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GLOBAL
ECONOMIC
RESEARCH

Global Macro Outlook

AUGUST 2020

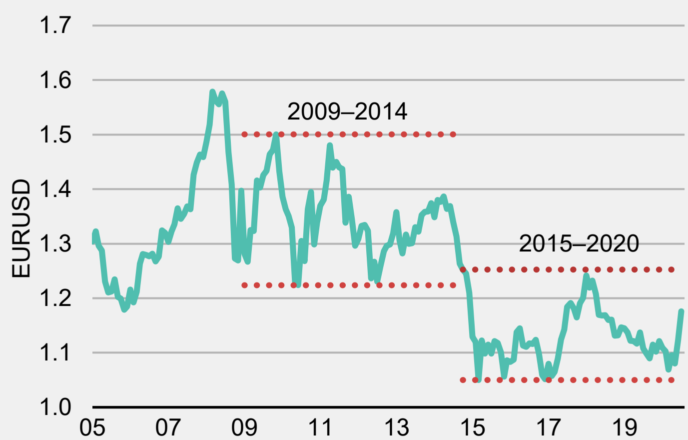
KEY FORECAST TRENDS

- The global economy received an unprecedented hit in the second quarter, with the US contracting by 9.5% and the Euro area by 12.1%.
- The only major economy to advance was China's, COVID-19's "first in, first out." Output there jumped 11.5% after a 10.0% drop in the first quarter.
- Similar rebounds are likely in other countries during the third quarter. But we caution against assuming this is a traditional "V-shaped" recovery.
- That's because a key component of any recovery is the level of activity. And even with a strong rebound in the third quarter, output in many economies is unlikely to return to pre-crisis levels until well into 2022.
- This shouldn't be a surprise. Measures to contain COVID-19 have created enormous dislocations, further virus outbreaks look inevitable and other threats loom—such as the deteriorating relationship between China and the West.
- The need for sustained fiscal stimulus remains compelling. The task for monetary policy is unchanged: keep bond yields and government funding costs low.
- The euro has risen in recent weeks and we expect this trend to continue. Our target range is 1.25–1.35 vs. the US dollar. This is not so much a weaker US dollar story, but recognition of the euro area's much-improved governance framework.

CONTENTS

Regime Shift

Euro Exchange Rate & Recent Trading Regimes

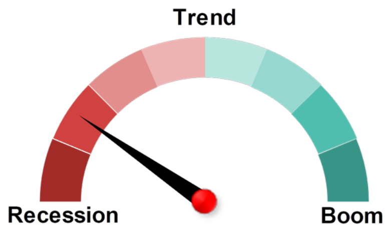


As of July 31, 2020
Source: Bloomberg

- The euro has traded in a weak range against the US dollar over the past five years. We think its recent rise is the beginning of a shift to a stronger regime.
- Part of this reflects Europe's superior handling of the COVID-19 crisis, while some is due to monetary-policy convergence.
- But the driving force is the recent improvement in euro-area governance, which has reduced the near-term tail risks of holding euros at a time when the outlook for US governance is uncertain.

GLOBAL FORECASTS

Economic Growth

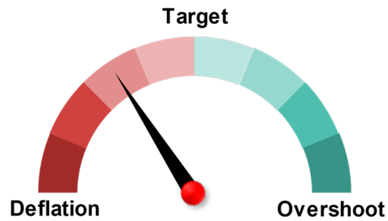


+ Output is rebounding as restrictions on economic and social activity are lifted.
+ While growth rates look strong, it will be some time before levels return to “normal.”

Key Risks

+ Downside: second lockdown
  Upside: early vaccine
+ Rising geopolitical tensions between China and the West

Inflation

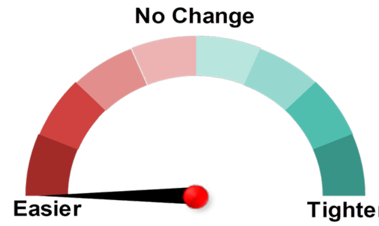


+ Near term, headline inflation is likely to be heavily influenced by volatile oil prices.
+ The immediate impact on core inflation is likely to be down, but longer-term pressure for higher inflation may be rising.

Key Risks

+ Oil prices
+ Will the coronavirus policy response reinforce secular forces for higher inflation?

Monetary Policy



+ The role of central banks in the current environment is to support fiscal policy by keeping bond yields low.
+ We therefore expect yields to remain close to, or below, zero for the foreseeable future.

Key Risks

+ Fiscal dominance/monetization
+ Are we sowing the seeds of an even bigger future debt crisis?

OUTLOOK

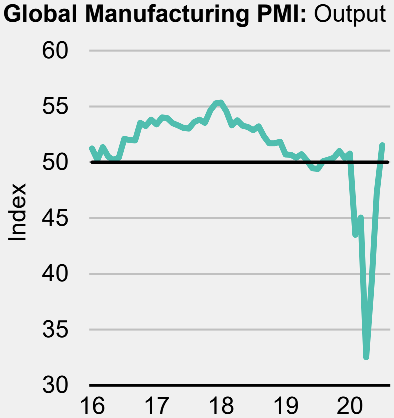
+ Our latest forecast for 2020 global economic growth is little changed at –4.5%. This masks an upward revision to euro-area growth (–7.5% from –10.0%), where second-quarter GDP was better than expected, and a downward revision to the US (–5.4% from –4.3%), where second-quarter GDP was slightly disappointing. Elsewhere, our forecasts are little changed, with China (1.1%) the only major economy likely to register positive growth this year.

+ We expect the global economy to expand by nearly 5% next year. While this looks like a “V-shaped” recovery, the level of output is likely to remain depressed. At the end of 2021, we expect output levels for the advanced economies to still be 2% below those at year-end 2019 and roughly 6% below an extrapolation of the pre-crisis trend.

+ The global economy’s growth prospects will depend critically on the virus’s future path, but ongoing policy support is also essential. There is little that monetary policy can do to directly influence the future path of output. But it can play an important supporting role by suppressing bond yields, keeping debt-servicing costs low and providing fiscal space for governments to support their economies. Interest rates are unlikely to rise much—if at all—in coming quarters.

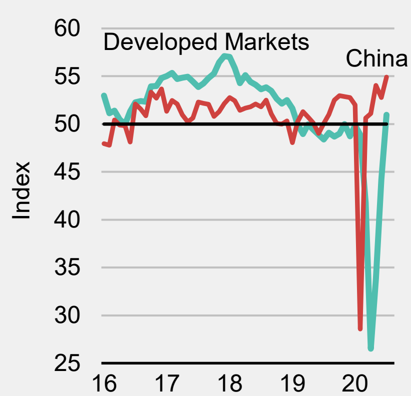
Global Cyclical Outlook: Recovering from a Deep Downturn

Global Manufacturing PMI: Output



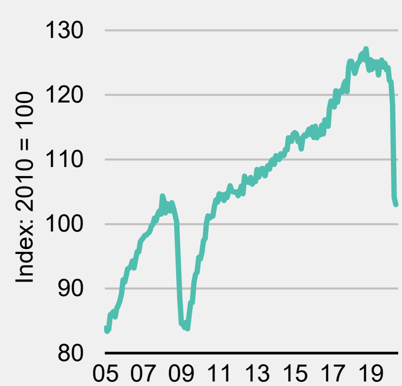
Through July 31, 2020
Source: Haver Analytics and IHS Markit

Manufacturing PMIs: Output



Through July 31, 2020
Source: Haver Analytics and IHS Markit

World Trade Volumes



Through May 31, 2020
Source: Haver Analytics

GLOBAL MARKET OUTLOOK: YIELD CURVES

GLOBAL YIELDS

Global—A key legacy of COVID-19 will be a huge increase in government debt, particularly in developed economies. This might normally be expected to put upward pressure on bond yields, but massive central bank bond purchases have helped prevent this. Implicit or explicit yield-curve control is likely to be a permanent feature.

US—Despite the Treasury's announcement of massive new supply to fund ongoing stimulus efforts, Federal Reserve purchases have helped to keep yields low. We expect this balance to persist—government spending will require more debt issuance and Fed purchases will keep that issuance affordable.

Euro Area—The European Central Bank (ECB) has extended and expanded its asset purchase program and is likely to place an effective cap on core and peripheral bond yields for some time.

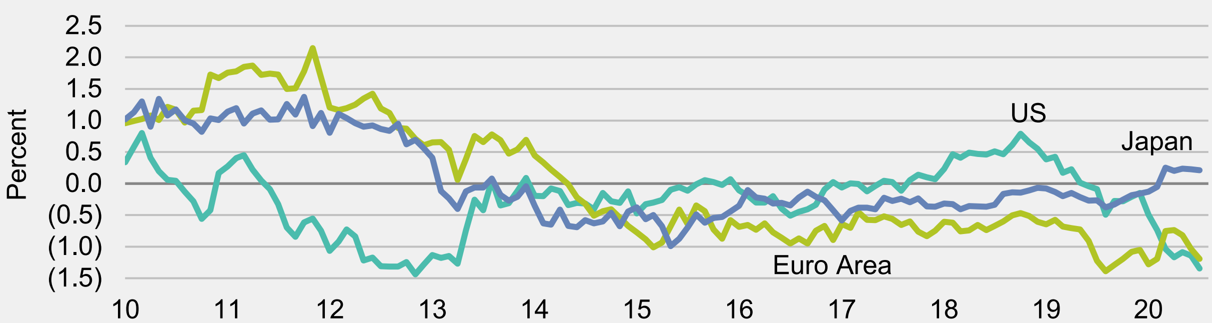
Japan—Tweaks from the Bank of Japan (BOJ)—dropping the Y80 trillion per annum purchase target—largely validate the status quo. Yield-curve control (YCC) should anchor 10-year yields close to zero for the foreseeable future.

10-Year Yields: AB vs. Consensus Year-End Forecasts (%)

	AB		Consensus	
	2020	2021	2020	2021
US	0.50	1.00	0.87	1.23
Euro Area	(0.50)	(0.35)	(0.37)	(0.14)
Japan	0.00	0.00	(0.01)	0.02
China	2.30	2.50	2.73	2.93

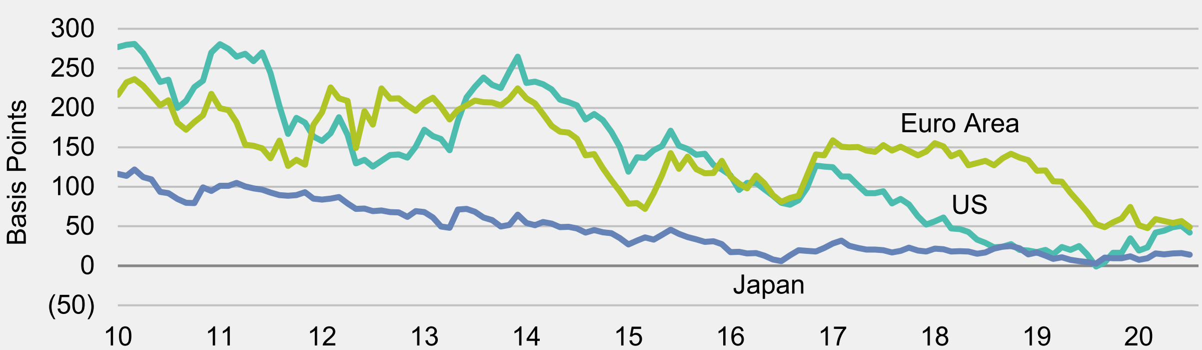
As of July 31, 2020
Source: Bloomberg and AB

Real 10-Year Bond Yields*



*Current 10-year bond yield less five-year/five-year-forward inflation swap
Through July 31, 2020
Source: Bloomberg and AB

Yield Curves: 10-Year Bond Yield Minus Two-Year Bond Yield



Through July 31, 2020
Source: Bloomberg and AB

GLOBAL MARKET OUTLOOK: CURRENCIES

FX FORECASTS

USD—The dollar remains the currency of choice for reserve managers, but some reallocation into euros appears likely as an improved governance environment in Europe reduces structural concern about the long-term future of the single currency.

EUR—Europe has handled the COVID-19 crisis well and activity is gaining pace across the region. The policy outlook has also brightened, with ECB bond purchases and the European Union's new recovery fund ensuring that all countries can use fiscal policy to support their economies as they begin to recover. We expect this improvement in governance to lead to a further appreciation of the euro and now target a range of 1.25 to 1.35 against the USD.

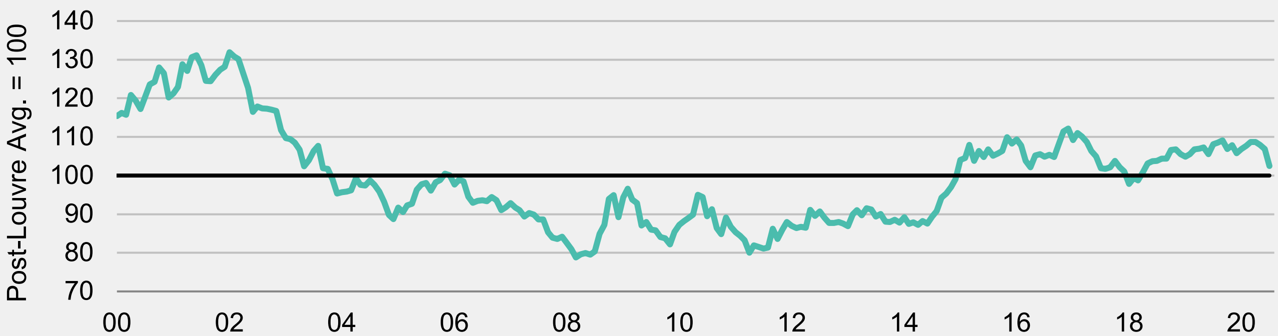
JPY—We see few Japan-specific reasons for a big shift in the yen. Policies in developed economies have converged with those in Japan. That said, we still think the yen retains its risk-off characteristics.

Global FX: AB vs. Consensus Year-End Forecasts (%)

	AB		Consensus	
	2020	2021	2020	2021
EUR/USD	1.30	1.30	1.15	1.18
USD/JPY	102	101	107	107
USD/CNY	6.85	6.80	7.01	6.90
EUR/GBP	0.96	0.96	0.90	0.88

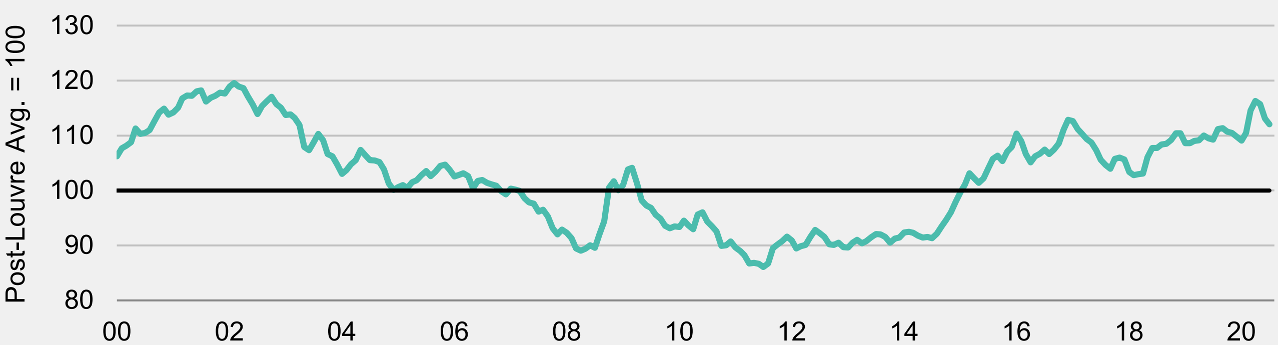
As of July 31, 2020
Source: Bloomberg and AB

Nominal USD Exchange Rate: US Dollar Index



Through July 31, 2020
Source: Bloomberg and AB

Real USD Broad Trade-Weighted Exchange Rate



Through July 31, 2020
Source: Haver Analytics and AB

US

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)	
	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F
US	(5.4)	3.6	0.5	2.5	0.13	0.13	0.50	1.00

OUTLOOK

+ The US forecast is largely on track, with a quick bounce back as the economy reopened giving way to a slow, grinding recovery from the COVID-19 pandemic. We think it will be several quarters before GDP returns to its pre-crisis level.
+ The most critical questions around the near-term outlook revolve around policy. Will Congress and the Trump administration agree on much-needed stimulus? Will the public health response allow schools to reopen, letting millions return to work? Answers to these questions, more than any new data, are keys to the economic outlook.
+ With the presidential election less than three months away, market and public attention is beginning to shift to it. If the contours of the campaign lead to more stimulus, this could be positive for the economy; if instead they lead to more disruptions, either health-related or in terms of social cohesion, it could have a negative impact.

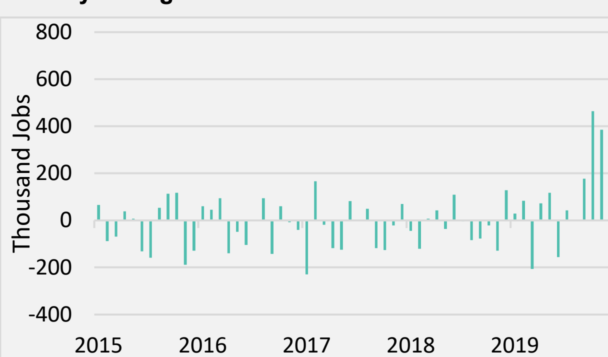
RISK FACTORS

+ As the last few weeks made clear, the coronavirus remains prevalent in the US. The spread and prevalence of the virus are still unpredictable but will clearly have consequences for the outlook.
+ Financial markets remain disconnected from the economic outlook, posing questions about the sustainability of asset prices if stimulus efforts run aground.

OVERVIEW

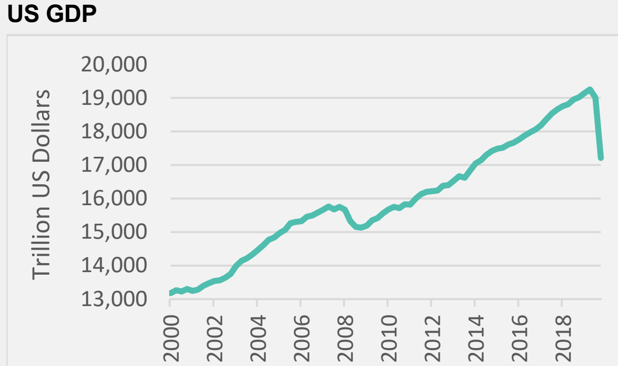
After a quick bounce off the bottom, economic growth has flattened over the past few weeks. Some of it was inevitable—after an initial spurt of pent-up activity, a slower pace of growth was always in the cards. Some, however, was due to the uniquely poor performance of the American public health response to the COVID-19 crisis. It's no coincidence that the pace of growth in Europe, where the virus is largely under control, has not flattened as much as the US. The good news is that the trajectory from here is largely dependent on policy decisions rather than economic variables. If Congress and the Trump administration can agree on an effective stimulus package, it should pave the way for a pickup in growth. And if public health policy is adequate to stem the COVID-19 tide, that would be an enormous help as well. Of course, effective policy cannot be assumed, especially with an election around the corner. Still, we generally expect that the economy will continue to expand, even if a bit more slowly than we hoped. Accommodative Fed policy has left the liquidity spigot flowing and financial markets healthy, which has kept overall financial conditions in a good place. For example, real yields are sharply negative, which means that businesses that can operate should also be able to fund themselves and be profitable. But time is of the essence—the longer the crisis, the larger the portion of economic damage that could be permanent rather than temporary.

Monthly Change in Permanent Job Losses



Through June 15, 2020
Source: Refinitiv Datastream

US GDP



Through May 15, 2020
Source: Refinitiv Datastream

Euro Area

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F
Euro Area	(7.5)	4.5	0.3	0.8	(0.50)	(0.50)	(0.50)	(0.35)	1.08	1.30

OUTLOOK

- Second-quarter GDP contracted by 12.1%. Although the steepest decline on record, this is somewhat smaller than preliminary guidance suggested by some national statistical offices, indicating either a smaller initial hit from COVID-19 lockdowns or a faster pace of recovery in May and June.
- We have revised our 2020 growth forecast to –7.5% from –10.0% previously but pushed our 2021 forecast down slightly to 4.5% from 5.0%. Superficially this looks like a “V-shaped” recovery, but this would leave the level of output at the end of 2021 roughly 3% below its 2019 year-end level.
- There are signs that the spread of COVID-19 is picking up as restrictions on economic and social activity are relaxed. While this warrants close monitoring, especially in Spain where the spread seems more advanced, we continue to think that this can be handled by targeted measures and that the risk of new national lockdowns remains low.
- The European Union’s new recovery fund should ensure that all European countries can provide the stimulus needed for their economies to recover from the COVID-19 pandemic. Largely because of the improvement in euro-area governance, we have raised our target range for the euro’s exchange rate against the USD to 1.25–1.35.

RISK FACTORS

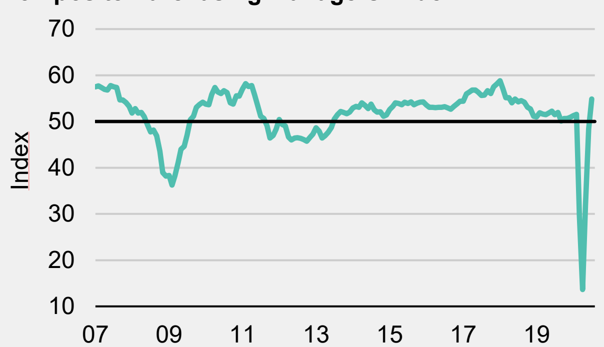
- Our forecasts assume no second wave of COVID-19 infections and no new national lockdowns. Should our assumptions be wrong, growth over the next two years could be lower than expected.
- Some recent data point to strong momentum and pent-up demand as countries emerge from lockdown. If this is sustained and accompanied by strong fiscal stimulus, growth could return quickly to pre-crisis levels.

OVERVIEW

The euro area contracted by a record 12.1% in the second quarter, dwarfing its 3.6% decline in the first quarter. Among the larger countries, the decline in output ranged from 10.1% in Germany to 18.5% in Spain. With Spain heavily dependent on summer tourism and signs emerging that the virus is picking up steam there more quickly than in other countries, this gap in economic performance is likely to widen. That’s why Europe’s leaders have agreed on €750 billion of joint funding to help the worst-hit economies recover.

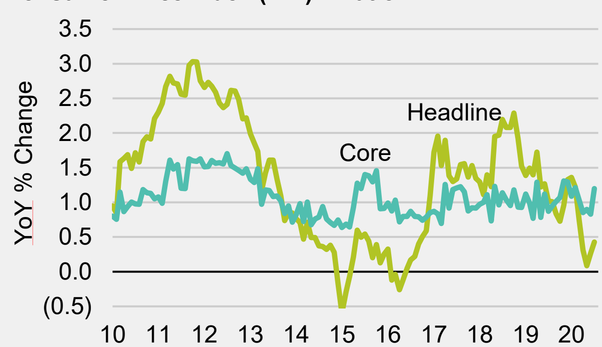
Overall, the second-quarter decline in output was better than initial guidance suggested. In France, GDP fell 12.4%, much smaller than the preliminary estimate of –17% published by the National Statistics Institute a few weeks ago. It’s not clear whether this means the economy experienced a smaller hit than initially thought, or if it is recovering more quickly than expected. Either way, the economy is in slightly better shape than thought a few weeks ago.

Composite Purchasing Managers’ Index



Through July 31, 2020
Source: Haver Analytics and IHS Markit

Consumer Price Index (CPI) Inflation



Through July 31, 2020
Source: Haver Analytics

China

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F
China	1.1	8.8	2.8	3.0	4.35	4.10	2.30	2.50	6.85	6.80

OUTLOOK

+ China's official real GDP growth rate will likely be about 1.1% in 2020, down from 6.1% in 2019. The decline's main drivers: weakness in capex and the impact from the COVID-19 epidemic. We expect 2021 growth to rebound to about 8.8%.
+ Continued monetary- and fiscal-policy easing should counter downward pressure on the economy, with the focus likely on infrastructure projects and property easing—measures most likely to help stabilize the economy.
+ Rising pork prices may push up inflation, but we don't think the increase will limit the central bank's policy easing.

RISK FACTORS

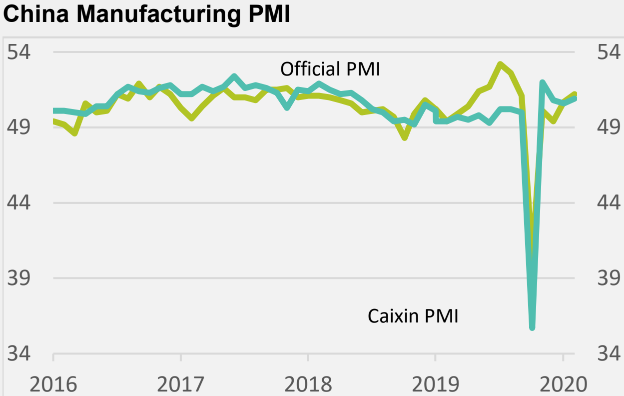
+ Policy easing may be less effective than expected if new economic data offer big surprises to the downside. This would put a sustained economic stabilization at risk for this year and the next.
+ With COVID-19 now a global pandemic, there will be further downward pressure on the Chinese economy from imported cases, weak external demand and disruption of their global supply chain.

OVERVIEW

China's second-quarter GDP surprised to the upside with a 3.2% year-over-year advance. This is on the back of China's "first in first out" economy amid the COVID-19 crisis, which allows for a faster-than-expected bounce back. We think the recovery will last into the third and fourth quarters, given current persistent monetary and fiscal easing policies. We are also seeing a declining risk of flooding's impact on the economic recovery. Meanwhile, auto sales have registered four consecutive months of positive growth, and cement prices are up owing to a strong pickup in infrastructure and property construction activities. All of these should bolster the economic recovery currently on track.

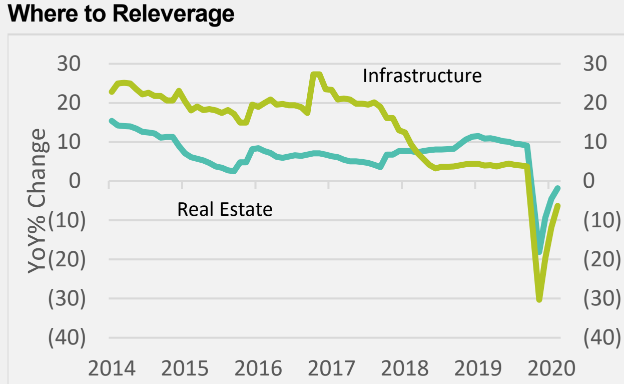
Policy easing expectations also slightly declined in July, as illustrated by China's central bank, the People's Bank of China, and at the recent politburo meeting. We think China doesn't need aggressive easing now. In our view, its economic recovery is on schedule, so *persistent* easing may be needed while *incremental* easing isn't. We also think that Chinese policymakers want to save some bullets for 2021 and 2022, when the global economy may experience tough times. We think monetary policy in the third quarter may be a bit tighter than market expectations, but fiscal policy will still be abundant through both special local government bond issuance and COVID-19-related bond issuance. Therefore, Chinese bond yields may face pressure in the third quarter. Regarding China's currency and a weaker US dollar, we think USD/CNY may appreciate to 6.85 over the next six months.

China Manufacturing PMI



Through June 30, 2020
Source: Bloomberg and AB

Where to Releverage



Through May 31, 2020
Source: Bloomberg and AB

Japan

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F
Japan	(4.0)	2.5	0.0	0.7	(0.10)	(0.10)	0.00	0.00	102	101

OUTLOOK

- New COVID-19 cases in Japan continue to climb, sparking second-wave fears.
- In addition to the impact of restrictions and consumer wariness, faltering recovery in global demand and confidence will also hurt the country's growth in coming quarters.
- Massive fiscal stimulus will help to support the post-restriction recovery facilitated by the Bank of Japan (BOJ).

RISK FACTORS

- A sharply stronger yen would apply an additional economic squeeze.

OVERVIEW

Japan's state of emergency was lifted on May 25, restrictions were relaxed, and mobility measures showed substantial improvement. A broad swathe of economic data shows an improvement from April/May lows, albeit only partially recovering lost ground. But the surge in cases though July has generated significant second-wave concerns and there's a clear risk that the growth profile for the second half of 2020 will remain patchy.

To cushion the COVID-19 impact, the government announced another fiscal package in May—amounting to Y117 trillion or 21% of GDP—on top of a nearly Y100 trillion package revealed in April. Not all of it is effective stimulus— "real water" in Japanese parlance—but the fiscal boost and budget-deficit blowout will nonetheless be substantial. With the BOJ dropping its Japanese Government Bond (JGB) purchase target in April—allowing "unlimited" bond buying—the extra bond issuance should easily be absorbed. Japan remains at the forefront of fiscal-monetary cooperation: "joined-at-the-hip" in global parlance.

Australia/New Zealand

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F
Australia	(4.4)	3.1	0.5	1.6	0.25	0.25	0.88	0.88	0.73	0.73
New Zealand	(5.5)	6.5	1.3	1.5	0.25	0.25	0.75	0.75	0.70	0.72

AUSTRALIA/NEW ZEALAND

- Until late June, the COVID-19 pandemic looked well under control in Australia and New Zealand—indeed, virtually eliminated in the latter. As a result, lockdowns and other restrictions were lifted, and activity was recovering smartly.
- But in Australia, the lifting of social distancing restrictions has brought a surge in cases—particularly in the state of Victoria—while a "Stage 4" lockdown was reimposed in the city of Melbourne and state borders closed.
- And while substantial stimulus—including a range of support measures like wage subsidies—are intended to cushion the economies through the shutdown, there remain questions over how long these measures will remain in place. Australia's JobKeeper program, for example, has been extended beyond its initial September expiry, but at a reduced rate. With lockdowns reimposed, and sectors such as international tourism and education far from "normal" any time soon, we're watching the risk of a premature unwind of fiscal support measures.
- On the monetary policy side, however, measures will remain in place. Both antipodean central banks will continue to anchor yields for an extended period via their quantitative easing/yield-curve control programs. In New Zealand, debate continues over whether the Reserve Bank of New Zealand (RBNZ) needs to do more—including a move to a negative-interest-rate policy and foreign asset purchases.

Canada

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F
Canada	(4.5)	3.3	0.5	2.5	0.25	0.25	0.50	1.00	1.30	1.30

OUTLOOK

- Canada's economy collapsed in the second quarter alongside the global economy, but we believe it will bounce back in the third quarter, again in lockstep with the global economy.
- The Bank of Canada will remain accommodative for the foreseeable future.

RISK FACTORS

- US politics, especially the upcoming election, seem less likely to have a meaningful impact on Canada this time around, but commodity prices remain volatile and could pose risks.

OVERVIEW

Canada's recession has a certain cause—COVID-19—but uncertain depth and duration. Policymakers have responded aggressively and effectively. This paves the way for an economic rebound, which is underway in the third quarter. It is likely that the next couple of months will look pretty good for Canada, but after that, things may get less certain.

UK

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F
UK	(10.0)	4.0	0.8	1.6	0.10	0.10	0.15	0.30	1.35	1.35

OUTLOOK

- The British government responded forcefully to support households and firms during the COVID-19 lockdown. But these efforts risk being undermined by a hesitant withdrawal of restrictions and inconsistent communication. Mobility indicators from Apple and Google data continue to suggest that activity is rising much more slowly in the UK than in other large European economies.
- We upgraded our euro-area growth forecast this month, but a similar move for the UK is not warranted. The monthly GDP series published by the Office for National Statistics shows that UK output rose by a disappointing 1.8% in May, following a cumulative decline of 25.9% for March and April. Barring significant upward revisions to these numbers, UK second-quarter GDP is more likely to approach (or be worse than) the 18.5% decline in Spain than the 12.1% drop in the euro area.
- The deadline has passed for extending the UK's Brexit transition phase. The best-case scenario for the end of the year is now a rudimentary trade deal, providing a zero-tariff regime for goods but with no provision for services and the UK leaving the EU's customs union. It is, however, equally possible that there won't be an agreement and that the trading relationship between the UK and EU will default to World Trade Organization (WTO) terms by year-end.
- Either of these two outcomes would be disruptive—both would once have been considered "hard Brexits." Coupled with a hesitant recovery from lockdown, UK growth looks set to underperform in coming quarters, even with more fiscal stimulus. The case for further monetary policy easing remains compelling, in our view.

RISK FACTORS

- The key risk factors likely to affect the economic outlook are how quickly the economy emerges from lockdown and Brexit negotiations. The UK outlook continues to be clouded by inconsistent communication.

Asia ex Japan

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F
Asia ex Jap/Ch	**(2.9)**	**4.9**	**1.9**	**2.5**	**1.98**	**1.74**	**3.72**	**3.87**	**—**	**—**
Hong Kong	(5.5)	4.0	2.8	2.5	1.00	0.90	0.76	0.77	7.78	7.80
India	(4.5)	6.0	3.4	3.9	3.00	2.50	5.80	6.00	77.00	76.00
Indonesia	(1.0)	5.0	3.0	3.2	4.00	3.50	7.80	8.00	15,000	14,500
South Korea	(0.2)	3.0	0.3	1.0	0.50	0.50	1.25	1.25	1,150	1,150
Thailand	(6.5)	3.5	(0.5)	0.8	0.50	0.50	1.00	1.00	32.00	32.50

OUTLOOK

+ The economic impact of COVID-19—travel restrictions, lockdowns, supply-chain disruption, weaker global demand and impaired confidence—remains the dominant driver.
+ In general, the virus is contained in most countries in the region. But more flags are being raised around second-wave risks.
+ Substantial monetary and fiscal support has been delivered. Questions persist around how far “unconventional” policies can be pushed, even if market concerns have subsided for now.

RISK FACTORS

+ COVID-19, US-China tensions

OVERVIEW

COVID-19 remains the key factor influencing the outlook in Asia ex Japan. Responses to the virus itself—including lockdowns, testing and case tracking—have been relatively successful. Taiwan and Korea stand out on this front. But in Thailand, Vietnam and Malaysia the case counts also remain low. Trends in India, Indonesia and, given recent case surges, the Philippines are still concerning, and these countries have rolled back their timelines to relax restrictions.

The economic policy response to date has been positive—with monetary easing and substantial fiscal support being delivered across the board. This should help underpin recovery. But across the region an end to the monetary easing cycle is close.

The anticipated headwind of weaker domestic demand from the US and Europe remains, particularly as those regions attempt to navigate the prospect of a second virus wave. It’s a reminder that even if COVID-19-related uncertainty begins to clear, the headwinds from other factors—deglobalization and US-China tensions—will remain stiff.

In addition, question marks remain over policy credibility. The Philippines, India and Indonesia, among others, have ventured down a path of unconventional monetary policy, intervening in domestic government bond markets to smooth volatility and facilitate ever-expanding fiscal deficit financing (forms of quantitative easing, if you like). Indonesia has gone the furthest here—with an explicit “burden-sharing” agreement between the finance ministry and the country’s central bank. To date, market concerns have been eased by the bank’s commitment that it is a “one off.” This may prove to be the case. But history tells us that advancing down this path seldom stops at the first step.

Latin America

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F
Latin America	**(7.7)**	**3.5**	**8.1**	**6.4**	**6.44**	**5.78**	**5.82**	**6.45**	**—**	**—**
Argentina	(9.5)	3.5	45.0	35.0	35.00	30.00	—	—	75.00	80.00
Brazil	(5.8)	3.0	3.4	3.6	2.00	2.50	6.80	7.50	5.25	5.00
Chile	(6.6)	5.1	2.7	2.0	0.50	0.75	2.50	3.00	830	850
Colombia	(6.5)	6.0	2.5	2.0	2.25	2.75	5.50	6.00	4,000	4,100
Mexico	(9.6)	2.2	3.4	3.0	4.50	4.50	5.50	6.25	24.00	24.50

OUTLOOK

+ Activity indicators show a recovery in June, despite the continued spread of the COVID-19 virus in the region. External accounts have improved owing to steep drops in activity while exports have not fallen in tandem for the most part.

+ Central banks have continued easing as output gaps remain largely negative and inflation expectations sit below the mid-level of the target.

RISK FACTORS

+ As COVID-19 spreads unfettered, risk of new closures persists. However, if they happen, closures would be targeted for specific regions and/or activities to try to diminish the impact to economic activity and already-strained fiscal accounts.

OVERVIEW

In Brazil, Covid-19 cases are still on the rise and the consumer sector remains severely impacted, but there are early signs of an improving economy. The July manufacturing PMI was 58.2, up from 51.6 in June and a low of 36 in April. GDP increased 1.3% month over month in May, but is still down significantly from pre-pandemic levels. We expect higher activity in non-retail sectors to show up in data in the coming months, as factories and primary sector operations resume. However, the recovery of the domestic economy will take time, especially in the retail and consumer services segments. Imports were down 35.9% year over year in July, and consumer assessment of current economic conditions are still well below first-quarter levels. The government is considering extending its direct transfer program to families but is starting to critically assess the fiscal implications of its generous stimulus programs. The central bank cut the Selic rate by 25 basis points (b.p.) in August, likely ending the easing cycle.

Mexico's second-quarter GDP release confirmed the sharp year-over-year drop in the industrial (–26%) and services sectors (–15.6%) due to the crisis. However, when combining April and May data, the quarterly result implies a strong activity rebound in June (+8.5% month over month). A reactivation in US demand would have been the largest positive contributor to the recovery while domestic demand would have remained weak. External accounts tell a similar picture, with exports recovering and imports subdued in June. While the use of fiscal policy for countercyclical purposes remains limited, the central bank still has room to continue cutting the intervention rate, but we expect cuts to be gradual.

Chile's Congress passed a constitutional change that allows emergency withdrawals of up to 10% from individual retirement accounts. The measure had strong opposition from the government, believing it would decrease the expected income replacement ratio for retirees. Despite the opposition, the new law enjoyed large support from Chileans and congressional members.

Argentina finished debt negotiations with external creditors in early August. The deal will restructure around US$60 billion in external debt and provide around US$36 billion of debt relief through substantive interest payment reductions and extension in maturities. The government announced that the country would need to negotiate with the International Monetary Fund (IMF) to postpone upcoming payments to that multilateral organization. The government's constraints on financing and an increase in the primary deficit have forced it to rely on credit from the central bank, increasing the likelihood of a spike in inflation that could hinder economic stability once activity resumes after the lockdown.

Eastern Europe, Middle East and Africa (EEMEA)

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F
EEMEA	**(5.3)**	**3.8**	**4.7**	**5.2**	**3.88**	**4.23**	**6.63**	**6.35**	**—**	**—**
Hungary	(5.7)	5.4	2.7	3.3	0.50	0.75	1.40	2.10	335	330
Poland	(4.5)	5.5	2.8	3.1	0.10	0.10	1.20	1.65	4.32	4.30
Russia	(4.9)	2.9	3.3	3.8	4.00	4.00	6.20	5.90	72.50	68.00
South Africa	(8.0)	2.7	3.4	3.9	3.50	4.00	9.05	9.45	17.00	17.80
Turkey	(4.2)	3.9	10.5	11.5	8.25	10.00	13.00	12.00	7.35	7.00

OUTLOOK

+ EEMEA real growth prospects have deteriorated markedly for 2020, owing to weaker external demand (a large euro-area recession) and domestic lockdown measures to contain the COVID-19 spread. Lower energy prices also weigh on real GDP growth for the region’s oil exporters.
+ Given a challenging growth outlook, central banks have eased monetary policy and implemented bond purchase programs to support domestic financial liquidity. While further modest interest-rate cuts are possible in Russia, other countries such as South Africa and Turkey have likely come to the end of their easing cycles.

RISK FACTORS

+ While the extent of the economic downturn in 2020 is becoming clearer, the shape of the recovery beyond this year remains highly uncertain. Governments’ exit strategies from current lockdown measures and their ability to prevent a second wave of infections will influence the shape of the recovery.

OVERVIEW

Renewed declines in Turkey’s net foreign assets amid apparent efforts to defend a certain USD/TRY level will remain a key market focus and a significant source of macroeconomic vulnerability. Pressures on the exchange rate have remain manifold: first, the country still posts a sizeable current account deficit as the trade shortfall has not adjusted meaningfully, while tourism revenues have declined significantly. At the same time, capital inflows have remained scarce. We don’t expect this trend to improve materially over the rest of 2020. Second, loose monetary policy and sticky inflation (especially service inflation) leave domestic interest rates deeply negative, between –4% and –5%. This encourages further dollarization and precious metals buying among corporates and households. True, the Turkish Central Bank (CBRT) signaled an end to its easing cycle based on rising inflation concerns. Yet the focus will increasingly be on the need for interest-rate hikes in the event of further FX weakness. It has long been one of the CBRT’s greatest challenges to proactively raise interest rates, and it remains to be seen whether authorities manage to stay ahead of the curve now.

We believe the South African Reserve Bank (SARB) concluded its easing cycle last month. While economic growth and inflation will remain low for the foreseeable future, fiscal risks argue strongly against any further compression in real rates. South Africa’s emergency financial assistance from the IMF was finally approved in July. The US$4.3 billion (100% of quota) approved under the IMF’s Rapid Financing Instrument, plus financing from other international financial institutions and robust domestic bond issuance, are keeping the financing equation broadly on target. But revenue underperformance risks further widening the budget deficit that was tabled in June’s Supplementary Budget (15.7% of GDP in FY20/21). South Africa’s handling of COVID-19 has generally been lauded, but some lingering restrictions seem excessive to us. Allegations that political considerations dominate social and economic measures to handle the pandemic, and the involvement of African National Congress members in COVID-19 related corruption, have undermined President Ramaphosa’s reform agenda.

Frontier Markets

Angola's short-term liquidity concerns have largely been addressed by a three-year debt moratorium from China and the G20 Debt Service Suspension Initiative (DSSI). The IMF was expected to approve a rapid financing facility at the end of July, but it was postponed at short notice. It's not clear whether the delay was due to a late request from the authorities to upsize the current program or whether the IMF remains uncomfortable with the debt trajectory. The IMF's stamp of approval will be important to avoid a relapse of sovereign bond prices. We think additional funding from the IMF will be approved next month. But elevated medium-term financing needs, and the dominance of external debt, point to a challenging period ahead.

In Ukraine, July proved volatile on the domestic political front following the resignation of National Bank of Ukraine (NBU) Governor Smoliy, the appointment of new Governor Shevchenko, and several changes to NBU board membership. We don't believe that explicit changes to NBU policy are on the cards, which would be a red flag in its IMF relationship. We recognize, however, the increased risk that the September review of the current stand-by agreement will be delayed. The IMF may seek time to assess the impact of recent NBU personnel changes and the removal of the public salary cap (which has not happened yet). Even if the upcoming review is delayed, we think the political class, President Zelenskiy in particular, remains committed to the IMF program. Against ongoing significant refinancing needs in 2021 and limited conditionality imposed by the program, we would expect a resumption of the IMF program in late 2020 or early 2021.

Facing significant fiscal challenges, Ecuador reached an agreement to restructure its external debt with bondholders and its largest bilateral creditor, China. With nearly 98% approval from bondholders, Ecuador amended the terms of its bonds and reduced financing costs by nearly US$16 billion over 10 years, including eliminating interest payments for the rest of 2020. Ecuador expects to receive an additional US$2.4 billion in new financing from China as part of the restructuring, which will help the country to close its nearly US$4 billion funding gap before the end of the year. The next step is to finalize a new agreement with the IMF, which will help keep Ecuador's fiscal consolidation reforms on track and unlock additional lending capacity by multilaterals. The details of the new IMF program should be determined over the next few weeks. With financing challenges largely solved, the attention will shift to the election cycle: presidential and congressional elections are scheduled for February 2021 and may feature former president, Rafael Correa, in some capacity (rumored as VP or a congressional candidate). Correa is a renowned left-wing populist. His return to Ecuadorian politics has caused many pundits to draw parallels with former President Cristina Fernandez de Kirchner's return to Argentine politics in 2019, which caused significant market turmoil.

	Real Growth (%)		Inflation (%)		Official Rates (%)		Long Rates (%)		FX Rates vs USD	
	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F	2020F	2021F
Global	(4.5)	4.8	1.7	2.5	1.51	1.43	1.53	1.79	-	-
Industrial Countries	(6.1)	3.8	0.4	1.7	(0.07)	(0.07)	0.14	0.45	-	-
Emerging Countries	(2.1)	6.4	3.6	3.6	3.97	3.72	3.73	3.88	-	-
EM ex China	(4.7)	4.3	4.3	4.2	3.72	3.46	5.04	5.20	-	-
United States	(5.4)	3.6	0.5	2.5	0.13	0.13	0.50	1.00	-	-
Canada	(4.5)	3.3	0.5	2.5	0.25	0.25	0.50	1.00	1.30	1.30
Europe	(7.8)	4.4	0.4	1.0	(0.37)	(0.37)	(0.35)	(0.20)	1.65	1.81
Euro Area	(7.5)	4.5	0.3	0.8	(0.50)	(0.50)	(0.50)	(0.35)	1.08	1.30
United Kingdom	(10.0)	4.0	0.8	1.6	0.10	0.10	0.15	0.30	1.35	1.35
Sweden	(5.5)	4.5	0.8	1.3	0.00	0.00	(0.15)	0.00	10.3	10.0
Norway	(5.0)	4.5	1.1	1.7	0.25	0.25	0.75	0.90	10.8	10.5
Japan	(4.0)	2.5	0.0	0.7	(0.10)	(0.10)	0.00	0.00	102	101
Australia	(4.4)	3.1	0.5	1.6	0.25	0.25	0.88	0.88	0.73	0.73
New Zealand	(5.5)	6.5	1.3	1.5	0.25	0.25	0.75	0.75	0.70	0.72
China	1.1	8.8	2.8	3.0	4.35	4.10	2.30	2.50	6.85	6.80
Asia ex Japan & China	(2.9)	4.9	1.9	2.5	1.98	1.74	3.72	3.87	-	-
Hong Kong	(5.5)	4.0	2.8	2.5	1.00	0.90	0.76	0.77	7.78	7.80
India	(4.5)	6.0	3.4	3.9	3.00	2.50	5.80	6.00	77.0	76.0
Indonesia	(1.0)	5.0	3.0	3.2	4.00	3.50	7.80	8.00	15,000	14,500
Korea	(0.2)	3.0	0.3	1.0	0.50	0.50	1.25	1.25	1,150	1,150
Thailand	(6.5)	3.5	(0.5)	0.8	0.50	0.50	1.00	1.00	32.0	32.5
Latin America	(7.7)	3.5	8.1	6.4	6.44	5.78	5.82	6.45	-	-
Argentina	(9.5)	3.5	45.0	35.0	35.00	30.00	0.00	0.00	75.0	80.0
Brazil	(5.8)	3.0	3.4	3.6	2.00	2.50	6.80	7.50	5.25	5.00
Chile	(6.6)	5.1	2.7	2.0	0.50	0.75	2.50	3.00	830	850
Colombia	(6.5)	6.0	2.5	2.0	2.25	2.75	5.50	6.00	4,000	4,100
Mexico	(9.6)	2.2	3.4	3.0	4.50	4.50	5.50	6.25	24.0	24.5
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South Africa	(8.0)	2.7	3.4	3.9	3.50	4.00	9.05	9.45	17.0	17.8
Turkey	(4.2)	3.9	10.5	11.5	8.25	10.00	13.00	12.00	7.35	7.00

Growth and inflation forecasts are calendar year averages.
Interest rate and FX rates are year end forecasts.
Long rates are 10-year yields unless otherwise indicated.
The long rates aggregate excludes Argentina; Argentina is not forecasted due to distortions in the local financial market.
Real growth aggregates represent 31 country forecasts not all of which are shown

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