REOPENING THE WORLD: BEWARE OF FALSE STARTS

Economic, Capital Markets and Industry Research

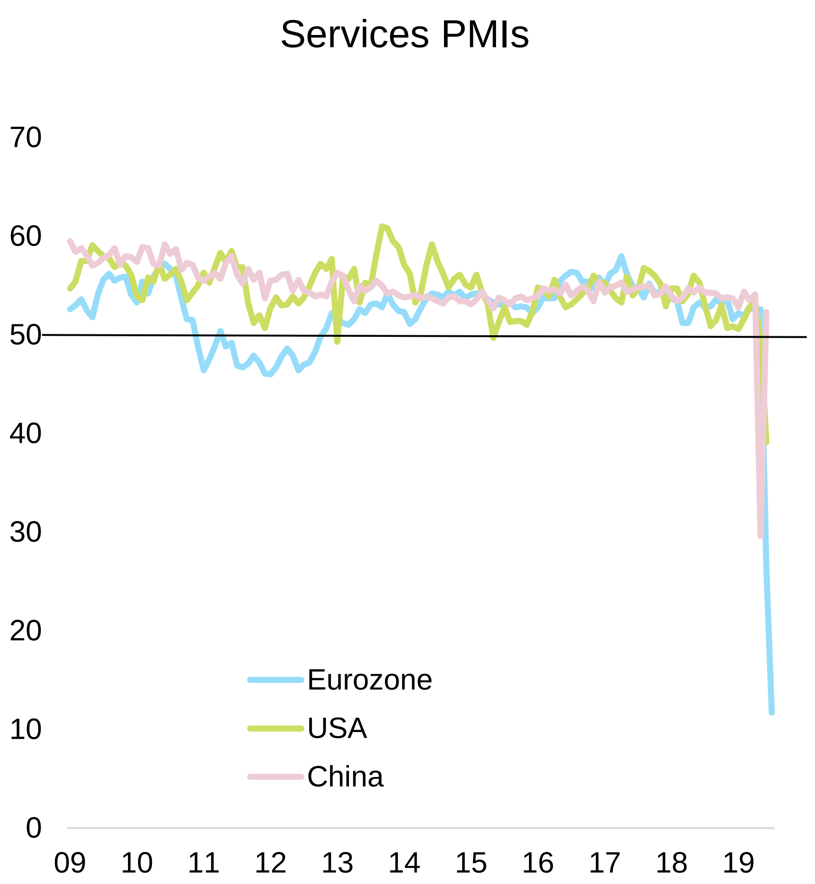
Global Economic Outlook

as of April 2020

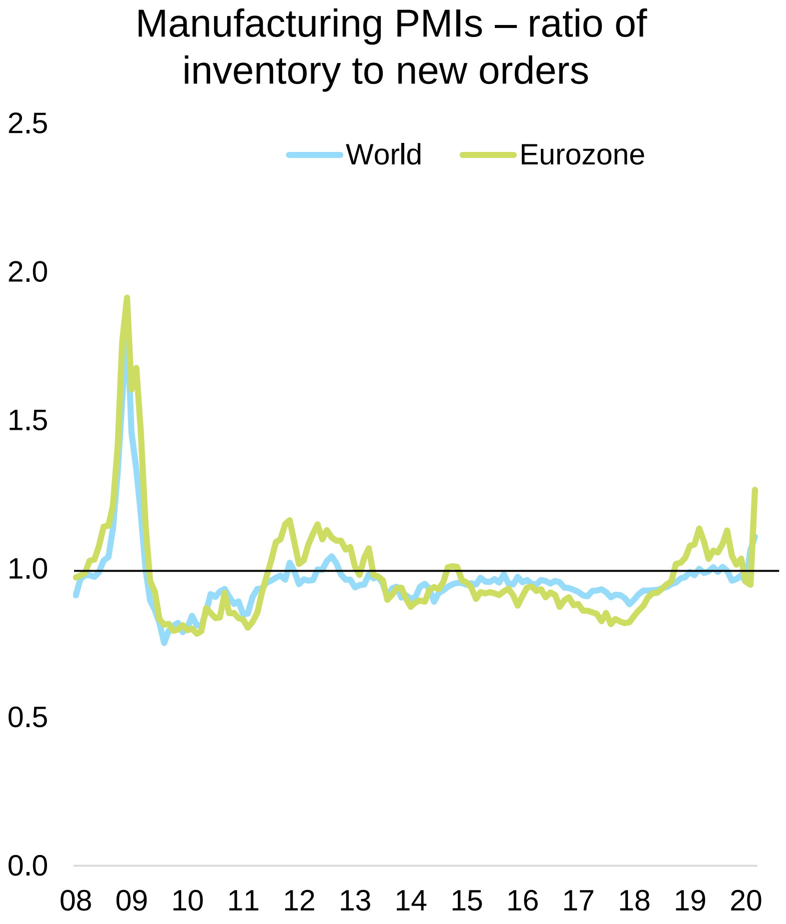
EULER HERMES

Allianz

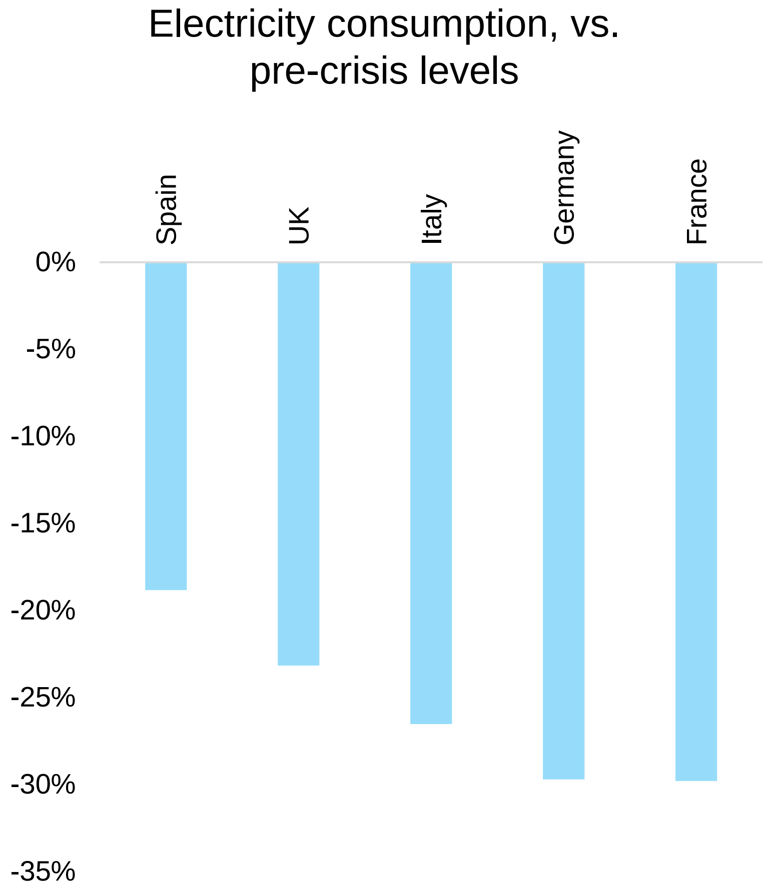
COVID-19: AN UNPRECEDENTED SHOCK (1/2)



Sources: Markit, Allianz Research



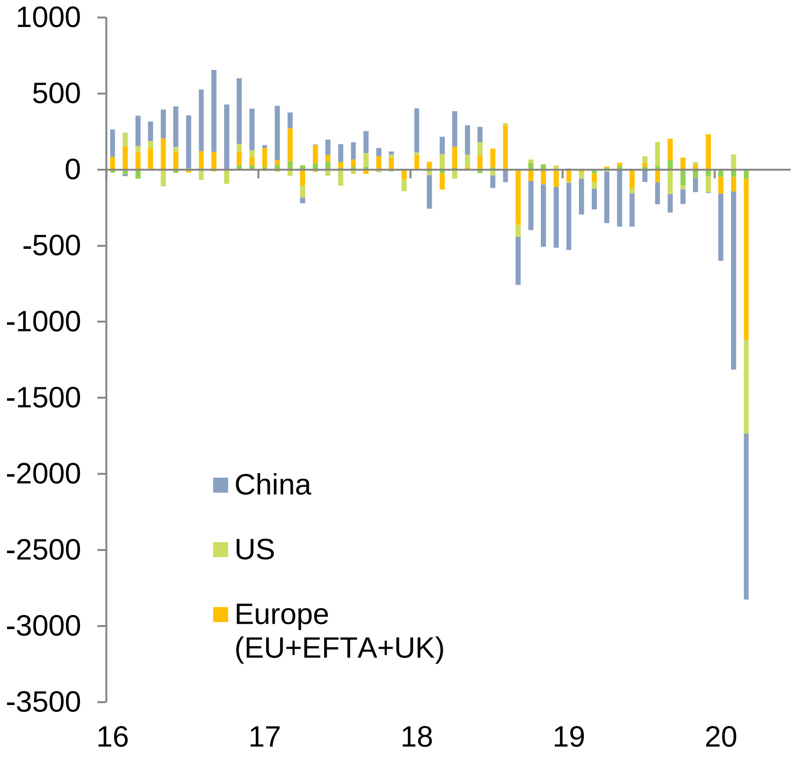
Sources: Markit, Allianz Research



Sources: Macrobond, Entso-e, Allianz Research

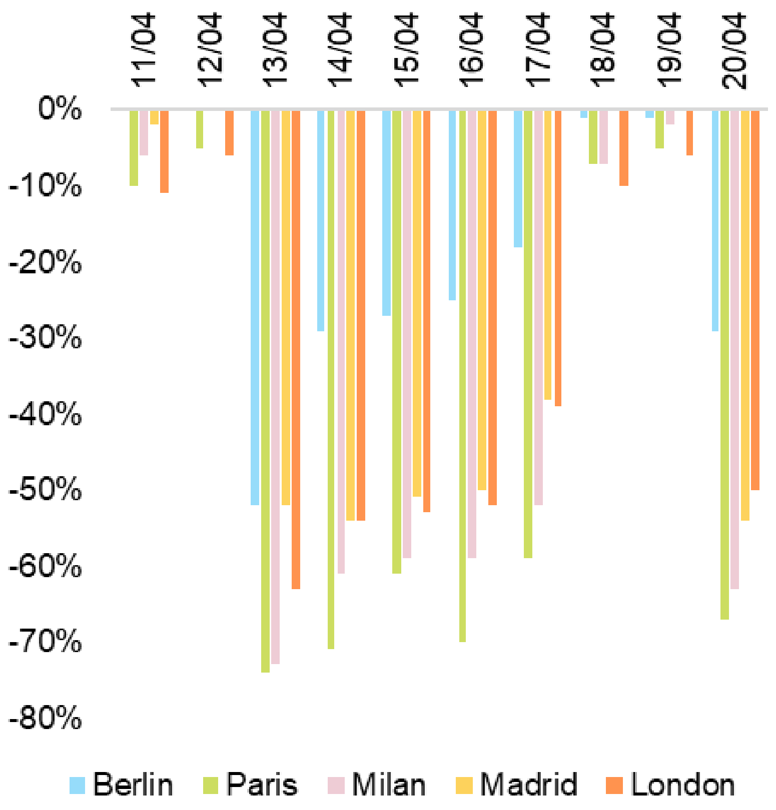
COVID-19: AN UNPRECEDENTED SHOCK (2/2)

Monthly car sales, annual change, ‘000



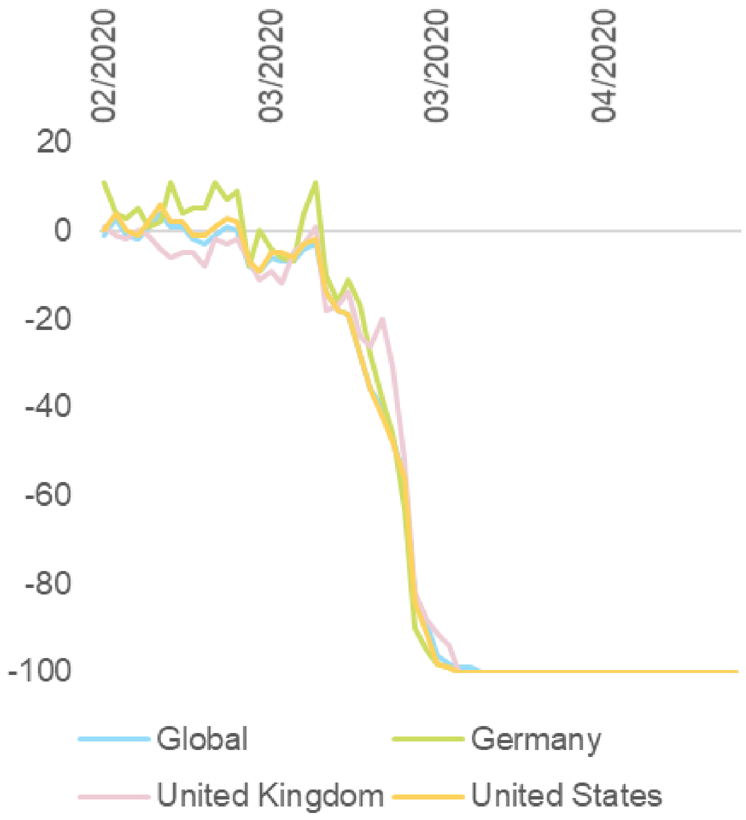
Sources: national sources, Allianz Research

Current traffic congestion vs 2019 average value



Sources: TomTom, Euler Hermes, Allianz Research

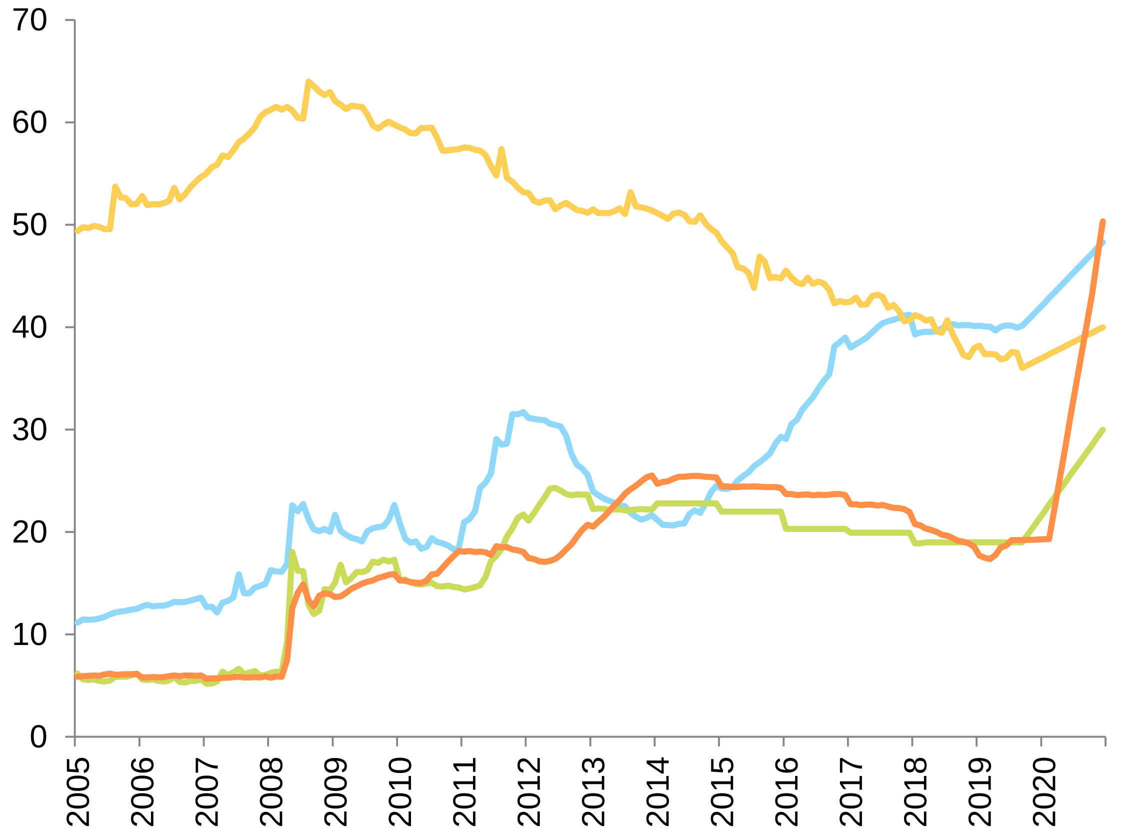
Seated Diners (y/y)



Sources: OpenTable, Euler Hermes, Allianz Research

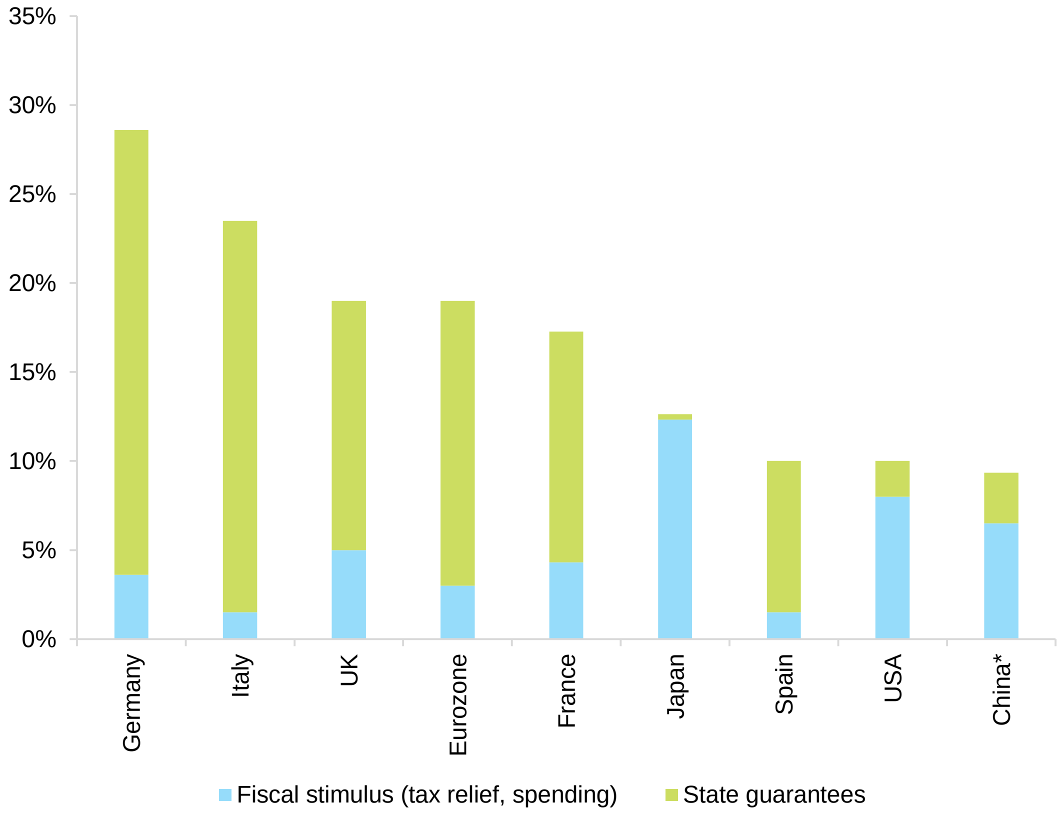
INITIAL RESPONSE: POLICY MAKERS' BAZOOKA

Central Bank balance sheets (% of GDP)



Sources: Official sources, Euler Hermes, Allianz Research

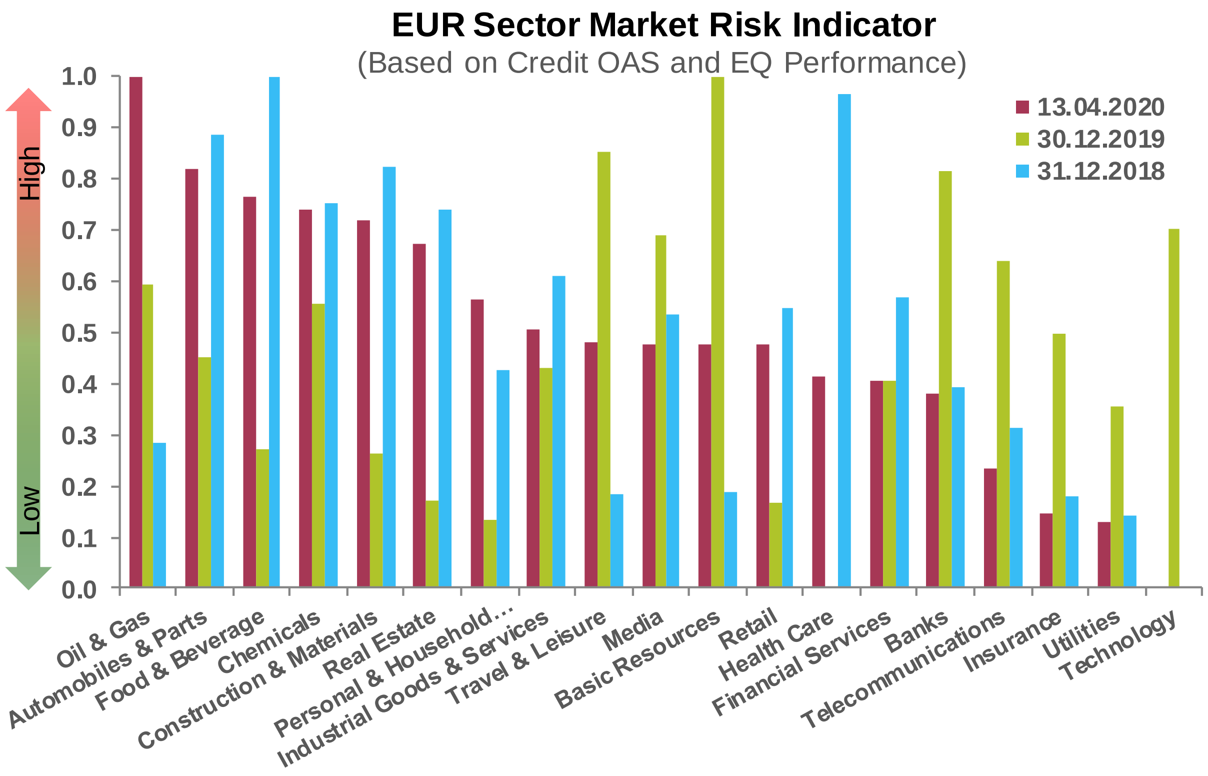
Fiscal policy: stimulus vs. State guarantees (% GDP)



** Total expected, and liquidity injections instead of State guarantees (the latter-one not being straightforward to estimate given the structure of the economy).*

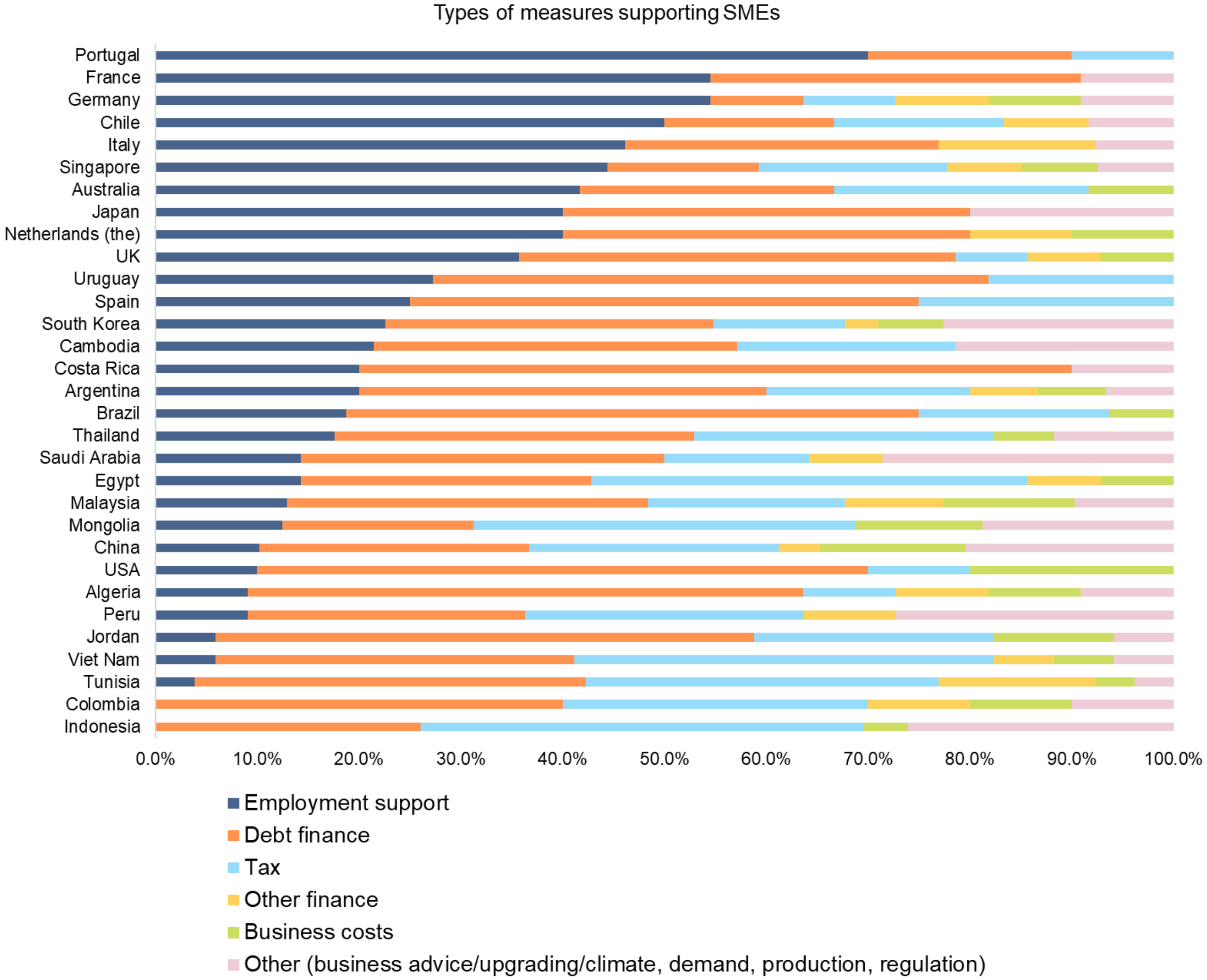
Sources: Official sources, Euler Hermes, Allianz Research

LIQUIDITY SHOCK: FOCUSING ON COMPANIES NEEDS, LARGE AND SMALL



In EUR terms, Oil & Gas and Automobiles & Parts have been the biggest losers of the Covid-19 pandemic. Consequently and according to their market performance both Equity and Credit markets keep considering both sectors as being the riskier sectors to invest. On the other end of the risk spectrum, Technology remains the safe haven sector with its recent re-risking being less pronounced than its peers.

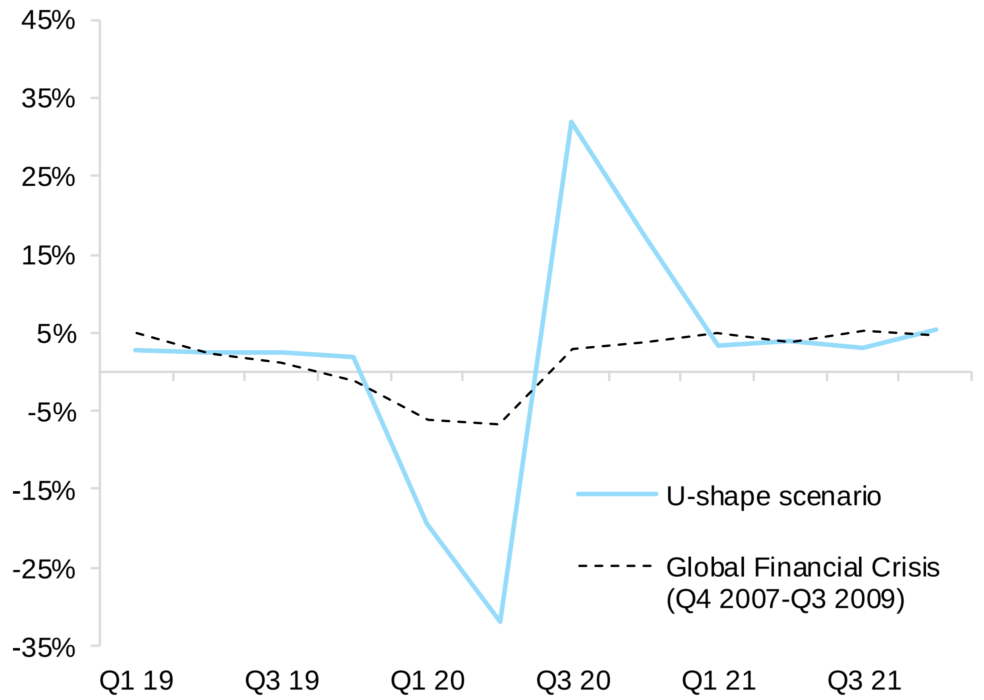
Sources: IHS, Allianz Research



Sources: World Bank, Euler Hermes, Allianz Research

THE GREAT LOCKDOWN: TWICE AS BAD AS THE 2009 GLOBAL FINANCIAL CRISIS

Global real global GDP growth, q/q annualized



Sources: Euler Hermes, Allianz Research

We expect the supply and demand shocks, especially through confinement measures, to push the global economy into recession in H1 2020 (4x the trough seen during the global financial crisis). We expect a U-shape recovery thereafter, supported by stimulus measures.

Real global GDP growth, annual, %

	2017	2018	2019	2020	2021
World GDP growth	**3.3**	**3.1**	**2.5**	**-3.3**	**5.6**
United States	2.4	2.9	2.3	-2.7	3.3
Latin America	**1.0**	**1.0**	**0.1**	**-4.1**	**3.7**
Brazil	1.3	1.3	1.1	-5.0	5.5
United Kingdom	1.8	1.3	1.4	-8.2	8.7
Eurozone members	**2.7**	**1.9**	**1.2**	**-9.3**	**9.3**
Germany	2.8	1.5	0.6	-8.9	8.7
France	2.4	1.7	1.3	-8.9	9.6
Italy	1.7	0.7	0.3	-11.4	11.0
Spain	2.9	2.4	2.0	-11.0	10.0
Russia	1.6	2.3	1.3	-2.5	5.2
Turkey	7.5	2.8	0.9	-3.3	7.6
Asia-Pacific	**5.2**	**4.7**	**4.3**	**-0.6**	**6.5**
China	6.9	6.7	6.1	1.8	8.5
Japan	2.2	0.3	0.7	-5.7	2.2
India	7.3	6.2	5.0	1.1	7.5
Middle East	**1.2**	**1.1**	**0.6**	**-4.5**	**2.4**
Saudi Arabia	-0.7	2.4	0.2	-2.0	2.0
Africa	**3.1**	**2.7**	**1.9**	**-1.6**	**3.6**
South Africa	1.4	0.8	0.3	-5.3	4.5

** Weights in global GDP at market price, 2019*

NB: fiscal year for India

Sources: Euler Hermes, Allianz Research

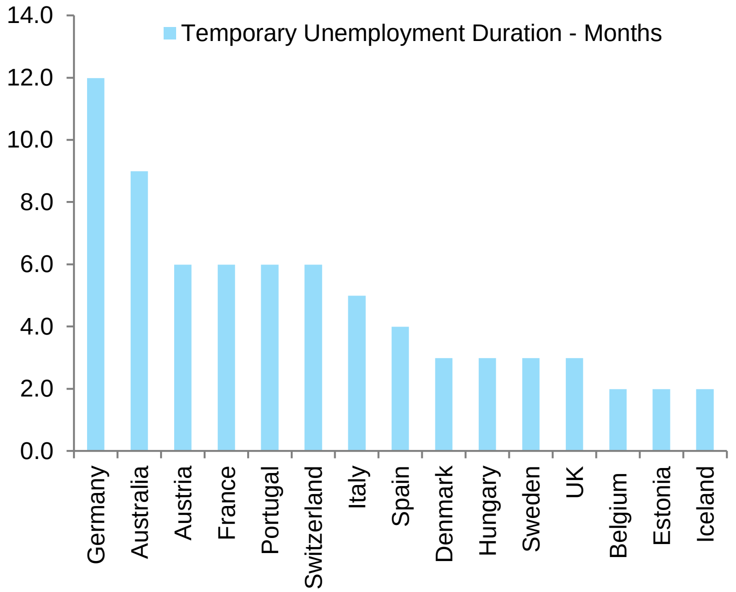
UP TO ONE THIRD OF PROTECTED JOBS TO BE LOST

Employment at risk and cost for public finances

Cost of *Kurzarbeit* from 65% to 84% of wages depending on the country	Compensation (incl. employer social contributions, EUR bn) at risk	Full time-jobs at risk in Million
Germany	34	12
France	43	11
Italy	29	9
Spain	18	8
UK	37	13
Belgium	8	2

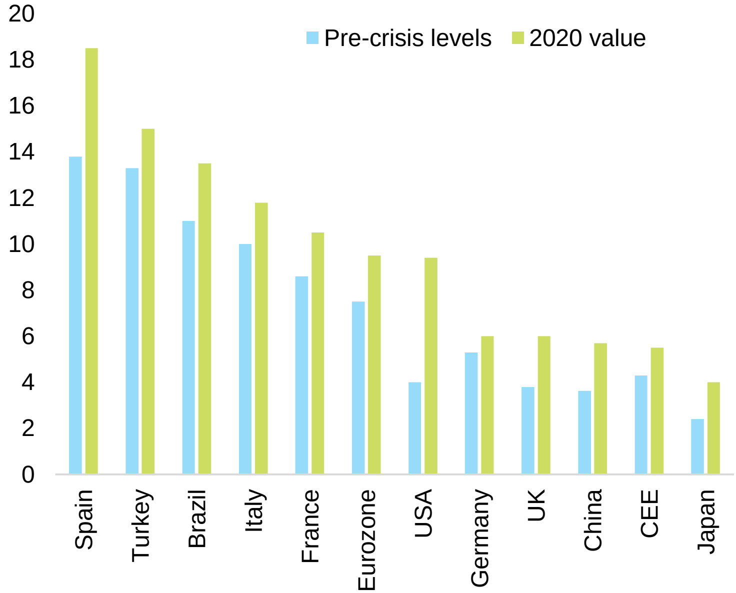
Sources: Eurostat, Euler Hermes, Allianz Research

Duration of temporary unemployment benefits



Sources: Euler Hermes, Allianz Research

Unemployment rates, %



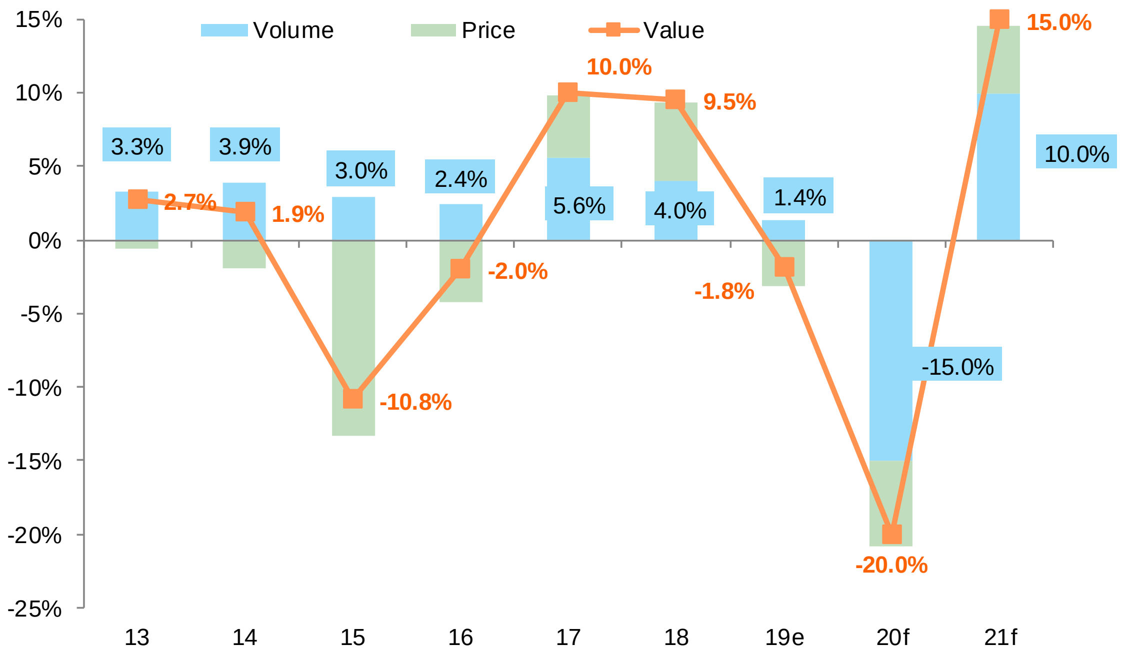
Sources: Euler Hermes, Allianz Research

A lockdown is estimated to shutdown 40% of the economy and hence put jobs at risk given the temporary pause of activity. We estimate 40 million people to be in need for partial unemployment benefits in the four biggest Eurozone countries.

We estimate that up to one third of partial unemployed would become unemployed by year-end due to the very gradual reopening of the economies will mean fixed costs would need to be reduced by companies, notably those in sectors where deconfinement is very slow. Hence, we estimate the Eurozone unemployment rate to rise by +2pp to 9.5% in 2020

GLOBAL TRADE: USD3.5TN LOSS IN 2020 AND PROTECTIONISM RELOADED

Global Trade growth in volume and value (%, y/y)



Sources: IHS Markit, Euler Hermes, Allianz Research

We expect two quarters of recession in trade in goods and services (Q1 and Q2) which will bring the annual figure to -15% in 2020. In value terms, plummeting commodity prices and a stronger USD will weigh on prices.

Protectionism will be a key feature of the life after Covid-19

Shorter supply chains likely to be in focus in the coming year

Rules on foreign investment likely to get tighter

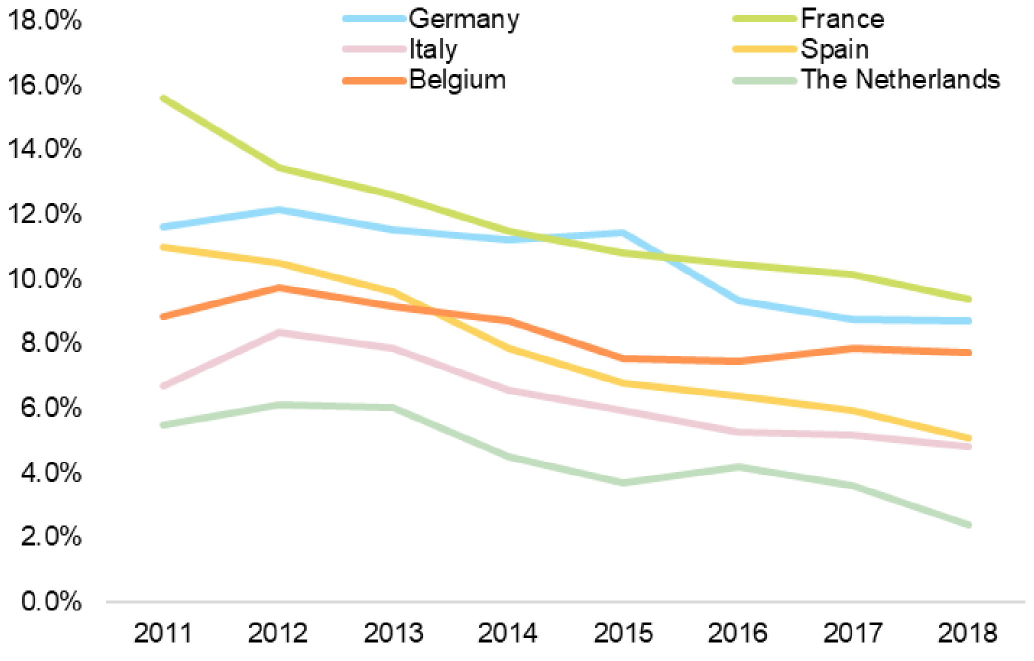
Nationalization are considered where necessary (air transport, banks…)

Sources: Euler Hermes, Allianz Research

UNCTAD predicts a drop in global FDI flows by up to -40% over 2020-2021. In addition, several FTAs (incl. with the UK) are likely to be delayed.

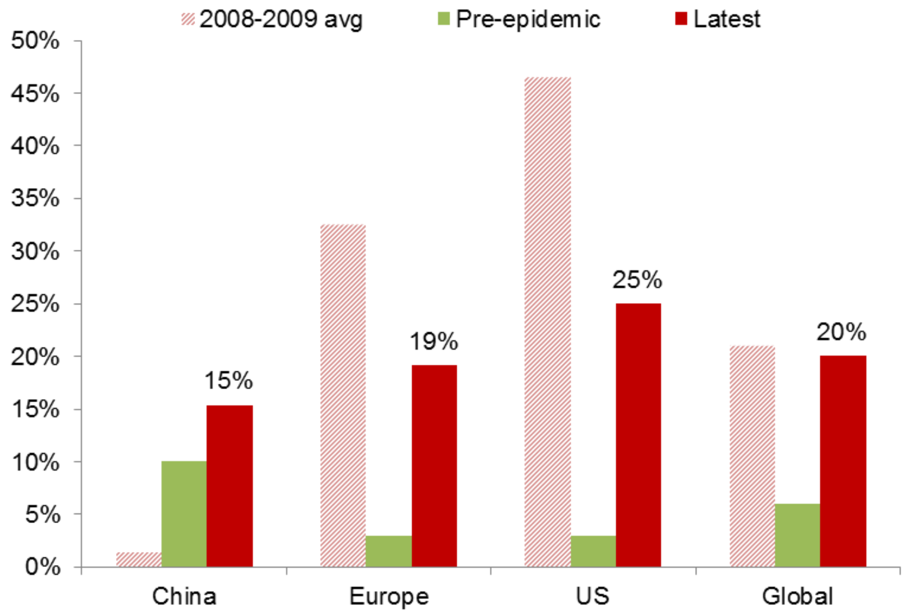
DESPITE UNPRECEDENTED SUPPORT, INSOLVENCIES ARE SET TO INCREASE BY +20% IN 2020

Share of SME & MidCaps at risk (close to zombies), % of total



Sources: Euler Hermes

2020 re-forecasts – selected key countries and region



Sources: national statistics, Euler Hermes, Allianz Research

We find that more than 13,000 SMEs & MidCaps (7% of total) in the six biggest Eurozone countries are at risk of going bust after persistent low profitability and turnover growth. We find that more than EUR500bn of turnover (or 4% of Eurozone GDP) could be at risk.

Final figures still depend on (i) the timing and magnitude of other policy measures yet to announced and (ii) the potential closures of business courts (which would create lags and delays in official registrations of liquidations and restructuring procedures).

HAPHAZARD OPENING: CARING, TESTING AND MONITORING CAPACITIES WILL BE ESSENTIAL

Deconfinement analytical framework

Initial conditions

1. **Readiness**, from a health sector and virus spread perspective. This includes the virus spread momentum, medical capacity, testing capacity, the use of technology tracing early on.
2. **Economic vulnerability** to prolonged confinement: GDP and employment structure (services, industry…), growth momentum, % of tourism in GDP, reliance on foreign labor, density of population in cities, political pressure, informality

Deconfinement strategy

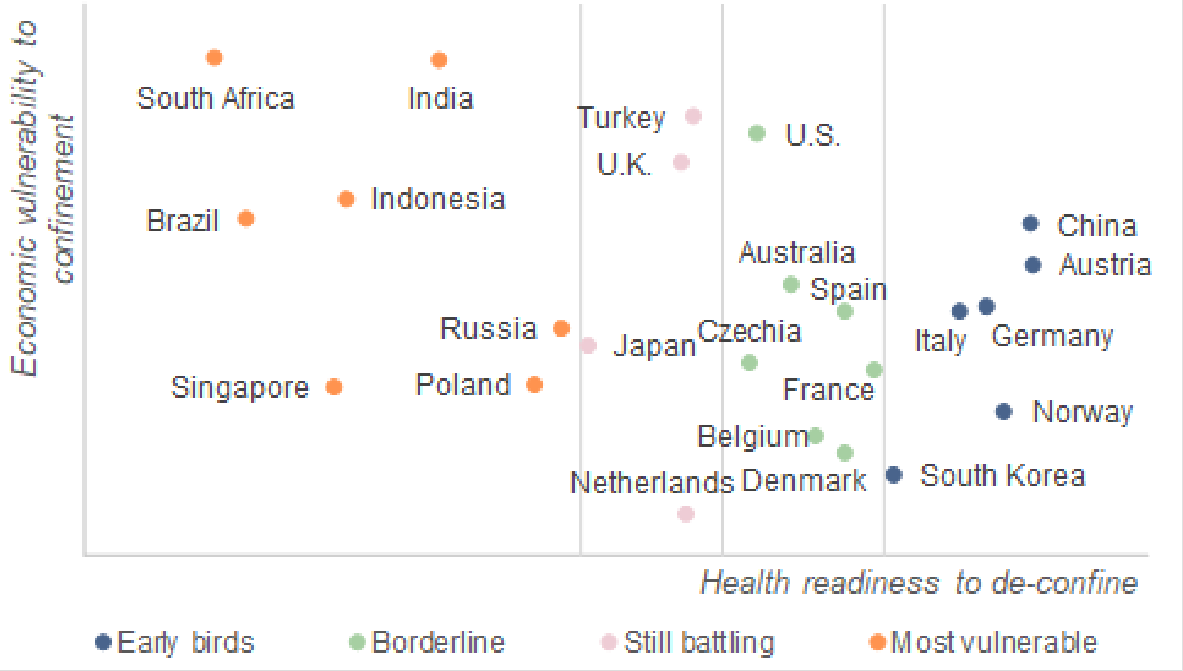
1. **Length** and timeline of deconfinement
2. **Geographic segmentation** (intra/interregional mobility)
3. **Restrictions on movements** (borders, trade, gatherings and demographic segmentation)
4. **Sector segmentation**: which shops open, industries restart, schools open
5. **Health response**: health protocols in the private and public sector, testing strategy

Impacts on the economy

1. **Shape of the recovery**: U-shape, L-shape, jump function (S-shaped)
2. **Time to reach pre-crisis activity** level and/or pre-crisis pace of growth
3. **Workforce impact**: unemployment increase, labor shortages in specific sectors
4. **Inflation impact**, especially in specific sectors
5. **"Paused" sectors vs. structurally damaged** ones (insolvencies)

Sources: various, Allianz Research

To understand exit strategies and their risks, we group countries over two dimensions that analyze their initial conditions and then break down deconfinement strategies and impacts.



Sources: Various, Allianz Research

4 clusters: EM (orange) more vulnerable, high risk of policy mistake; early birds (blue), gradual deconfinement, first mover disadvantage; borderline (green) risk of secondary infections; still battling (pink), potential of on/off deconfinement and very gradual

COVID-19: WHAT IT TAKES TO GET BACK TO BUSINESS AS USUAL

Fresh virus outbreak – back to stage 1

Stage 1: Full lockdowns to 'flatten the curve'

- Expand healthcare capacity (treatment, testing, monitoring)
- Fiscal / monetary safety nets to reduce downside risks & cushion economic blow

You are here!

Stage 2: Gradual opening of national economies

- Mass testing, tracking & isolation of new cases
- Ongoing targeted confinement measures incl. border restrictions & event bans
- Policy to focus on boosting economic recovery prospects

Stage 3: Global economy getting back on track

- Bans on large events & border restrictions to be eased as pandemics around the globe end
- Ongoing fiscal & monetary policy support aimed at providing tailwind to rebound

Stage 4: Habemus vaccine!

- Global rollout allows for return to normalcy without border restrictions, testing & bans on large events
- Policy support can be gradually withdrawn

Sources: OECD, Allianz Research

COVID-19 POLICY MENU: FROM RELIEF TO RECOVERY, FROM DEBT TO CASH, FROM DEFLATION TO REFLATION

Stage 1: national lockdowns

- **Whatever it takes: lifeline stimulus and emergency liquidity support**
- Fiscal policy: Double-digit fiscal deficits with tax deferrals, employment protection and public guarantees to support corporates cash flows and debt redemptions
- Monetary policy: massive asset purchases (corporate and sovereign), lower rates, direct credit provisions

Stage 2: De-confinement

- **Targeted relief: shifts the focus from liquidity to solvency support with targeted and increasingly conditional support**
- Fiscal policy: consumer-oriented policies (VAT tax cuts, adaptive social protection, vouchers) to boost consumption and avoid sparking off social discontent. Maintaining fiscal relief measures to hardest hit sectors: air transport, hotels and accommodation and retail, and support companies that start to export again.
- Monetary policy: continue asset purchases and other exceptional liquidity providing measures

Stage 3: International opening

- **Preparing the recovery, from emergency relief to stimulus: policies should plant the seeds of the recovery.**
- Fiscal policy: active labor policies to incentivize employment growth, incentivizing investment through accelerated amortization and targeted lending, and boosting trade finance could also be catalysts for the recovery
- Monetary policy: continued asset purchases and low interest rates

Stage 4: Sanitary normalcy

- **Engines of the global economy are back in action and the time has come to tackle the legacy issues of the crisis**
- Fiscal policy: Preparing for the future in stage 4 means investing in public health and infrastructure, scaling up the green stimulus and innovation policy, investing in local production capacity for key medical equipment, improving social redistribution and re-thinking the role of governments and central banks in the economy.
- Monetary policy: Gradual slowdown in net asset purchase pace, re-calibration of reinvestment policies

Sources: Various, Allianz Research

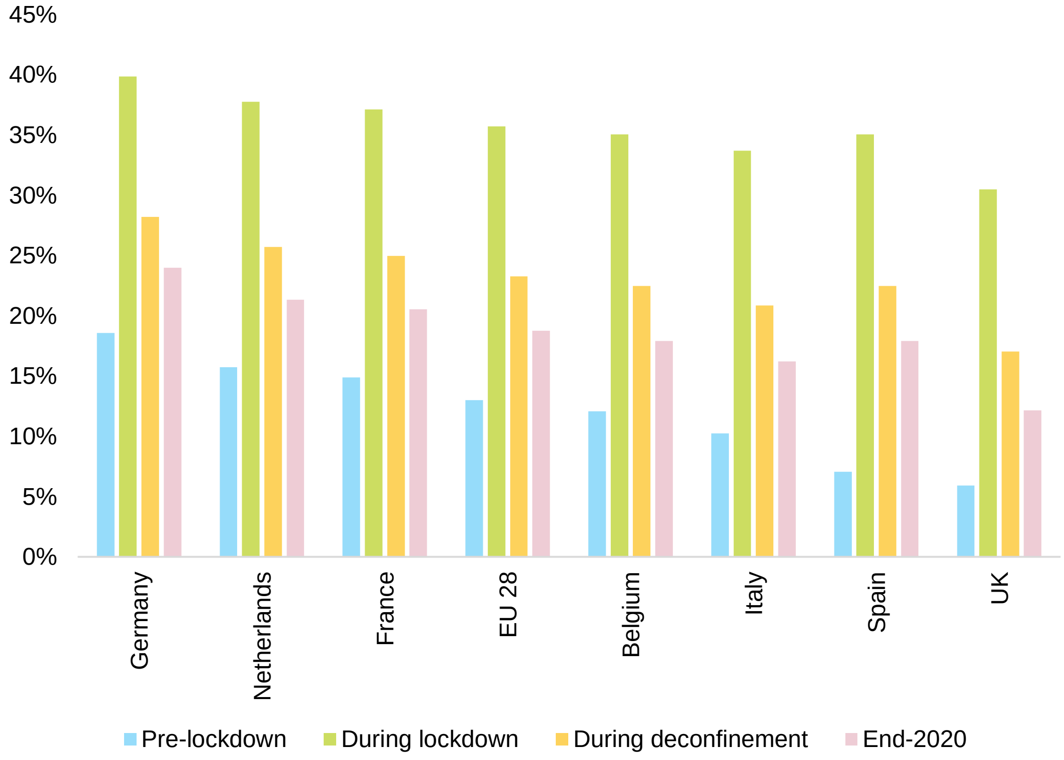
AGILE POLICY: FROM SAFETY NET TO SPRINGBOARD, AVOIDING PRECAUTIONARY SAVINGS

Expected fiscal stimulus during the recovery (% of GDP)

	Fiscal relief announced (local currency)	Fiscal deficit (2020)	Public debt (2020)	Expected fiscal relief in the second phase	Expected recovery fiscal stimulus package
Germany	3.6%	-7.0	72	2.0%	2.0%
France	4.7%	-11.0	118	0.5%	2.0%
Italy	1.4%	-13.6	169	1.0%	1.0%
Spain	1.8%	-7.8	116	1.0%	1.5%
UK	2.9%	-7.4	93	1.5%	2.0%
US	10.8%	-12.0	90		10.0%

Sources: National sources, Allianz Research

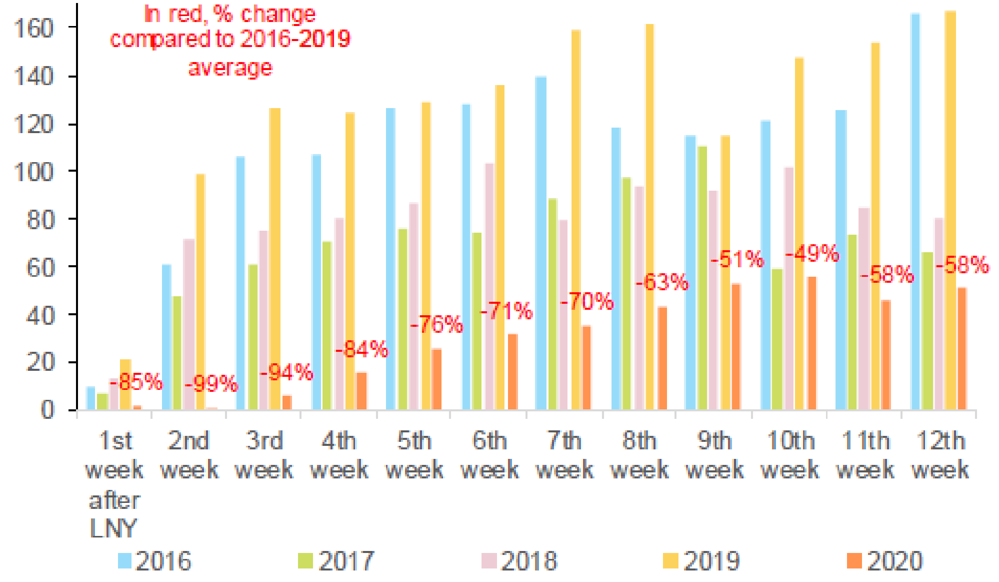
Saving rates, % of gross disposable income



Sources: Eurostat, Allianz Research

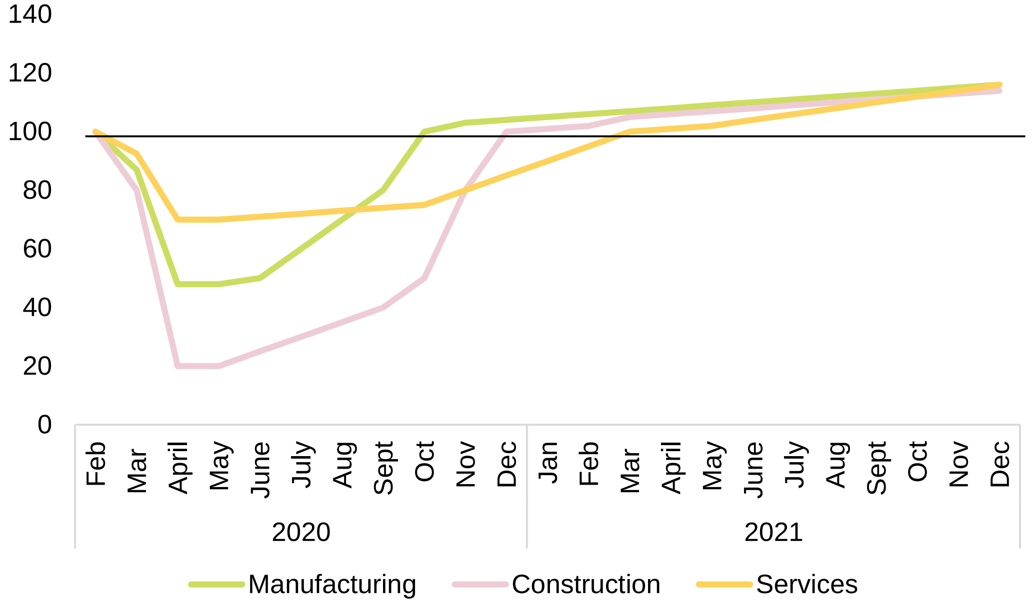
STAGE 2 TO LAST: ACTIVITY 70% TO 80% BELOW FULL CAPACITY FOR 2 TO 3 QUARTERS

China property transaction volume (30 main cities), base 100 = 30 days before Lunar New Year



Sources: Wind, Allianz Research

UK value added by sector, Feb 2020 = 100



Sources: Eurostat, ONS, Allianz Research

Lessons learned from China show us that one month after the number of domestic Covid-19 infections dropped near 0, production activities are still 80-85% of their usual levels, while consumer spending on durable goods remains at c.65% of normal levels.

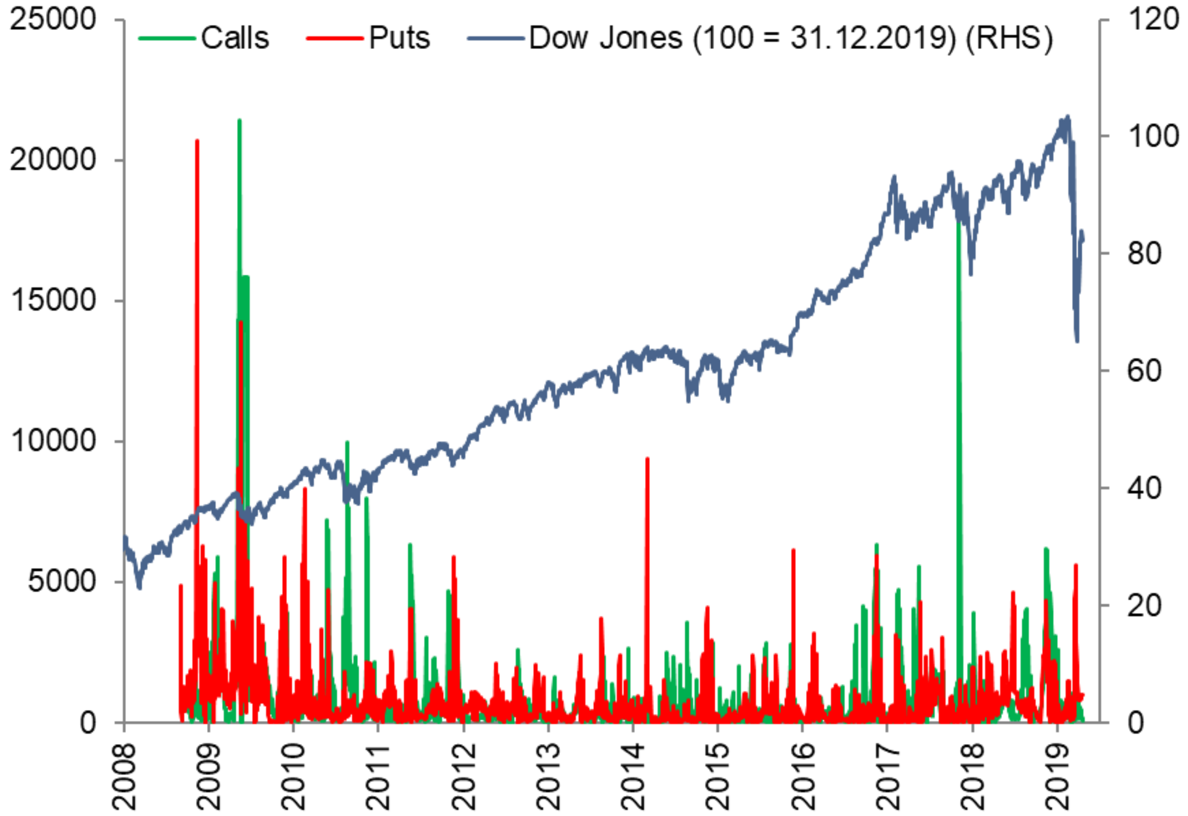
Our central scenario remains U-shaped, which means that the economies will be functioning at 70% to 80% of their potential for 2-3 quarters with transport, travel, retail, hospitality on pause for longer

MARKETS: IT CAN STILL GET WORSE BEFORE IT GETS BETTER

US Equity vs US yields vs Gold

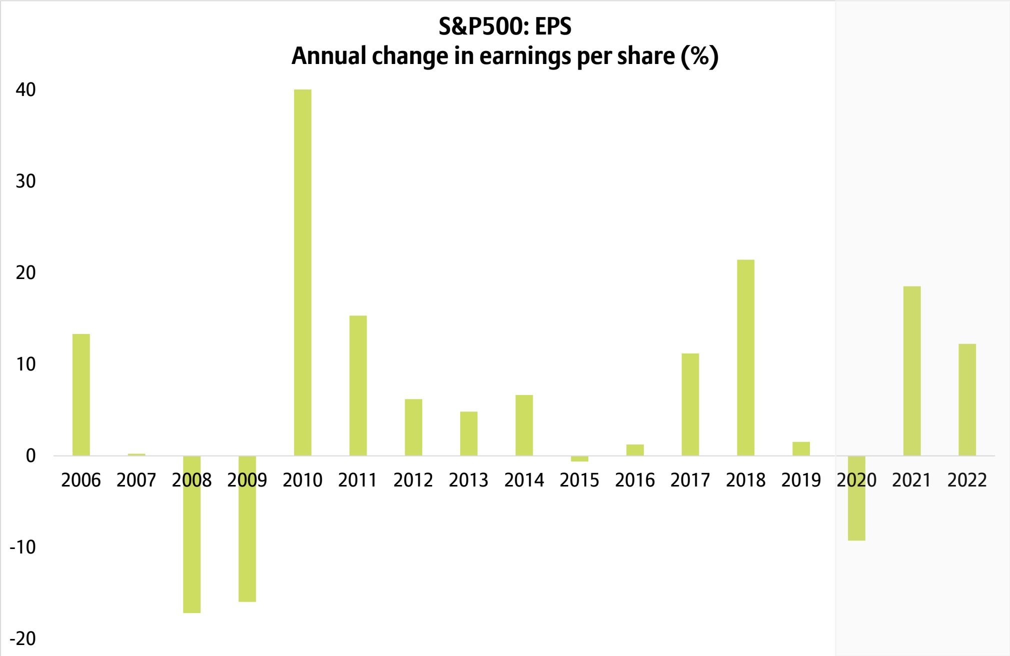
Sources: Bloomberg, Allianz Research

Dow Jones - 10% Delta Calls and Puts Open interest



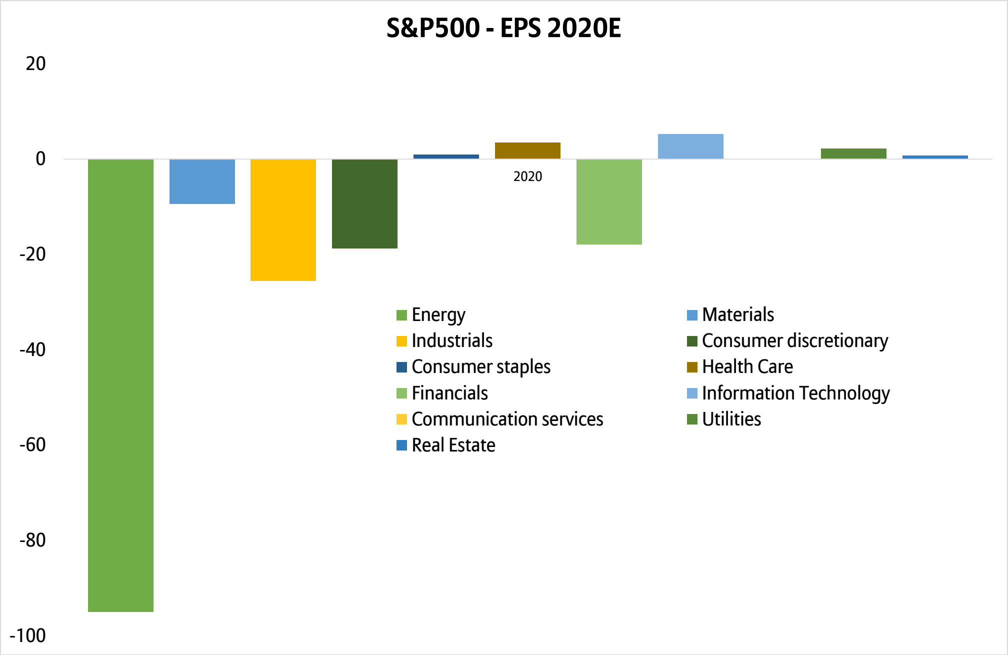
Sources: Bloomberg, Allianz Research

BRACE YOURSELF FOR THE EARNINGS SEASON



Source: FactSet, Refinitiv, Allianz Research

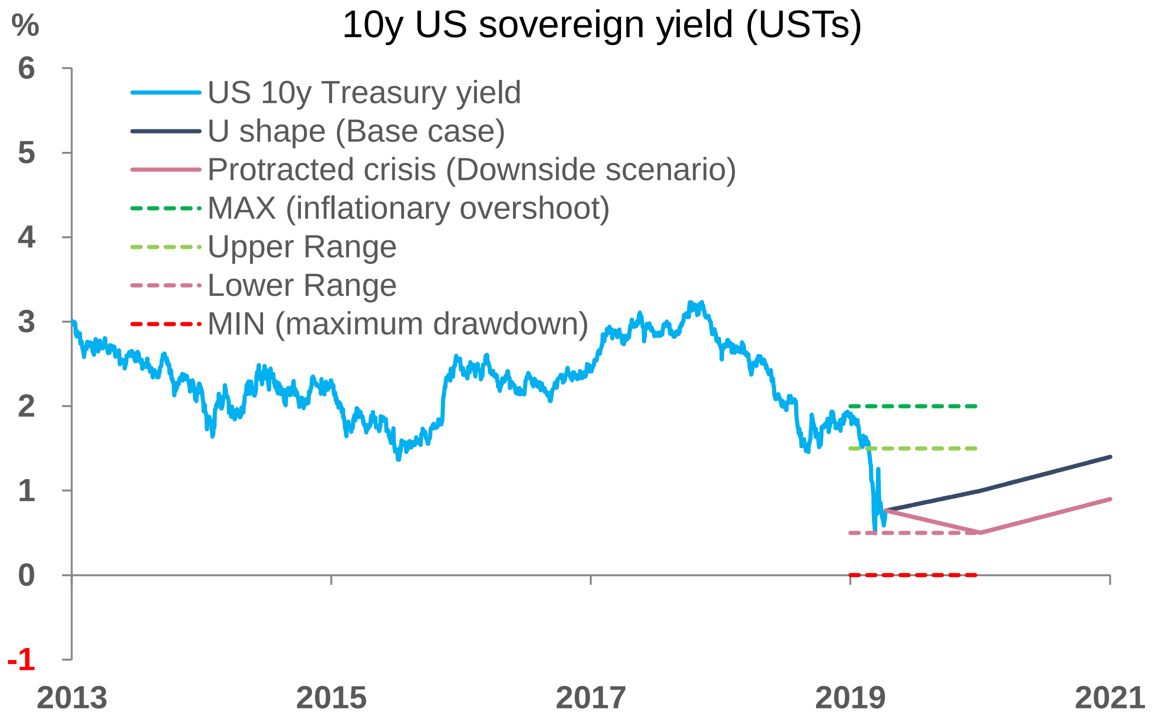
The market is expecting earnings per share to go down as much as -9% in 2020. However, it also implies a sharp recovery in 2021 and 2022. If companies do not meet market expectations, a further decrease in equity prices is likely.

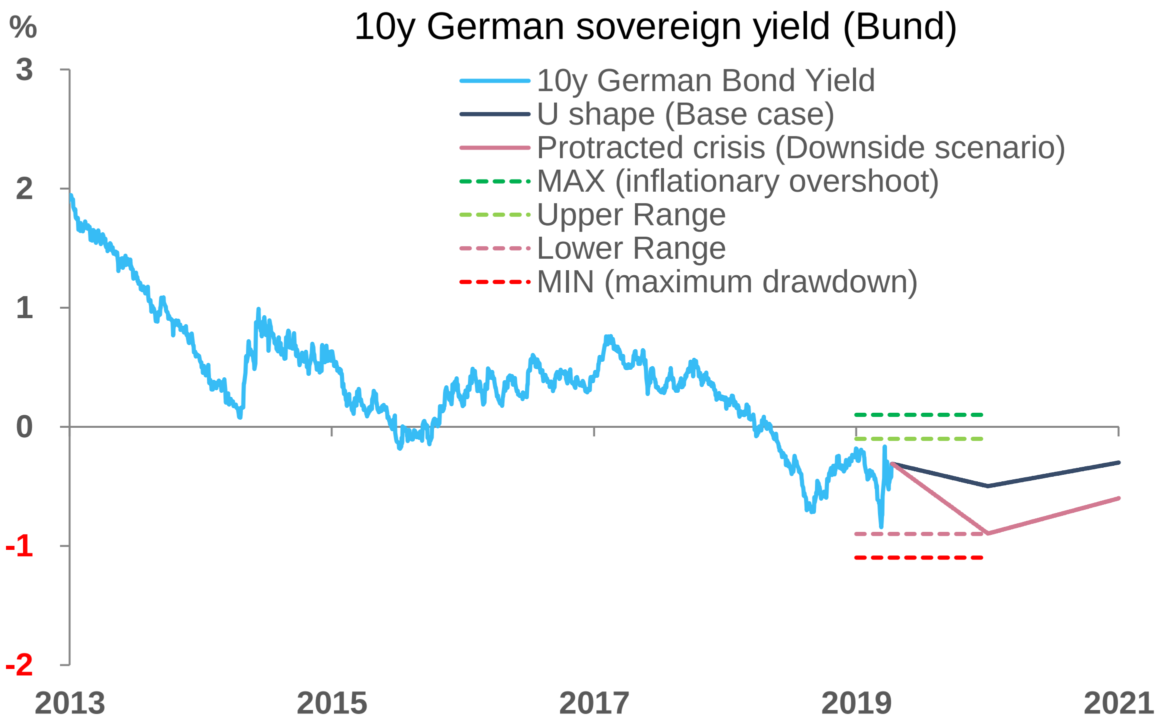


Source: FactSet, Refinitiv, Allianz Research

Energy and Industrials sectors seem to be the hardest hit by the COVID-19 recession. Market implies up to -95% correction in earnings per share in the Energy sector and -25% in Industrials.

GLOBAL BONDS LOWER FOR LONGER



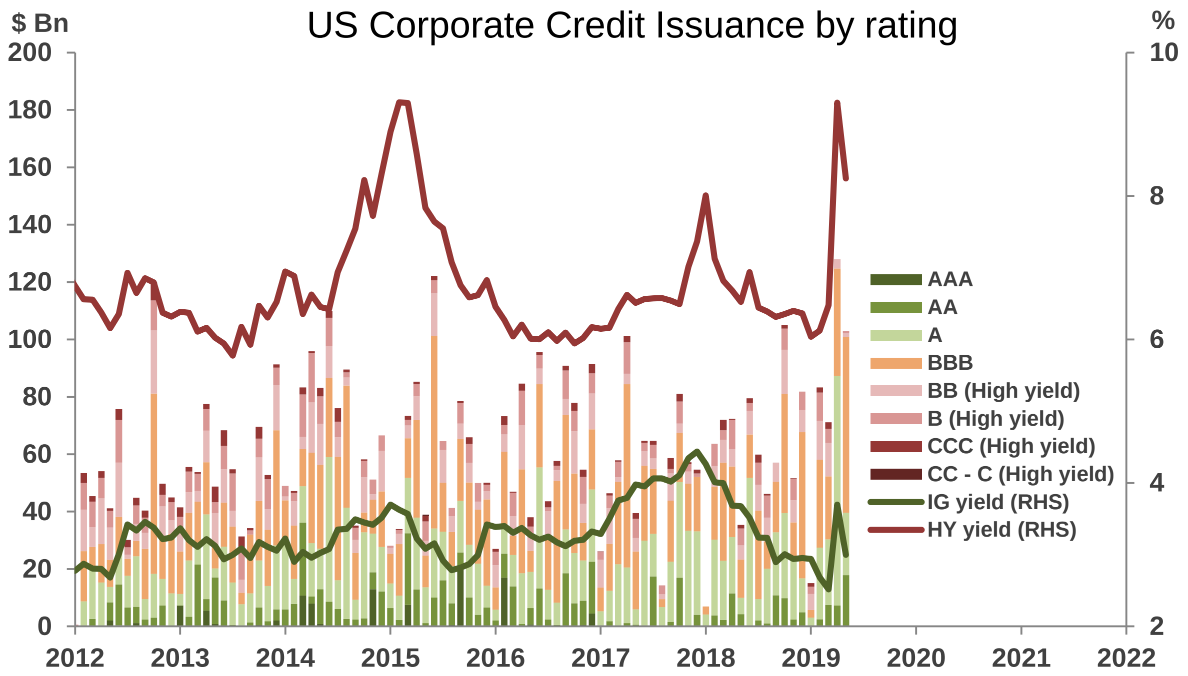


Recently, US long-term sovereign yields have crossed the lower-bound of our fundamental valuation model for a short period of time implying a quick reversal to fundamental level (1%). With that in mind, we expect long-term US yields to slowly converge towards fair value (1%) by year-end acknowledging a non-negligible risk of far lower (0-0.25%) intra-year yields.

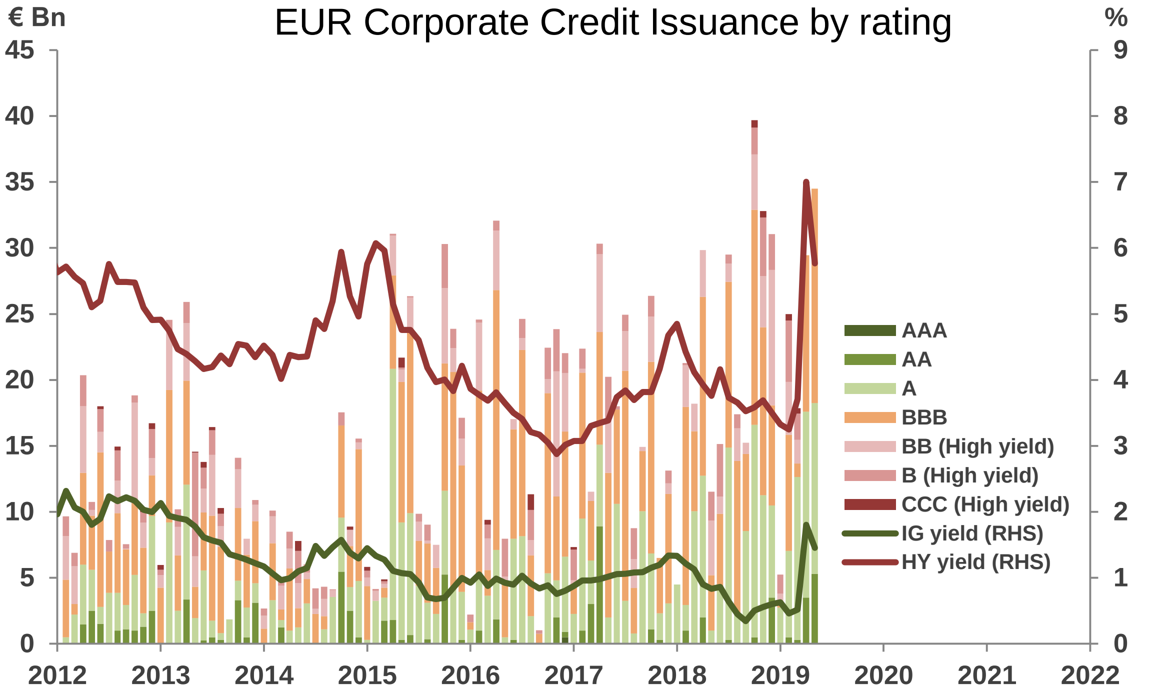
Similarly, but not as extreme as in the US case, long-term German government bond yields have been roaming around the lower end of our fundamental valuation model. At this level we do not expect bunds to follow a downward trajectory but it is reasonable to believe yields could visit the -1/-1.1% limit for a short period of time to slowly reverse to fair value (-0.5%) by year end.

Source: Refinitiv, AZ Research

CORPORATES IN A RUSH FOR MARKET FINANCING



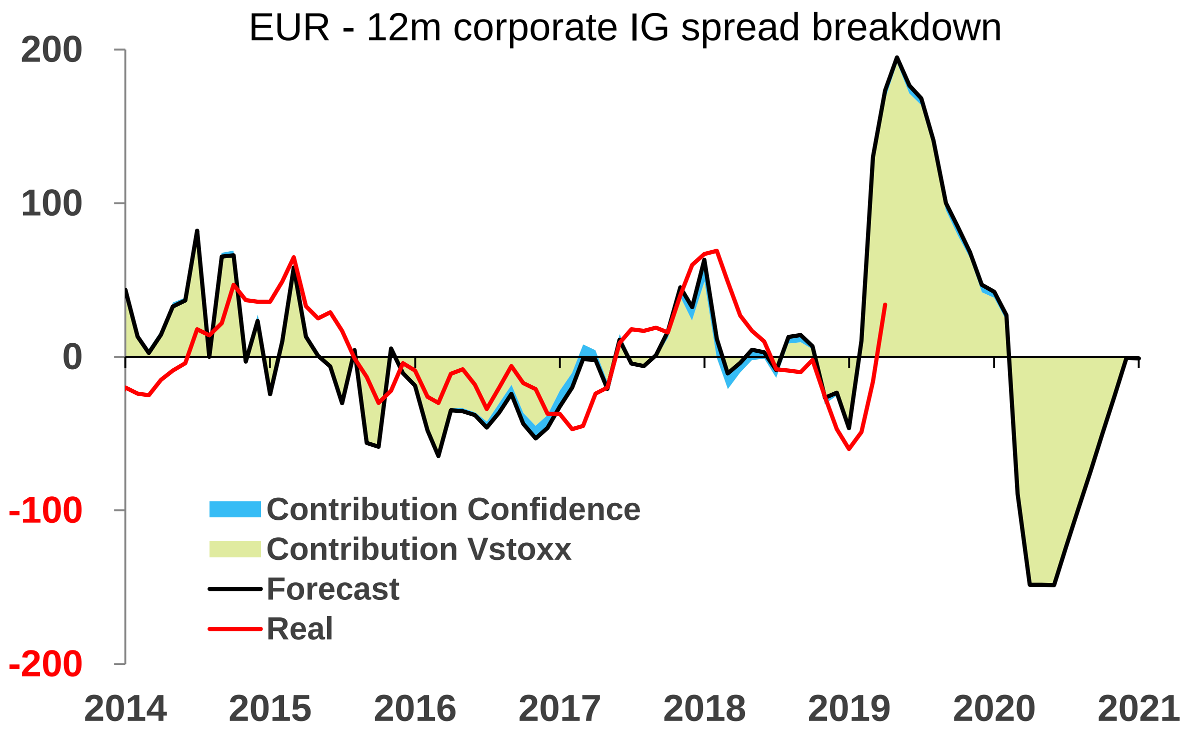
The recent market turmoil has imposed a considerable toll on corporate credit as the cost of market-financing has been on ever increasing rampage since the beginning of the outbreak. Interestingly, despite the recent increase in financing costs both USD and EUR corporate markets have remained extremely active in March-April with issuance volumes reaching previous highs.

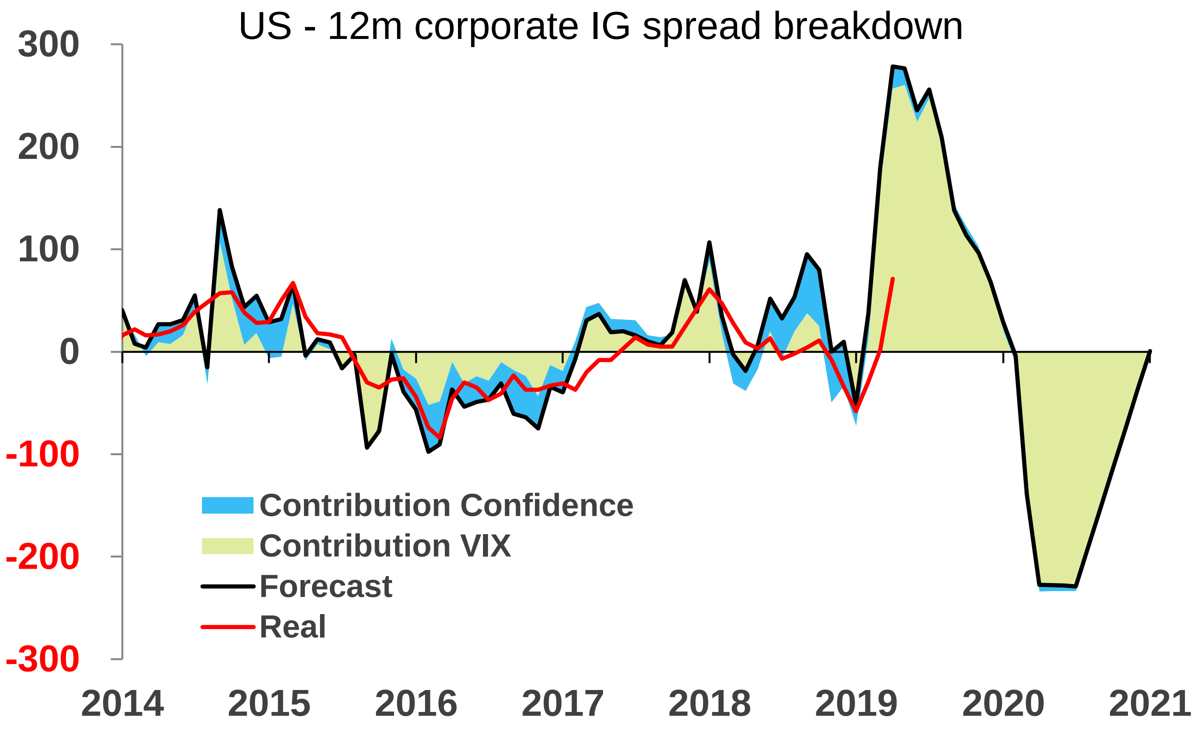


The single-A and BBB rating buckets remain the major issuers while sub investment grade companies have disappeared from the market. This reflects that the flight for quality y remains in place, with the running assumption of a substantial Covid-19 driven impact on current and future demand, specially in less solvent companies.

Source: IFR, S&P, Refinitiv, AZ Research

GLOBAL CORPORATE CREDIT: ONE OF THE MOST AFFECTED ASSET CLASSES





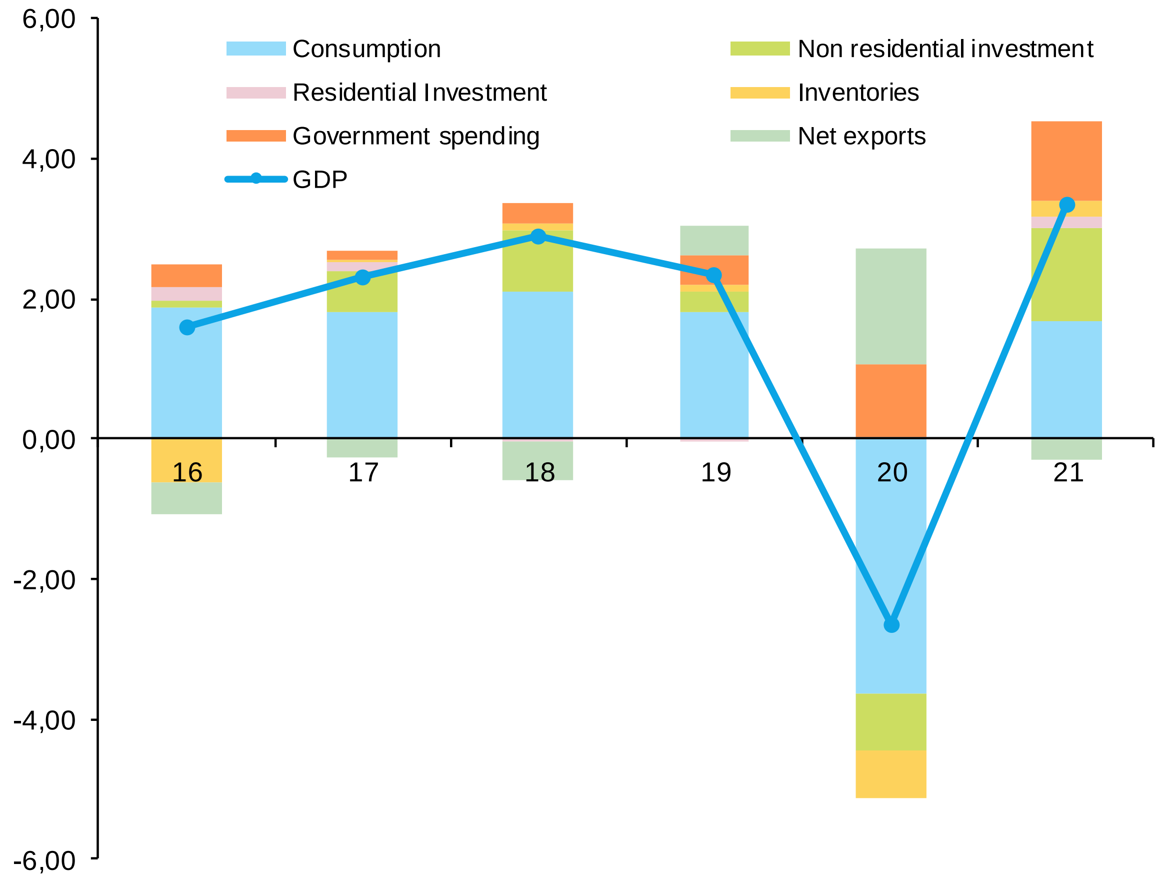
When it comes to the current determinants of corporate spreads movements, the component directly linked with equity volatility remains the sole determinant of the past spread behavior both within the investment grade and high yield spectrum. Because of that, it is a necessary condition for equity volatility to start declining in order to see lower spreads.

Needless to say that at the time equity volatility starts its retracting trend, it is to be expected for the confidence component (linked to GDP) to start exerting a structural widening pressure on spreads preventing those from reversing to previous lows. This will hold true specially in the high yield spread as some issuers may become unwanted casualties of this uncertain period.

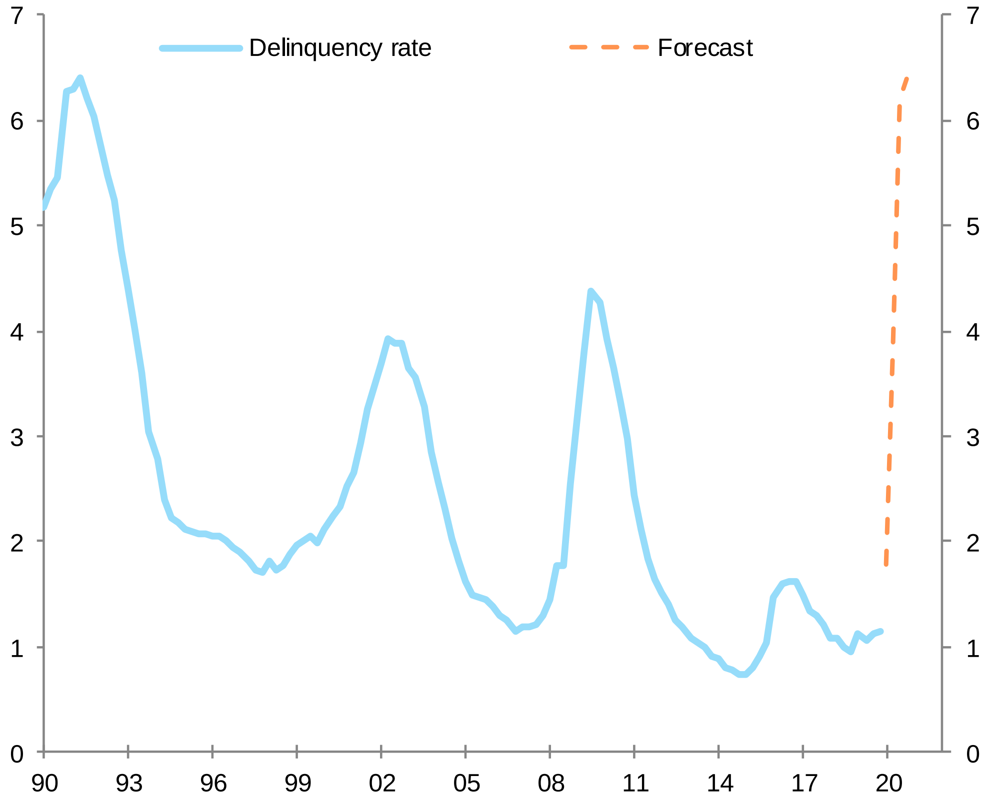
Sources: Refinitiv, AZ Research

US: DELINQUENCIES TO SURGE

Contribution to US GDP growth (%, y/y)



US Delinquency rate of industrial and commercial loans (% of total)

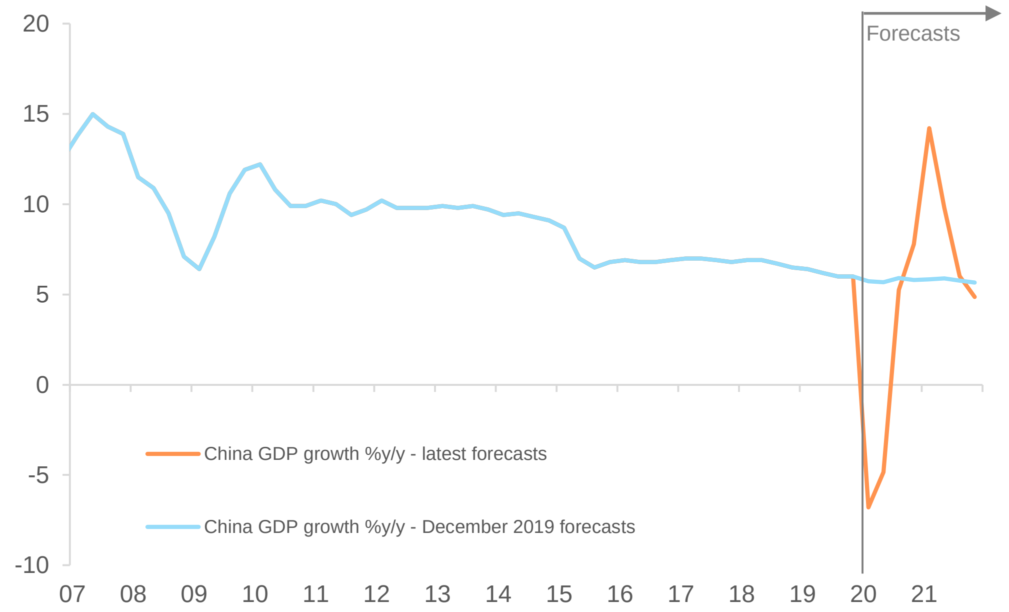


US GDP should decline by -30% q/q annualized in Q2 2020. We expect the US GDP to decline by -2.7% y/y in 2020 and rebound at 3.3% y/y in 2021

We estimate the delinquency rate with the unemployment rate (size of the shock), the credit gap to GDP (fragility factor) and public expenditures (as % of GDP, economic policy reaction factor). In 2020, this delinquency rate could reach a record high since the 1990s.

CHINA GROWTH IN 2020 REVISED DOWN TO 1.8%

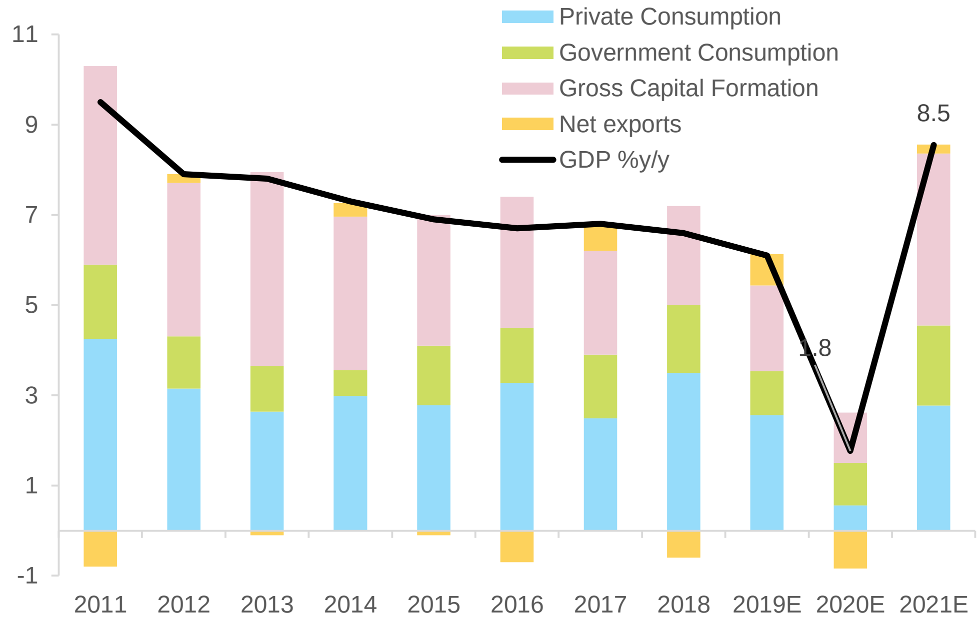
GDP growth (%y/y)



Source: National statistics, Allianz Research

Activity data at the beginning of the year declined to record lows. GDP growth declined by -6.8% y/y in Q1, and we expect economic activity to fully resume around June 2020.

GDP growth (%) & breakdown of contributions (pp)

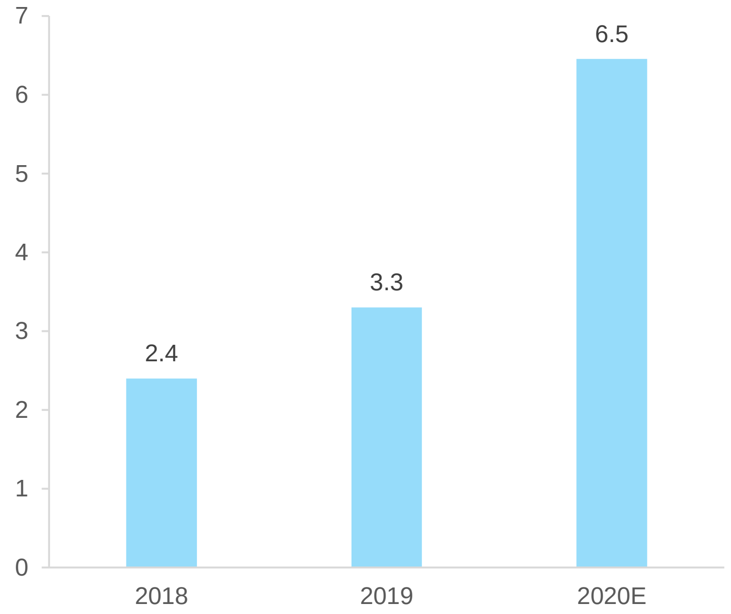


Source: National statistics, Allianz Research

After the slump of Q1, we expect a gradual recovery thereafter, particularly visible in H2. This should be possible thanks to some catch-up from pent-up production and policy support. We expect 2020 GDP growth at +1.8%.

CHINA POLICY MIX: FURTHER EASING TO COME

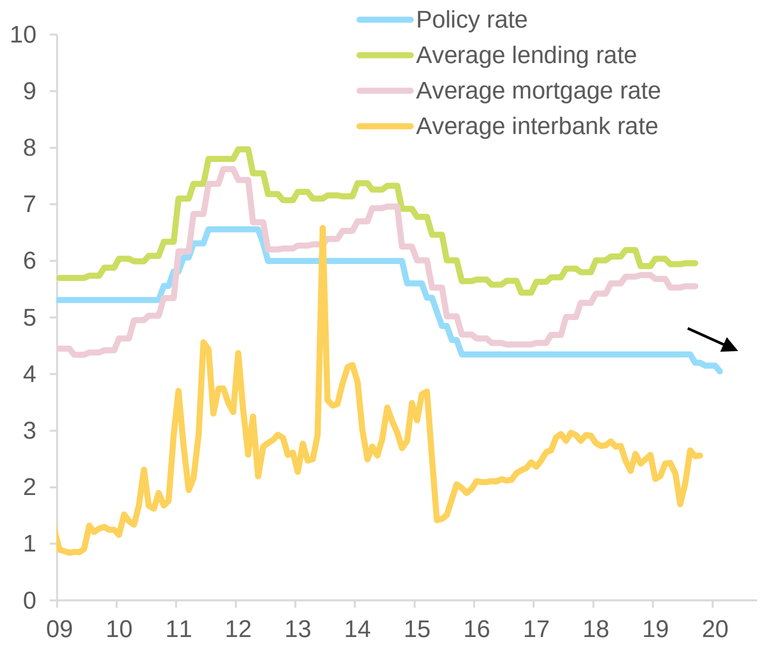
Size of fiscal stimulus package (% of GDP)



Source: Allianz Research

Fiscal easing is likely to increase in 2020. We now expect fiscal support amounting to 6.5% of GDP, up from 2.7% forecast before the COVID-19 outbreak.

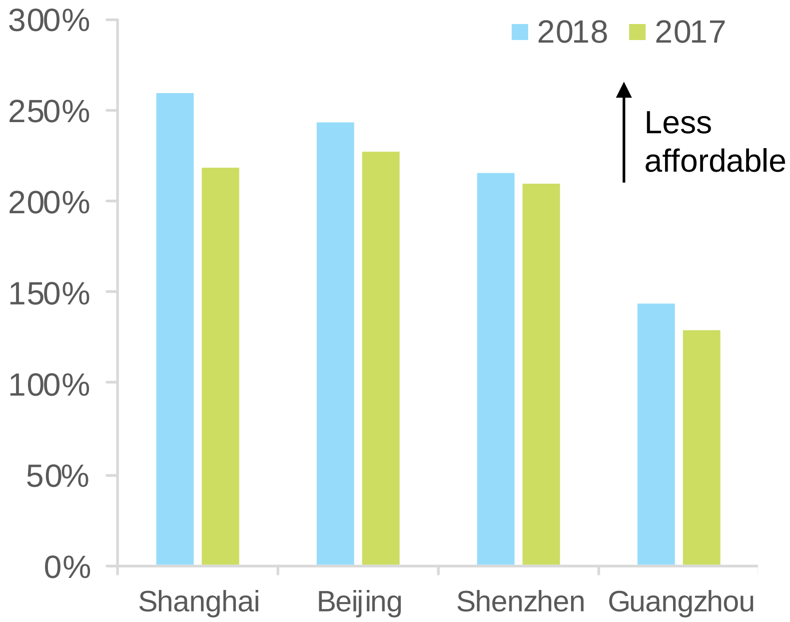
Interest rates (%)



Source: Datastream, Allianz Research

On the monetary side, the PBOC should continue easing. Over 2020, we expect cuts in the policy rate worth 40bp in total, and the Reserve Requirement Ratios for large banks to be lowered by 150bp overall.

Housing affordability (cost as % of income)

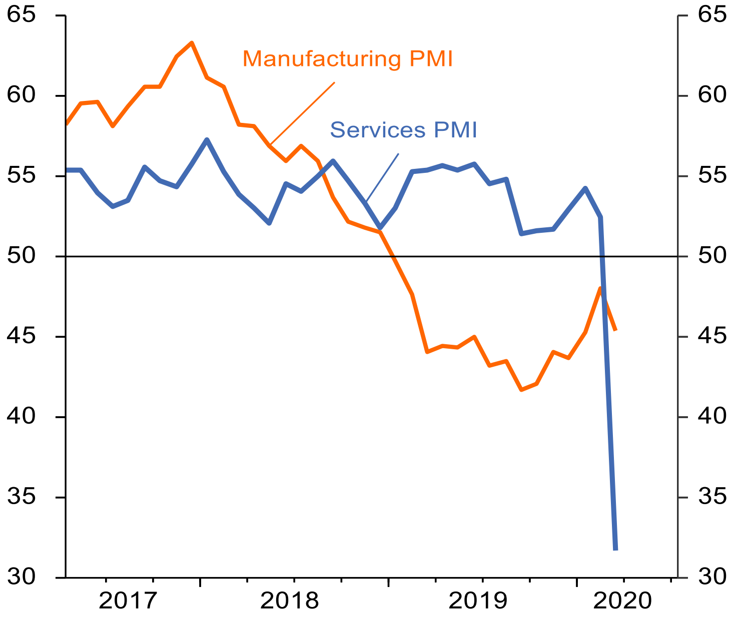


Source: Bloomberg, Allianz Research

Authorities still seem reluctant to use the housing sector as a cyclical stabiliser, as they may be more concerned with housing affordability. Credit conditions may be loosened only marginally.

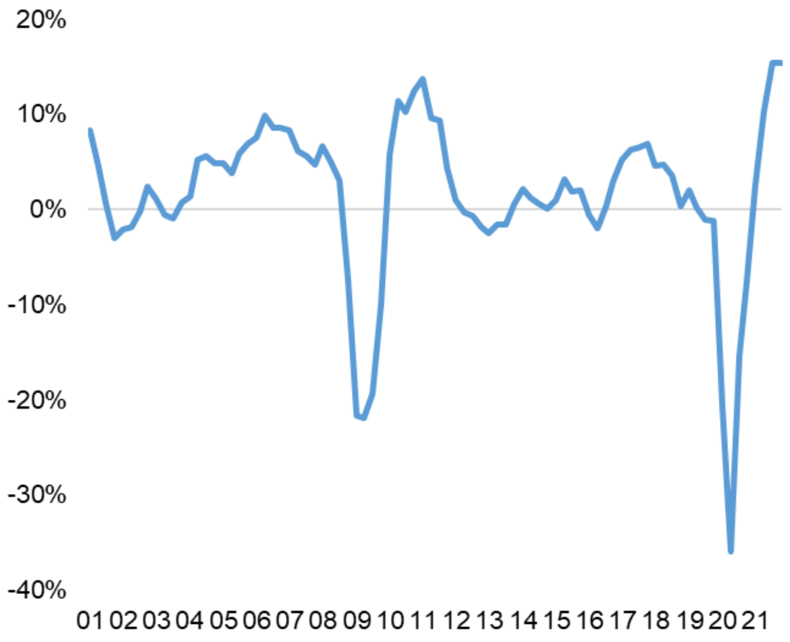
EUROPEAN CORPORATES: EXPECT DECREASING TURNOVERS AND DETERIORATING MARGINS

Eurozone PMIs



Sources: Refinitiv, Allianz Research

Turnover growth (y/y), manufacturing sector



Sources: Eurostat, Euler Hermes, Allianz Research

Input and selling prices, Manufacturing PMI

Sources: Eurostat, Euler Hermes, Allianz Research

The Eurozone is facing an unprecedented economic setback in terms of size and speed, with the contraction in GDP driven above all by the services sector.

In the context of the COVID-19 crisis, we estimate that turnovers of Eurozone companies could fall by more than -30% y/y at the peak of the crisis in Q2.

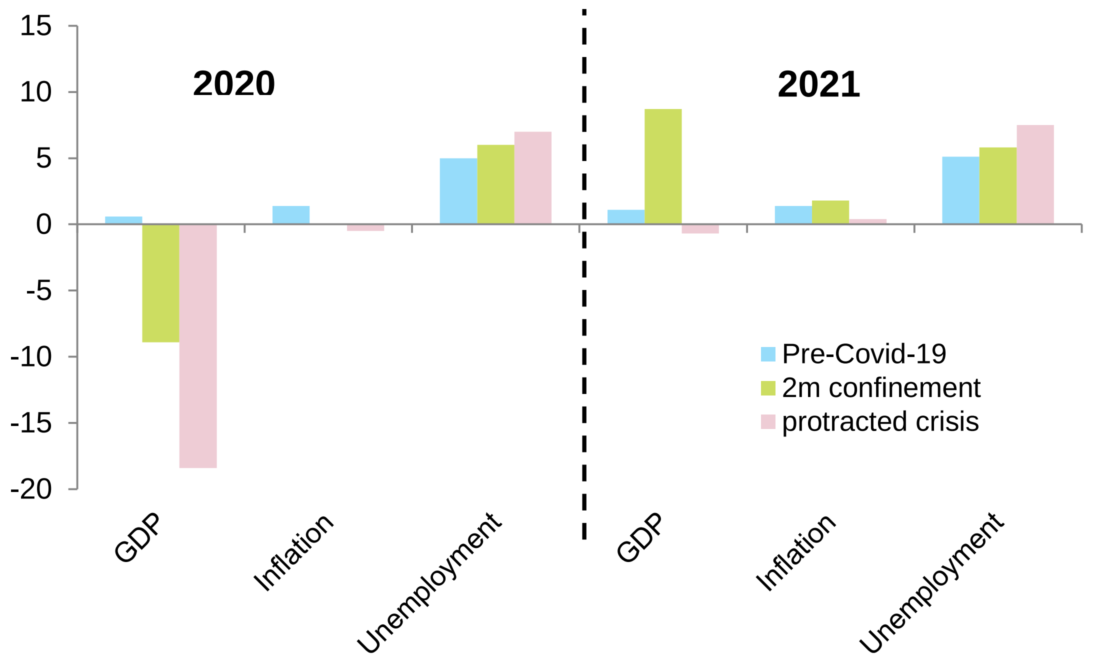
Companies are facing an strong increase in their inventory to new orders ratio, which can announce further downside pressures on selling prices

GERMANY: SHARPEST SLOWDOWN SINCE WW II

Germany: IFO survey & real GDP (y/y, %)

Sources: Allianz Research

Germany: Economic impact under different scenarios



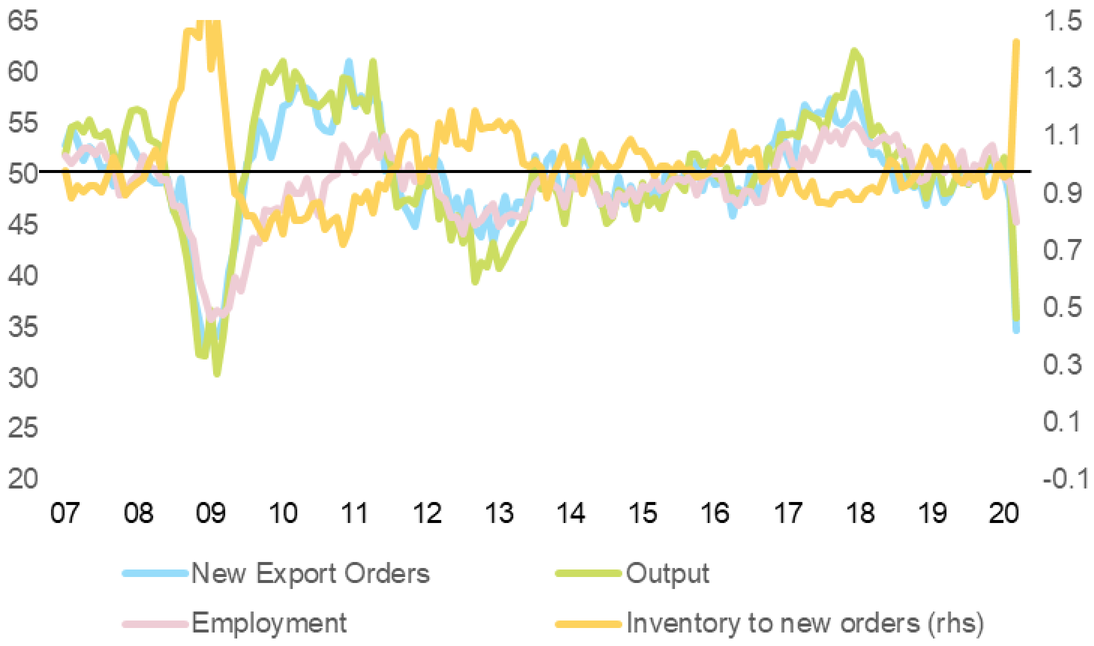
Sources: Refinitiv, Allianz Research

Available high frequency data suggests that the German economy moved from a timid recovery in Jan/Feb to a full-blown recession a la 2008/9 within a month's time. The IFO survey currently suggests that German GDP contracted by 4% y/y in March and that further pain is ahead.

Our estimates show that a 2month lockdown in Germany would see the economy contract by -8.9% in 2020 followed by a u-shaped recovery from H2 onwards. Meanwhile in our adverse protracted crisis scenario GDP could plunge 20% this year with no rebound in sight.

FRANCE: RECORD HIGH SHOCK ON PRIVATE CONSUMPTION AND INVESTMENT IN Q2

Manufacturing PMI components



Sources: AGI, Allianz Research

Transposing the Chinese shock on France bring the total level of activity in the manufacturing sector at levels similar to 2009. The inventory to new orders ratio is expected to go significantly above 1, which is a sign of future downside pressures on firms' turnovers

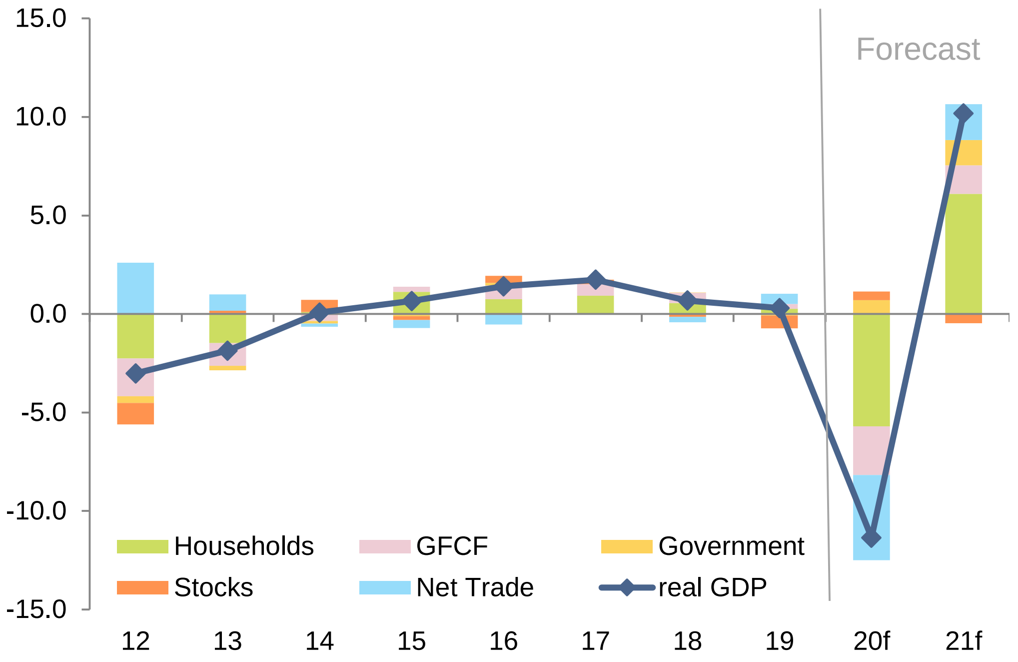
	2017	2018	2019	2020	2021
GDP	2,4	1,7	1,3	-8,9	9,6
Consumer Spending	1,6	0,9	1,2	-13,1	14,6
Public Spending	1,5	0,8	1,3	3,3	3,7
Investment	5,0	2,8	3,6	-13,1	0,1
Construction	6,6	2,0	2,1	-13,3	-3,4
Equipment	4,5	3,0	4,1	-13,0	1,2
Stocks	0,2	-0,2	-0,4	-0,8	0,8
Exports	4,0	3,5	1,9	-10,6	8,5
Imports	4,1	1,2	2,2	-13,3	6,6
Net exports	-0,1	0,7	-0,1	1,0	0,6

Sources: Insee, Allianz Research

Domestic demand will fall sharply in 2020 which will trigger a massive drop in imports. A destocking is expected at the exit of the crisis.

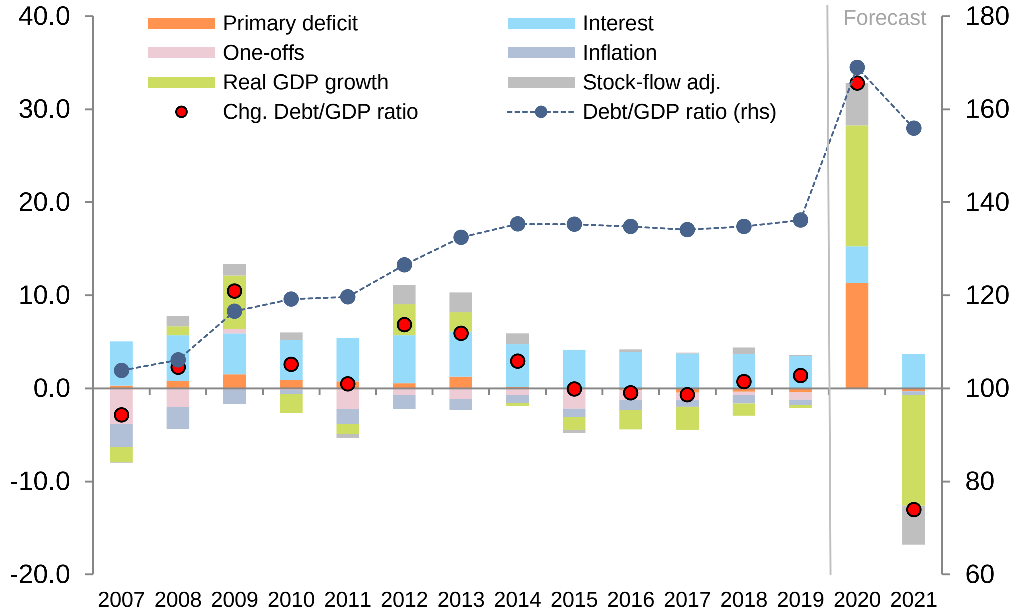
ITALY: DEEP RECESSION EXPECTED

GDP by component, %



Sources: Refinitiv, Allianz Research

Public debt in % of GDP (contributions)



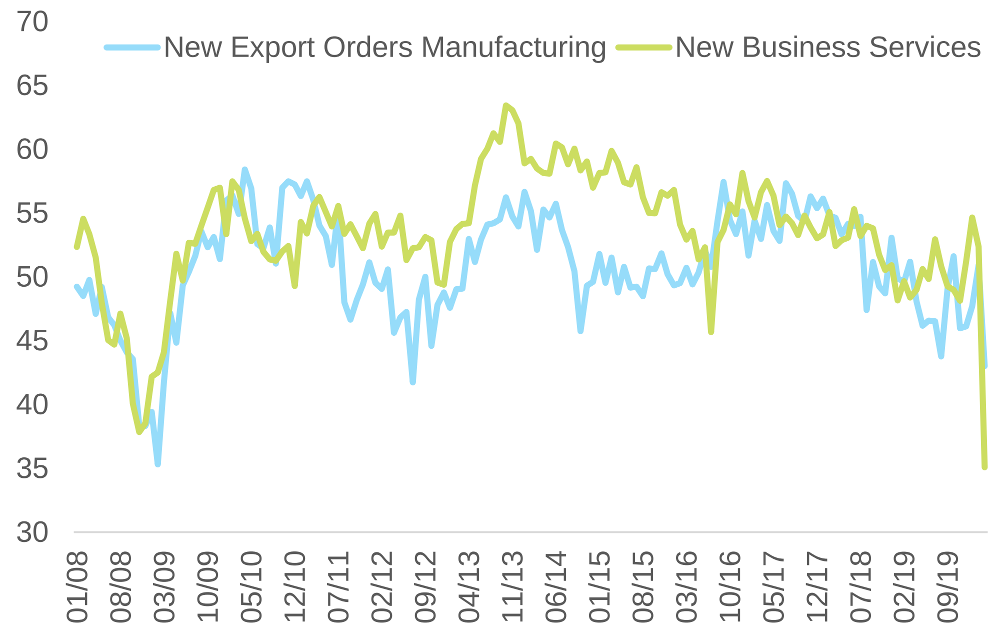
Sources: Refinitiv, Allianz Research

In 2020: major consumption shock in Q1 and Q2, while investment will suffer from uncertainty and funding constraints due banking vulnerability. Trade balance will deteriorate strongly due to slump in tourism receipts. In 2021: rebound thanks to fiscal stimulus.

Public debt will increase strongly 2020 due to stabilization and stimulus measures. ECB support contains risk of rising spreads. Debt sustainability not at risk in the short term. Debt/GDP will remain above 150% for increased period of time.

UK: A MASSIVE DOMESTIC SHOCK WHICH WILL DRIVE GDP DOWN BY MORE THAN 8% IN 2020

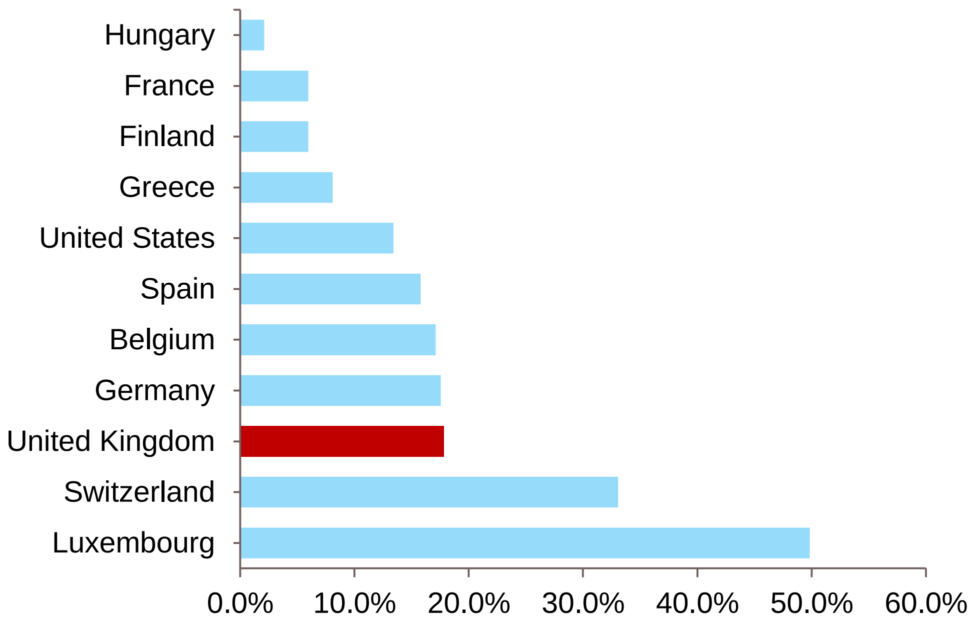
Purchasing Managers Index (PMI) by sector



Sources: Bloomberg, Allanz Research

The Covid-19 lockdown has been a massive shock for the services sector. In the manufacturing sector, new orders have also registered significant deterioration, but more should come in April

Share of foreign workers in total employment

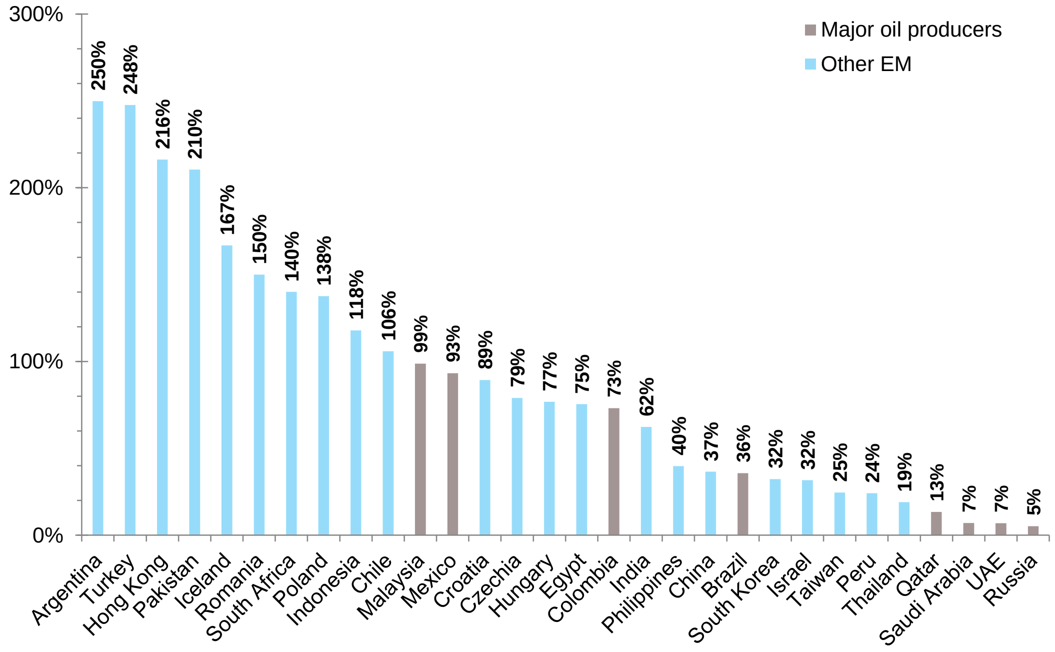


Sources: International Labor Organization, Allianz Research

The UK high dependency on foreign workers will continue to keep upside pressure on wages due to higher labor shortages. This adds pressure on a faster deconfinement.

EMERGING MARKETS: SUDDEN STOPS, CURRENCIES, AND CORPORATES

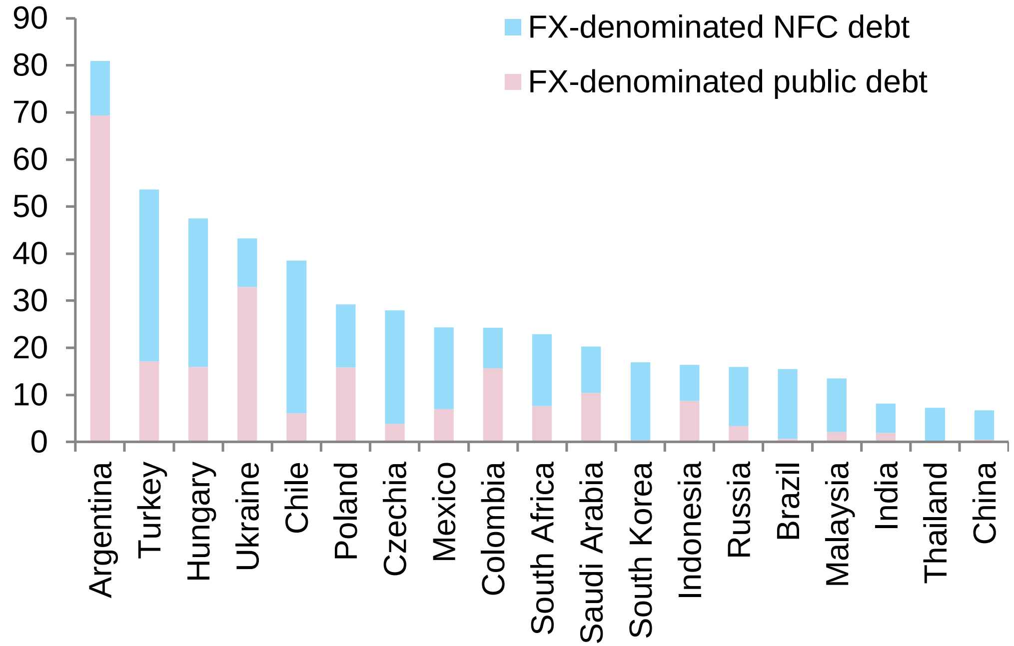
Emerging Markets: Gross external financing requirement (% of FX reserves)



Sources: IHS Markit, Allianz Research

Risk appetite likely to deteriorate in markets with high gross external financing requirements.

Foreign exchange-denominated sovereign and NFC debt (% of GDP), Q3 2019, selected EM



Sources: National statistics, IIF, Allianz Research

Argentina has the highest share of FX-denominated debt to GDP (80%). And most of that is sovereign debt.

Corporate FX debt is the highest in Turkey, Hungary and Chile.

EMERGING EUROPE: GROWTH FORECAST REVISIONS AND POLICY LEEWAY

2020 GDP growth forecasts

Real GDP growth	2019	2020 Dec. forecasts	2020	2021
Emerging Europe	**2.2**	***2.1***	**-3.8**	**6.2**
Poland	4.1	*3.1*	-3.8	6.6
Czechia	2.4	*2.2*	-7.5	8.5
Romania	4.1	*2.8*	-5.5	6.0
Hungary	4.9	*3.0*	-5.0	5.5
Slovakia	2.3	*2.3*	-8.0	7.0
Croatia	2.9	*2.4*	-7.0	7.0
Bulgaria	3.7	*2.7*	-4.5	5.0
Slovenia	2.4	*2.5*	-6.0	6.5
Lithuania	3.9	*2.5*	-5.8	6.0
Latvia	2.2	*2.4*	-6.0	6.2
Estonia	4.3	*2.7*	-6.2	6.0
Turkey	0.9	*4.1*	-3.3	7.6
Serbia	4.1	*2.6*	-3.6	4.0
Russia	1.3	*1.9*	-2.5	5.2
Ukraine	3.2	*3.0*	-5.8	6.0
Azerbaijan	2.2	*2.3*	-5.0	6.0
Kazakhstan	4.5	*3.5*	-3.0	4.0

Sources: National statistics, IHS Markit, Allianz Research

Sharp downward revision of 2020 growth due to confinement measures, especially in EU member states which are additionally very export-dependent on the Eurozone.

Monetary policy leeway

	Inflation target	Inflation Q4 2019	Inflation latest month	Policy rate	Monetary policy leeway
Poland	2.5%	2.8%	4.7%	0.50%	
Czechia	2.0%	3.0%	3.7%	1.00%	
Romania	2.5%	3.7%	3.0%	2.00%	
Hungary	3.0%	3.4%	4.4%	0.90%	
Slovakia*	2.0%	2.9%	2.9%	0.00%	
Croatia	-	0.9%	1.5%	2.50%	
Bulgaria**	2.0%	3.1%	3.7%	0.00%	
Russia	4.0%	3.5%	2.3%	6.00%	
Turkey	5.0%	10.3%	12.4%	9.75%	

* Slovakia is a Eurozone member, thus monetary policy is set by the ECB.

** Bulgaria has currency board with a peg to the EUR, thus it follows the monetary policy of the ECB.

Sources: National statistics, IHS Markit, Allianz Research

Monetary policy leeway is limited, in theory. Yet, and despite elevated inflation, the central banks of Czechia, Poland, Romania and Turkey cut rates at Emergency meetings in mid-March.

Fiscal policy leeway (2019 ratios)

	Fiscal balance % of GDP	Public debt % of GDP	Fiscal policy leeway
Poland	-1.9%	47.5%	
Czechia	0.3%	32.0%	
Romania	-3.8%	36.0%	
Hungary	-1.9%	69.0%	
Slovakia	-1.2%	48.0%	
Croatia	0.1%	71.5%	
Bulgaria	1.0%	21.0%	
Russia	1.8%	15.0%	
Turkey	-5.0%	32.3%	
Orange	if <-3%	if >50%	

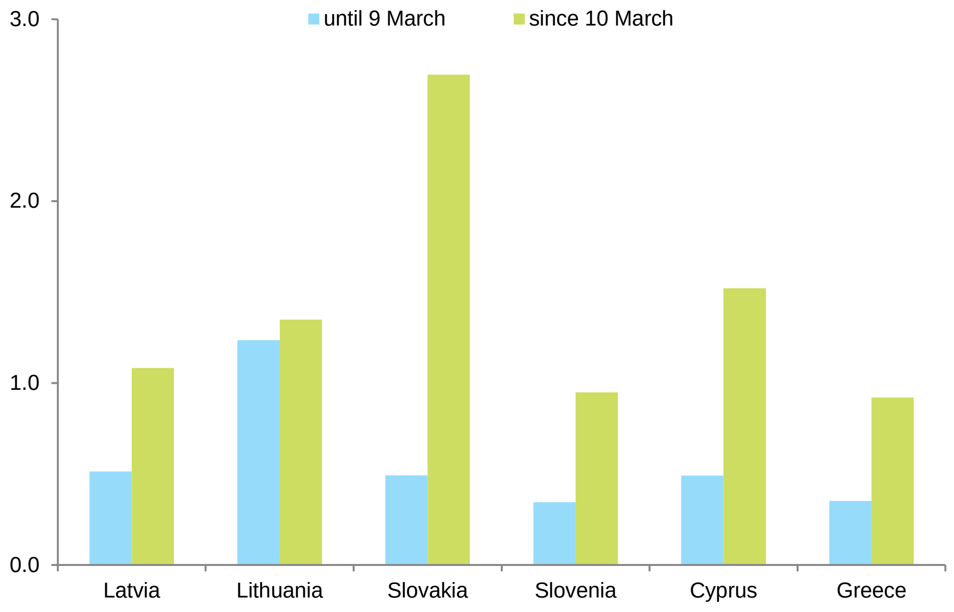
Sources: Eurostat, IHS Markit, Allianz Research

Fortunately all countries have fiscal policy leeway and most have already announced large stimulus measures.

But fiscal deficits and public debt ratios will rise markedly.

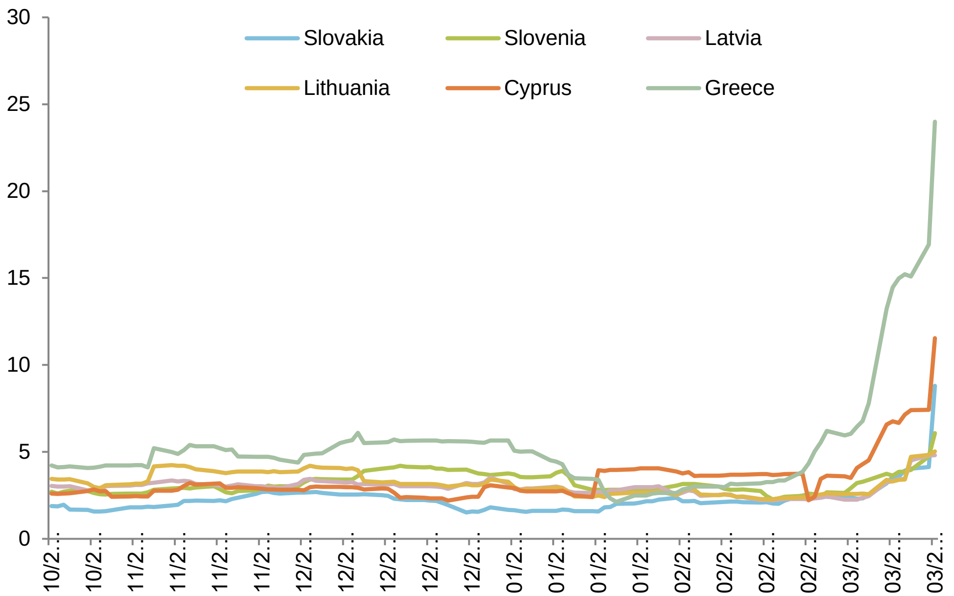
EMERGING EUROPE: SOUNDING THE LIQUIDITY ALARM

Bid-Ask spreads widening strongly
(10y tenor)



Sources: Bloomberg Allianz Research

Risk of liquidity bifurcation
(daily spread volatility)



Sources: Refinitiv, Allianz Research

Sharp increases in liquidity costs in peripheral markets indicate reduced supply by market makers. Also visible in volumes and immediacy of transactions.

Risk of liquidity bifurcation: liquid bonds becoming more liquid and illiquid ones more illiquid. Risk of an accident (impaired market access) cannot be excluded in such a volatile environment.

ASIA-PACIFIC: POLICIES AIMING TO CUSHION THE ECONOMIC BLOW OF COVID-19

Real GDP growth (%)

	2018	2019	U-shape scenario		Protracted crisis scenario	
			2020	2021	2020	2021
Asia-Pacific	4.8	4.3	-0.6	6.5	-9.8	-0.1
Australia	2.7	1.8	-5.0	3.5	-13.6	-4.8
China	6.7	6.1	1.8	8.5	-6.6	1.8
Hong Kong	2.9	-1.2	-4.7	4.5	-16.0	-4.4
India	6.2	5.0	1.1	7.5	-12.8	2.2
Indonesia	5.2	5.0	0.9	6.7	-7.1	0.3
Japan	0.3	0.7	-5.7	2.2	-15.9	-5.1
Malaysia	4.7	4.3	-3.2	6.2	-14.3	-2.4
New Zealand	3.2	2.2	-5.2	3.0	-13.9	-5.4
Philippines	6.2	5.9	-2.6	7.7	-11.3	-0.5
Singapore	3.5	0.7	-4.1	4.9	-15.4	-3.5
South Korea	2.7	2.0	-2.5	4.5	-11.1	-2.1
Taiw an	2.7	2.7	-2.0	4.7	-11.0	-1.2
Thailand	4.1	2.4	-4.1	6.6	-15.3	-1.8
Vietnam	7.1	7.0	3.1	6.7	-0.9	2.5

Source: National Statistics, Allianz Research

We expect Asia-Pacific GDP growth in 2020 at -0.6%, after 4.3% in 2019. Most economies are likely to experience a full year recession, before a recovery in 2021.

Monetary policy leeway

	Inflation Target	Inflation 2019 Q4	Inflation latest month	Policy rate	Monetary policy leeway
Australia	2%-3%	1.8%	1.8%	0.25%	
China	3.0%	4.2%	5.2%	4.05%	
India	4.0%	5.8%	6.6%	4.40%	
Indonesia	3.5% +/-1%	2.7%	3.0%	4.50%	
Japan	2.0%	0.5%	0.5%	-0.10%	
Malaysia*	-	1.0%	1.6%	2.50%	
New Zealand	1%-3%	1.9%	1.9%	0.25%	
Philippines	3% +/-1%	1.5%	2.6%	3.25%	
South Korea	2.0%	0.0%	1.1%	0.75%	
Taiwan*	-	0.4%	-0.2%	1.13%	
Thailand	2.5% +/-1.5%	0.6%	0.7%	0.75%	
Vietnam*	-	2.2%	5.4%	5.00%	

* no explicit inflation targeting framework

Light red when policy rate < latest inflation, green otherwise

Source: National Statistics, Allianz Research

Most central banks in Asia-Pacific have been aggressively cutting policy rates, with some now pursuing unconventional easing measures. Inflationary and FX pressures need to be watched.

Fiscal policy leeway

2019	Fiscal balance % of GDP	Public debt % of GDP	Fiscal leeway
Australia	-0.7%	42%	
China	-6.1%	55%	
Hong Kong	0.6%	0%	
India	-7.5%	69%	
Indonesia	-1.9%	30%	
Japan	-3.0%	246%	
Malaysia	-3.0%	56%	
New Zealand	0.1%	29%	
Philippines	-1.1%	39%	
Singapore	4.3%	114%	
South Korea	0.7%	41%	
Taiwan	-1.3%	33%	
Thailand	-0.2%	42%	
Vietnam	-4.4%	54%	
Light red	if < -3%	if > 50%	

Source: National Statistics, Allianz Research

Given the leeway, all economies have announced fiscal stimulus, in particular in Japan, Australia, Singapore, Malaysia, Thailand and New Zealand.

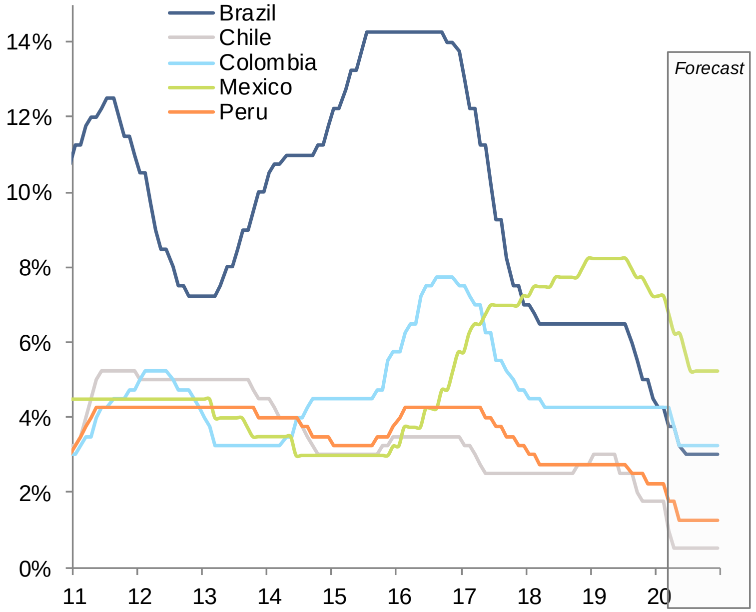
LATIN AMERICA: RECESSION, LOWER POLICY RATES AND HIGHER PUBLIC DEBT BURDENS

GDP growth forecasts (%, y/y, excluding Venezuela)

	2017	2018	2019	2020	2021
Argentina	2.7	-2.5	-2.2	-6.0	3.5
Brazil	1.3	1.3	1.1	-5.0	5.5
Chile	1.2	3.9	1.0	-3.7	2.3
Colombia	1.4	2.5	3.3	-1.0	1.7
Mexico	2.1	2.1	-0.1	-4.5	3.6
Peru	2.5	4.0	2.2	-1.7	2.4
Latin America	1.8	1.5	0.8	-3.8	3.6

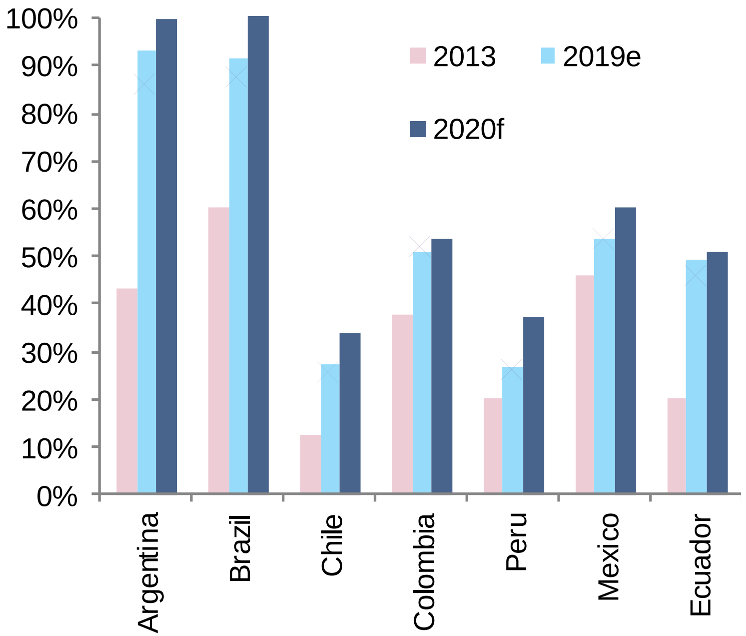
Sources: IHS Markit, Euler Hermes, Allianz Research

Central bank policy rates (%)



Sources: IHS Markit, Euler Hermes, Allianz Research

Public debt to GDP ratios (% GDP)



Sources: IHS Markit, Euler Hermes, Allianz Research

We see Latin America entering its deepest recession on record this year (-3.8%) due to the external shock and strict lockdowns shock.

Central banks already cut rates to support activity. More easing to come, despite pressures on currencies, and even unconventional policies.

Lower fiscal revenues due to oil and lower growth, depressed activity and fiscal stimulus will contribute to increase the public debt burden.

MIDDLE EAST: GROWTH FORECAST REVISIONS

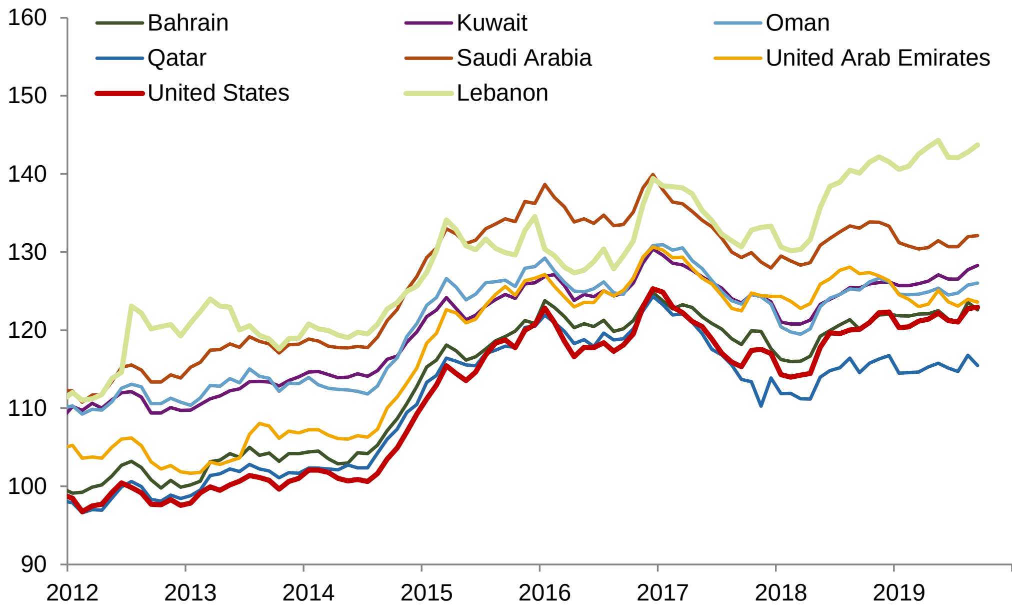
2020 GDP growth forecasts

Real GDP growth	2019	*2020 Dec. forecasts*	2020	2021
Middle East	**0.1**	***1.4***	**-5.1**	**2.2**
Saudi A.	0.3	*1.2*	-2.0	2.0
UAE	2.2	*2.0*	-2.5	1.5
Qatar	0.7	*2.0*	-1.5	2.0
Kuwait	0.9	*1.0*	-2.2	1.5
Oman	1.3	*1.7*	-3.0	2.2
Bahrain	1.2	*1.8*	-1.9	2.0
Iran	-7.0	*-1.0*	-15.0	3.0
Israel	3.3	*3.3*	-2.5	3.3
Iraq	3.3	*3.0*	-10.0	3.0
Lebanon	-0.2	*0.5*	-13.0	-2.0
Jordan	2.1	*2.0*	-3.0	2.4

Sources: National statistics, IHS Markit, Allianz Research

The Middle East region as a whole will experience a sharp contraction in 2020. The recovery in 2021 will be moderate only.

Real Effective Exchange Rate

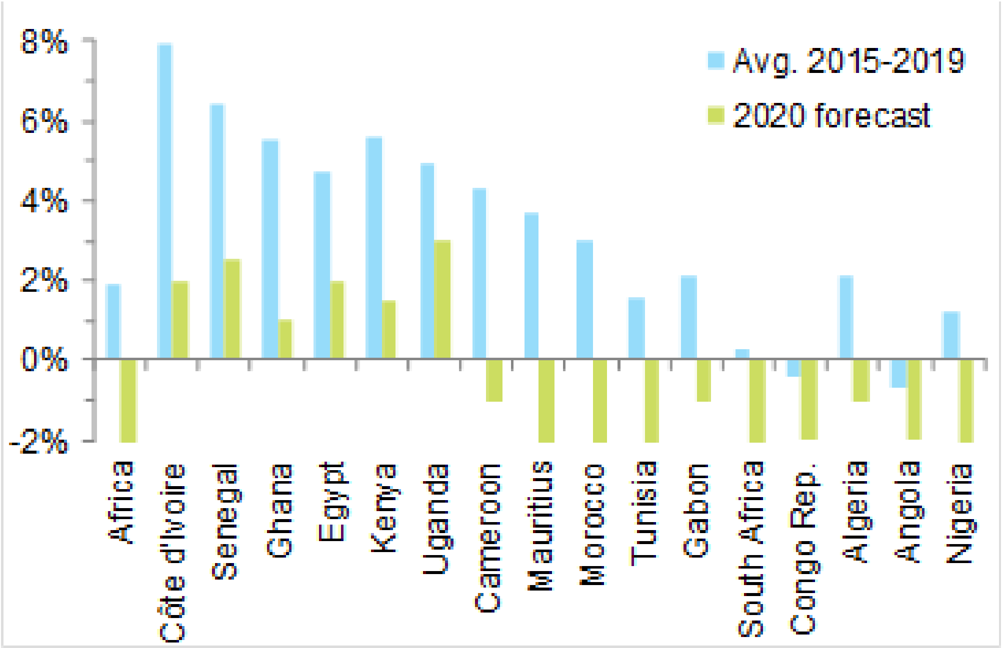


Sources: Bruegel, IHS Markit, Allianz Research

GCC states will follow the monetary policy stance of the US and have sufficient assets to maintain their currency pegs. Oman and Bahrain are weaker but will get support from their larger neighbors, if needed. Lebanon's currency is clearly overvalued.

AFRICA: STRONG DECELERATION AND LIMITED LEEWAY TO COPE WITH CURRENCY DEPRECIATIONS

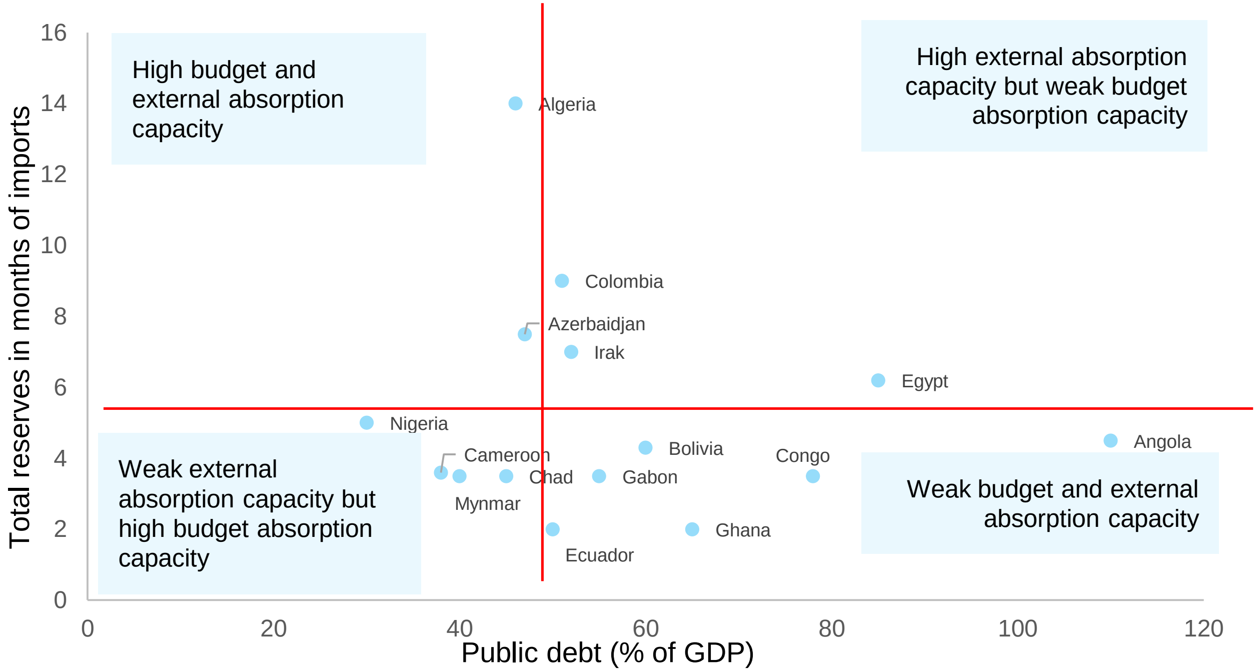
Real GDP growth



Sources: IHS Markit, IMF, Allianz Research

Growth will disappoint in many countries in Africa: all will experience a deceleration and major oil producers will see a contraction. Countries in recession: South Africa, Congo, Algeria, Angola, Nigeria, Gabon , Tunisia, Morocco

Foreign exchange reserves and public debt



Sources: IMF, Allianz Research

Some countries are more exposed than others to possible liquidity shocks. Angola, Gabon, Congo and Ghana are expected to be at the center of the storm.

WHAT COULD GO WRONG: SEVEN POSSIBLE SINS

A second (more severe) outbreak of the virus, which would keep the global economy below pre-crisis levels. until the end of 2021

Long-lasting uncertainty and low confidence delaying investment and boosting precautionary savings.

Risks to the banking and real estate sector, as a side effect of a violent surge in high-risk lending and non-payment cash-strained companies

Policy mistakes – insufficient support from central banks – and the lack of adequate fiscal burden-sharing in the Eurozone to trigger a relapse and a sovereign debt crisis.

Unaddressed rising inequalities resulting in higher social discontent and political tensions, notably in Emerging Markets.

Shorter supply chains driving protectionist measures across the world and feeding into structurally lower corporate margins.

Excess moral hazard creating a collective risk of more inflation (if central banks go overboard with monetization), debt restructuring and increased taxes.

WHAT COULD GO WRONG? PROTRACTED CRISIS (1/2)

	U Shape Scenario	Protracted Crisis
Covid19 assumptions	Peak in May. Exit by September. Containment lasts three months in Europe and US. Border closure lifted by end of year.	12-18 months sanitary crisis with possible reinfection. Borders stay closed and intermittent domestic confinement prevail.
Scenario in a nutshell	Technical recession in H1 in most of Europe and Asia. Recovery is U-shaped and inflationary. Unprecedented policy mix to mitigate shock and help protect the web.	L-Shaped recovery with debt monetization, systemic equity/credit/ liquidity issues and direct actions by policy makers disrupt market roles for years to come. Hard to restart engines

Macroeconomics	Unit	2020			2021	
		U Shape Scenario	**Maximum drawdown** qoq annualized	**Protracted crisis**	**U Shape Scenario**	**Protracted crisis**
Real GDP		**2 months confinement & very progressive deconfinement. Not back to pre-crisis levels before mid-2021.**				
Global	%	-3.3	-25 to -35	-7.0	5.6	0.1
EMU	%	-9.3		-20.0	9.2	-2.5
US	%	-2.7		-6.0	3.3	-0.1
China	%	1.8		-6.6	8.5	1.8
Inflation						
EMU	%	0.2		-0.6	1.6	0.2
US	%	1.2		-2.5	2.5	-0.4
Unemployment rate						
EMU	%	9.5		11.0	8.0	11.5
US	%	9.4		12.0	13.3	17.0
Other Indicators						
Global trade (volume)	%	-15.0		-30.0	10.0	-10
Global automotive (volume of sales)	%	-15.0		-40 / -45	10.0	-5 / -10
Global business insolvencies	%	20		35 / 40	2.0	20 / 25

WHAT COULD GO WRONG? PROTRACTED CRISIS (2/2)

year-end figures *(MIN to be considered as intra-2020 limit)*	Latest Value	Unit	2020 U Shape Scenario	2020 Protracted crisis	2020 MIN (maximum drawdown)	2021 U Shape Scenario	2021 Protracted crisis
Eurozone							
Sovereign Rates							
10y yield "risk-free" sovereign (Bunds)	-0.3	%	-0.5	-0.9	-1.1	-0.3	-0.6
10y Swap Rate	0.0	%	0.0	-0.4	-0.6	0.3	-0.3
20y Swap Rate	0.2	%	0.3	-0.2	-0.3	0.7	0.0
10y yield other sovereign (Italy)	1.7	%	1.7	2.7	3.9	1.4	1.7
Italy - Germany spread (10y)	197	bps	220	360	500	170	230
10y yield other sovereign (France)	0.2	%	0.4	1.0	0.1	0.1	0.5
France - Germany spread (10y)	48	bps	90	190	120	40	110
10y yield other sovereign (Spain)	0.8	%	0.6	1.2	1.9	0.4	1.0
Spain - Germany spread (10y)	115	bps	110	210	300	70	160
Corporate Credit Spreads							
Investment grade credit spreads	224	bps	180	230	300	150	190
High yield credit spreads	695	bps	750	850	1650	600	700
Equities							
MSCI EMU: total return p.a. *(Reference point 31.12.2019)*	-23	%	-22	-39	-55	10	-10
Expected Recovery from last traded value		%	7	-15	-38	18	-24
United States							
Sovereign Rates							
10y yield "risk-free" sovereign (Treasuries)	0.8	%	1.0	0.5	0.0	1.4	0.9
10y US - 10y Bund Rate Difference	108	bps	150	140	110	170	160
Corporate Credit Spreads							
Investment grade credit spreads	283	bps	230	280	450	180	220
High yield credit spreads	881	bps	800	900	1650	650	750
Equities							
MSCI USA: total return p.a. in USD *(Reference point 31.12.2019)*	-12	%	-20	-35	-50	15	-3
Expected Recovery from last traded value		%	-1	-20	-38	13	-22
Emerging Markets							
Sovereign Rates							
Hard Currency Yield (USD)	7.2	%	5.5	7.0	8.0	5.1	5.7
Hard Currency Spread (USD)	647	bps	450	650	800	370	480
Equities							
MSCI EM: total return p.a. in USD *(Reference point 31.12.2019)*	-19	%	-24	-42	-60	20	-8
Expected Recovery from last traded value		%	-3	-26	-49	17	-32

MID-TERM: CRISIS LEGACY

Strong state, redux

The role of the state vis-à-vis markets has been strengthened:

- Expect more assertive and interventionist governments
- Expect more basic needs and goods – from (green) infrastructure to health – provided by the state

De-globalization/-chinification

The close interlinkages between states has been put into question

- Expect states to reduce their foreign reliance on “strategic” goods (from drugs to batteries)
- Expect companies to shorten their supply chains

Social risk

Inequality trifecta (income, wealth and opportunities) exacerbated by health, housing, and digital differences

- Expect social unrest
- Expect surge in demand for more (income) protection and security

Identity politics 2.0

Authoritarian vs democratic state: Who can better fight a pandemic?

- Expect checks and balances to be put to the test, and politicization of economic carnage
- Expect rivalries (US/China/Europe)

Risk aversion/awareness

Trust in financial market stability & functioning has been challenged

- Expect investors to shift to more defensive strategies
- Expect more demand for risk cover

Increase in productivity/digital

The way we work has been changed

- Expect more flexible team structures and remote working, pushing up productivity by around 5% (according to several studies)
- Expect less business trips

THANK YOU

Economic, Capital Markets
and Industry Research

Global Economic Outlook

as of April 2020

EULER HERMES

Allianz