EMBARGOED UNTIL: 11.30AM THURSDAY 12 AUGUST 2021

THE FORWARD VIEW – GLOBAL

AUGUST 2021

National Australia Bank

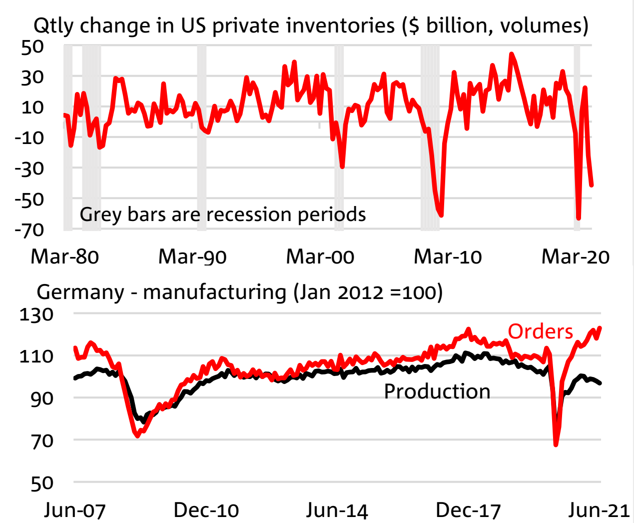
Differing vaccination rates are driving a divide between economic groups

- There are growing signs of a divide between advanced economies and emerging markets in indicators such as equity indices, purchasing manager indices and mobility data. In part this appears related to generally higher COVID-19 vaccination rates in advanced economies – which are allowing a greater degree of openness despite the spread of variants such as Delta – while various EMs are forced to impose restrictions.
- There are concerns around China's economic growth, following a Delta variant COVID-19 outbreak that started in mid-July. Chinese authorities have introduced mass testing and travel restrictions, along with localised closures of events and businesses, but it will be critical to see if China can control the outbreak without harsh countermeasures that would slow economic activity. This outbreak could further disrupt global supply chains – where shortages and rising commodity prices are flowing through into strong producer price increases.
- Our global forecast for 2021 is marginally weaker this month – with growth of 6.2% – compared with 6.3% previously. This slightly weaker rate of growth reflects downgrades to our forecasts for the United States, Japan, the United Kingdom and Canada, marginally offset by an upgrade to our forecasts for the Euro-zone. Our global forecasts for 2022 and 2023 are unchanged (at 4.6% and 3.5% respectively). Risk around our India and China forecasts appears weighted to the downside – particularly if China's measures to limit the spread of its current COVID-19 outbreak leads to a significant slowing in economic activity.

Global Growth Forecasts
(% change)

	2019	2020	2021	2022	2023
US	2.3	-3.4	6.2	4.3	2.1
Euro-zone	1.4	-6.5	4.8	4.4	2.1
Japan	0.0	-4.7	2.3	3.7	1.0
UK	1.4	-9.8	7.1	6.1	2.3
Canada	1.9	-5.3	6.1	3.9	2.5
China	6.0	2.3	9.5	5.8	5.6
India	4.8	-7.0	9.0	6.1	5.6
Latin America	0.1	-6.7	5.6	2.4	1.7
Other East Asia	3.5	-2.9	5.1	4.8	4.7
Australia	1.9	-2.4	3.8	3.9	2.5
NZ	2.4	-2.9	5.7	2.9	2.0
Global	**2.8**	**-3.3**	**6.2**	**4.6**	**3.5**

Global supply disruption – inventory falls & prodn struggling to meet orders



CONTENTS

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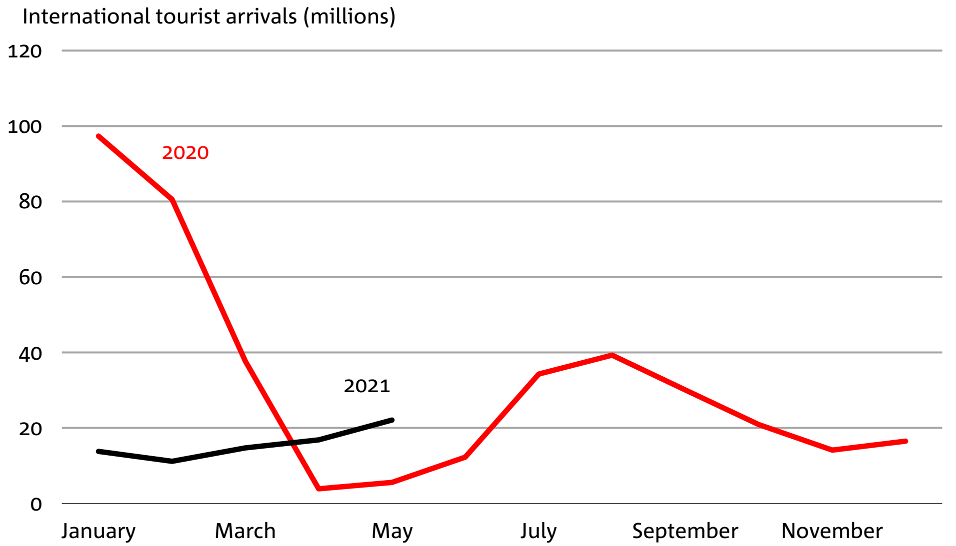
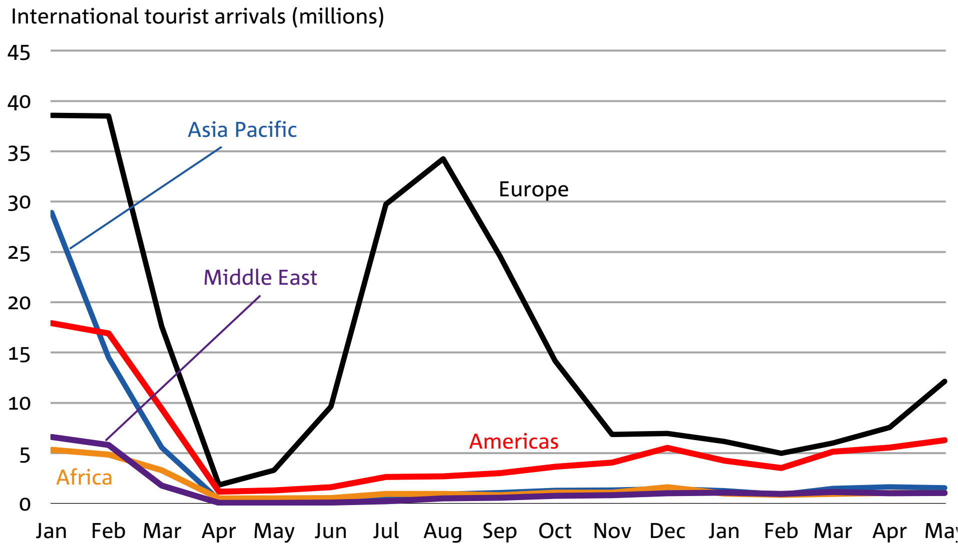
CHARTS OF THE MONTH

International tourism has been among the hardest hit by the pandemic – with restrictions constraining the sector's recovery. Countries with large shares of total exports hit harder than others. Full recovery remains several years away.

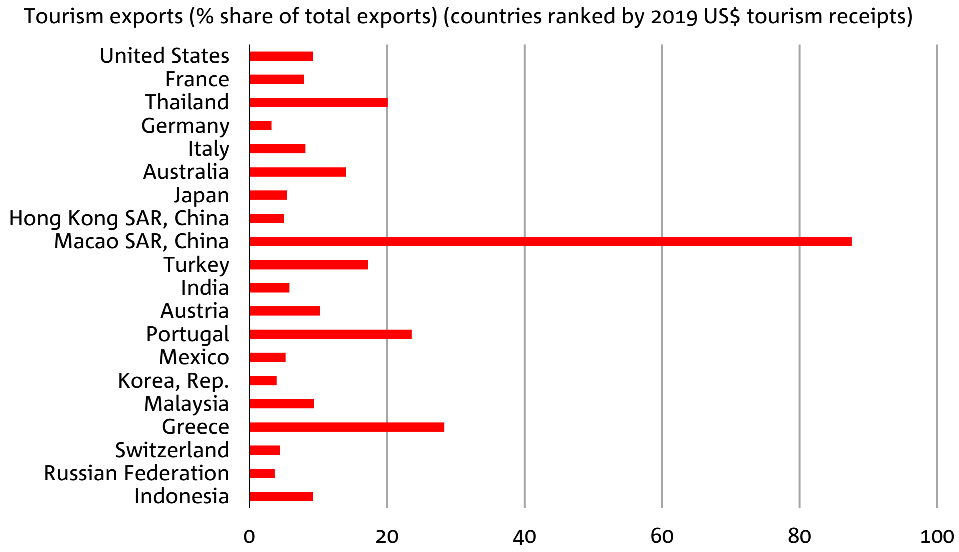
Global tourism has been slow to recover from COVID-19. Arrivals up yoy in May but well below pre-pandemic levels



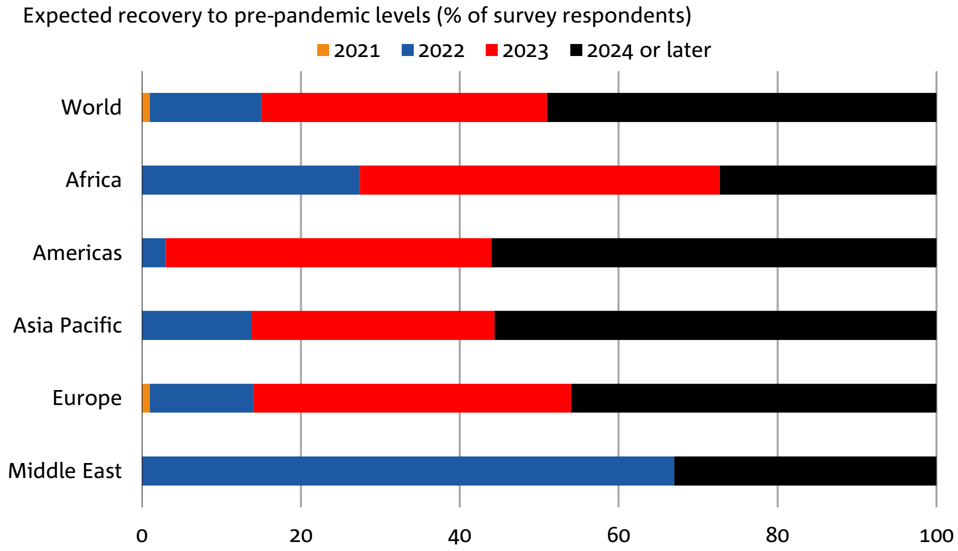
Europe & Americas back above 30% of Jan-20 levels, Asia Pacific lagging way behind (near 5%)



Countries with larger tourism share of exports have been impacted more heavily



Surveyed tourism experts do not anticipate a full recovery before 2023, if not later



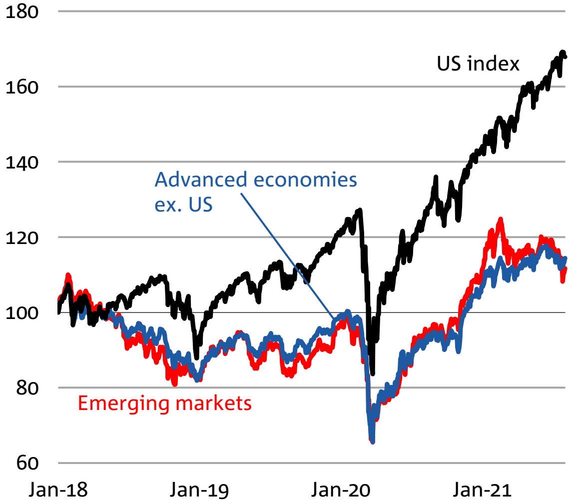
Sources: UN World Tourism Organization, World Bank, NAB Economics

FINANCIAL AND COMMODITY MARKETS

Signs of a divide between AEs and EMs in equities; supply side pressures driving producer prices higher

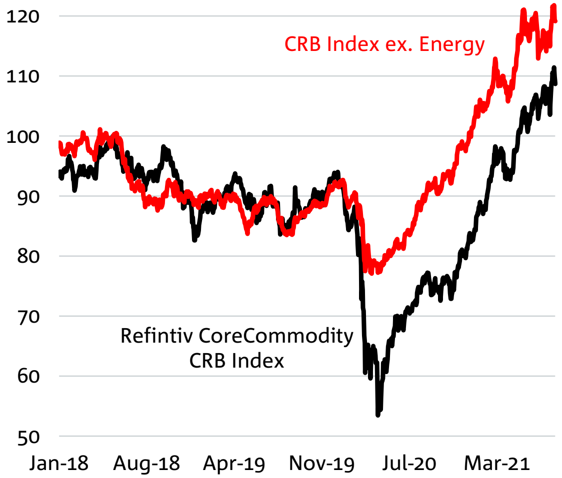
Mixed trends in equities; US at record highs, EMs retreating

MSCI Equity Indices (1 Jan 18=100)



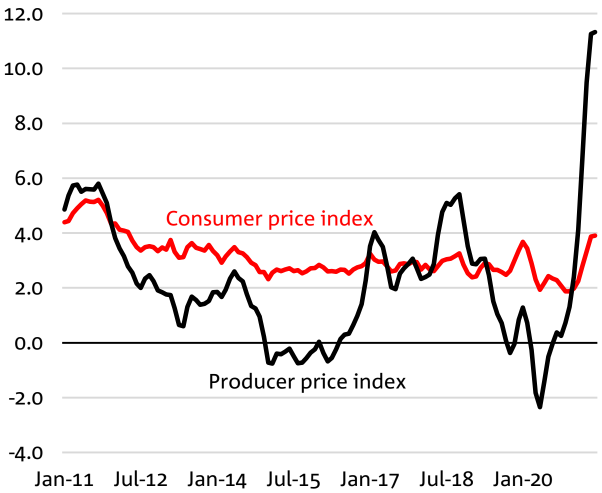
Commodity prices rise to highest levels since December 2014

Commodity indices (23 May 18 =100)



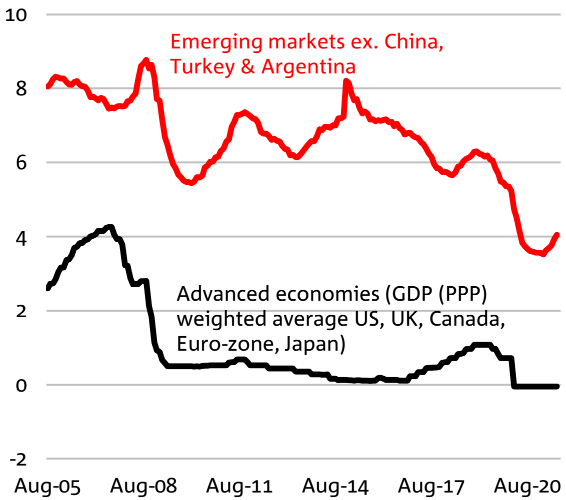
Producer prices have surged, led by increases in EMs

Global inflation (yoy%)



Modest upturn in EM policy rates; AE central banks to keep rates low

Average central bank policy rates (%)



- Trends in global equity markets were highly divergent in July. Markets in the United States continue to trend higher – with the US MSCI index recording another record high in late July (before easing marginally from this peak). In contrast, the equity index for other advanced economies has drifted lower since late June, while emerging markets (EMs) have fallen more significantly. In large part this reflects a sell off in Chinese equity markets in response to a regulatory crackdown on the technology sector, however reports suggest international investors are increasingly favouring advanced economy equity markets where vaccination rates are higher.
- Commodity prices have pushed higher once again. In late July, the Refinitiv CoreCommodity CRB Index rose to its highest level since December 2014. Given China's critical role in these markets – as the largest consumer of most commodities – the current COVID-19 outbreak in the country presents downside risk to commodity prices in the near term.
- Supply chain issues – including rising commodity prices and shortages of key inputs (such as semi-conductors) – continue to have an impact on global manufacturing production. This is reflected in higher producer prices, which rose by around 11.3% yoy in June, unchanged from May. As the global recovery was more advanced in June 2020 (versus May), the base effects were smaller this month – meaning that compared with the same period in 2019, producer prices were up by 9.8% in June (compared with 8.6% in May). As noted above, the COVID-19 outbreak in China could further disrupt global supply chains.
- Rising producer prices have flowed through into higher consumer prices – which rose by 3.9% yoy in June (again unchanged from the increase in May, but stronger compared to 2019). EMs saw larger increases in both producer and consumer prices in June.
- Despite the inflationary pressure, major central banks appear unlikely to raise policy rates in the near term, with monetary policy adjustments set to come by adjusting asset purchases. The Bank of Canada started to taper asset purchases in April, while the US Federal Reserve is expected to start this process in either late 2021 or early 2022. While the European Central Bank's Pandemic Emergency Purchase Program is scheduled to end in March 2022, but asset purchases, at least to some degree, will continue beyond this time. In contrast, a few EM central banks (most notably Russia and Brazil) have increased rates – with a large increase expected in Brazil in August – in response to inflationary pressures.

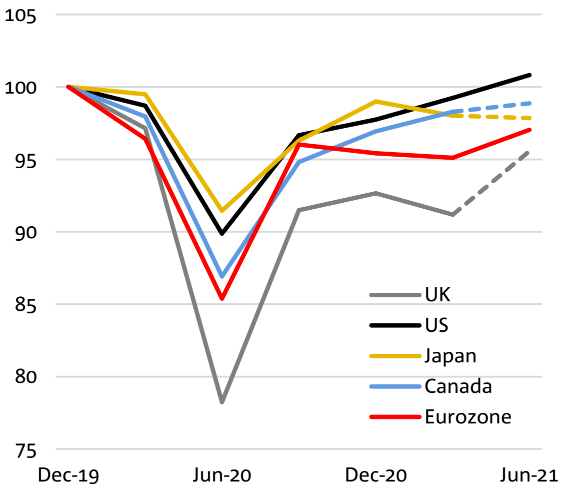
 Sources: Bloomberg, Refinitiv, NAB Economics

ADVANCED ECONOMIES

The US and Euro-zone grew rapidly in Q2; surveys point to AE growth continuing into Q3, despite Delta

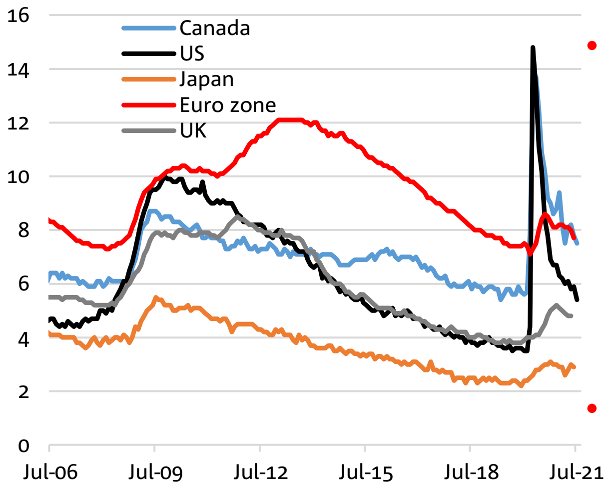
US GDP back to pre-COVID level

Major AE GDP (Q4 2019 = 100, dash line indicate forecast)



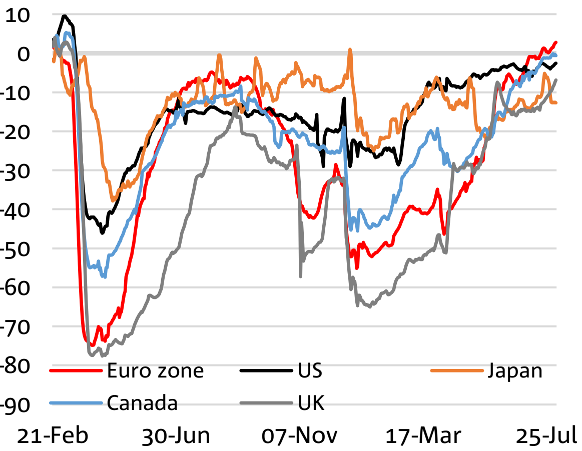
Unemployment yet to fully recover

Unemployment rate (%)



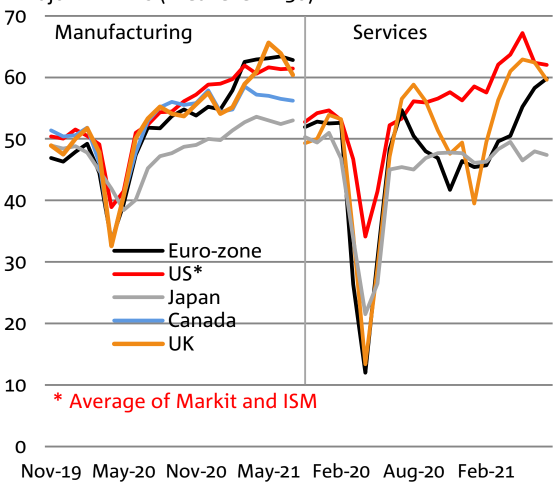
Delta outbreaks have not led to a major reduction in mobility

Google mobility report-visits: recreation. & retail (% devn from baseline, 7 day m.a.)



Business surveys still generally at a high level

Major AE PMIs (Breakeven = 50)



Sources: Refinitiv, IHS Markit, https://www.google.com/covid19/mobility/, NAB Economics

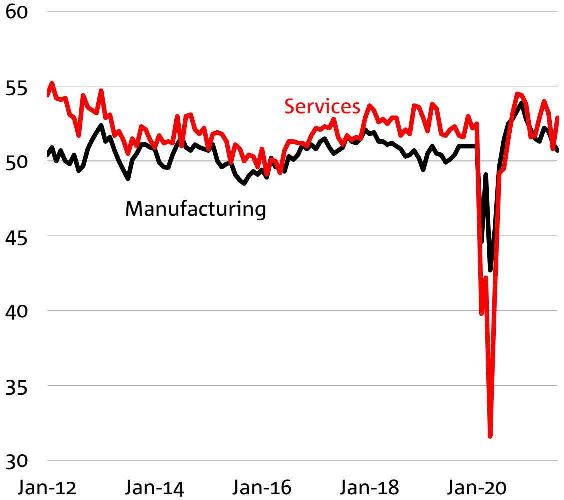
- As expected there was very strong growth in both US and Euro-zone Q2 GDP. US GDP increased by 1.6% q/q (similar to Q1) while Euro-zone growth was even stronger at 2.0% q/q. For the other major advanced economies (AEs) we expect to a see a range of Q2 outcomes – from strong (UK) to weak (Japan) with Canada in-between.
- These growth differentials are in part due to COVID-19 and the different time countries impose (and then leave) restrictions. However, the economic impact with each wave appears to be declining. This reflects a number of factors, including the progress in rolling out vaccines which was a factor in the UK's July decision to complete the last step of its re-opening plan even as cases surged. New cases in the UK have since dropped and have levelled off in the European Union, but they are still rising rapidly in the US and Japan. As yet, there has been little move towards a material re-introduction of restrictions in the US but parts of Japan remain in a 'quasi state-of-emergency' (which was extended this week).
- That said, some consumption indicators for Japan have held up surprisingly well, suggesting some upside risk to our expectation of a small fall in Q2 GDP. This can also be seen in mobility indicators which are largely moving sideways. There have been some restrictions introduced in parts of Europe but their impact appears limited (with mobility continuing to rise). Even absent restrictions, rising case numbers can lead to consumers being more cautious, which represents a downside risk to our forecasts. That said, while recent monthly business survey readings have been mixed in terms of direction, they generally remain at a high level, suggesting the AE recovery is on track.
- US GDP is now above its pre-COVID level, the only major AE to have reached this milestone. Given economies should grow over time, this leaves a large output gap, even for the US. This is reflected in unemployment rates which are yet to return to pre-COVID levels. While their initial experience was very different – in part due to the differing government support (income support vs wage subsidies) – most AEs are seeing improvement, even if it hasn't been a smooth process.
- Supply bottlenecks are a factor that have held back the recovery, but they should turn into a tailwind as they are addressed. Surveys show supplier delivery times are at elevated levels. Reflecting this, the strong demand in the US in H1 2021 was met through a run down in inventories (to an extent unprecedented outside of a recession). Similarly German manufacturing production has been unable to keep up with incoming orders. (See Charts on page 1.)

EMERGING MARKET ECONOMIES

EM manufacturing continues to slow, with China's COVID outbreak a global risk

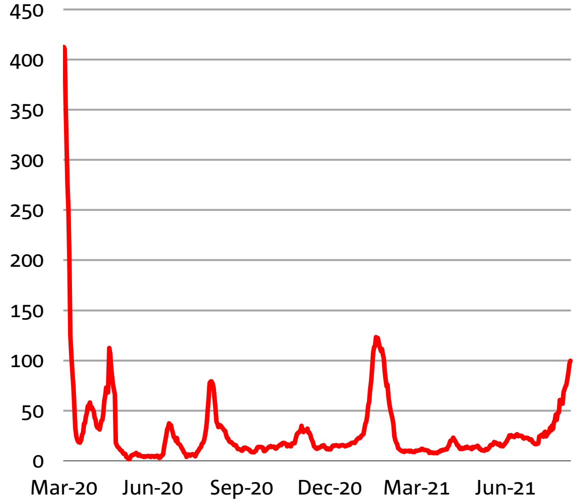
Diverging trends in PMI surveys, with China leading mfg lower

Emerging market PMI (Breakeven = 50)



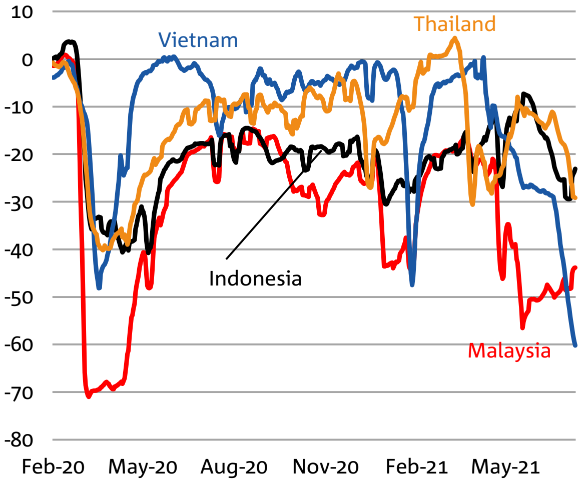
China's latest COVID outbreak small so far, but risk of spread

China new COVID-19 cases (rolling 7 day average)



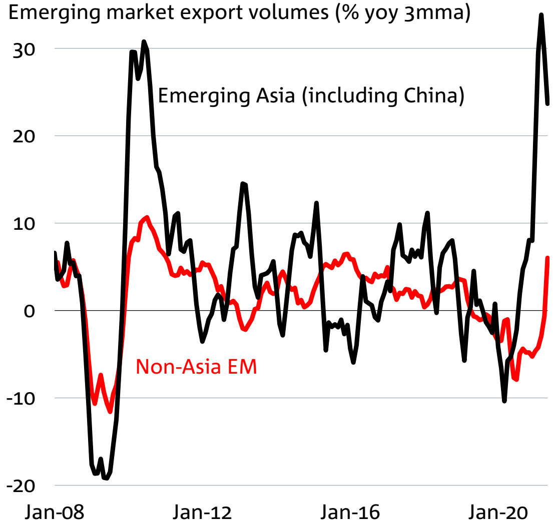
Mobility data highlight the impact of outbreaks in East Asia

Google mobility data - % deviation from baseline (7 day avg - retail & workplaces)



Asia drives export growth, non-Asia growth may be short term

Emerging market export volumes (% yoy 3mma)



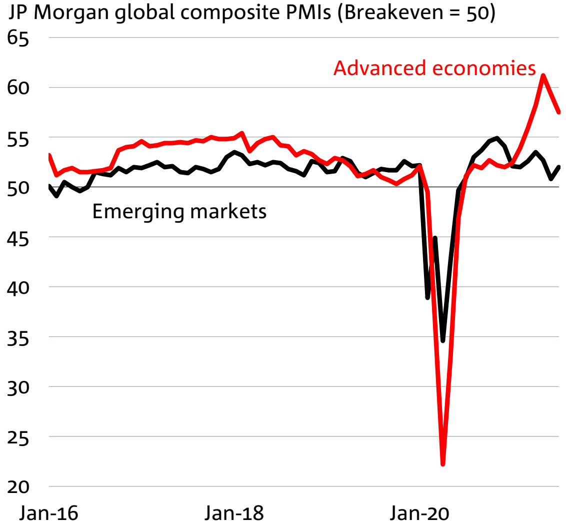
- Purchasing manager indices provide a rapid indication of conditions across a broad range of countries. PMIs for emerging markets were mixed in July – with a further easing in the manufacturing measure in contrast with a stronger services reading.
- The EM manufacturing PMI was at 50.7 points in July (from 51.2 points in June). The easing in this measure was driven by a sharp downturn in Indonesia (from 53.5 points to 40.1 points in July) and a further slowing in China (to essentially neutral levels). In contrast, there was a strong recovery in the Indian manufacturing PMI, as COVID-19 restrictions have been eased.
- The EM services PMI rose strongly – up to 52.9 points in July (from 50.8 points previously). Both China and India recorded strong increases in their services measures – however the China reading was ahead of a fresh COVID-19 outbreak which could dent the sector.
- Concerns around China's economic growth have been raised by a COVID-19 outbreak in mid-July (the first significant spread since January 2021). The outbreak of the Delta variant started in the city of Nanjing but has since spread to other localities, including Beijing. In response, Chinese authorities have introduced mass testing and travel restrictions, along with localised closures of events and businesses, but it will be critical to see if China can control the outbreak without harsh countermeasures that would slow economic activity.
- Earlier COVID-19 outbreaks have impacted East Asia – including in countries such as Vietnam that had previously managed to avoid widespread outbreaks. Google Mobility data show a sharp downturn in movements in Vietnam, Thailand and Indonesia in recent times, as these countries attempt to control spread of the virus.
- Global trade is of greater importance for emerging markets than advanced economies, however these data are somewhat lagged compared with PMI or mobility data. EM trade volumes grew strongly up to May (the most recent month available) – in part due to base effects (given that major COVID-19 shutdowns ranged across March through May 2020).
- Previous months had seen growth in export volumes dominated by China and other East Asian EMs, however there was a sizeable upturn in non-Asian growth in May, which largely reflected the sharp downturn recorded in May 2020. This suggests that this upturn may not persist.

Sources: Refinitiv, IHS Markit, https://www.google.com/covid19/mobility/, CPB, NAB Economics

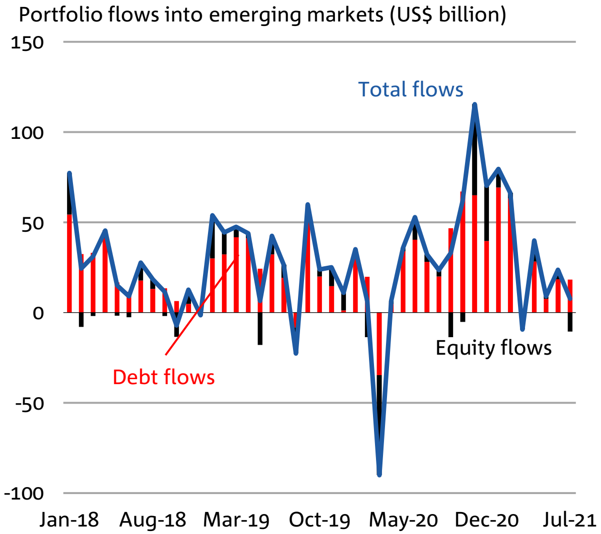
GLOBAL FORECASTS, POLICIES AND RISKS

COVID-19 remains the key risk, with higher vaccinated AEs currently faring better

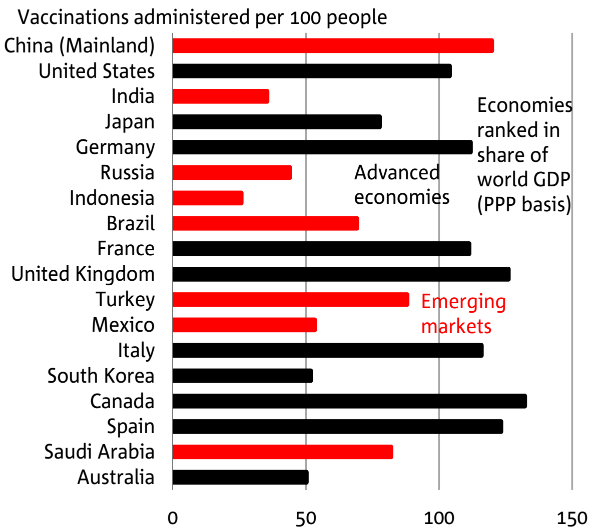
Wide gap between PMI readings for AEs and EMs



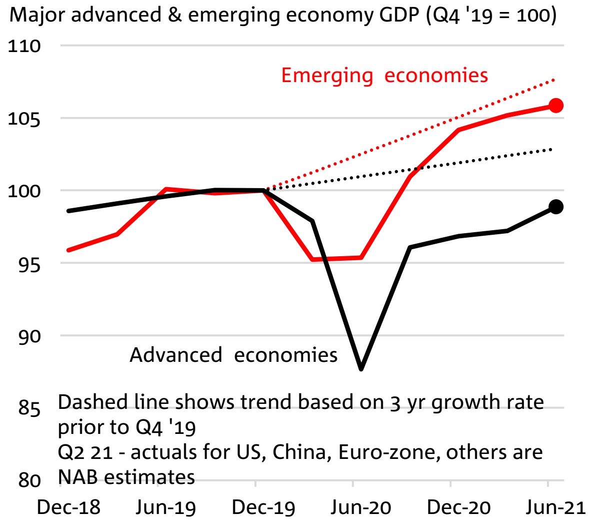
Weaker capital inflows to EMs in 2021 than in late 2020



AEs generally outperforming EMs in vaccine rollout



EMs had quick recovery; vaccines/ COVID outbreaks now impacting



- The aggregate readings for global purchasing manager indices remain historically strong, albeit the JP Morgan global composite PMI was a little softer in July – at 55.7 points (compared with 56.6 points in June). This decline was primarily driven by an easing in the global services measure – with manufacturing having remained relatively stable in recent months.
- That said, these global PMI measures are more heavily weighted towards advanced economies than global GDP (on a purchasing power parity basis) – meaning that this apparent strength may not translate into strong growth for the quarter. The emerging market composite measure peaked in November 2020 and has subsequently trended lower – initially reflecting China's comparatively rapid recovery from COVID-19, but more recently the impact of fresh outbreaks in other major EM economies.
- Softer EM equity market performance was consistent with outflows from these markets in July. Overall, portfolio flows (the sum of equity and debt flows) into emerging markets have slowed considerably in 2021 – compared with peaks in November 2020. If investor preferences favour advanced economies over emerging markets (on the basis of higher vaccination rates supporting stronger growth prospects), this adds some additional downside risk to emerging markets.
- COVID-19 remains the most significant risk to our global outlook, with emerging markets generally more vulnerable to COVID-19 outbreaks than advanced economies, due to typically lower vaccination rates. There are concerns that newer COVID-19 variants, most notably delta – which is spreading in a wide range of countries – may require higher rates of immunisation to reach herd immunity. It is also possible that vaccines with lower efficacy rates (more commonly used in emerging economies) may provide limited protection against this and other variants.
- Our global forecast for 2021 is marginally weaker this month – with growth of 6.2% – compared with 6.3% previously. This slightly weaker rate of growth reflects downgrades to our forecasts for the United States, Japan, the United Kingdom and Canada, marginally offset by an upgrade to our forecasts for the Euro-zone. Our global forecasts for 2022 and 2023 are unchanged (at 4.6% and 3.5% respectively).
- At this stage, our forecasts for India, China and Indonesia are unchanged, however risk appears weighted to the downside – particularly if China's measures to limit the spread of its current COVID-19 outbreak leads to a significant slowing in economic activity.

Sources: Refinitiv, IHS Markit, IIF, Our World in Data, NAB Economics.

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