EMBARGOED UNTIL: 11.30AM THURSDAY 16 SEPTEMBER 2021

THE FORWARD VIEW – GLOBAL

SEPTEMBER 2021

National Australia Bank

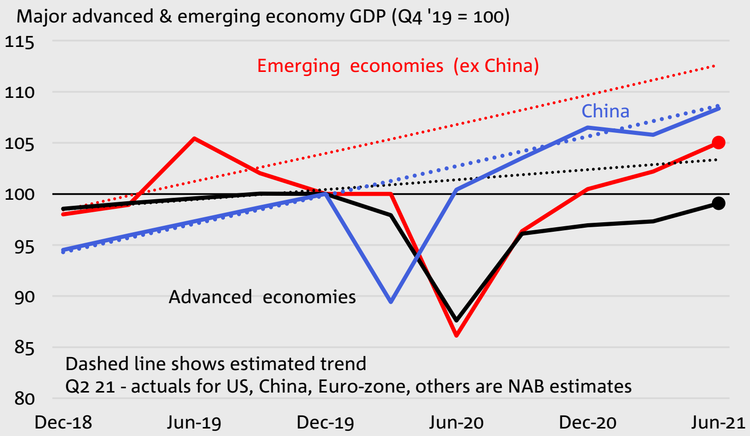
Strong economic growth in Q2 is set to falter in Q3

- The latest available GDP data showed strong growth in both advanced economies and emerging markets in Q2 2021. More recent indicators, such as purchasing manager indices, point to weaker conditions in Q3 – in a large part reflecting the impact of COVID-19 restrictions (particularly in China).
- COVID-19 remains the main risk to our global economic outlook, with emerging market economies more exposed to the risk of outbreaks due to their typically lower vaccination rates than advanced economies. The latest forecasts from the Economist Intelligence Unit suggest that much of Africa and South East Asia will not reach widespread vaccination coverage until 2023.
- Inflationary pressures have increased globally since late 2020 – in part due to supply chain disruptions, shortages of key inputs and rising commodity prices. This is also acting as a brake on the recovery. Although some of these pressures are temporary, some, such as the temporary shortages of semi-conductors, are likely to take some time to resolve. For now, major central banks are remaining on hold. Tapering and, in most cases, eventually ceasing asset purchases, will be the first stages towards normalising monetary policy, but it is likely to be some time before major central banks start to lift policy rates.
- Overall, we have revised down our global forecast to 6.0% for 2021 (from 6.2% in August) – reflecting weaker forecasts for China, India and, to a lesser extent, the US. Our forecast for 2022 is unchanged at 4.6% - with a stronger outlook for China and India offset by a weaker one for the US, Euro-zone and Japan – as is the forecast for 2023, at the long term average of 3.5%.

Global Growth Forecasts
(% change)

	2019	2020	2021	2022	2023
US	2.3	-3.4	6.0	4.1	2.1
Euro-zone	1.5	-6.5	5.2	4.0	2.1
Japan	0.0	-4.7	2.6	3.3	1.0
UK	1.4	-9.8	6.6	6.2	2.4
Canada	1.9	-5.3	5.5	4.0	2.5
China	6.0	2.3	8.7	5.9	5.7
India	4.8	-7.0	8.0	6.8	5.6
Latin America	0.1	-6.7	5.8	2.4	1.7
Other East Asia	3.5	-2.9	4.8	4.8	4.7
Australia	1.9	-2.4	3.3	2.9	2.3
NZ	2.4	-2.9	3.7	4.3	1.9
Global	**2.8**	**-3.3**	**6.0**	**4.6**	**3.5**

Excluding China, major economies have struggled to return to their earlier trend growth path



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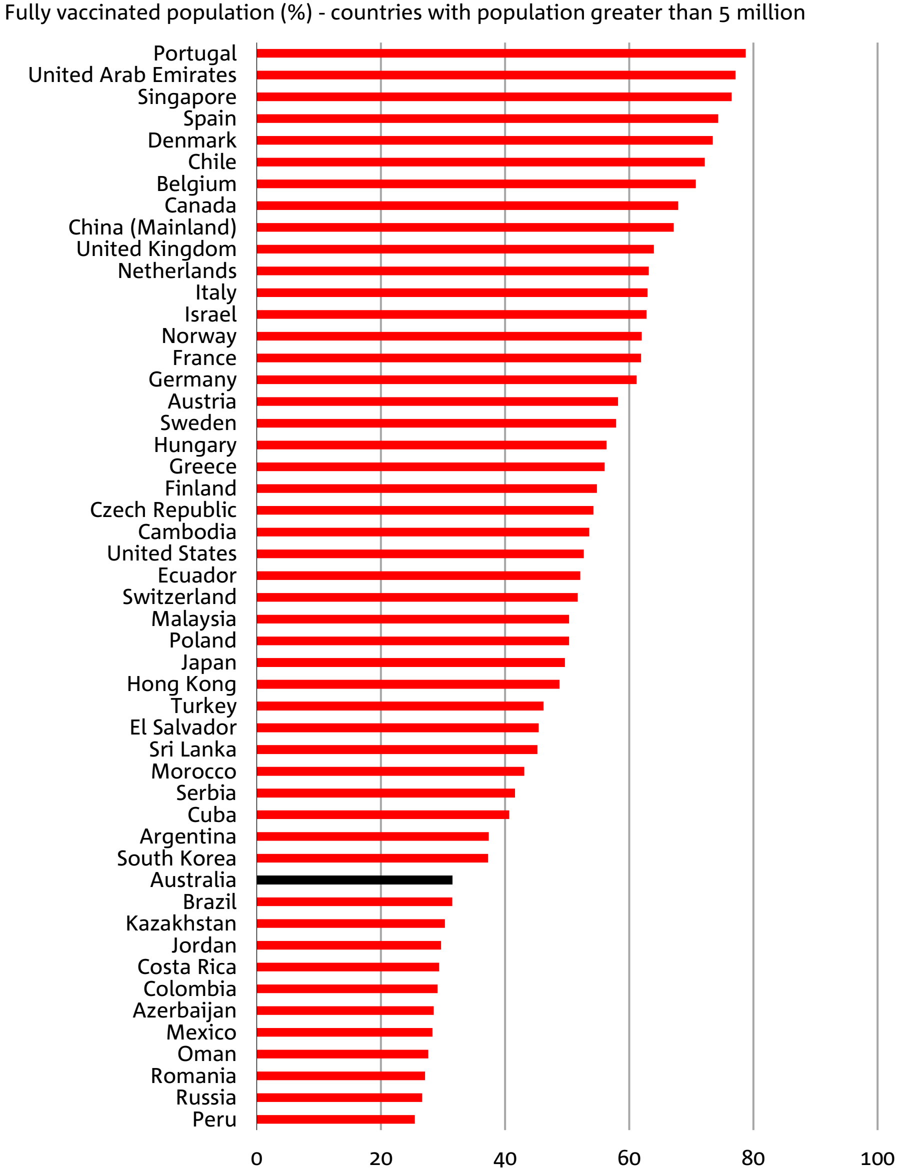
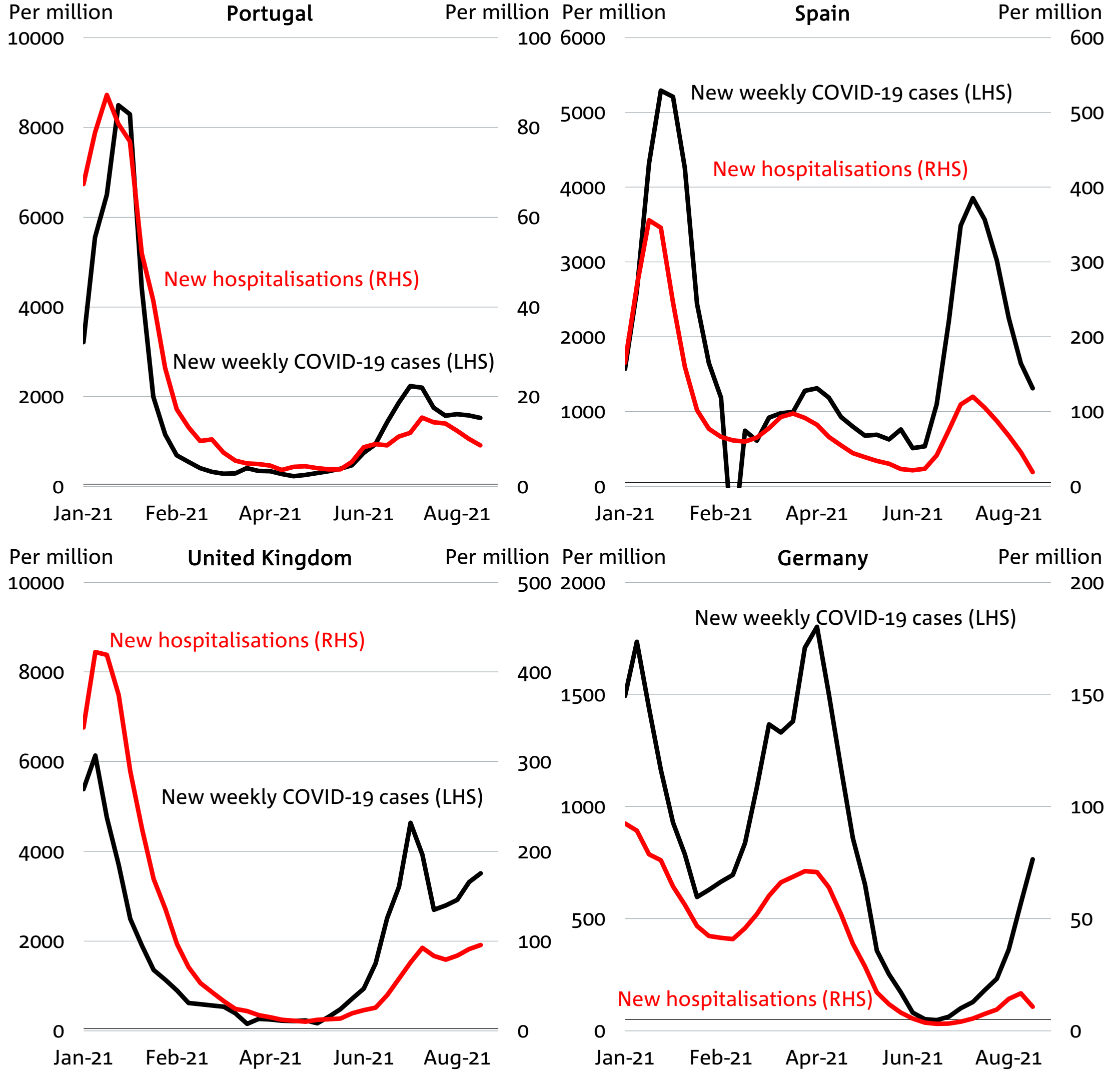
CHARTS OF THE MONTH

Global vaccine distribution remains highly uneven, with AEs generally having better access. Higher vaccinated countries showing a breakdown of the relationship between new cases and new hospitalisations – presenting a path to a post-COVID-19 world

Advanced economies generally have the highest rates of COVID-19 vaccination



Higher vaccinated countries starting to show a break between new COVID-19 cases and new hospitalisations



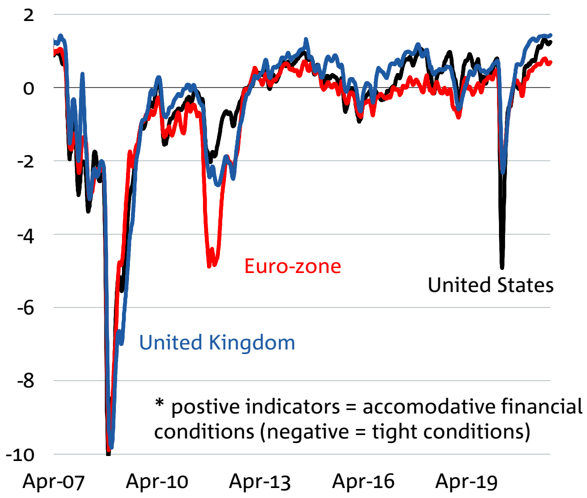
 Sources: Refinitiv, Our World in Data, NAB Economics

FINANCIAL AND COMMODITY MARKETS

Financial conditions positive, but central banks are starting to (or soon to start) winding back support

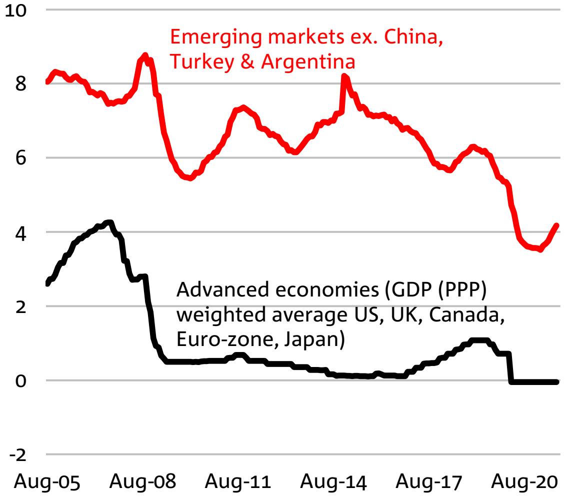
Financial conditions remain accommodative in AEs…

Financial conditions indices (rolling monthly average)*



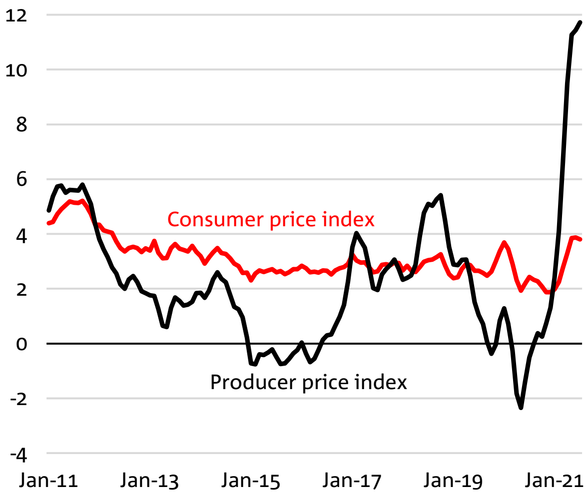
…with central banks keeping policy rates low

Average central bank policy rates (%)



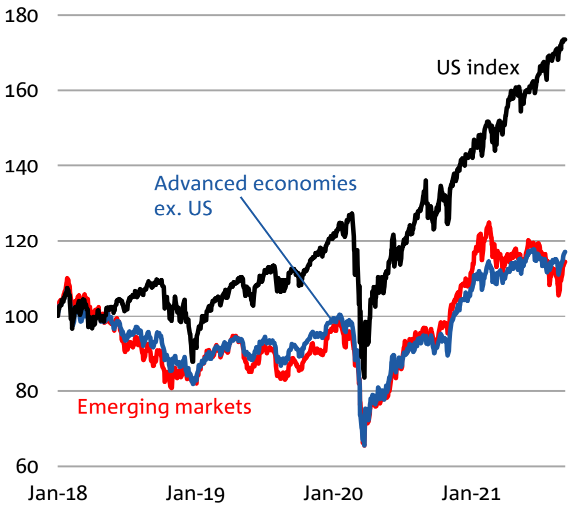
Too early to suggest that a peak in consumer price inflation

Global inflation (yoy%)



US equity markets diverge from others

MSCI Equity Indices (1 Jan 18=100)



- Financial conditions remain broadly positive – with monetary authorities generally providing an accommodative environment to underpin the economic recovery from COVID-19. Bloomberg's Financial Conditions Indices (which cover a range of advanced economies) have remained strongly positive since November 2020, in part reflecting the policy support from central banks.
- The majority of central banks have kept policy rates low since the start of the pandemic and a broad range have implemented unconventional measures. Despite rising inflationary pressures, advanced economy (AE) central banks have held rates steady, with some (such as the Bank of Canada) starting to taper asset purchases, with the Fed expected to follow soon. Some emerging market (EM) central banks have raised rates in recent months – including Brazil, Russia and Mexico – however they remain low compared with pre-pandemic levels. Tapering and, in most cases, eventually ceasing asset purchases, will be the first stage towards normalising monetary policy, but it is likely to be some time before major central banks start to lift policy rates.
- Inflationary pressures have increased globally since late 2020 – as supply chain disruptions, shortages of key inputs and rising commodity prices flowed through into higher producer prices and then into consumer prices. Although some of these pressures are temporary, some of these factors, such as the temporary shortages of semi-conductors, are likely to take some time to resolve. Our estimate of global consumer prices rose by 3.8% yoy in July (down from 3.9% yoy in June), however it is too soon to suggest inflation has peaked – particularly given that producer prices accelerated in July.
- Trends in global equity markets remained divergent in August. US equity markets (as measured by the US MSCI index) rose to fresh record highs in early September (continuing a trend evident since November 2020). In contrast, other AE equity markets have broadly tracked sideways since July (albeit with an uptick in early September). In contrast, EM equity markets are below peaks recorded in mid-February. While there has been a recent improvement – with prices up from mid-August cyclical lows – there are concerns that the unequal distribution of COVID-19 vaccines between advanced economies and emerging markets could result in capital being withdrawn from EMs.
- Global commodity prices have continued to trend higher, albeit the rate of increase appears to be slowing and there has been greater volatility in recent weeks – in part reflecting uncertainty around demand due to China's recent COVID-19 outbreak.

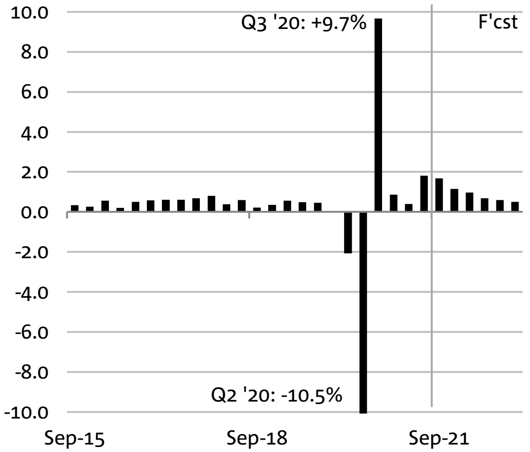
 Sources: Bloomberg, Refinitiv, NAB Economics

ADVANCED ECONOMIES

Major AE growth strong in Q2; supply disruptions/COVID waves suggest downside risk to a Q3 repeat

Overall major AE growth was strong in Q2

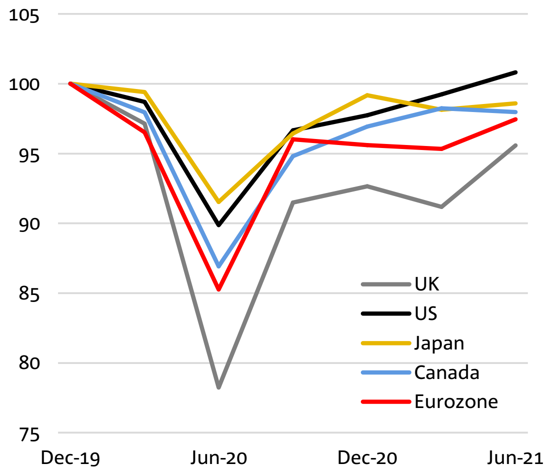
GDP growth - major AEs (q/q%)*



* US, Euro-zone, Japan, UK, Canada

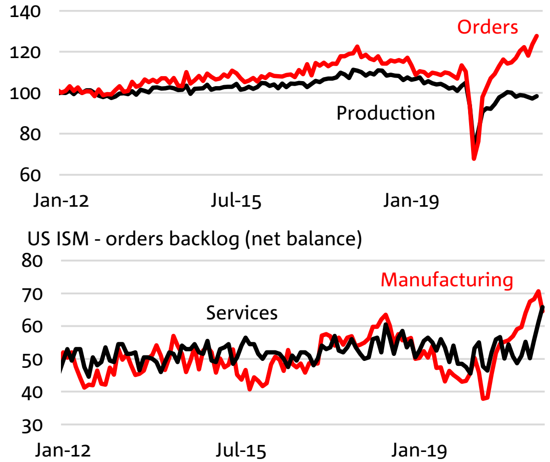
But with large divergences by region/country

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



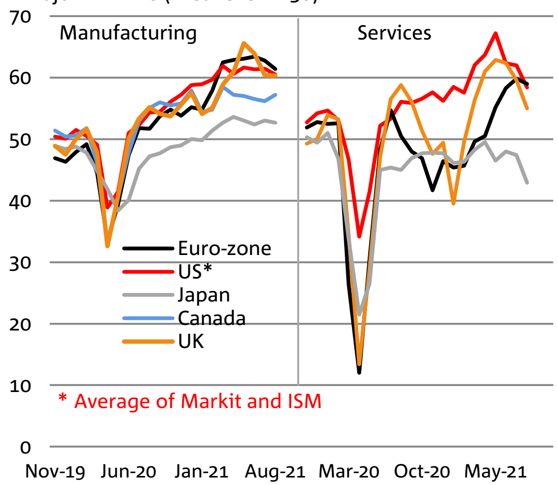
Further strong growth will require supply constraints to ease

Germany - manufacturing (Jan 2012 =100)



Surveys still solid but services PMIs have come-off

Major AE PMIs (Breakeven = 50)



- Major advance economy (AE) GDP grew strongly in Q2 (1.8% q/q), but with large differences across countries. We expect strong growth in the second half of 2021 (particularly Q3) but ongoing supply disruptions and high COVID-19 case numbers point to the risk that some of the forecast growth may be delayed. On the positive side, it appears the most recent COVID-19 wave may have peaked in the major AEs.
- Q2 growth was strongest in the UK (4.8% q/q), the Euro-zone (2.2% q/q) and the United States (1.6% q/q). For the UK and Euro-zone this was driven by the easing of COVID-19 activity restrictions (which had seen GDP fall in Q1). US growth was unchanged from the prior quarter not only due to easing restrictions but also substantial fiscal stimulus.
- Growth in Japan was more modest, but was higher than expected, at 0.5% q/q. This followed a fall in Q1 of -1.1%q/q, so overall the on-and-off again states of emergency have held the economy back. Canada, where GDP declined -0.3%q/q, also had lockdowns in March/April with a staggered re-opening from late May.
- While we expect aggregate major AE growth to slow from here, we still forecast strong growth in the second half of 2021. Whether this is realised or not will in part depend on how rapidly supply issues are addressed. Supplier delivery times have been elevated in the PMI surveys for a while but may have peaked, but order backlogs are still high. The car industry continues to feel the impact of a semi-conductor shortage. Toyota has announced a 40% cut in planned global production for September (but kept its annual target) and with cars hard to come by, there was an 11% fall in US auto sales in August.
- Also uncertain is how strongly households react to persistent COVID-19 headwinds. In Japan, the current state of emergency for 19 prefectures was recently extended to the end of the month. Even absent new restrictions, the increase in COVID-19 cases that started in early July in the US, early August in the UK and (more modestly) Canada may hold growth back Q3 growth, as it induces consumer caution about in-person activities and disrupts labour supply. However, daily new cases in the US and (more tentatively) the UK may have peaked, are now falling in Japan and have fallen in the European Union since late July.
- Services sector PMIs (outside of the Euro-zone), have fallen notably over recent months, likely reflecting the combination of on-going COVID-19 headwinds and a fading boost from the easing of restrictions. Manufacturing surveys generally remain elevated but, as noted above, supply issues will need to ease for this to translate into strong growth.

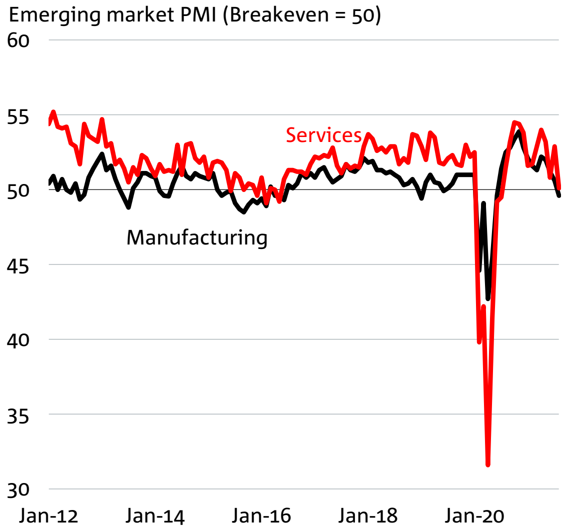
Sources: Refinitiv, NAB Economics

EMERGING MARKET ECONOMIES

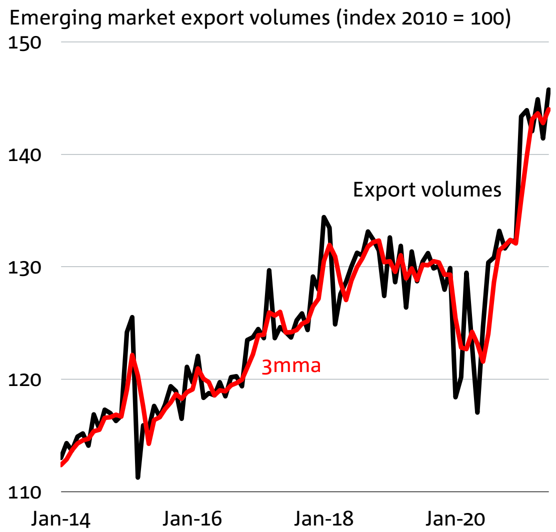
Strong growth in Q2 2021 looks set to fade; PMIs, exports and IP showing weaker trends

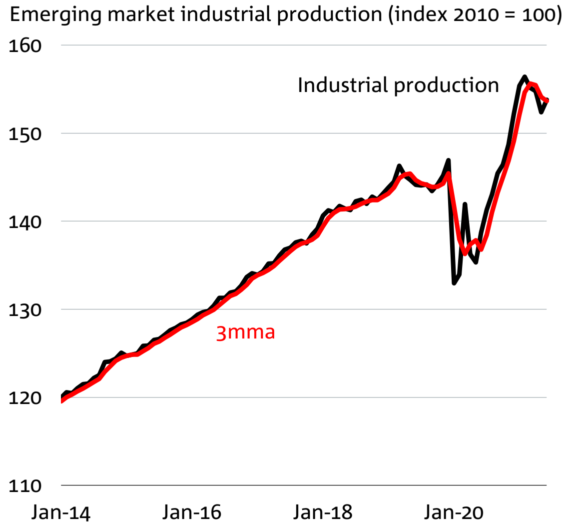
Strong economic growth in EMs in Q2…

…but PMI surveys suggest this strength will not continue in Q3



Year-on-year growth in EM export volumes and industrial production remains strong, but limited growth since early 2021





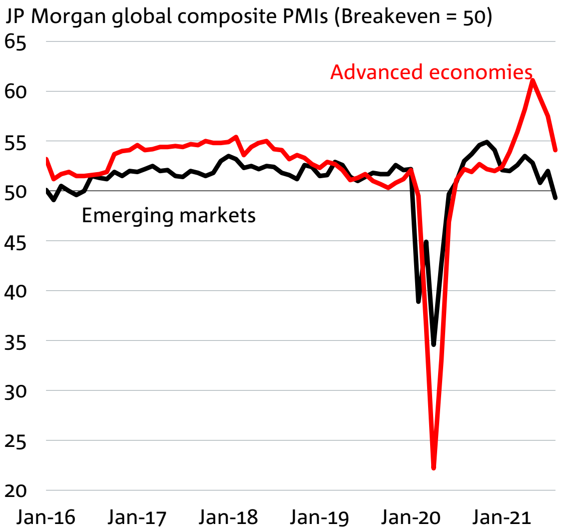
- Emerging markets grew strongly in Q2 2021 – with the five largest economies increasing by an estimated 11% yoy (albeit Russia's growth rate was unavailable at the time of writing). This increase was primarily driven by China and India, with more modest contributions from Brazil and our estimate for Russia.
- Although base effects contributed to this strength – with most emerging markets (excluding China) suffering a steep downturn in Q2 2020 due to measures to control the spread of COVID-19, quarterly growth data also strengthened. In quarter-on-quarter terms, growth rebounded strongly in Q2 – up 3.0%, compared with 0.2% in Q1 – with China the main driver.
- This strength appears unlikely to continue into Q3. Purchasing manager indices provide more up-to-date indicators of underlying conditions, with both manufacturing and services measures lower since recent peaks in April. The EM manufacturing PMI was at slightly contractionary 49.6 points in August (from 50.6 points previously). Both India and China recorded weaker outcomes in August – with the latter turning negative.
- There continues to be a stark difference within East Asian manufacturing PMIs, with strongly positive conditions for high tech producers such as South Korea, Taiwan and Singapore, and negative conditions for lower cost producers in the region.
- The downturn in the EM services PMI was larger – down to 50.1 points (from 52.9 points in July). China's outcome was particularly negative in August – in response to restrictions introduced to control its recent COVID-19 outbreak – while Brazil was moderately negative.
- Global trade and industrial production data are available to June 2021, and these continue to show impressive growth in year-on-year terms. Emerging market export volumes rose by 16.9% yoy in June, with growth led by China and East Asia, while other markets have only shown signs of growth in the most recent few months. A similar trend has been evident in industrial production.
- That said, this growth trend is largely driven by base effects. There has been limited growth in either export volumes or industrial production since early in 2021. Combined with the more negative COVID-19 trends for emerging markets (when compared with advanced economies), this points to weaker growth prospects for these economies in H2 2021.

Sources: Refinitiv, IHS Markit, CPB, NAB Economics

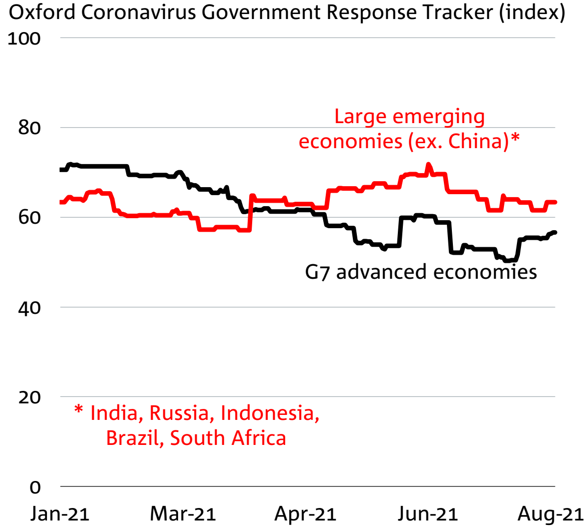
GLOBAL FORECASTS, POLICIES AND RISKS

Vaccine disparity impacting the growth prospects of different countries and regions

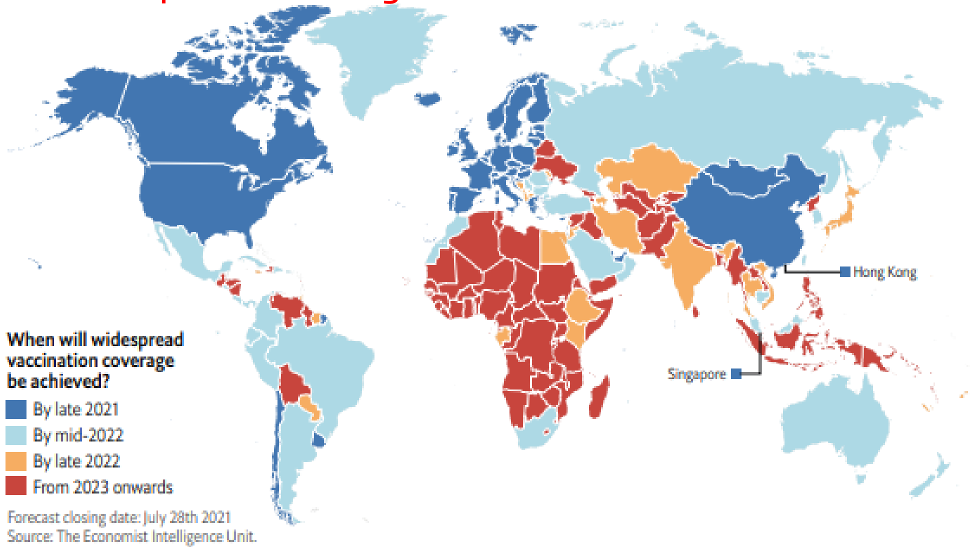
PMI measures point to weaker conditions in EMs



COVID restrictions trending lower in advanced economies



Ongoing delays to vaccine roll out, with some EMs waiting until 2023 for widespread coverage



- Global purchasing manager indices provide some of the most timely indicators of underlying economic conditions. The JP Morgan global composite PMI softened in August, down to 52.6 points (from 55.7 points in July). Although this was a result that is relatively positive, it masks some divergent trends between advanced economies and emerging markets – with the EM measure turning negative in August.
- We have revised down our forecast for global economic growth in 2021 – driven largely by a weaker outlook for the two largest emerging markets, along with a softer outlook for the United States.
- Chinese authorities rapidly imposed restrictions to control the spread of COVID-19 in mid-July. This resulted in a month-on-month slowdown in industrial production and retail sales in July. We have revised growth for China to 8.7% in 2021 (from 9.5% previously), with a modest upward revision for 2022 and 2023.
- India – the world's third largest economy on a purchasing power parity basis – recorded weaker than anticipated growth in Q2 2021, due to COVID-19 restrictions during the quarter. Although high frequency activity indicators – such as Google Mobility – suggest a subsequent recovery in activity, we have lowered our forecast for India in 2021 to 8.0% (from 9.0% previously), while we have slightly raised our forecast for 2022.
- COVID-19 remains the main risk to our global economic outlook, with emerging market economies more exposed to the risk of outbreaks due to their typically lower vaccination rates than advanced economies. The latest forecasts from the Economist Intelligence Unit suggest that much of Africa and South East Asia will not reach widespread vaccination coverage until 2023. Resulting supply disruptions may also affected AE growth.
- Higher vaccination rates in advanced economies has resulted in an easing in restrictions (when compared with the start of the year) – as measured by the Oxford Coronavirus Government Response Tracker. In contrast, while restrictions for large emerging markets (excluding China) are lower than recent peaks in June, they are essentially unchanged since the start of the year.
- Overall, we have revised down our global forecast to 6.0% for 2021 (from 6.2% in August). While we have revised up the growth outlook for China and India in 2022, this was offset by downgrades to the US, Euro-zone and Japan – meaning that our forecast for 2022 is unchanged at 4.6%. We continue to anticipate global growth easing to its long term average of 3.5% in 2023.

Sources: Refinitiv, IHS Markit, Our World in Data, Economist Intelligence Unit, NAB Economics

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