Prospects

Aperiodic – No. 21/002 – 6 December 2021

The point of view

Macroeconomic Scenario for 2021-2022: lasting scars after a chaotic recovery

After a persistently anaemic H1, vaccines and 'soft lockdown' strategies along with generous – and crucial – fiscal stimulus measures are opening the door to a modest yet, like the crisis, uneven recovery. This type of environment – marked by a slow, likely chaotic recovery; multiple uncertainties; and as easy a monetary policy stance as can be sustained – is good for keeping rates extremely low.

What will growth look like and how vigorous it will be? Will we still be governed by the pandemic and the trade-off between growth and health safety? It is a delicate bargain that we can only hope will be less radical than in 2020. Vaccines and 'soft lockdown' strategies are stirring hopes that growth can finally jump the 'stop-and-go' track of 2020. After a persistently anaemic H1, the recovery, nursed along by monetary and fiscal policy, is nonetheless expected to be modest and uneven. And then, the gradual reduction in stimulus plans will reveal the lasting scars of the economic shock wrought by this pandemic.

First off: a quick world tour by major geographic region. In the **US**, while the nature and timing of a new stimulus plan have yet to be defined, the resurgent virus is casting the shadow of a steep decline in H121. The acceleration expected for the second part of the year should lead to a recovery of 3.1% after 2020's limited contraction of 3.6%. At end-2021, GDP in volume terms is still expected to be slightly below its pre-crisis (ie, end-2019) level. In the **Eurozone**, where the consumer and corporate stimulus pipeline is expected to stay open, growth should hover around 3.8% after its 7.4% contraction in 2020. Based on structural features (including the sector breakdown of supply and jobs, the weight of services, export capacity and the suitability of exported products) and national strategies (the health/economy trade-off, how ample and effective the support measures are), both the extent of the shock and the speed and strength of the recovery will vary dramatically. Thus, at end-2021, although Eurozone GDP is still forecast at 2.4% below its pre-crisis level, the gap should be limited to 2.0% in Germany while remaining close to 7.4% in Spain and edging close to 2.2% and 3.9%, respectively, in France and Italy. In the **United Kingdom**, whether or not a minimum trade agreement is reached to prevent the hardest Brexit, the fallout of the pandemic will be joined by a de-nesting process. Following a major 2020 ontraction estimated at 11.1%, growth is expected to approach 4.5%, leaving GDP 3.8% below its pre-crisis level at end-2021.

In **emerging countries**, the economic recovery will be more difficult and more radically uneven than 2021 growth forecasts suggest. On the heels of a scant 3% contraction in 2020 should come a recovery of close to 5.6%. Behind this figure lies a very diverse landscape: an optical illusion masking both the immediate effects of the crisis, derived from stricter and more varied monetary and budgetary constraints than in the developed universe, and its lasting consequences in the form of a deepening structural gap between emerging Asian countries and the others. Asia, especially North Asia, has suffered less, and is preparing to rebound better, with China in the lead. In **China**, growth should once again approach 8% in 2021 after having paid only very modest dues in 2020, as it slowed to

2.6% while escaping the recession. So, can we count on China's energy to whip Asia into shape and get the rest of the world back on track, based on what happened in 2009? Well, no. As most of the catching-up has been exhausted, Chinese growth has slowed, and China no longer has the torque to tow the rest of the world behind it. In addition, it no longer wants to, as evidenced by its new 'dual circulation' strategy aimed at limiting its foreign dependence.

In essence, then, each will have to fall back on its own strengths: **the large economies will be further aided** by massive fiscal stimulus packages, ultra-accommodative monetary policies and favourable financial terms, which will also relieve emerging countries' external funding constraints. In response to the crisis, **the monetary levees have actually broken**, and accommodation seems to be nearly maxed out. And while some sacred cows may yet topple (eg, the assumption of negative rates in the UK, which cannot be ruled out), it does appear that the monetary policy easing exercise has come to an end (in the sense of new tools) and that we should count on improvements/extensions to existing mechanisms. Although these mechanisms seem to be calibrated for an end to the crisis, they will have to be supplemented by fiscal policy to consolidate the recovery, once the exceptional stimulus packages have been reduced. Looking at Japan, where monetary innovation went very far, we see that fiscal policy plays a more direct role in reducing the output gap. And the Bank of Japan supports it, acting as a 'built-in stabiliser' of long-term rates by controlling the yield curve.

This environment is marked by a slow, probably chaotic recovery; multiple uncertainties; and monetary policy easing: a good environment for keeping interest rates extremely low. Good news will have to materialise on both the health and the economic front for any recovery to take shape; but even then, it will be limited by the absence of inflation and the capacity surplus. In addition, past and future interest rate trends can only be judged on the basis of progress in the Eurozone, where clear solidarity has prevented fragmentation, risk premiums paid by the so-called peripheral countries have been reduced, and the EUR has done well. Therefore, our scenario puts end-2021 US and German ten-year sovereign yields at close to 1.25% and 0.40%, respectively, coupled with spreads of 20bp, 50bp and 100bp vs the German Bund yield for France, Spain and Italy. In line with a recovery scenario – even one that is timid and out of sync – the USD, that unbeatable counter-cyclical, could depreciate to the benefit of the EUR and currencies that are pro-cyclical or carried by risk appetite. The depreciation of the USD would, however, be limited by the resurgence of Chinese-American tensions weighing especially heavy on Asian currencies: the crisis has only temporarily eclipsed the dissensions between the US and China.

While the timetable for the 'resumption of hostilities' is uncertain (with the US transitioning to a new administration, putting out domestic fires, and rebuilding its international bridges), and while Joe Biden's presidency does promise a change in tone (less unilateral, more predictable and quieter!), the roots of American resentment remain. The bogus de-escalation of US-China trade tensions cannot hide the 'dislocation'. Rising protectionism and political risk went a long way towards slowing down hyper-globalisation. The crisis should do much to regionalise areas of growth, as evidenced by the signing of the Regional Comprehensive Economic Partnership uniting China, ASEAN member countries, and major US allies (Australia, South Korea, Japan and New Zealand). **This crisis has accelerated fragmentation and exacerbated weaknesses. It may also leave us with growing disparities in performance, growth outlook, and social indicators, especially in emerging countries.** ■

Catherine LEBOUGRE
catherine.lebougre@credit-agricole-sa.fr

Consult the publication: https://etudes-economiques.credit-agricole.com/en/Publication-EN/2020-Decembre/World-Macroeconomic-Scenario-for-2021-2022

Consult our last publications

Date	Title	Theme
22/12/2020	Germany – 2021-2022 scenario: growth hinges on containing the risks to health and expansionary fiscal policy	Germany
22/12/2020	France – 2021-2022 Scenario: What will the end of the crisis look like for France?	France
22/12/2020	Italy – Monthly News Digest	Italy
17/12/2020	United Kingdom – 2021-2022 Scenario: we are not out of the woods yet	UK
17/12/2020	World – Macroeconomic Scenario for 2021-2022: lasting scars after a chaotic recovery	World
17/12/2020	World – 2021-2022 Macroeconomic Scenario: economic and financial forecasts	World
17/12/2020	France – Residential real estate: Market resilient in the coronavirus pandemic	France, real estate
11/12/2020	France – Projecting GDP in this unusual crisis: a few words of explanation	France
10/12/2020	The lurking BEAST: the ECB's risk scenario and its implications	Eurozone
03/12/2020	How is the crisis affecting business?	Eurozone
26/11/2020	Update on emerging sovereign credit ratings	Emerging countries
18/11/2020	Central bank digital currency: an opportunity or a threat for banks?	Banks
10/11/2020	A short-lived upturn? Sketching out 2021	Eurozone
04/11/2020	United States: a crisis of legitimacy	United States

Crédit Agricole S.A. — Group Economic Research
12 place des Etats-Unis – 92127 Montrouge Cedex
Publication Manager and chief Editor: Isabelle Job-Bazille
Information center: Dominique Petit - **Statistics:** Robin Mourier
Contact: *publication.eco@credit-agricole-sa.fr*

Access and subscribe to our free online publications:
Internal Website: https://portaileco.ca-sa.adsi.credit-agricole.fr/en
Website: http://etudes-economiques.credit-agricole.com
iPad: Etudes ECO application available in App store platform
Android: Etudes ECO application available in Google Play