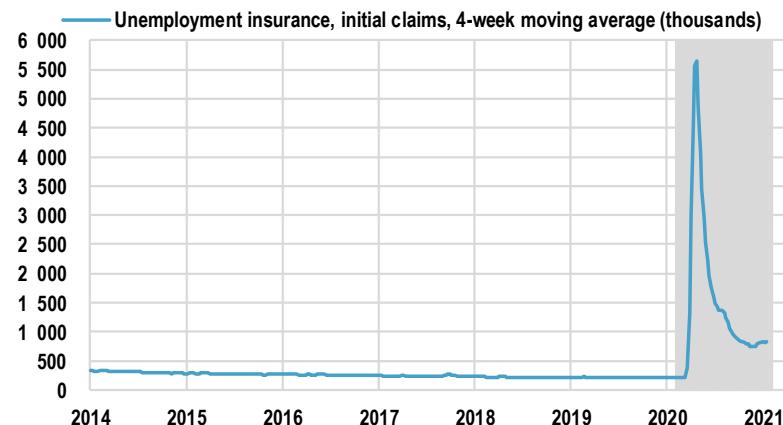


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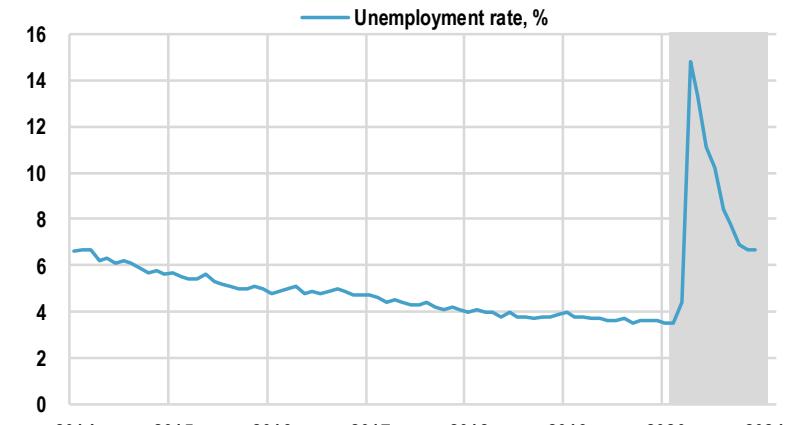
US: creating the jobs that have been lost last year will take a lot of time

Initial claims for unemployment insurance (weekly)



Source: US Department of Labor, NBER, BNP Paribas

title



Source: BLS, NBER, BNP Paribas

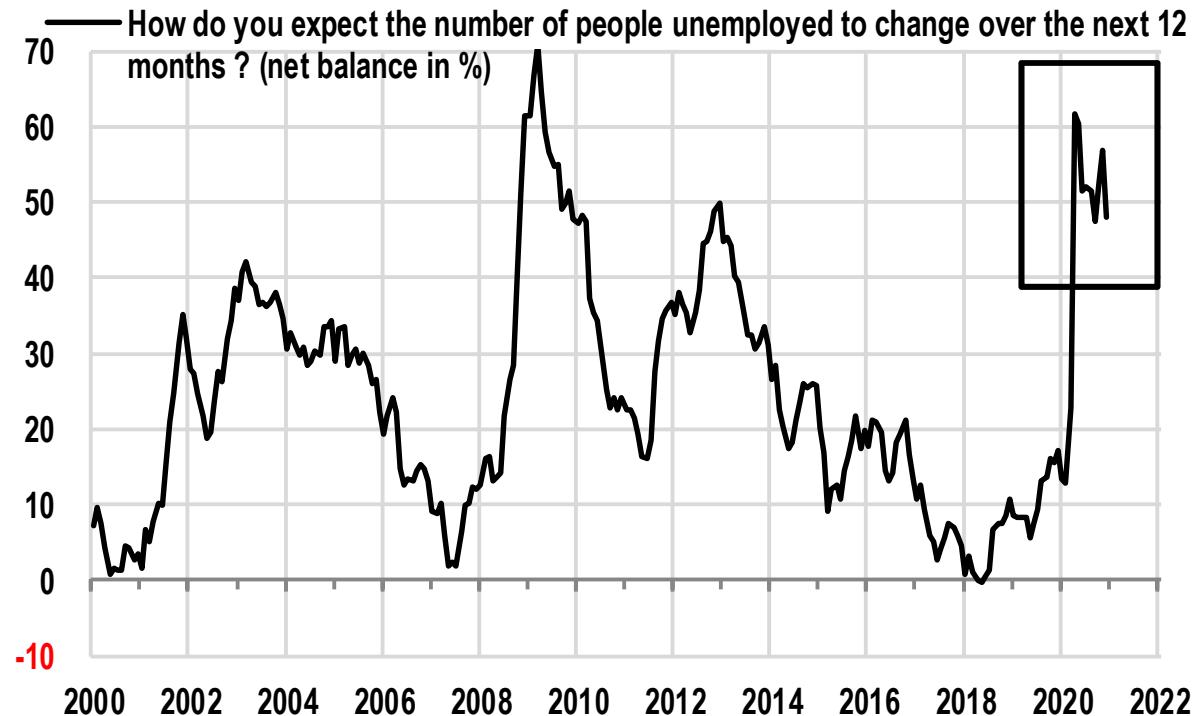


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Eurozone: household unemployment expectations remain high, which is a headwind for spending

Euro zone: consumer survey, unemployment expectations



Source: European Commission surveys, BNP Paribas

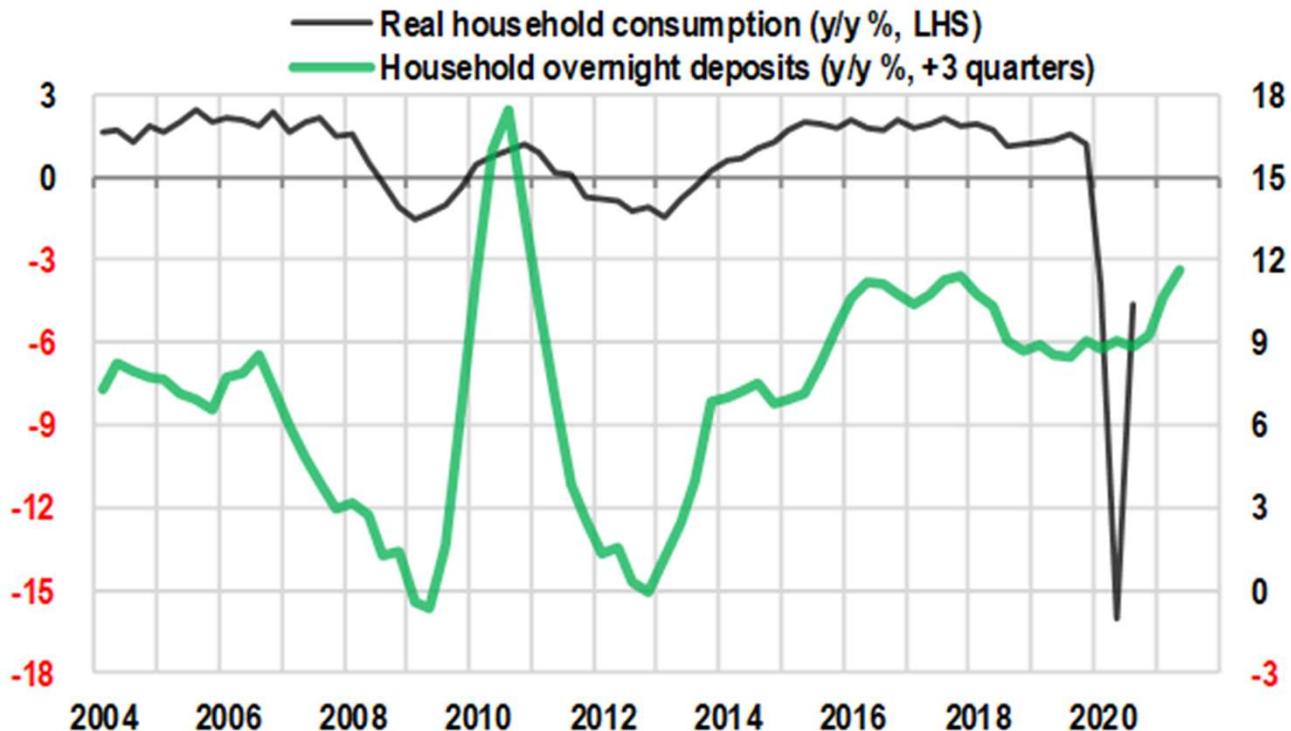


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However, strong increase in overnight deposits of households could eventually boost spending

Household overnight deposits vs private consumption



Source: ECB, Eurostat, BNP Paribas

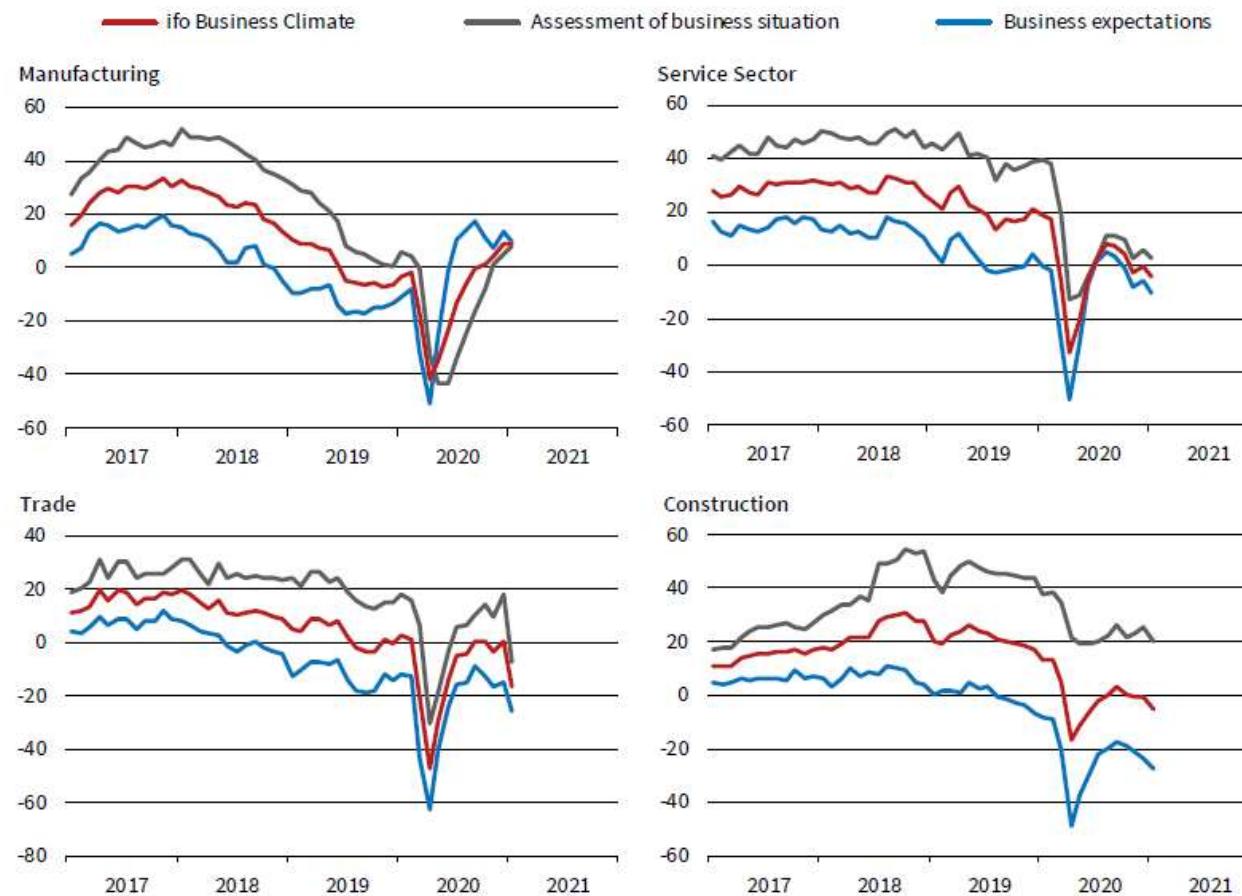


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Germany: business climate deteriorates

ifo Business Climate, Business Situation, and Expectations by Sector
Balances, seasonally adjusted



Source: ifo Business Survey, January 2021.

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Source: IFO

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Germany: export expectations improve

ifo Export Expectations
Results of the ifo Business Survey for January 2021

ifo Export Expectations Improved Noticeably

Munich, January 26, 2021 – Sentiment among German exporters has become considerably brighter. In January, the ifo Export Expectations in manufacturing rose from 1.9 points to 6.0 points. This is its highest level since October. Clarity on Brexit and the US presidency, a robust industrial economy, and the start of vaccination campaigns worldwide led to cautious optimism in the German export sector.

Manufacturers of computers and electrical equipment expect to see major increases in exports. Companies in mechanical engineering and the chemical industry are also confident about their future exports. Expectations among food and beverage manufacturers also saw a marked recovery. They currently assume their export business will hold steady. The international market is still difficult for Germany's clothing industry. Furniture manufacturers also expect their international sales to decline.



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Source: ifo Business Survey, January 2021.

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Source: IFO

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FOCUS ON THE NORDICS*

*PREPARED BY HUBERT DE BAROCHEZ



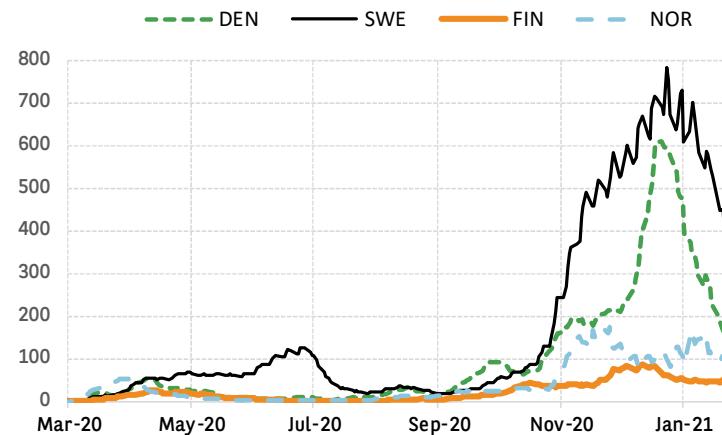
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Nordics – Sanitary situation

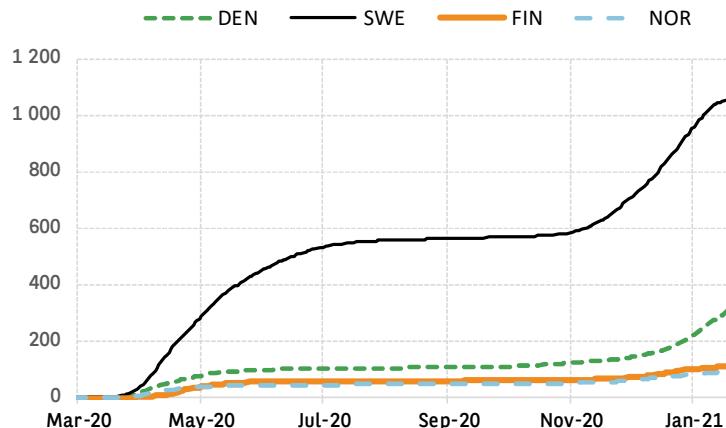
- Sweden is the Nordic country most affected by the pandemic
- Finland & Norway have managed to keep the pandemic under control
- Denmark is a bit more affected than Finland and Norway, but largely ahead in vaccinating its population

New cases per million people (7-day average)



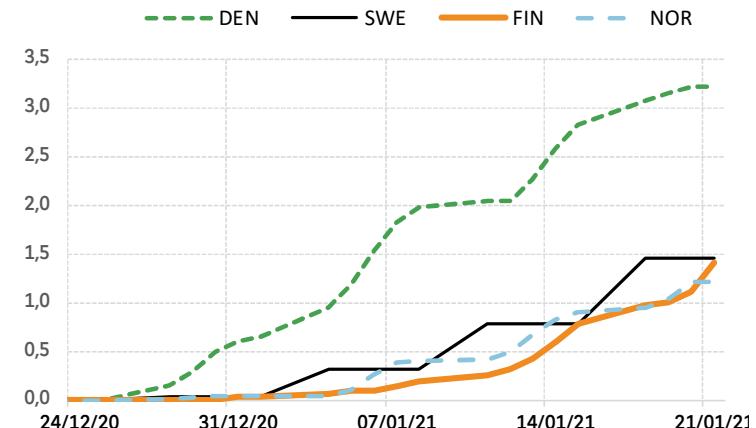
Source: Refinitiv

Total deaths per million people



Source: Refinitiv

Vaccinations per hundred people



Source: Our World In Data, Refinitiv

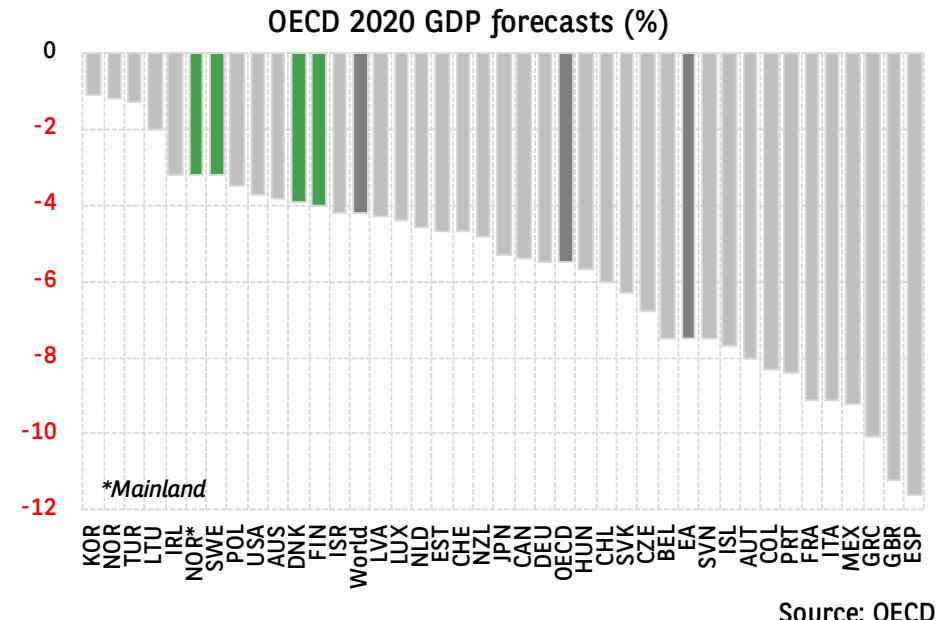


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Nordics – Economic situation

- Nordic countries' economies have been among the least affected by the crisis
- 2020:
 - GDP contractions of 3½-4½ per cent
 - Inflation below 1% (except in Norway)
- 2021:
 - GDP to rebound by roughly 3%
 - Inflation to bounce back a bit



	GDP				Inflation			
	2019	2020F	2021F	2022F	2019	2020F	2021F	2022F
Denmark	2,8	-3,9	3,5	2,4	0,7	0,3	1,1	1,3
Sweden	1,3	-3,4	3,3	2,4	1,7	0,6	0,8	1,3
Finland	1,1	-4,3	2,9	2,2	1,1	0,4	1,1	1,4
Norway	1,2	-3,6	2,8	2,1	2,3	1,3	1,8	2,0
Euro area	1,3	-7,8	4,2	3,0	1,2	0,3	1,1	1,3

Source: European Commission

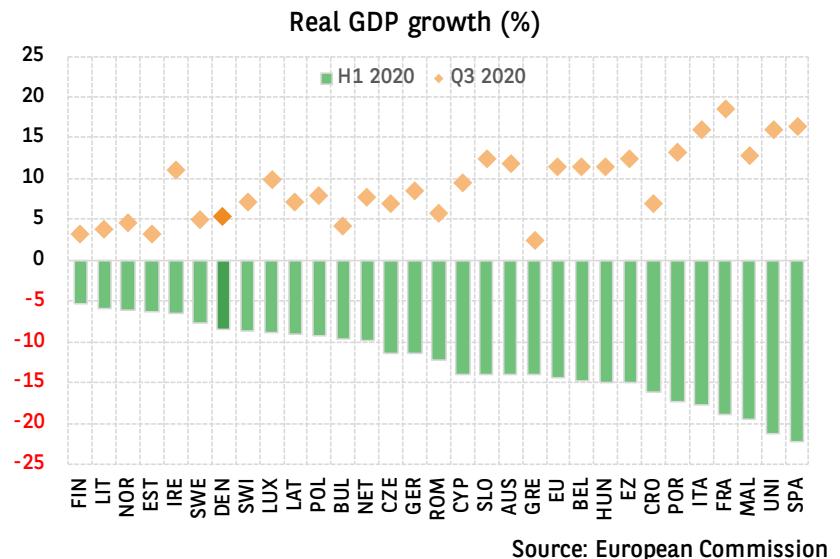


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Nordics – Denmark

- **GDP dropped by 8.5% in H1 2020**
- **One of the most resilient in Europe, but hardest hit among Nordic economies**
 - Big contraction in exports
(Although goods exports held up due to agricultural and pharmaceutical exports – less sensitive to business cycle)
- Investment to fall by nearly 5% in 2020, but to be supported in the years ahead by:
 - Normalisation of external demand
 - Government's recovery package
(focused mainly on green investment)
- **12pp rise in debt-to-GDP ratio in 2020**
 - Government deficit
 - GDP contraction
 - Tax deferrals
- **But:**
 - Effects will be largely reversed in 2021
 - Debt-to-GDP ratio still quite low (45% in 2020) and expected to fall back



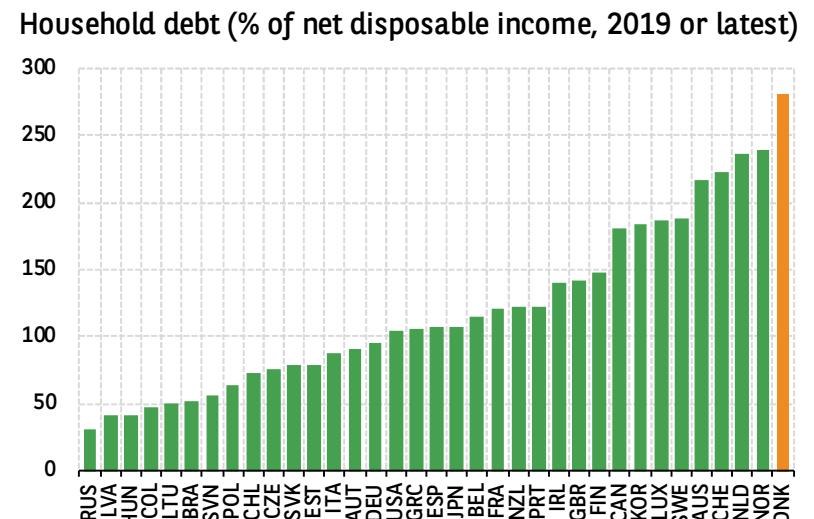
Nordics – Denmark

- **Strong recovery expected :**
 - Only 3.9% contraction in 2020 as a whole
 - 3.5% rebound in 2021 (see table)
- **Rapid pace of vaccinations gives hopes that severe restrictions won't be needed anymore**

	2019	2020F	2021F	2022F
GDP (%)	2.8	-3.9	3.5	2.4
Inflation (%)	0.7	0.3	1.1	1.3
Unemployment (%)	5.0	6.1	5.8	5.5
Gov. balance (% of GDP)	3.8	-4.2	-2.5	-1.9
Gov. debt (% of GDP)	33.3	45.0	41.1	40.9

Source: European Commission

- Key short-term downside risk:
 - **External environment:** due to economy's reliance on trade
- Other downside risk:
 - **Brexit disruptions** and economic situation in the UK, an important trading partner
- Key long-term downside risk:
 - **Household debt:** OECD country with highest debt-to-income ratio (see chart)



Source: OECD

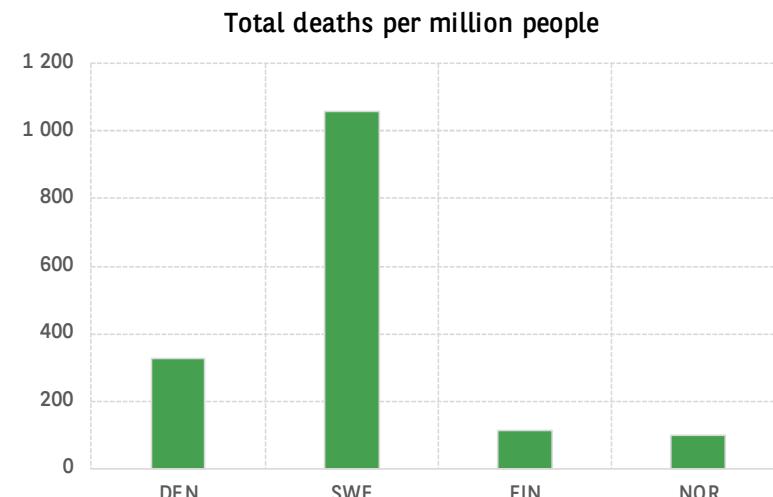


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Nordics – Sweden

- **GDP contracted by 7.6% in H1 2020**
 - Mainly due to private consumption and exports
 - Despite resilience in public and housing investment
- The authorities imposed **less stringent restriction measures** (no national lockdown)...
- ... but the **GDP contraction was as severe as in other Nordic countries**
- ... and **this strategy did not prevent a second wave**
 - Sweden shows mortality rates 10x higher than those of Norway or Finland (see chart)
 - More stringent measures implemented since
- **Consumption and exports to recover strongly** in 2021 and 2022, as the sanitary situation improves
- But **investment likely to remain relatively muted** – due to low capacity utilization and uncertainty
- Key downside risk:
 - **External environment** remaining weak
- Key challenge:
 - Support young, low-skilled and foreign-born **unemployment**



Source: Refinitiv

	2019	2020F	2021F	2022F
GDP (%)	1.3	-3.4	3.3	2.4
Inflation (%)	1.7	0.6	0.8	1.3
Unemployment (%)	6.8	8.8	9.2	8.1
Gov. balance (% of GDP)	0.5	-3.9	-2.5	-1.4
Gov. debt (% of GDP)	35.1	39.9	40.5	40.3

Source: European Commission

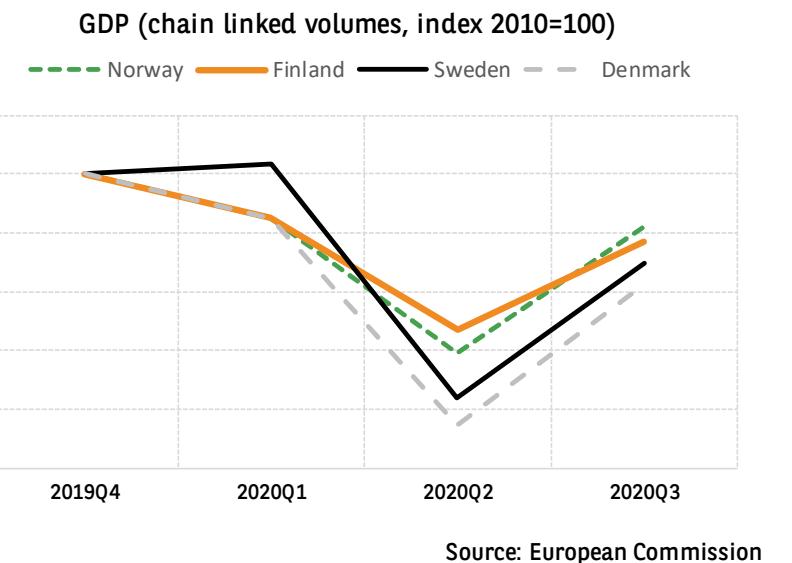


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Nordics – Finland

- **GDP contracted by “only” 5.3% in H1 2020**
 - Main hit from private consumption
- **Smallest fall in Europe**
 - Authorities able to contain the pandemic without imposing measures as strict as elsewhere
 - Larger decrease in imports than exports
 - Minor decrease in investment and public spending
- **But recovery less vigorous than elsewhere –** particularly compared to Nordic neighbours
 - Economy was already showing signs of weakness before the pandemic (GDP contracted in Q4 2019)
- **Second wave to slow economic recovery...**
- **... but resilience & fiscal space to boost economy thereafter**
- Long term challenge: **keep public finances on sustainable path** amid unfavourable demographics



	2019	2020F	2021F	2022F
GDP (%)	1.1	-4.3	2.9	2.2
Inflation (%)	1.1	0.4	1.1	1.4
Unemployment (%)	6.7	7.9	7.7	7.4
Gov. balance (% of GDP)	-1.0	-7.6	-4.8	-3.4
Gov. debt (% of GDP)	59.3	69.8	71.8	72.5

Source: European Commission

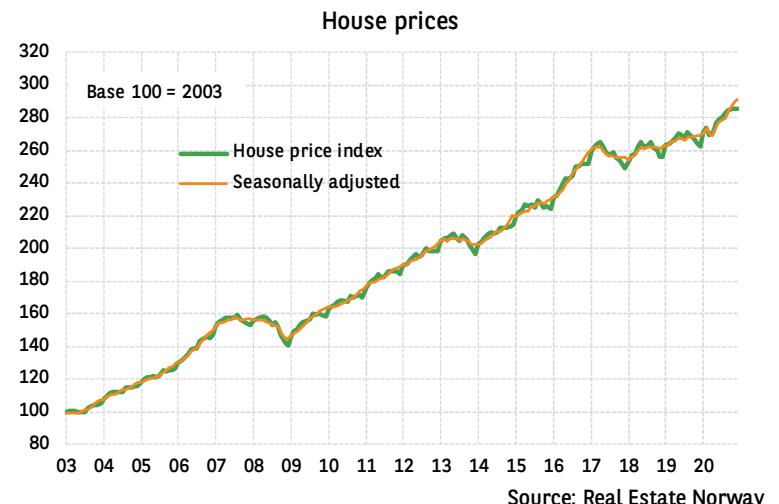


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Nordics – Norway

- Norway hit by the **Covid-19 pandemic** and the resulting **sharp drop in oil prices**
- **But the economy has proved to be very resilient: only a 3.6% GDP contraction expected in 2020** (mainly due to a fall in private consumption)
- Sanitary situation broadly under control: lowest mortality rate in continental Europe
- **Helped by fiscal and monetary support**
 - Quarterly fiscal deficit for first time since mid-1990s
- Key external risks:
 - **Energy prices** and resource sector investment
 - **Situation of main trading partners**
- Key domestic risk:
 - **Rising house prices** (+8.4% in 2020, +67% since 2010, see chart) and **household indebtedness** (debt-to-income ratio above 200%)



	2019	2020F	2021F	2022F
GDP (%)	1.2	-3.6	2.8	2.1
Inflation (%)	2.3	1.3	1.8	2.0
Unemployment (%)	3.5	5.3	4.8	4.1
Gov. balance (% of GDP)	6.4	3.1	7.8	8.5
Gov. debt (% of GDP)	40.4	46.2	43.7	40.5

Source: European Commission



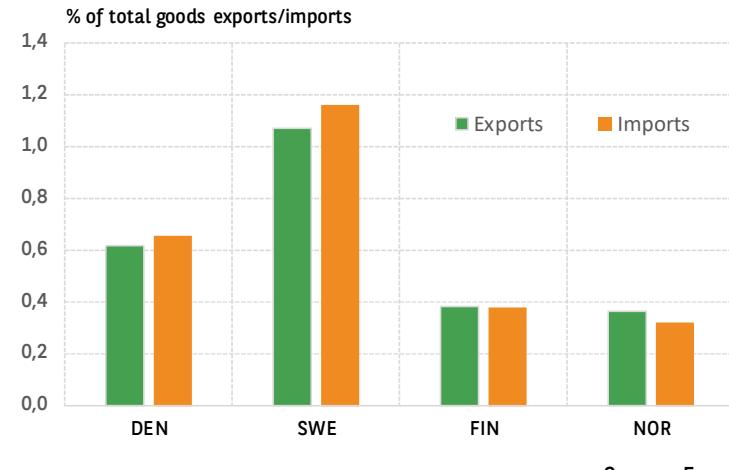
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Nordics – Trade relationship with France

- Trade with the Nordics (DK, SE, FN, NO) represents 2.5% of France's total trade (top chart)
- Trade with France represents 3-4% of the Nordics' total trade (bottom chart)
- France's main exports:
 - Machinery & transport equipment
 - Chemicals
 - Manufactured goods
- France's main imports:
 - Denmark, Sweden & Finland: Machinery & transport equipment, Manufactured goods, Chemicals
 - Norway: Mineral fuels

Share of French goods exports going to/imports coming from the Nordics



Source: Eurostat

Share of goods exports going to/imports coming from France



Source: Eurostat

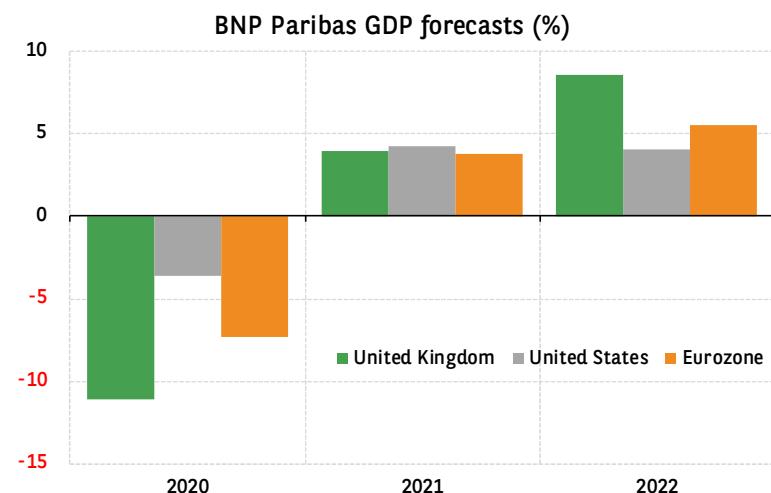


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Brexit – Consequences for the UK

- **UK economy affected mainly through trade**
 - ~45% of all UK exports go to the EU
- Thanks to the deal, **no tariffs or quotas for the exchange of goods...**
- ... but **new non-tariff barriers** have appeared
 - Paperwork, administrative procedures, border controls, rules of origins, etc.
- ... and **services exchanges will also be less fluid**
 - No recognition of professional qualifications
- **BNP Paribas GDP forecasts:**
 - **Small rebound in 2021**
 - **Economy starts to catch-up in 2022**
- In the long term, GDP also affected by:
 - Lower investment and productivity
 - Higher structural unemployment

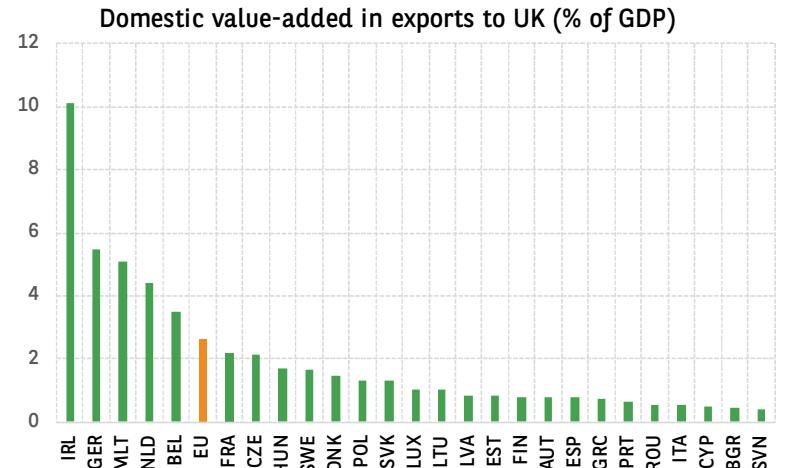


Brexit – Consequences for the EU

- **EU less exposed to UK than UK is exposed to EU**
 - <10% of all EU exports go to the UK
 - >40% of all UK exports go to the EU
- **EU countries most exposed to the UK**
 - Countries' share of goods exports going to the UK (% of country's total goods exports)
 1. Ireland: 10.3%
 2. Netherlands: 8.1%
 3. Belgium: 7.6%
 4. France: 6.8%
 5. Spain: 6.8% - EU average: 6.1% of EU GDP
 - EU countries' domestic value-added in exports to UK (% of country's GDP)
 1. Ireland: 10.1%
 2. Germany: 5.5%
 3. Malta: 5.1%
 4. Netherlands: 4.4%
 5. Belgium: 3.5% - EU average: 2.6% of EU GDP



Source: Eurostat



Source: Chen et al. (2017)



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FOCUS ON FRANCE*

* PREPARED BY HÉLÈNE BAUDCHON



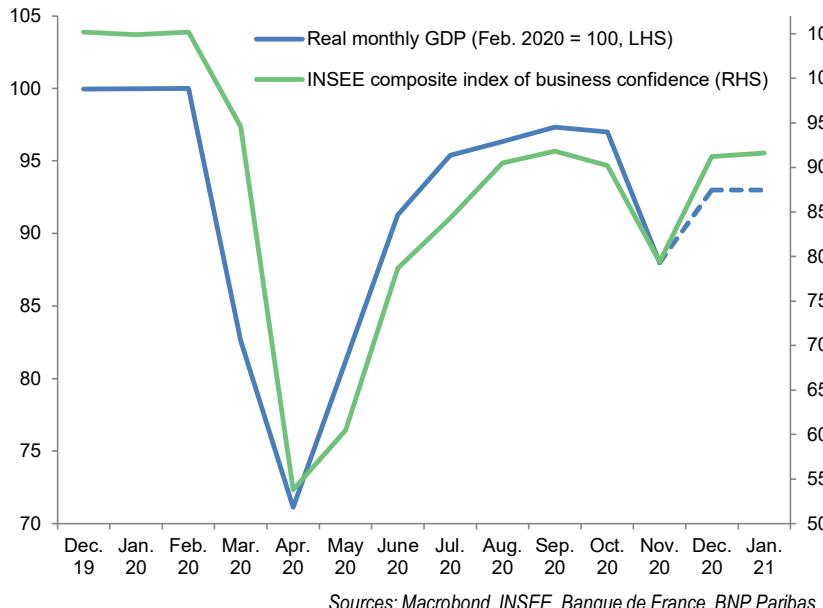
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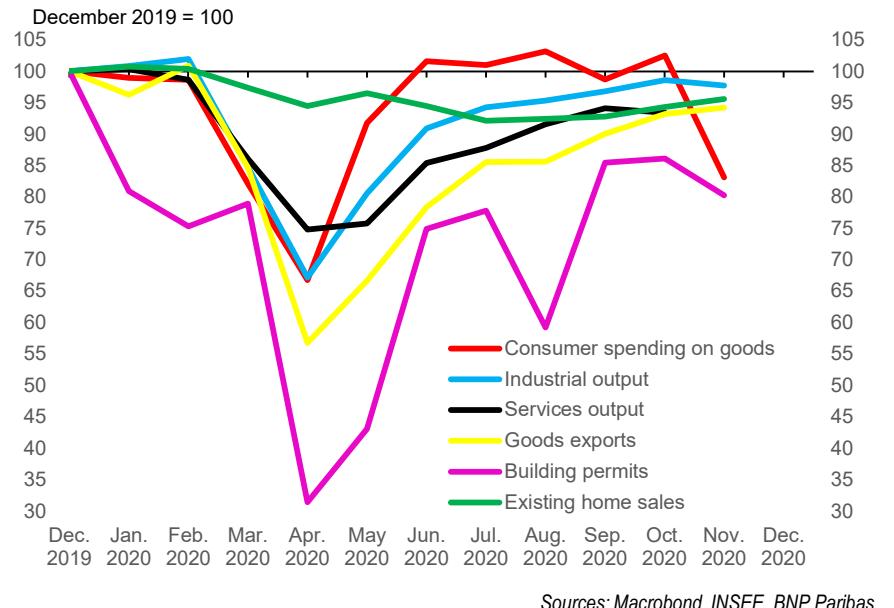
2020: the great contraction

- Plunge in GDP (expected contraction of 9%) linked to the lockdown stringency and to the sectoral structure of the French economy. A W-shaped scenario in parallel with the pandemic's waves (2nd "V" less marked than the 1st).
- A rebound in a series of indicators in May and June at the exit of the Spring lockdown illustrated the economy's capacity to rebound. This was seen in PMIs, consumer spending on goods, firm creation, hiring and car registrations. However, other key indicators recovered in a more limited way, a reminder of the headwinds at work (INSEE confidence surveys, production, exports).
- In April 2020, economic activity troughed at 70% of its normal level (immediate loss of 30%), before recovering to 97% in October, falling back again to 88% in November (2nd lockdown), picking up to 93% in December, staying there in January 2021 (preliminary estimate).

Monthly GDP estimate and business confidence



Covid-19 shock on a set of monthly hard data

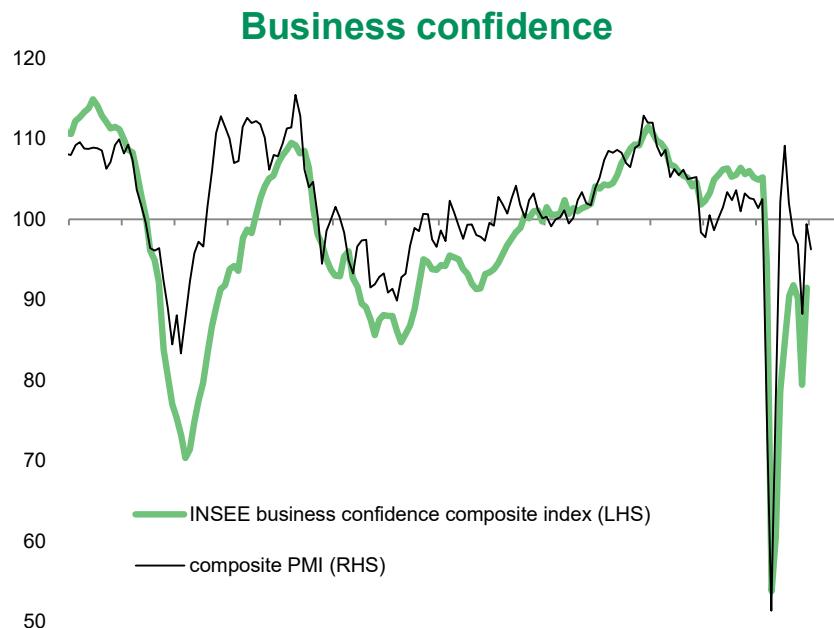


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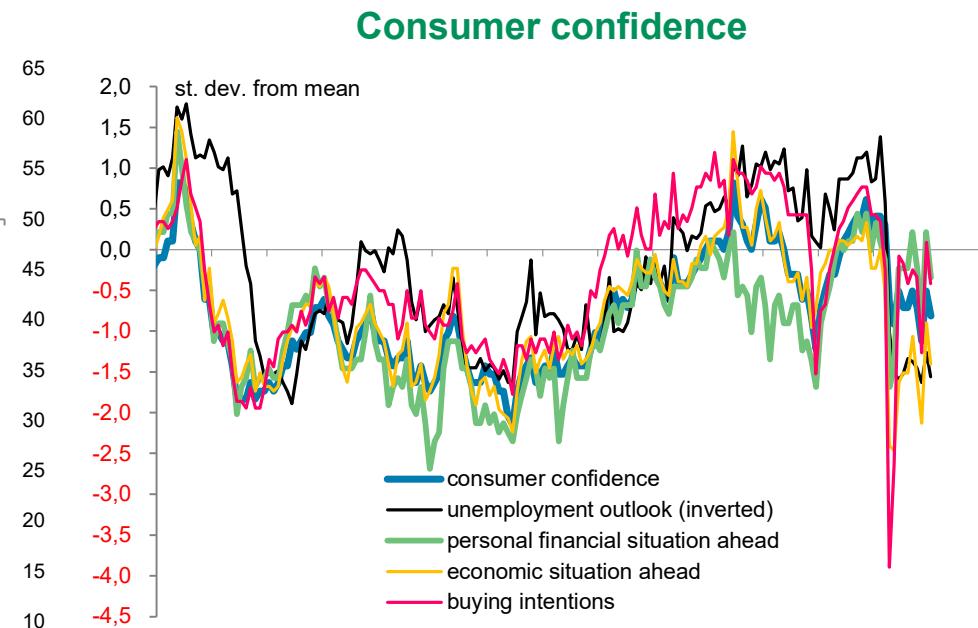
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Macroeconomic situation at the start of 2021

- There is light at the end of the tunnel resulting from the vaccination programme but at the moment it is like the flickering glimmer of a candle. The health situation remains worrying, lockdown measures are more likely to be tightened than loosened, before the vaccination campaign starts to improve the situation.
- Confidence and activity are therefore at risk of relapsing in early 2021.
- Business confidence was hit harder than consumer confidence recovering further afterwards, although both indicators were still at depressed levels at December 2020 (below the 100 benchmark).



Sources: Macrobond, INSEE, Markit, BNP Paribas



Sources: Macrobond, INSEE, BNP Paribas



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2021 economic outlook: a significant but incomplete rebound (1)

- We expect 2021 growth to reach 5.5%. All the ground lost in 2020 will not be recouped (Q4 2021 GDP to remain 1% below its pre-crisis Q4 2019 level; similar gap for the EMU). 2022 is expected to mark the full return to normal. The rebound is:
 - ... supported by the gradual catch-up of normal levels of activity, the effects of the emergency package and the recovery *France Relance* plan, and the ongoing massive vaccination campaign.
 - ... but undermined by the lingering Covid-19 related risks, sector disparities and the weakened shape of the economy.

Real GDP (index, Q4 2019 = 100)

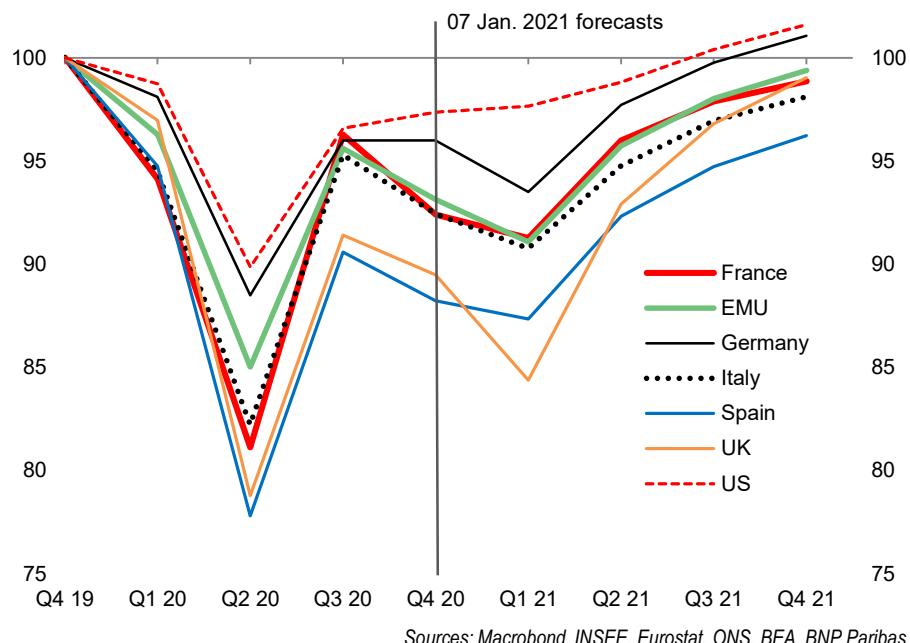
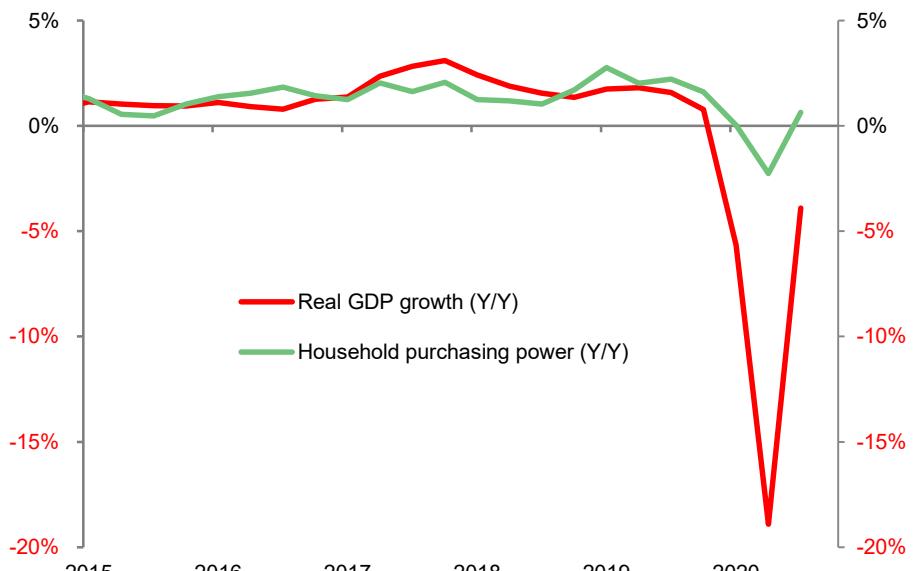


Illustration of the cushioning impact of the emergency package measures

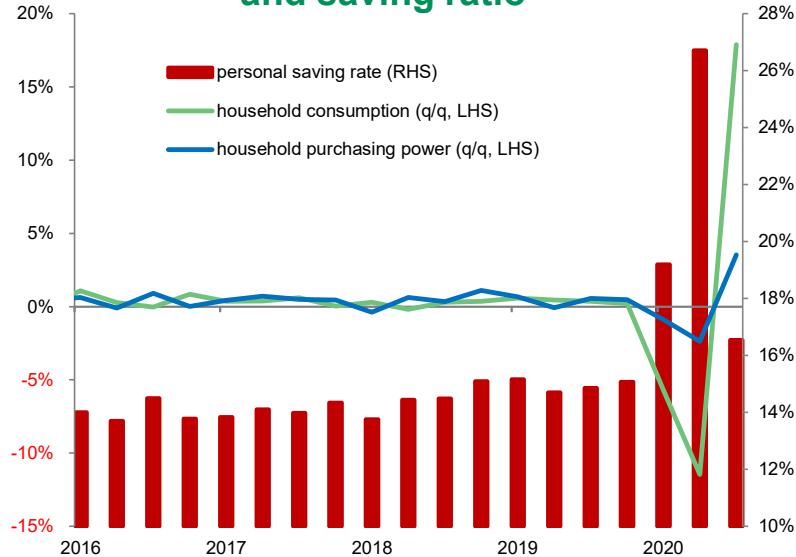


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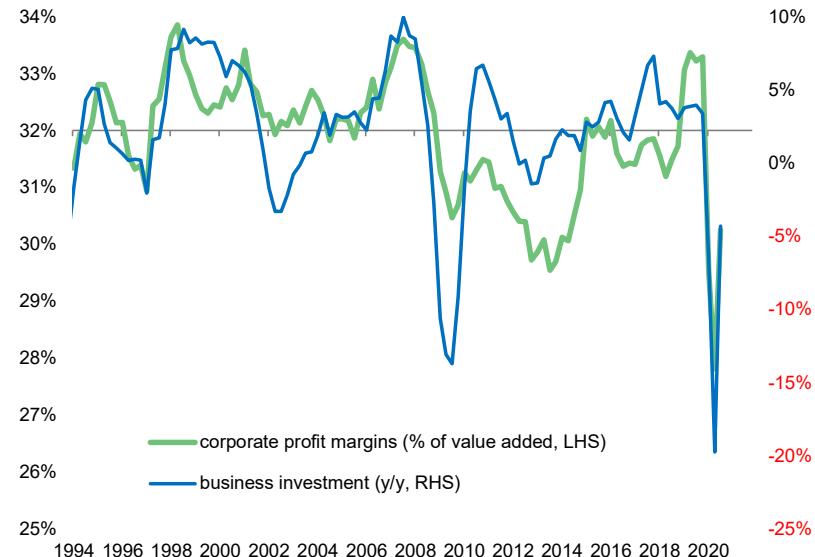
2021 economic outlook: A significant but incomplete rebound (2)

Household consumption, purchasing power and saving ratio



Sources: Macrobond, INSEE, BNP Paribas

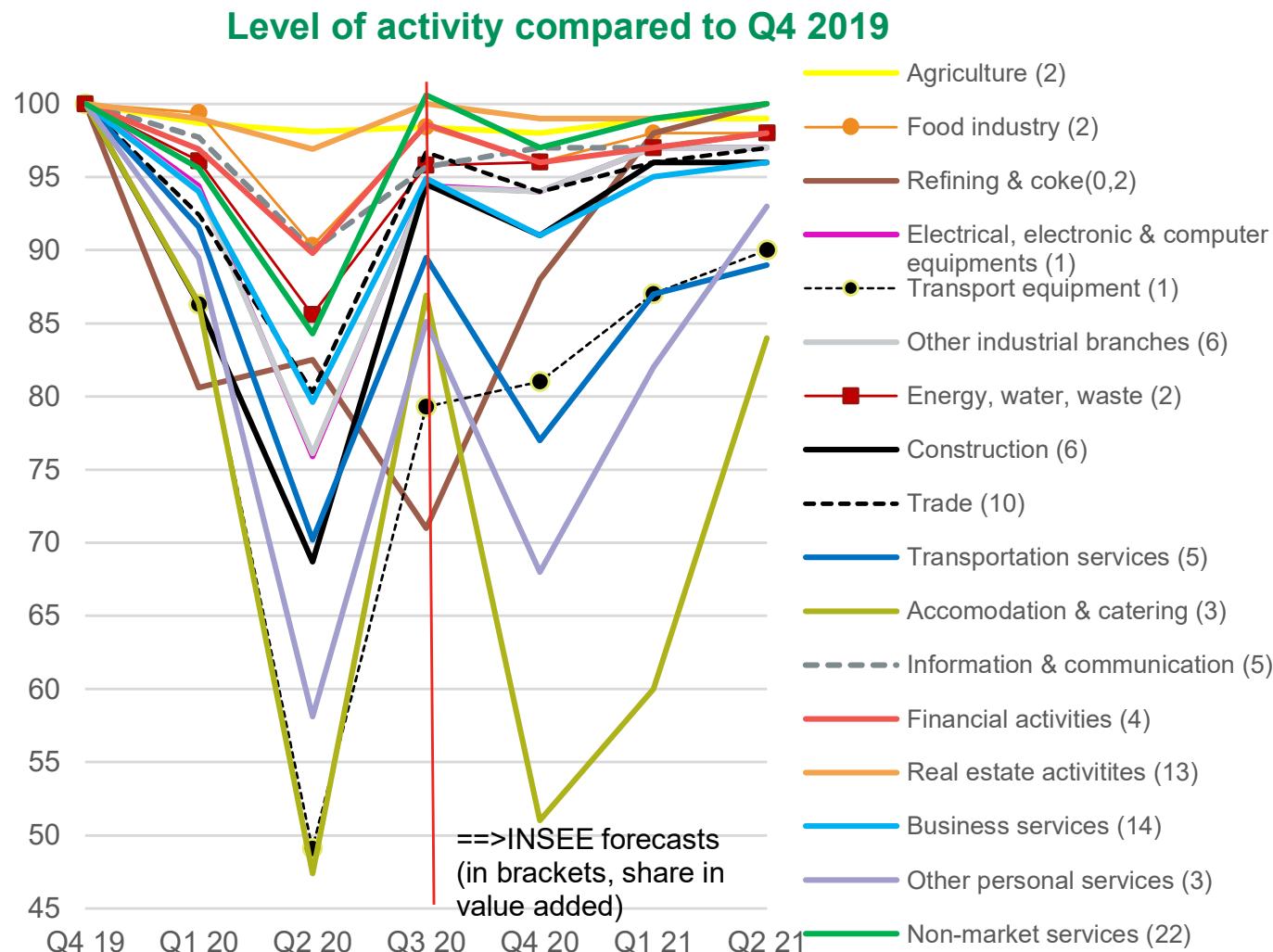
Business investment and profit margins



Sources: Macrobond, INSEE, BNP Paribas

- **Household consumption** has room to rebound strongly, thanks to the cushioning effect of emergency measures on disposable income and the size of enforced savings built up during the lockdowns. The extent to which consumers will tap into these savings is key and depends on their confidence in the health situation and the labour market. The better these are, the less these enforced savings will turn into precautionary savings.
- **Business investment** dynamics are the other major factor. We see a positive outlook on the basis of its relative resilience in 2020 (only a slightly bigger fall than GDP, contrary to normal), supportive monetary and financial conditions, and also because the corporate sector and investment will benefit from numerous measures in the recovery plan. However, higher indebtedness, weakened balance sheets and lingering uncertainty will hamper the recovery.

Big sector differences



Sources: Macrobond, INSEE (15 Dec. 2020 estimates and forecasts), BNP Paribas



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How deep a 'valley': a scenario analysis for France

	No change in current measures					No change in measures but rising impact			Tighter measures but half as tight as in November			Tighter measures, same intensity as November measures			Moderate tightening			Tightening with same intensity as April			
	Oct	Nov	Dec	Jan	Feb	Mar	Jan	Feb	Mar	Jan	Feb	Mar	Jan	Feb	Mar	Jan	Feb	Mar	Jan	Feb	Mar
activity level in % of normal	97	88	93	93	93	93	93	92	91	93	88	88	93	84	84	93	90	90	93	75	75
QoQ growth real GDP Q1 2021				0.4			-0.7			-3.2			-6.1			-1.8			-12.6		

Our current forecast: -1.2%



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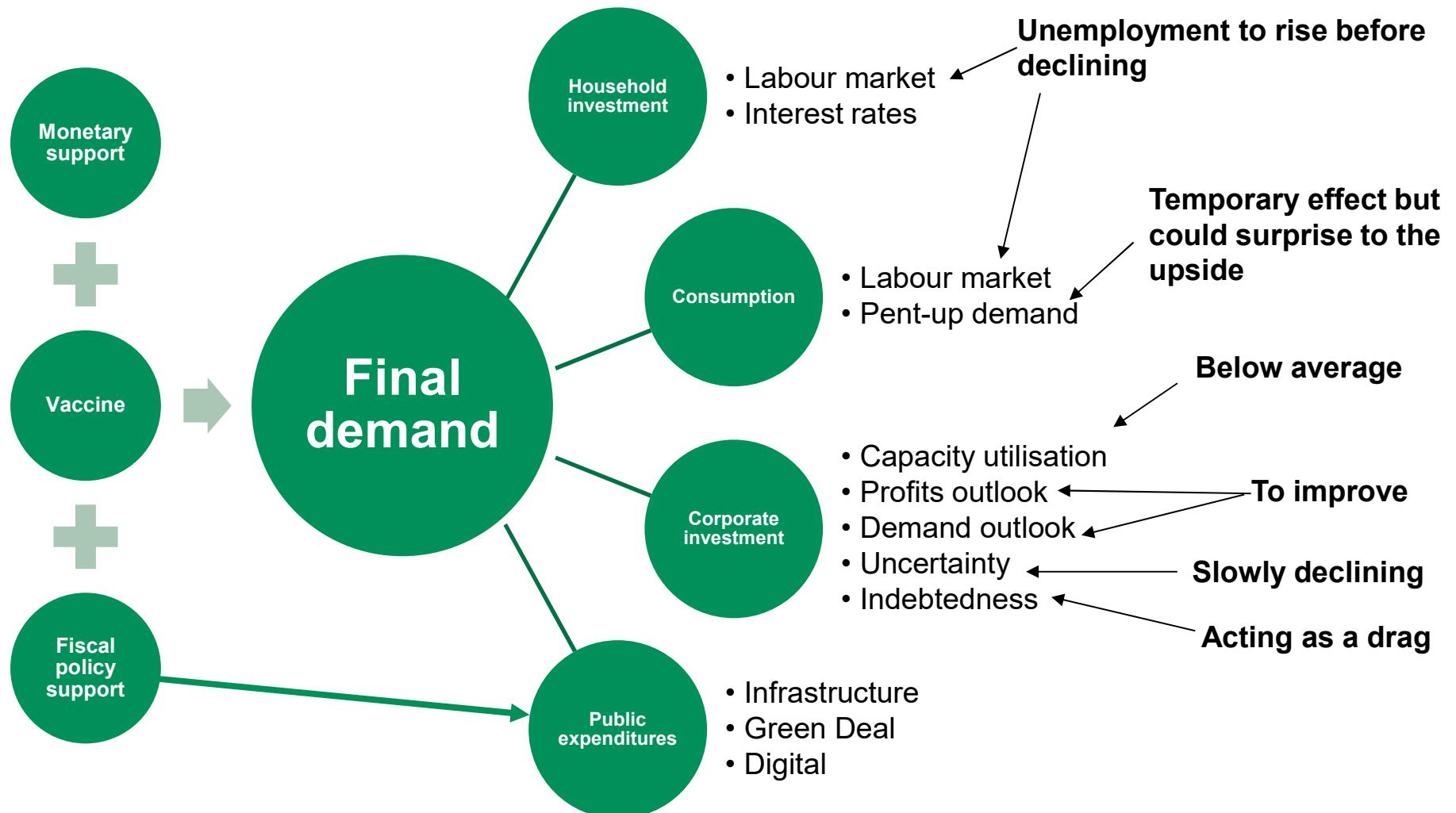
DRIVERS OF THE RECOVERY



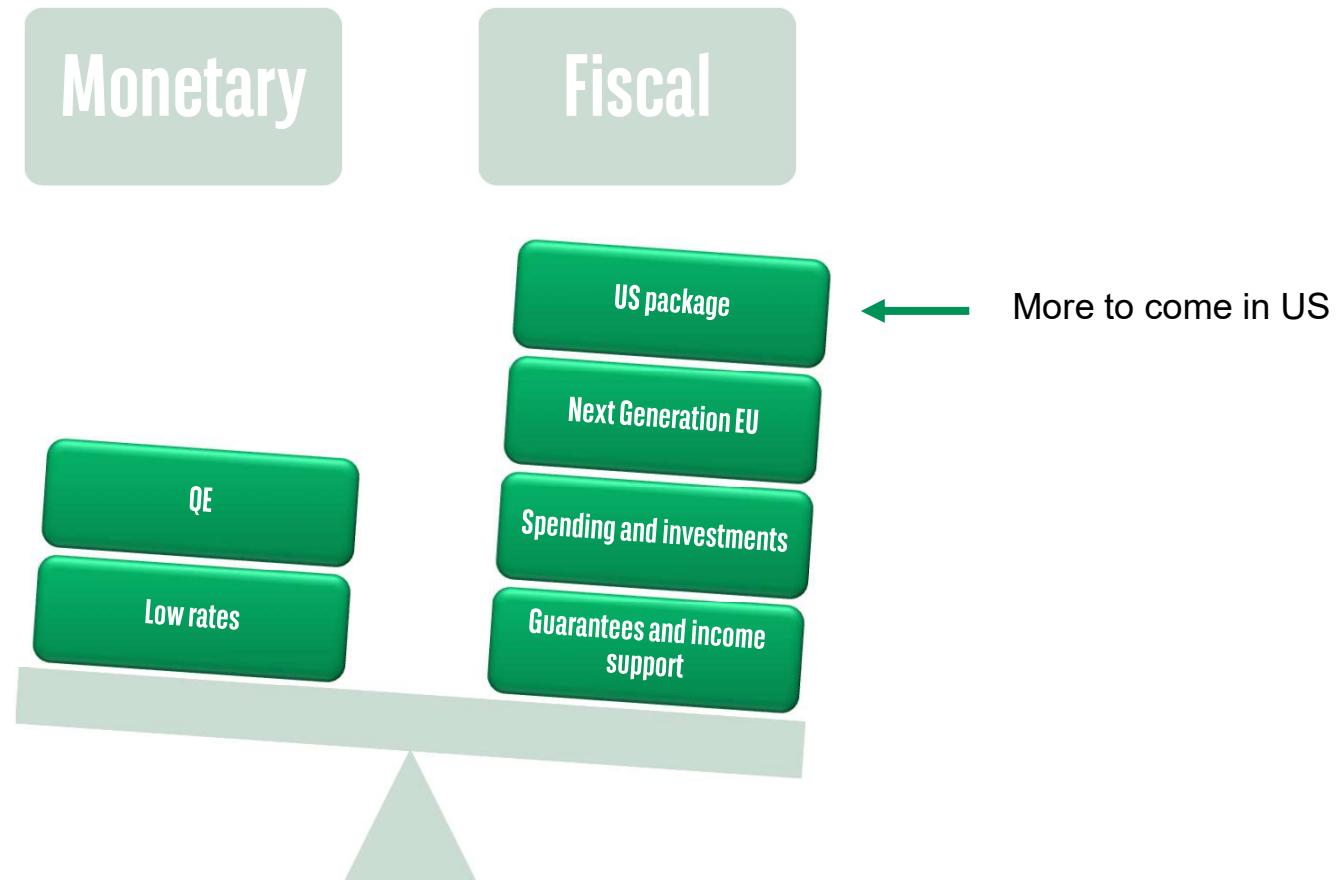
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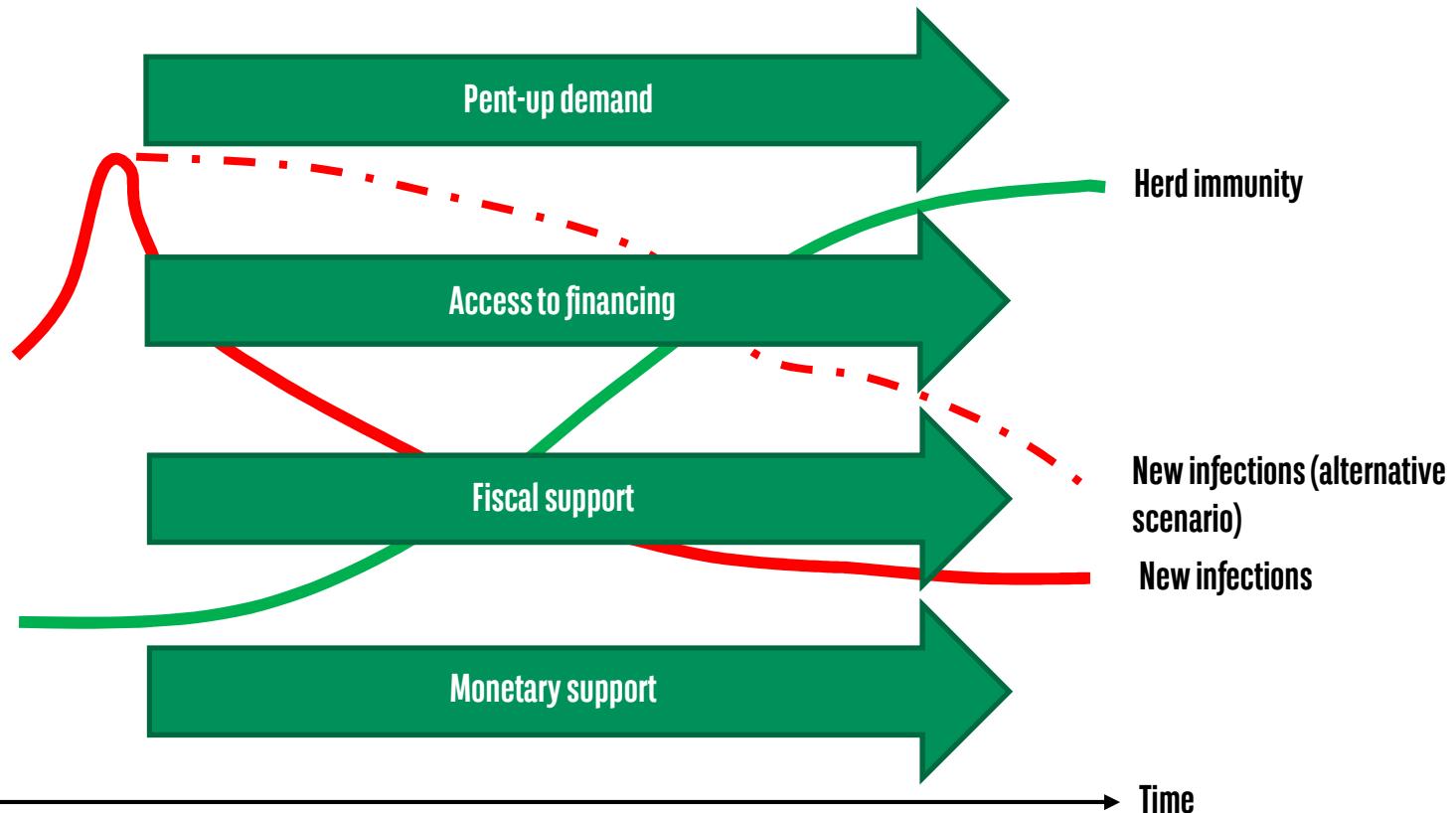
Drivers of the recovery in 2021



Ongoing policy support. More to come in US



2021: gradual shift of emphasis with a potential of upside surprise



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TOPICS TO MONITOR IN 2021 (AND BEYOND)



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Topics to monitor in 2021

1. Pent-up demand to trigger temporary inflation pick-up in sectors which have suffered from restrictions
2. Should reaching a state of herd immunity take more time, maintaining restrictions may be necessary, with a negative impact on demand, corporate investment, employment
3. Brexit: relief about a no-tariffs/no-quotas agreement but concern about non-tariff barriers
4. Which exit strategy for ECB's PEPP and Fed's QE: monetary policy, today's relief, tomorrow's headache?
5. Speed of deploying Next Generation EU money
6. US/China: change in style does not mean the going will be easy
7. The scarring effects of the pandemic: unemployment and corporate defaults



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FORECASTS



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IMF World Economic Outlook, update January 2021

January
2021

International Monetary Fund

WORLD ECONOMIC OUTLOOK UPDATE

Policy Support and Vaccines Expected to Lift Activity

- *Although recent vaccine approvals have raised hopes of a turnaround in the pandemic later this year, renewed waves and new variants of the virus pose concerns for the outlook. Amid exceptional uncertainty, the global economy is projected to grow 5.5 percent in 2021 and 4.2 percent in 2022. The 2021 forecast is revised up 0.3 percentage point relative to the previous forecast, reflecting expectations of a vaccine-powered strengthening of activity later in the year and additional policy support in a few large economies.*



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IMF World Economic Outlook, update January 2021

Table 1. Overview of the *World Economic Outlook* Projections
(Percent change, unless noted otherwise)



	Year over Year						Q4 over Q4 2/		
	Estimate		Projections		Difference from October 2020 WEO Projections 1/		Estimate		
	2019	2020	2021	2022	2021	2022	2020	2021	2022
World Output	2.8	-3.5	5.5	4.2	0.3	0.0	-1.4	4.2	3.7
Advanced Economies	1.6	-4.9	4.3	3.1	0.4	0.2	-3.9	4.6	1.9
United States	2.2	-3.4	5.1	2.5	2.0	-0.4	-2.1	4.0	2.0
Euro Area	1.3	-7.2	4.2	3.6	-1.0	0.5	-6.8	5.8	2.0
Germany	0.6	-5.4	3.5	3.1	-0.7	0.0	-5.3	5.2	1.7
France	1.5	-9.0	5.5	4.1	-0.5	1.2	-8.2	7.4	2.0
Italy	0.3	-9.2	3.0	3.6	-2.2	1.0	-8.3	4.2	2.3
Spain	2.0	-11.1	5.9	4.7	-1.3	0.2	-9.8	7.1	2.0
Japan	0.3	-5.1	3.1	2.4	0.8	0.7	-2.3	2.7	1.6
United Kingdom	1.4	-10.0	4.5	5.0	-1.4	1.8	-8.3	6.0	1.9
Canada	1.9	-5.5	3.6	4.1	-1.6	0.7	-4.0	3.7	2.7
Other Advanced Economies 3/	1.8	-2.5	3.6	3.1	0.0	0.0	-2.2	4.5	1.9
Emerging Market and Developing Economies	3.6	-2.4	6.3	5.0	0.3	-0.1	0.9	3.7	5.4
Emerging and Developing Asia	5.4	-1.1	8.3	5.9	0.3	-0.4	3.2	3.8	6.4
China	6.0	2.3	8.1	5.6	-0.1	-0.2	6.2	4.2	6.0
India 4/	4.2	-8.0	11.5	6.8	2.7	-1.2	0.6	1.7	7.8
ASEAN-5 5/	4.9	-3.7	5.2	6.0	-1.0	0.3	-3.2	5.2	6.1



Economic Scenario

UNITED STATES

With a drop in GDP of an estimated 3.6% in 2020, the USA has experienced a record-breaking recession, albeit one that has been less severe than in most other countries. The health cost of the Covid-19 epidemic has, however, been immense, with the USA having the highest number of deaths in the world and suffering a higher mortality rate than the European Union. As we move into winter, the disease is surging again, forcing certain states, such as New York and California, to tighten social distancing measures. Although the economy had seemed able to avoid a further contraction, it could be flatlining at the start of the new year, although a gradual return to normal is then expected as vaccines become available.

CHINA

After plummeting in Q1 2020, economic activity has experienced a V-shaped rebound since Q2. The recovery has first been driven principally by industrial production and investment in infrastructure projects and the real estate sector. Then exports have strengthened, supported by the rebound in global demand. Finally, the services sector and private consumption have regained growth momentum since last summer. In the short term, fiscal policy should continue to support economic growth. Domestic credit conditions, which have been eased prudently in 2020, have started to be tightened since Q4, as the authorities aim to contain risks in the financial system.

EUROZONE

After a solid rebound in Q3 2020 (+12.6%), even exceeding expectations, Eurozone GDP should slow sharply in Q4 2020. Given the resurgence of the pandemic and the implementation of new sanitary restrictions in most of the member states, the recovery is losing momentum. The activity loss caused by the Covid-19 crisis is unlikely to be fully erased before year-end 2021. Despite the hopes raised by the vaccines, worries about the pandemic and unemployment trends in eurozone member states in the months ahead are shaking consumer confidence, which remains low. The risk of corporate defaults continues to rise as long as the pandemic is not completely under control, which is undermining private investment. Support from fiscal policy at both the national and European levels will be essential, as is maintaining an accommodating and flexible monetary policy.

FRANCE

The risks have materialized for a W-shaped growth profile. After the massive recessionary shock of H1 2020 due to the first lockdown, the economy vigorously recovered in Q3 before relapsing again in Q4 under the impact of a new lockdown designed to curb the second wave of the Covid-19 pandemic. Yet the second V is bound to be less pronounced than the first: on the downside because the second lockdown was not as restrictive nor as long, and on the upside because this time the restrictive measures will be lifted gradually and conditionally. Major fiscal resources have been deployed that effectively buffered the double shock, but still the economy has been weakened, which is straining its rebound capacity. The start-up of a massive vaccination campaign in 2021 raises hopes that we might be seeing the light at the end of the tunnel. Growth should also get a boost from the first effects of the France Relance stimulus package. French GDP is expected to catch up pre-crisis levels during 2022 and the economy to return to 100% of its normal functioning. Inflation is also expected to pick up, but will hold at extremely low levels.



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Real GDP growth (1)

New forecasts

	Annual growth (% y/y)				Quarterly growth (% q/q)							
					2020				2021			
	2019 ⁽¹⁾	2020	2021	2022	Q1 ⁽¹⁾	Q2 ⁽¹⁾	Q3 ⁽¹⁾	Q4	Q1	Q2	Q3	Q4
US	2.2	-3.6	4.2	4.1	-1.3	-9.0	7.4	0.8	0.3	1.2	1.6	1.2
Eurozone	1.3	-7.3	3.8	5.5	-3.7	-11.7	12.5	-2.6	-2.2	5.1	2.4	1.4
Germany	0.6	-5.6	2.7	5.1	-1.9	-9.8	8.5	0.0	-2.6	4.5	2.1	1.3
France	1.5	-9.0	5.5	4.7	-5.9	-13.8	18.7	-4.0	-1.2	5.2	2.0	1.0
Italy	0.3	-9.0	4.5	4.4	-5.5	-13.0	15.9	-3.0	-1.8	4.4	2.3	1.2
Spain	2.0	-11.6	5.4	5.9	-5.3	-17.9	16.4	-2.6	-1.0	5.7	2.6	1.6
China	6.1	2.3	9.5	5.3	-10.0	11.7	2.7	2.8	1.4	1.2	1.2	1.1
Japan	0.3	-5.3	1.1	3.0	-0.5	-8.3	5.3	0.8	-1.2	0.9	1.0	1.0
UK	1.5	-11.1	4.0	8.6	-2.5	-19.8	15.5	-2.1	-5.7	10.1	4.2	2.3
EM aggregate	2.5	-6.1	6.0	3.8	-0.2	-13.1	9.9	1.1	1.8	0.9	1.2	0.8
Latam	0.5	-7.2	3.5	2.7	-1.8	-13.6	9.6	1.9	0.3	0.5	0.7	0.7
CEEMEA	1.8	-3.6	3.7	3.4	0.8	-6.9	5.3	-1.2	2.2	0.7	1.4	0.4
EM Asia	4.0	-7.7	8.7	4.5	-0.3	-17.7	13.6	2.6	2.1	1.3	1.4	1.1

Sources: National sources, BNP Paribas forecasts

Previous forecasts

	Annual growth (% y/y)				Quarterly growth (% q/q)			
					2020			
	2019 ⁽¹⁾	2020	2021	2022	Q1 ⁽¹⁾	Q2 ⁽¹⁾	Q3 ⁽²⁾	Q4
Global ⁽³⁾		2.9	-4.0	5.6	4.0			
US	2.2	-3.6	3.7	3.2	-1.3	-9.0	7.4	0.8
Eurozone	1.3	-7.5	5.6	3.9	-3.7	-11.8	12.7	-3.7
Germany	0.6	-5.9	4.2	3.6	-1.9	-9.8	8.2	-1.7
France	1.5	-9.5	6.3	3.8	-5.9	-13.7	18.2	-5.0
Italy	0.3	-9.1	6.0	3.4	-5.5	-13.0	16.1	-4.0
Spain	2.0	-11.8	7.0	4.9	-5.2	-17.8	16.7	-4.3
China	6.1	2.0	8.6	5.3	-10.0	11.7	2.7	2.0
Japan	0.7	-5.4	1.5	1.8	-0.6	-8.2	5.0	0.6
UK	1.5	-11.5	6.4	6.8	-2.5	-19.8	15.5	-3.7

Source: BNP Paribas Global Markets

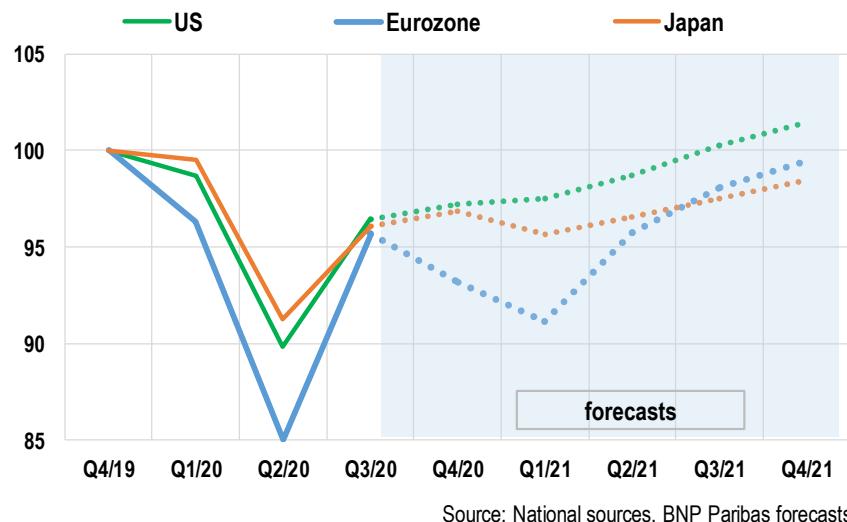


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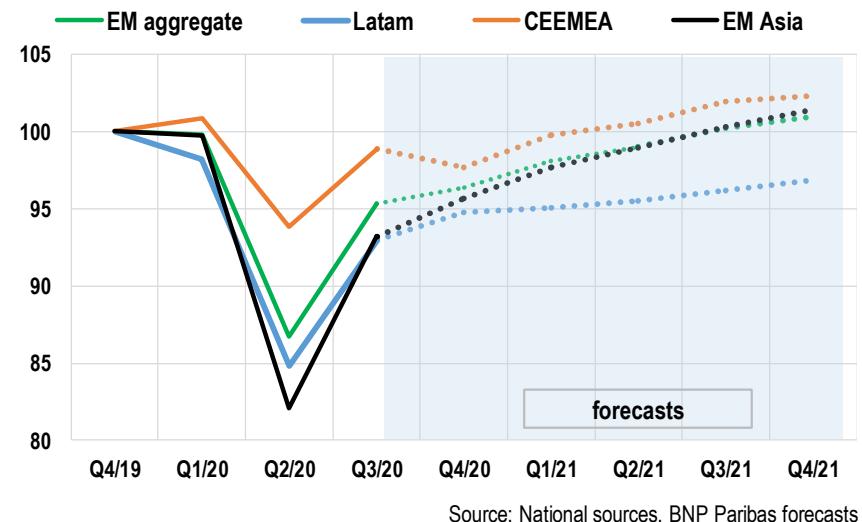
The bank for a changing world

Need to look beyond the double-dip recession in the eurozone

Real GDP, Q4 2019 = 100



Real GDP, Q4 2019 = 100



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Real GDP growth (2)

	Annual growth (% y/y)				Quarterly growth (% q/q)							
					2020				2021			
	2019 ⁽¹⁾	2020	2021	2022	Q1 ⁽¹⁾	Q2 ⁽¹⁾	Q3 ⁽²⁾	Q4	Q1	Q2	Q3	Q4
EM aggregate⁽⁴⁾	2.5	-6.1	6.0	3.8	-0.2	-13.1	9.9	1.1	1.8	0.9	1.2	0.8
Latam	0.5	-7.2	3.5	2.7	-1.8	-13.6	9.6	1.9	0.3	0.5	0.7	0.7
Argentina	-2.1	-11.0	5.0	2.0	-4.2	-16.2	10.0	5.0	0.5	0.0	0.5	0.0
Brazil	1.1	-4.5	3.0	3.0	-2.5	-9.7	8.5	2.1	-0.5	0.0	0.5	1.0
Chile	1.2	-6.0	5.0	2.5	3.0	-13.5	5.2	6.3	0.9	0.0	0.5	0.8
Colombia	3.2	-7.5	5.0	3.0	-1.4	-16.1	8.7	4.0	0.8	0.5	1.5	1.0
Mexico	-0.3	-9.5	3.0	2.3	-1.2	-17.3	12.0	-1.0	1.0	1.4	0.7	0.5
CEEMEA	1.8	-3.5	3.7	3.4	0.8	-6.9	5.3	-1.2	2.2	0.7	1.4	0.4
Czech Rep.	2.4	-7.0	4.5	4.4	-3.4	-8.7	6.2	-3.1	3.1	2.2	1.8	1.0
Egypt	5.6	3.6	3.7	4.7	2.3	0.8	-2.8	3.0	2.6	1.0	-3.0	3.1
Hungary	4.9	-6.0	5.2	4.4	-0.4	-14.5	11.3	-2.8	3.3	2.2	1.0	0.9
Poland	4.1	-3.3	4.9	4.3	-0.4	-9.0	7.7	-2.6	2.8	2.0	1.6	0.9
Romania	4.2	-5.7	4.6	4.9	0.3	-11.9	5.6	-2.2	3.5	2.5	1.5	1.4
Russia	1.3	-4.5	3.8	3.0	-0.9	-3.2	1.9	-0.3	0.7	0.4	1.4	0.2
Saudi Arabia	0.3	-4.3	2.9	3.7	9.4	-8.6	2.1	-4.7	4.2	3.7	1.0	0.4
South Africa	0.2	-8.0	2.5	1.3	-0.5	-17.0	13.0	0.3	0.5	0.2	0.2	0.2
Turkey	0.9	-1.0	4.5	3.5	-0.1	-11.0	15.7	-1.1	0.2	-0.5	3.4	0.3
EM Asia⁽⁵⁾	4.0	-7.7	8.7	4.5	-0.3	-17.7	13.6	2.6	2.1	1.3	1.4	1.1
India	4.2	-11.4	11.6	5.0	0.6	-25.6	20.0	3.0	3.0	1.3	1.5	1.0
Indonesia	5.0	-2.0	5.8	4.5	-0.8	-6.8	3.2	2.8	1.5	1.8	1.4	1.2
Malaysia	4.3	-5.0	7.5	3.9	-2.0	-16.5	18.2	2.5	0.5	0.8	0.9	1.0
South Korea	2.0	-1.0	3.1	2.9	-1.3	-3.2	1.9	1.5	0.5	0.7	1.0	1.0
Thailand	2.4	-6.6	4.2	3.7	-2.5	-9.7	6.5	0.5	1.0	1.3	1.5	2.0

(1) 2019 and Q1 and Q2 2020 data are actual. (2) Q3 data are a combination of preliminary and final reported data. (3) Global growth forecasts are based on BNP Paribas country estimates (as shown in the table), which account for about 82% of world GDP, and IMF forecasts for the remaining 18% of the world. The countries are GDP-weighted using IMF GDP PPP data. (4) The EM aggregate is GDP-weighted using IMF 2019 GDP PPP data and includes the EM economies shown plus Bahrain, Kuwait, Oman, Qatar and UAE, and excludes China. (5) The EM Asia aggregate excludes China. Sources: National statistical agencies, Macrobond, BNP Paribas forecasts

Source: BNP Paribas Global Markets



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The bank for a changing world

Inflation

	Annual rate (% y/y)				Quarterly rate (% y/y)							
					2020				2021			
	2019 ⁽¹⁾	2020	2021	2022	Q1 ⁽¹⁾	Q2 ⁽¹⁾	Q3 ⁽¹⁾	Q4	Q1	Q2	Q3	Q4
US	1.8	1.3	1.9	1.9	2.1	0.4	1.3	1.4	1.5	2.7	1.9	1.7
Eurozone	1.2	0.2	0.8	1.3	1.1	0.2	0	-0.4	0	0.7	1.2	1.5
China	2.9	2.6	2.3	2.8	4.9	2.7	2.3	0.5	0.7	2.6	2.8	3.3
Japan	0.5	0	-0.4	-0.3	0.5	0.1	0.2	-0.7	-0.7	-0.3	-0.2	-0.3
UK	1.8	0.9	1.5	2.1	1.7	0.6	0.6	0.7	0.8	1.6	1.5	1.8

	Annual rate (% y/y)				Quarterly rate (% y/y)							
					2020				2021			
	2019 ⁽¹⁾	2020	2021	2022	Q1 ⁽¹⁾	Q2 ⁽¹⁾	Q3 ⁽¹⁾	Q4	Q1	Q2	Q3	Q4
EM aggregate ⁽²⁾	4	3.7	3.6	3.5	4	3.5	3.8	3.6	3.8	4	3.3	3.3
Latam ⁽³⁾	3.6	3.2	3.7	3.6	3.7	2.4	3	3.5	3.3	4.1	3.9	3.3
Argentina	53.5	42.6	56.3	41.8	50.4	43.9	39.8	36.3	43.9	54	62.1	65.3
Brazil	3.7	3.1	4	4	3.8	2.1	2.6	3.7	3.5	4.7	4.5	3.3
Chile	2.3	3.1	3.5	3.1	3.7	2.9	2.7	3	2.9	3.5	3.9	3.5
Colombia	3.5	2.5	2.5	3.1	3.7	2.3	1.9	1.9	1.9	2.3	2.8	2.9
Mexico	3.7	3.5	3.6	3.6	3.4	2.8	3.9	3.8	3.6	4	3.4	3.4
CEEMEA	4.9	4.3	4.6	4.5	4.4	3.9	4.4	4.5	4.4	4.9	4.5	4.7
Czech Rep.	2.8	3.3	2.3	2.5	3.6	3.1	3.4	3.1	2.1	2.3	2.3	2.5
Egypt	9.2	4.5	5.2	5.3	5.4	5.4	3.3	4.1	4.9	4.5	6.1	5.5
Hungary	3	3.3	3.5	3.3	4.3	2.5	3.7	2.9	3	3.7	3.4	3.8
Poland	2.4	3.3	2.4	2.7	4.5	3.2	3	2.5	1.6	2.4	2.6	2.9
Romania	3.9	2.8	3	3.2	3.2	2.5	2.6	2.7	2.6	2.9	3.2	3.3
Russia	4.3	3.4	3.5	3.5	2.6	3.2	3.7	4	3.8	3.7	3.5	3.2
Saudi Arabia	-1.2	3.3	2.5	2.7	1.1	1	6	5.1	3.7	4.6	-0.2	1.8
South Africa	4.1	3.2	3.5	4	4.4	2.4	3.1	2.8	2.5	3.4	3.8	4
Turkey	15.2	12.2	12.6	10.5	13.3	11.9	11.5	11.9	12.2	12.6	12.8	12.8
EM Asia ⁽⁴⁾	3.4	3.6	2.8	2.8	3.9	3.7	3.7	2.9	3.6	3.3	2.1	2.3
India	4.8	5.8	4.3	3.8	5.8	6.2	6.3	5	6	5	3	3.2
Indonesia	2.7	1.9	1.7	2	2.9	2	1.3	1.5	1.3	1.7	1.9	2
Malaysia	0.7	-1.2	-0.3	1	-0.1	-1.9	-1.4	-1.5	-0.7	-0.5	-0.1	0
South Korea	0.4	0.6	1.1	1.2	1.2	-0.1	0.6	0.5	0.7	1.6	1	1.1
Thailand	0.7	-1.3	-0.7	0.5	-0.5	-1.6	-1.1	-2.0	-1.5	-0.5	-0.6	0

Source: BNP Paribas Global Markets



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Interest rates

	Spot ⁽¹⁾	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q4 2022
US						
IOER	0.10	0.10	0.10	0.10	0.10	0.10
2-year	0.17	0.20	0.20	0.25	0.30	0.50
10-year	0.85	1.10	1.20	1.30	1.40	1.50
Eurozone						
Deposit	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
2-year ⁽²⁾	-0.73	-0.60	-0.65	-0.65	-0.60	-0.40
10-year ⁽²⁾	-0.55	-0.35	-0.50	-0.40	-0.20	0.10
10y spreads to Germany (bp)						
France	23	25	25	25	30	40
Italy	121	110	110	120	140	160
Spain	64	70	70	80	80	90
UK						
Bank Rate	0.10	0.10	0.10	0.10	0.10	0.10
2-year	-0.02	-0.05	-0.05	0.00	0.05	0.20
10-year	0.33	0.40	0.40	0.50	0.60	0.75
Japan						
IOER	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
2-year	-0.14	-0.15	-0.1	-0.1	-0.1	-0.1
10-year	0.02	0.05	0.05	0.1	0.1	0.15

(1) Spot rates as at 18 November. (2) German benchmark

Sources: Bloomberg, BNP Paribas forecasts (Market Economics, Interest Rate Strategy)

- In the US, policy should remain on hold for quite some time, considering that the FOMC wants inflation to move beyond 2% to make up for past below target inflation. To this end, it has decided at its December meeting that the current pace of asset purchases will be maintained 'until substantial further progress has been made' toward reaching its goals in terms of maximum employment and inflation. Should the economic situation worsen, more measures are to be expected.
- Treasury yields should move higher on the back of fiscal stimulus and the economic recovery and because the Fed will accept and actually wants inflation to rise beyond 2%.
- In the eurozone, at its December meeting, the ECB has eased policy further. In particular, it has decided to increase the envelope of the pandemic emergency purchase programme (PEPP) and to extend its horizon for net purchases to at least the end of March 2022. These measures aim to support the economy so as to create a pick-up in inflation, which has dropped to a very low level.
- This very accommodative stance –which will be maintained for a long time- should keep a lid on sovereign bond spreads, although at some point, speculation that the PEPP's end date might not be prolonged any further should cause some spread widening.
- As usual, eurozone bond yields will be very much influenced by what happens to US yields. The prospect of a more lasting recovery as a vaccine will be deployed, should contribute to somewhat higher bond yields.
- The Bank of Japan is expected to maintain its current policy stance including its yield curve control strategy.

Source: BNP Paribas Global Markets



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Exchange rates, oil

- We expect the dollar to weaken further versus the euro.
- Due to the limited short-term interest rate differential, international investors incur low costs when they want to hedge their dollar exposure
- The euro is still undervalued versus the dollar
- The Fed's new strategy of targeting average inflation implies a more dovish stance compared to the ECB.
- The 'risk-on' environment is also supportive for the euro.
- Similar arguments apply for the dollar versus the yen.

	Spot ⁽¹⁾	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q4 2022
EURUSD	1.19	1.22	1.24	1.25	1.25	1.30
EURJPY	123	1.23	124	123	123	124
GBPUSD	1.33	1.39	1.41	1.44	1.44	1.49
USDJPY	104	101	100	98	98	95
USDCNY	6.55	6.45	6.40	6.35	6.30	6.50

(1) Spot rates as at 18 November

Sources: Macrobond, BNP Paribas forecasts (FX Strategy)

	Q1 2021	Q2 2021	Q3 2021	Q4 2021	2020	2021
ICE Brent	56	54	55	59	43	56

Sources: Bloomberg, BNP Paribas. Period-average forecasts



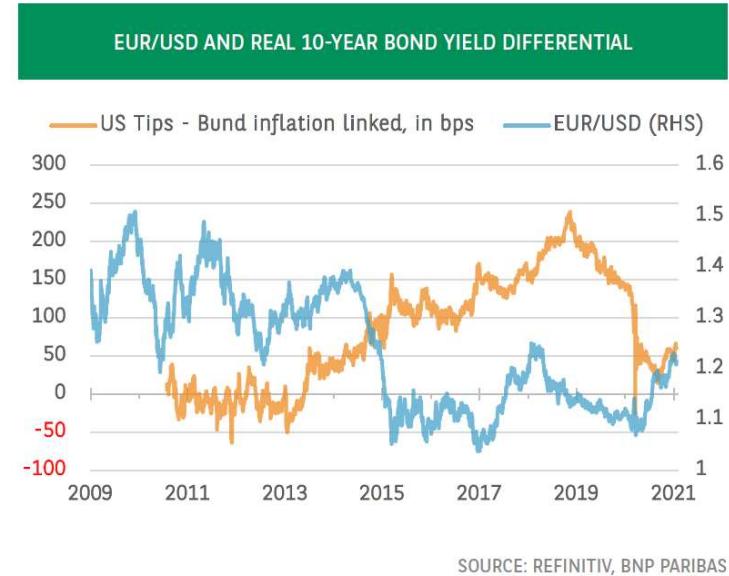
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Source: BNP Paribas Global Markets

The (un)surprising weakening of the dollar

- the real bond yield differential has increased as of late, but this has not stopped the dollar from weakening. Moreover, it appears that since 2011, the correlation between the real yield difference and the EUR/USD exchange rate has been positive, rather than negative, as the capital flow model of exchange rates would imply.
- Several factors have played a role in the depreciation of the dollar in the past several months.
 - the new strategy of the Federal Reserve of targeting average inflation
 - the rising real yield differential could be associated with the huge US fiscal stimulus and the ensuing rising borrowing requirements
 - historically, the combination of a very accommodative US monetary policy and improving prospects for the global economy typically have caused capital flows from the US to the rest of the world.
 - the short-term interest rate differential between the US and the eurozone has narrowed significantly in 2020. For European investors with big historical holdings of US assets, hedging this currency exposure has become very cheap. The increased hedging of existing exposures is likely to weigh has weighed on the dollar
 - the fair value of the dollar versus the euro –based on the long-term relationship between the exchange rate and economic variables- is around 1.34, so this level can act as a magnet when other factors are ‘pushing’ the currency in this direction.



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The (un)surprising weakening of the dollar: what could change it

- In theory, a sudden change in guidance from the central banks could play a role. However, this is very unlikely.
 - The Federal Reserve will not be in a hurry to adopt a more hawkish tone whereas the ECB's policy is already very accommodative. This sets the bar very high for more accommodation.
- Another factor could be a sudden drop in risk appetite of international investors.
 - A move into a 'risk-off' environment is typically associated with a strengthening of the dollar on the back of US investors reducing overseas exposure.
 - However, unless there would be an abrupt, considerable deterioration of the economic outlook, such a risk-off phase should be short-lived.
- A more intriguing question is whether a further widening of the yield differential and a weakening of the dollar could end up becoming self-correcting.
 - For investors who intend to hold on to their bonds until maturity and are not subject to mark-to-market accounting, at some point the yield gap will become compelling and offer enough protection against a potential further depreciation of the dollar. A 200bp yield gap versus Bunds for a 10-year maturity offers a lot of downside protection for the currency.
 - For marked-to-market investors, this argument does not apply. Moreover, they may consider US treasuries as being riskier than Eurozone bonds based on the outlook for GDP growth and inflation.
- The biggest risk for a change in direction would be a repetition of the 'taper tantrum' of 2013 with the Federal Reserve starting to point towards a possible beginning of the normalisation of its policy. However, such a change in guidance is not to be expected anytime soon: the Fed wants to overshoot its inflation target first.



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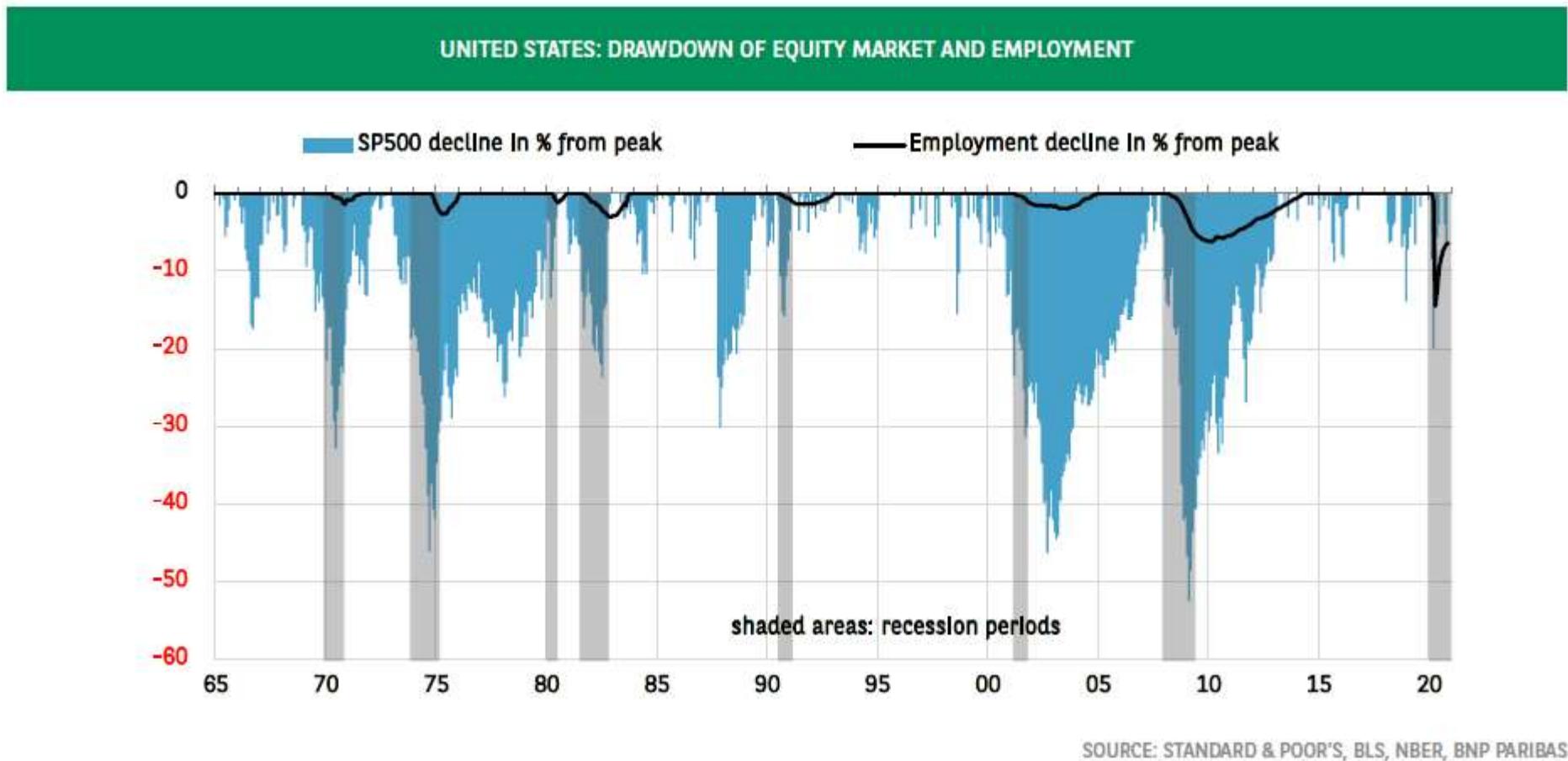
FINANCIAL MARKETS IN 2021: AN ECONOMIST'S PERSPECTIVE



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US equities and the economy: worlds apart? (1)



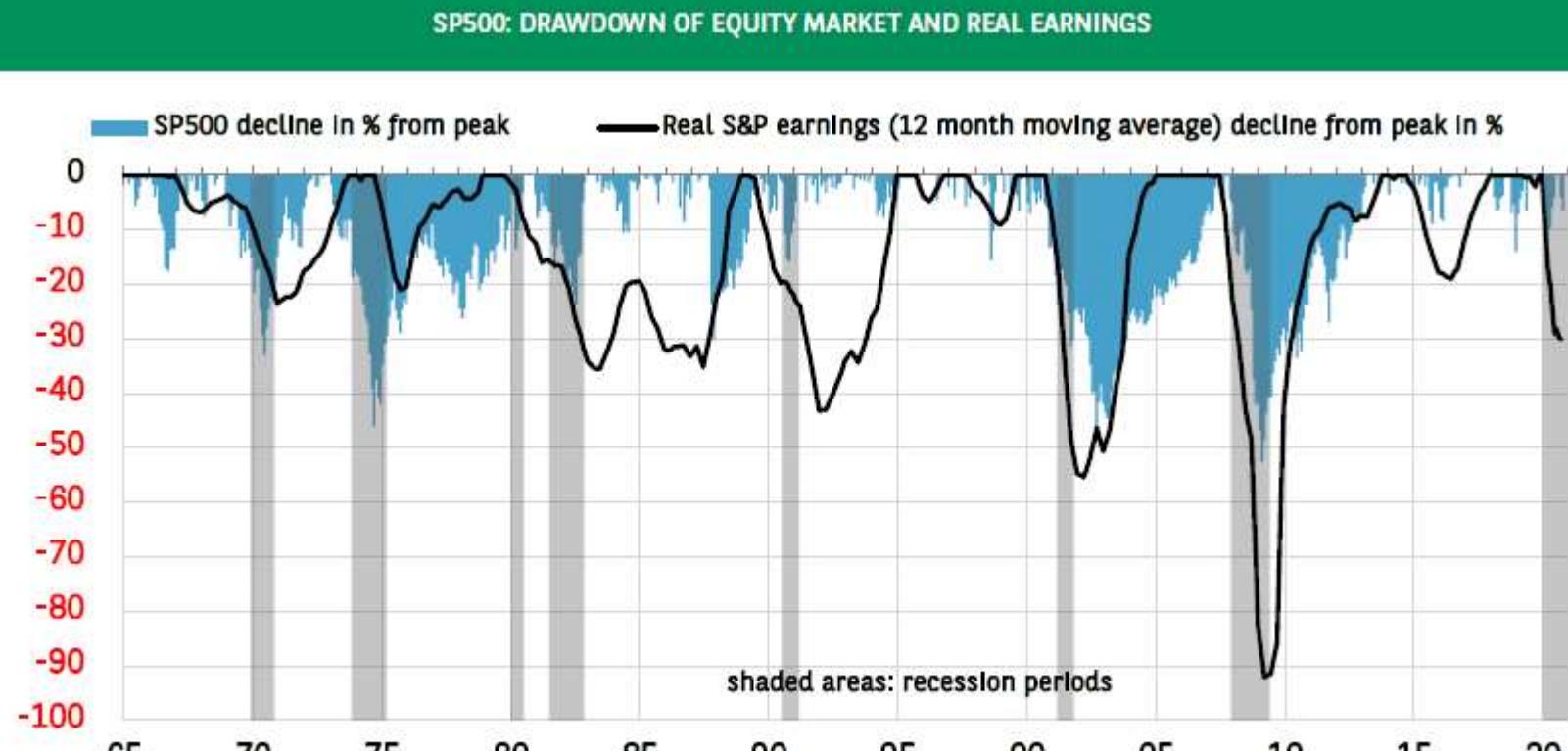
Drawdown = distance in % from the latest historical peak



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US equities and the economy: worlds apart? (2)



SOURCE: STANDARD & POOR'S, ROBERT SHILLER WEBSITE, NBER, BNP PARIBAS

Drawdown = distance in % from the latest historical peak



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What might explain the (apparent) anomaly between the US equity market and the economy?*

1. Massive easing of monetary policy
2. Decline of treasury yields
3. The credible promise to do more if necessary (the 'Powell put')
4. Specific decision by the Fed to buy corporate paper
 - Reduces default risk, which in turn is beneficial for equity market sentiment
5. Fiscal policy reaction
 - *"While the coronavirus economic shock appears to be the largest on record, the fiscal response has also been the fastest and largest response for any postwar downturn."* (J. Powell)
 - This should influence growth expectations, at a minimum by reducing the risk of extremely negative outcomes.
6. The distribution of risks has evolved.
 - In the course of 2019 and at the start of this year, surveys showed that US CFOs considered there was a high risk of a recession in the foreseeable future.
 - Considering the equity market declines during recessions, one can argue that risk was very much tilted to the downside: the likelihood of a big drawdown was higher than the possibility of an equivalent increase in share prices.
 - Following the market decline due to the pandemic and given the reaction of monetary and fiscal policy, it can be argued that risk quickly became less asymmetric than at the start of the year.
7. Recession-related uncertainty
 - This concerns the depth and length of the recession as well as the pace of recovery thereafter.
 - Recessions tend to differ quite a bit in terms of length and depth so anticipating the trough of the cycle is tricky.
 - If we consider that the lower cyclical turning point has been reached when activity indicators start to pick up again, this would imply that the current recession should be a very short one: the contraction was triggered by the lockdown and the recovery should be initiated by the gradual easing of the lockdown.
 - This last point implies that the usual uncertainty about the duration of a recession should be very limited, which, in addition, allows investors to look more confidently to the 'other side of the valley' and pay less attention to the depth of the recession.
8. Investors adopt a short investment horizon
9. Investors consider it is premature to speculate on second wave risk
10. Equity rally has a rather narrow base (type of stocks doing well)



Impact on growth: announcement of vaccine cuts tail risk...

- The announcement that a Covid-19 vaccine that is under development is highly effective caused major reactions in financial markets, reflecting a feeling that the growth outlook has changed.
- The prospect of a vaccine offers hope that in the medium run activity will normalise, but the **positive impact on growth will take time to materialise**.
- Clearly, the view that better times are ahead of us very much depends on the horizon one takes: many countries are still in lockdown, which weighs on the short-term growth outlook.
- However, decisions of households and businesses not only depend on **expected growth** of income and profits but also on the **distribution** around the growth forecast.
- The **prospect of a vaccine reduces the probability of very negative outcomes and this reduction in uncertainty should eventually contribute to a pick-up in growth**.
- Corporate investments (which are irreversible long-horizon decisions) should eventually be a key beneficiary of a reduction in uncertainty

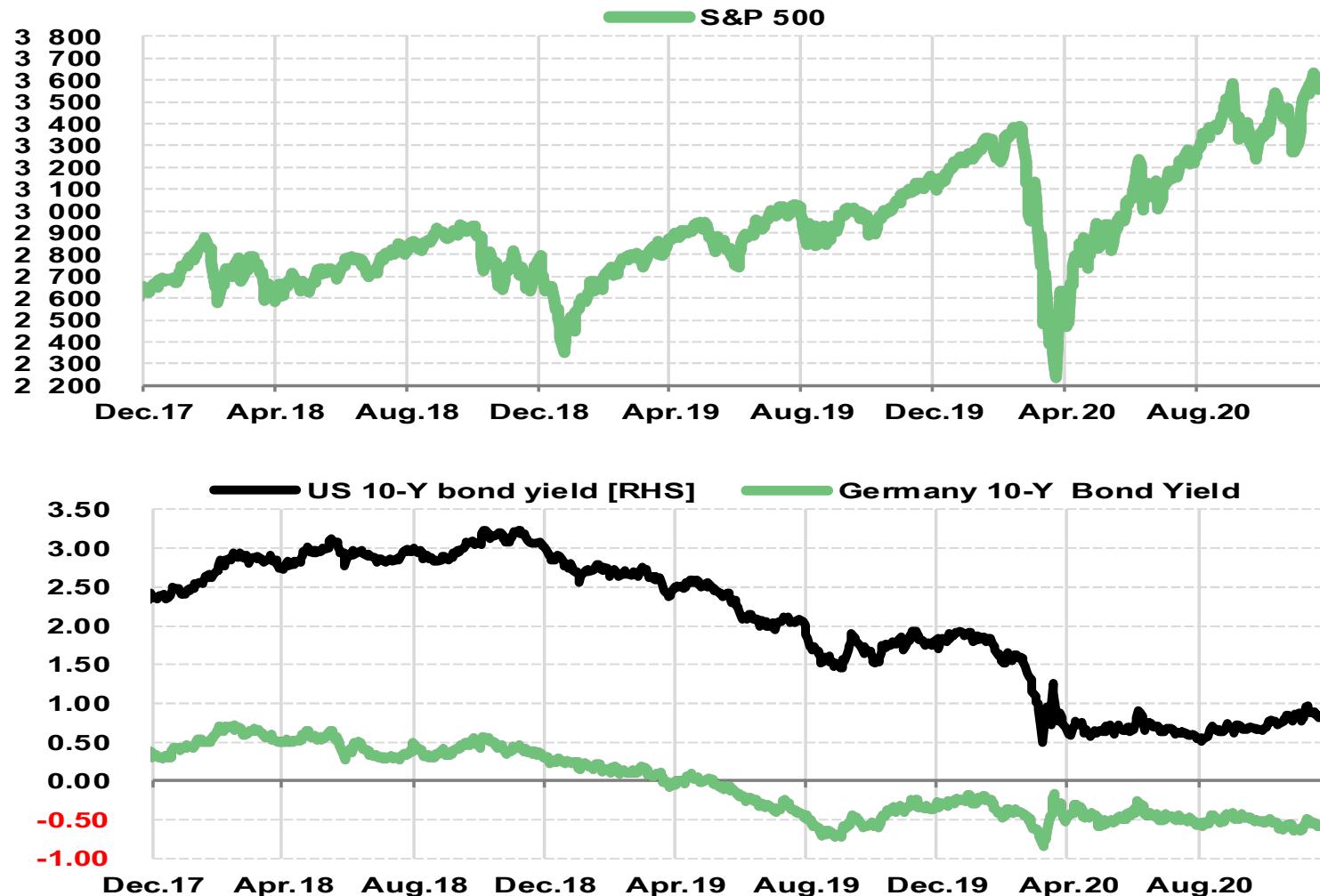


... and hence required risk premium

1. Compensation for extreme negative events (tail risk) is a key driver of the required risk premium
2. Announcement of a vaccine reduces uncertainty and tail risk
3. This reduces the required risk premium
4. As a consequence, there is an instantaneous price increase of risky assets
5. Sovereign bonds see a drop in price because the demand for hedges against tail risk drops



Why has the correlation structure between equities and bonds changed in 2020?



Source : Refinitiv, BNP Paribas



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The effective lower bound of policy rates, QE and the willingness to take risk

1. Portfolio rebalancing: “climbing the risk ladder”
2. Belief in put option offered by central bank => less tail risk than before
3. Zero interest rates and the rationale for doing market timing:
 1. It can be demonstrated that the break-even skill level –which is required to be able to add value by doing market timing- rises when the interest rate declines.
 2. This implies that investors might prefer to refrain from market timing and remain invested in equities, unless the near-term outlook fundamentally changes.
 3. This creates an attitude of “keeping the foot on the throttle” unless central banks would tighten aggressively (very unlikely for years to come) or recession risk would rise significantly (very unlikely at the current juncture)
4. **However, this pushes up equity valuations, so meeting earnings expectations becomes even more important**



Monetary policy: today's relief, tomorrow's headache?

- The Federal Reserve and the ECB have been highly successful in influencing asset prices as part of their effort to cushion the shock to the economy from the Covid-19 pandemic.
- However, one might wonder whether today's relief could cause an investor's headache tomorrow.
- The difficulty of an exit strategy does not imply that certain monetary tools should not be used in the first place. After all, they do have positive effects.
- However, the likelihood of a bumpy normalisation process of monetary policy calls for careful preparation by central banks as well as investors.
- **These considerations could become particularly relevant should the recovery in 2021 end up surprising to the upside.**
- **The end of net purchases in the context of the ECB's PEPP should push up bond yields and cause some widening of sovereign spreads**

Recent financial history reminds us that this is a genuine risk. In 2013, Fed Chair Ben Bernanke triggered the 'taper tantrum' by suggesting that the Federal Reserve might reduce the pace of its asset purchases. It remains to be seen how markets will react when the ECB will announce, one day, that it is contemplating to scale back or even stop its net purchases under the Pandemic Emergency Purchase Programme.

Another question concerns the new inflation targeting strategy of the Federal Reserve, introduced at the end of the summer. Committing to accept a moderate overshooting of the inflation target during a certain time represents an invitation for investors to take more risk. This begs the question how these investors will react when inflation has reached 2%. Their reaction will not only be strongly influenced by the perceived reaction function of the Federal Reserve but also by the vagueness of the latter's new strategy.



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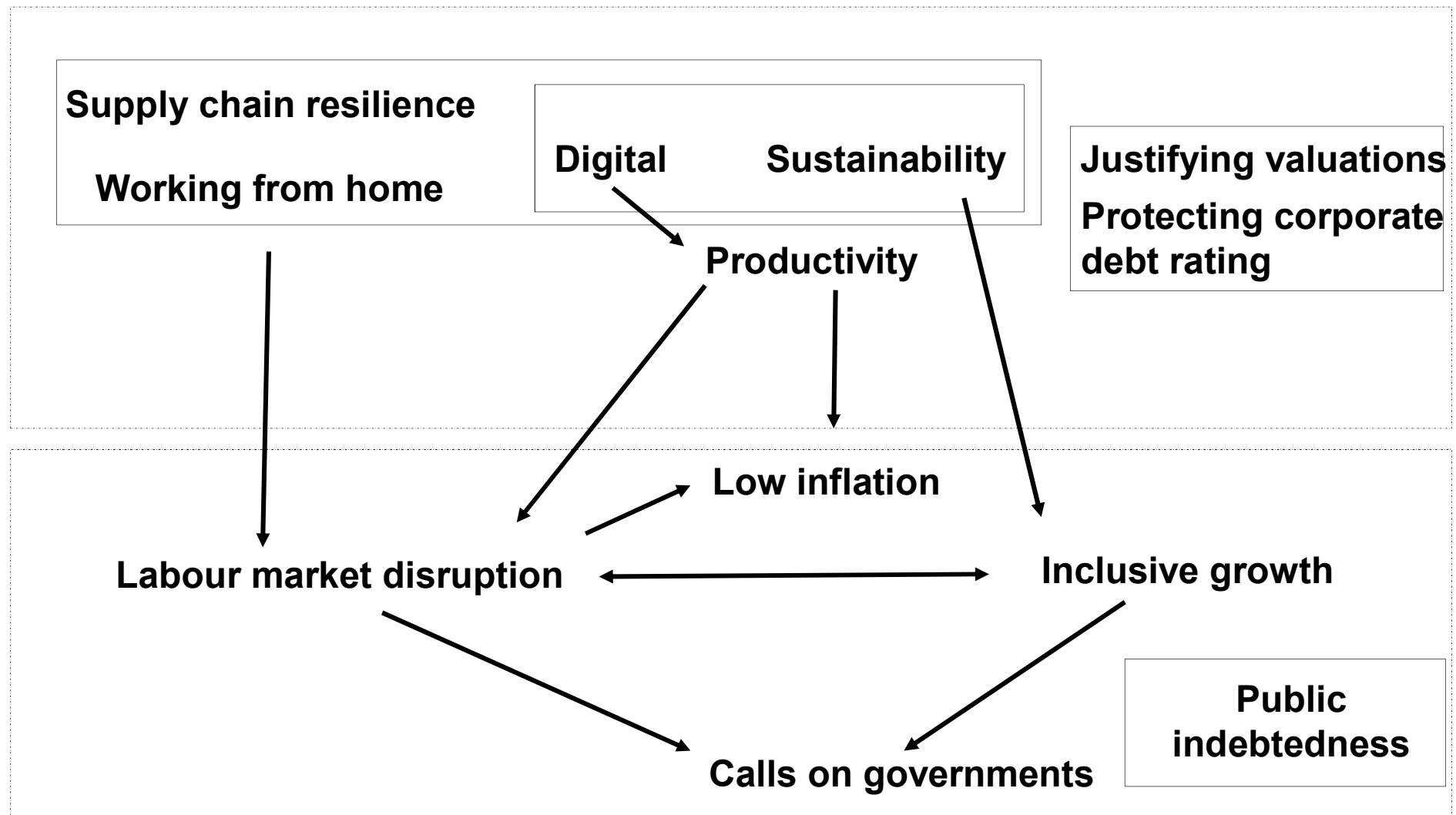
LONGER-TERM CONSEQUENCES OF THE PANDEMIC



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Longer term consequences of the pandemic



Just published

ECO PERSPECTIVES

1st quarter 2021



EDITORIAL

2

After a most difficult year, cautiously hopeful for 2021

Until the very end, 2020 has been a difficult year, to say the least. However, there are reasons to be cautiously hopeful about the economy in 2021...

UNITED STATES	CHINA	JAPAN	EUROZONE
4 Change of scenery	6 The tightening in credit conditions is a delicate exercise	8 A very gradual normalisation process	9 Cautious but hopeful
GERMANY	FRANCE	ITALY	SPAIN
11 Income uncertainty boosts precautionary savings	13 Light at the end of the tunnel	15 Coping with the second wave	17 A fiscal stimulus monitored closely by Brussels
BELGIUM	AUSTRIA	FINLAND	GREECE
19 Structural impact limited so far, but eventually bill comes due	21 Corporate sector severely weakened by Covid-19 crisis	22 A resilient, but not very dynamic, economy	23 A slower recovery than other countries in 2021?
UNITED KINGDOM	SWEDEN	NORWAY	DENMARK
24 Another contraction in Q4, before the definitive recovery?	26 A hard-hit economy	27 One of the least affected developed economies	28 Uncertainty remains

FORECASTS

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ECONOMIC RESEARCH



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ECO EMERGING

1st quarter 2021



EDITORIAL

2

As the new year gets underway, emerging countries are benefiting from a combination of favourable factors for a recovery (catching-up movements in foreign trade, a weak dollar, rising commodity prices, and domestic financing costs that are lower than pre-crisis levels). Yet lots of uncertainty and threats remain...

CHINA	INDIA	MALAYSIA
3 First signs of credit policy tightening	5 Structural reforms instead of fiscal support	7 Priority on fiscal support
VIETNAM	BRAZIL	PERU
9 Strong performances	11 A fragile outlook dominated by concerns over the epidemic and fiscal woes	13 No exception
ISRAEL	RUSSIA	POLAND
15 Favourable prospects despite fiscal uncertainty	17 A fragile recovery but resilient fundamentals	19 A resilient economy
CZECH REPUBLIC	ETHIOPIA	TUNISIA
21 An accumulation of shocks has hit growth	23 Disrupted momentum	25 Another high-risk year

ECONOMIC RESEARCH



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