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Brian Davidson, CFA



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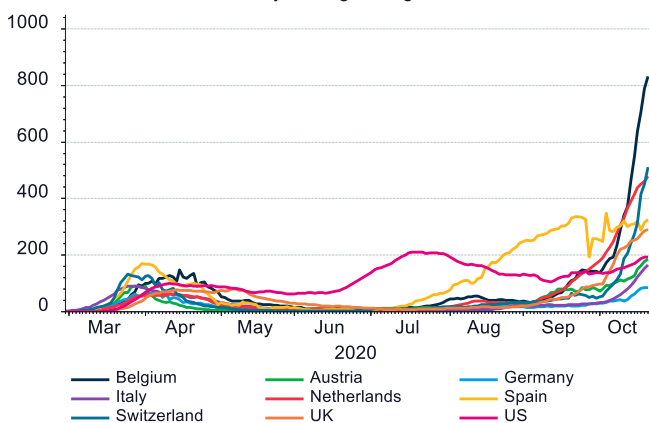
Headlines

- Case numbers are rising sharply in Europe, particularly in some smaller countries such as Belgium and Switzerland
- Localised lockdowns are being imposed in some regions of Europe, which will slow economic growth, although our central case remains that global activity will return to pre-COVID levels early next year
- China's Q3 data confirm that, officially, a V-shaped recovery is complete, while the details point to somewhat more balanced growth than in Q2 (notwithstanding the usual doubts about the accuracy of official Chinese economic data)

It is now more than seven months since the World Health Organisation declared the coronavirus outbreak a global pandemic, yet many uncertainties remain, ranging from exactly how the virus is transmitted to what the correct policy response should be. A lot of energy and column space has been dedicated to these issues; and indeed, the lack of certainty is exacerbating political disagreements, reflected in the standoff between central UK government and the mayor of Greater Manchester. The 'Interesting Reading' section of today's *Recovery Watch* contains an article about k (a measure of whether the virus is spreading in a steady manner or dispersing in big bursts via super-spreader events), and how more focus on this and less focus on R_0 could lead to more effective policy responses. But ultimately, the focus of our analysis is what *will* happen and not what *should* happen - and the related economic consequences.

COVID-19 new daily cases, Europe and US

Per million residents, seven-day moving average



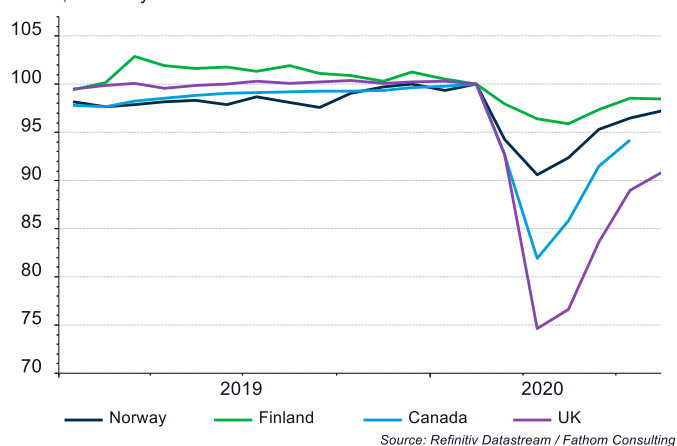
Source: Refinitiv Datastream / Fathom Consulting



So far, the economic recovery has been about as V-shaped as could have been expected in many places (see the chart below, for those countries that report monthly GDP). But the recent spike in cases in Europe — and subsequent increase in localised lockdowns (with national lockdowns not ruled out) — increase the possibility of the final stages of a V-shaped recovery not materialising, or indeed the prospect of another letter forming. But there are three reasons we are sticking with a V (or at least a V drawn by someone with a shaky hand) as our central case for now. First, new restrictions are likely to be less onerous than they were in Q1 and Q2 this year. Second, many people have adapted their routines to live with lockdown measures (i.e. find ways to work from home and to consume despite restrictions). Third — and this one is key — government support packages remain generous.

Monthly GDP outturns

Index, February 2020 = 100



Of course, a further rise in new case numbers and restrictions will lead to more business closures and an increase in unemployment (reflected by the first chart below), but fiscal support packages, should they materialise, will not only soften the blow, they will create pent-up demand for spending next year (second chart below, which shows the bump in post-transfer income in the US earlier this year). We will be keeping a close eye on developments, including case numbers, government restrictions and offsetting support measures, and will be updating our forecasts accordingly.

US unemployment, permanent job losers

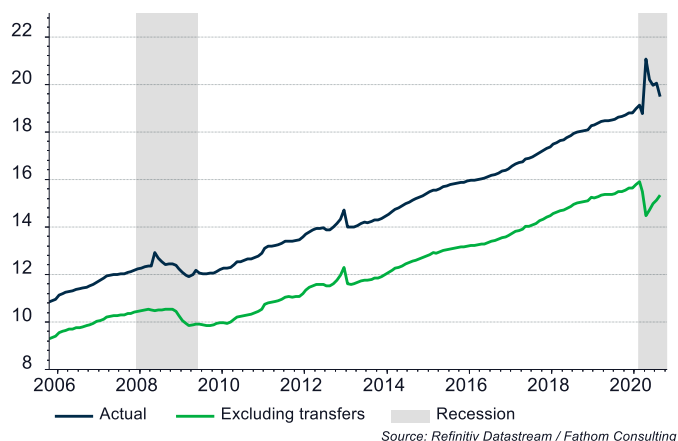
Thousands





US personal income, annualised rate

USD, trillions, current prices



China was one of the first nations to reveal its Q3 GDP this week, reporting a strong annual growth rate of 4.9%, up from 3.2% in Q2. This outturn was slightly below consensus, but it accompanied a flurry of other strong data points for September, such as retail sales (which rose 3.3% in the twelve months to September). China had reported solid growth in Q2. We suspect that not only was that overstated, but a large amount of the growth was through government-directed spending rather than underlying demand. The Q3 figures suggest however that consumer demand is returning and that the recovery is gaining traction — the usual caveats over the accuracy of official Chinese data notwithstanding. Our measure of Chinese economic activity — the CMI 3.0 (blue line in the chart below) — suggests that annual growth was a more modest 3.4% in September (and 1.8% in Q3 as a whole), although this is still an impressive outturn.

Fathom CMI 3.0 and GDP

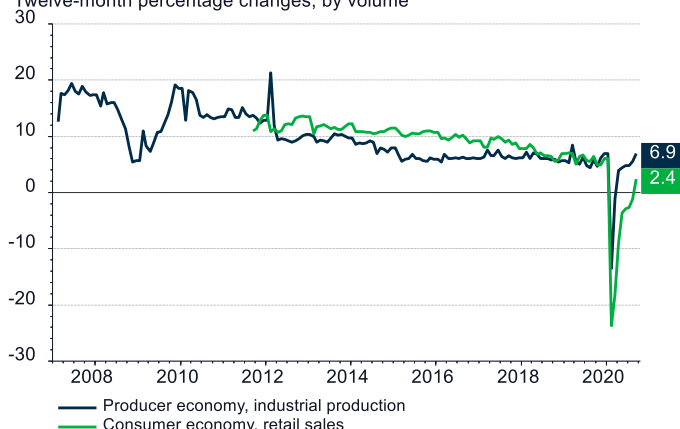
Four-quarter percentage changes





China's uneven recovery

Twelve-month percentage changes, by volume



Source: Refinitiv Datastream / Fathom Consulting

A less positive aspect of China's GDP print (at least from a sustainability perspective) was the increase in real estate investment growth, which was 5.6% higher in the first three quarters of 2020 relative to the same period last year. This was significantly higher than total investment, which climbed 0.8% over the same period. China's housing market is suffering from huge overcapacity, which is reflected by the time taken to finish construction (one of our suite of proprietary indicators) below. The jobs market in China has also shown elements of improvement according to official figures revealed this week, with the surveyed unemployment rate falling to 5.4% in September¹, from 5.6% in August. Nevertheless, the underemployment rate is likely to be far higher, a point reflected by another one of our proprietary indicators, the CUUI (China Urban Underemployment Indicator).

China time taken to finish construction

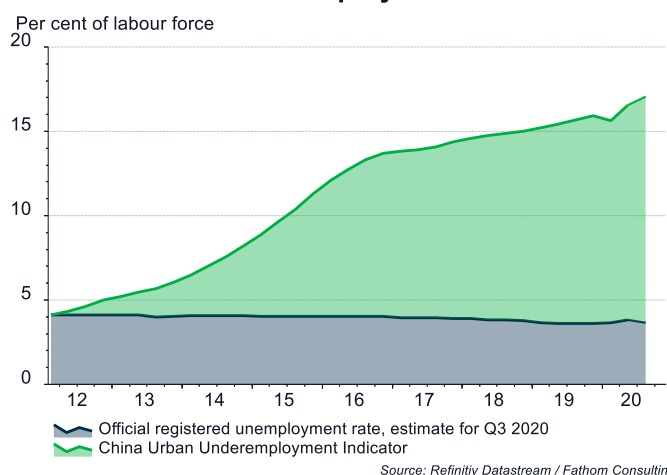
Years, seasonally adjusted



Source: Refinitiv Datastream / Fathom Consulting



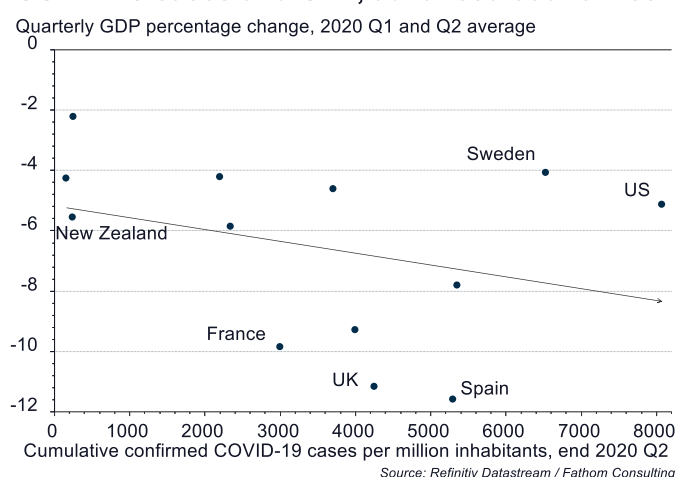
China's Urban Underemployment Indicator



Declining unemployment and solid economic growth in the world's second largest economy is clearly positive for global demand, but China's economic performance is unlikely to be particularly useful for predicting the outcome in other countries, due to: a) structural differences between their economy and those in other countries, and b) the fact that China seems to have got the virus under control while many other large economies have not.

Finally, in a speech this week Dr Gertjan Vlieghe, an external member of the Bank of England's MPC, dismissed the notion that there was a trade-off between economic performance and public health. He cited evidence that most of the damage to the economy was due to voluntary behaviour changes and not government-mandated changes, and that voluntary changes to behaviour were related to the spread of the virus in the community (see 'Interesting Reading' for more information). It is hard to see any clear evidence to support Dr Vlieghe's point in the first two quarters of this year in the charts below — in advanced economies, the relationship between confirmed COVID case numbers and economic outcomes is very weak at best, while in emerging markets there is a weak relationship, but in the opposite direction (i.e. lower case numbers are consistent with worse economic outcomes). Our own analysis has found that changes in behaviour have greater explanatory power for changes in GDP than do restrictive policy measures.

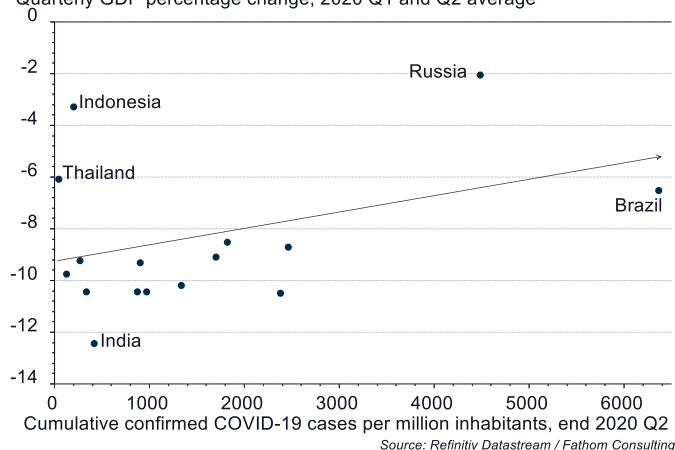
COVID-19 cases and GDP, advanced economies





COVID-19 cases and GDP, emerging markets

Quarterly GDP percentage change, 2020 Q1 and Q2 average



[1] China reports two unemployment rates - a 'surveyed' rate and a 'registered' rate. The registered rate tends to be lower than the surveyed rate and is reported with a lag. The CUUI chart uses registered unemployment rate

Interesting reading

- How greater focus on the variable k may be a smarter approach to fighting COVID: <https://www.theatlantic.com/health/archive/2020/09/k-overlooked-variable-driving-pandemic/616548/>
- Speech by MPC external member Dr Gertjan Vlieghe assessing the pandemic's impact on the UK economy: <https://www.bankofengland.co.uk/speech/2020/gertjan-vlieghe-speech-assessing-the-health-of-the-economy>
- A lengthy critique of Sweden's handling of the virus: <https://time.com/5899432/sweden-coronavirus-disaster/>
- Tensions emerge between Zambia and China over debt repayment: <https://www.ft.com/content/aa43fb1c-8f44-495a-a9b5-69a00c7db4a9>

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29 October 2020 - 4:00PM GMT

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Fathom Consulting
47 Beviden Street
London
N1 6BH
Tel: +44 (0)20 7796 9561



Contact information
brian.davidson@fathom-consulting.com
0203 879 9813
www.fathom-consulting.com

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