

# August Economic Update: A cruel summer

## In this bundle



### August Economic Update: A cruel summer

We've seen historic dismal numbers this quarter, but they are painful illustrations of the costs of a lockdown. In the second half of the year, the...

By Carsten Brzeski, James Knightley and Peter Vanden Houte



### United States

#### US: Forget the "V"

With virus fears on the rise, jobs being lost and incomes squeezed, we feel the second phase of the recovery will be much more challenging, especially in...

By James Knightley



### Eurozone: Better, but the fear factor remains

After the historic GDP contraction in 2Q, Eurozone economic figures have improved, though the flare-up of Covid-19 infections has placed a burden on the...

By Peter Vanden Houte



### FX | China

#### China's tech war with the US has made us revise our yuan forecast

The persistence of the technology war is hurting long term Chinese growth and the yuan's strength. Although we're revising our yuan forecast, it...



### FX

#### FX: King dollar loses its crown

The dollar's four percent decline in July marked its largest monthly drop since 2010. Driving this decline is both a re-rating of the European...

By Chris Turner



---

Report | 6 August 2020

## August Economic Update: A cruel summer

We've seen historic dismal numbers this quarter, but they are painful illustrations of the costs of a lockdown. In the second half of the year, the shape of the rebound will depend on authorities withstanding local curfews rather than larger-scale lockdowns. Nonetheless, the jury is still out on the long-term and permanent costs of this crisis



Source: Shutterstock

It's a cruel summer.

Back in 1984, Bananarama were singing about hot summer streets, unsuccessful attempts to smile and being left on their own.

A feeling many will have these days when wanderlust has to be subdued and the nearby lake has to make up for a sandy coastal beach. The summer is also cruel as it finally added numbers to the Covid-19 crisis. For most economies, the GDP data for the second quarter followed the pattern of 'worst quarter since x years for country y'. We only had to fill in the numbers.

In all honesty, as severe as these GDP readings were, they are yesterday's story. In fact, they are a painful illustration of the costs of a lockdown. The longer and the stricter a lockdown, the more severe was the impact on the economy. This pattern nicely explains the differences across the Eurozone. The (too) early lifting of lockdown measures in the US is also the main reason why the contraction was somewhat less severe than in the Eurozone. At the same time, China's recovery

continued. The fact that Chinese exports in June surprised to the upside could be another sign that the Eurozone and the US are recovering.









Monthly data since May have kept hopes for a v-shaped recovery alive

Looking ahead, monthly data since May have kept hopes for a v-shaped recovery alive. Or let's better call this a v-shaped rebound. Whether it is the traditional macro indicators or the more experimental data, they have all surged until July. It is now up to the hard data to follow suit. It will take until the hard July data before we really know whether the initial and more mechanical rebound after lifted lockdown measures, will turn into a strong and sustainable recovery or rather a quick flattening out.

Several factors will determine the shape of the recovery in the second half of the year. The experiences of many Asian countries and first European countries show that new outbreaks of the virus cannot be prevented. The only question is whether authorities can withstand local curfews rather than larger-scale lockdowns. Also, the permanent damage of the crisis is still hard to gauge but it is hard to believe that sectors like retail, leisure or tourism have already seen the full and final impact from the crisis on employment. 'High uncertainty' will be the key phrase for all forecasters and policymakers. It will take until September before the global economy will get new guidance from macro data, policymakers and politics.

With regards to politics, now that European leaders have shown solidarity and agreed on a historic deal (which will have stronger symbolic than economic impact), financial markets' focus will probably shift to the US presidential elections. Given the experiences of the last few years, the election campaign alone has the potential of sending some shock waves to the global economy.

Looks as if all of us better fill up the tank to prepare for an action-loaded autumn season. Happy staycation.

<p><b>United States of Trump</b></p>  <p><b>Trump re-elected</b></p> <p> <b>Increased likelihood</b></p> <p>President Trump's approval rating has remained relatively stable around 42%, with a majority of Americans now expecting him to be re-elected in 2020. This view, along with the continuation of relatively positive economic conditions, has strengthened his chances for re-election.</p> <p>Although the continuation of trade tensions with China and the sharp increase in risk of a military conflict with Iran remain concerns, the potential for some form of agreement to be reached still exists, further assisting this scenario.</p>	<p><b>A Republican phoenix</b></p>  <p><b>Non-Trump Republican elected</b></p> <p> <b>Decreased likelihood</b></p> <p>This scenario is reliant on President Trump not running for re-election, a prospect that has continued to diminish.</p> <p>Following the release of the Mueller report, which did not make a judgement on whether President Trump obstructed justice, and the poor performance of former Massachusetts governor Bill Weld, the only other declared candidate for the nomination, President Trump launched his re-election campaign in Florida in mid-June. It seems unlikely that President Trump will not be the Republican nominee for President.</p>
<p><b>Consensus builders emerge</b></p>  <p><b>Centrist Democrat elected</b></p> <p> <b>Increased likelihood</b></p> <p>The emergence of Joe Biden as the frontrunner in the Democratic primary, and the increased likelihood of President Trump standing as the Republican nominee have strengthened the odds of this scenario.</p> <p>While positive economic figures mean the likelihood of this scenario has increased less than that for Trump re-elected, the signalling of future interest rate cuts, a sign of weakening economic conditions, indicates that this scenario is more likely than either <i>A Republican Phoenix</i> or <i>A New New Deal</i>.</p>	<p><b>A New New Deal</b></p>  <p><b>Populist Democrat elected</b></p> <p> <b>No overall change</b></p> <p>All three candidates which can be considered Populist (Sanders, Warren and Buttigieg) are polling within the top 5 of Democratic presidential nominees, giving this wing of the party momentum and press attention to make the campaign issues focused.</p> <p>This creates a positive pull on the likelihood of scenario 4.</p> <p>However, the positive performance of the US economy continues to serve as a mitigant against this scenario, leading to its classification of no change since our assessment in April.</p>

Source: ING, Oxford Analytica

**Author**

**Carsten Brzeski**

Global Head of Macro

[carsten.brzeski@ing.de](mailto:carsten.brzeski@ing.de)

**James Knightley**

Chief International Economist, US

[james.knightley@ing.com](mailto:james.knightley@ing.com)

**Peter Vanden Houte**

Chief Economist, Belgium, Luxembourg, Eurozone

[peter.vandenhoute@ing.com](mailto:peter.vandenhoute@ing.com)

**Iris Pang**

Chief Economist, Greater China

[iris.pang@asia.ing.com](mailto:iris.pang@asia.ing.com)

## US: Forget the “V”

With virus fears on the rise, jobs being lost and incomes squeezed, we feel the second phase of the recovery will be much more challenging, especially in the absence of a new broad and substantial fiscal package. And all of this suggests, financial markets optimism on a 'v' - shaped rebound could be severely tested in the next couple of months



Source: Shutterstock

Movement of people wearing a protective mask and maintaining social distance, Domino Park, Brooklyn

US economic output plunged 10.6% through the first half of the year. Yet as containment measures were eased through May and June the economy has bounced back strongly, led by the US consumer. There was certainly plenty of pent-up demand as we escaped the confines of our homes, but substantial stimulus from both the Federal Reserve and the Federal government undoubtedly fueled the recovery story.

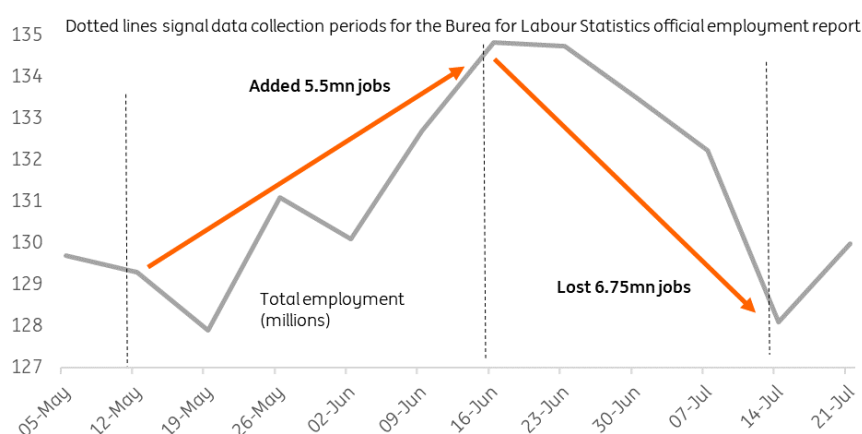
Aggressive central bank action lowered borrowing costs, kept credit flowing and supported confidence and asset prices. Meanwhile, a \$2+ trillion fiscal package provided a critical lifeline to households and businesses. Unfortunately, there are growing challenges to the recovery story.

Firstly, the recent spike in Covid-19 cases is hurting confidence. It is also leading many State

Governors to reverse course on their re-opening plans as they worry about strains on their healthcare systems if rising infection rates are left unchecked. The result is that businesses that had re-opened are being forced to close again with workers losing their jobs.

The Census Bureau's new Household Pulse survey suggests that employment may have reversed much of its gains since May. Perhaps most critically for near-term consumer spending the US\$600/week unemployment benefit boost given to 30 million claimants ended in July. Talks on another fiscal stimulus are dragging but in all likelihood, it might be replaced with something much smaller in size.

## Census Bureau Household pulse - employment millions



So, with virus fears on the rise, jobs being lost and incomes squeezed, the second phase of the recovery will be more challenging. In the absence of a timely and substantial fiscal package we should be braced for the threat of weaker employment and spending numbers, which will provide a major test for financial market optimism on the “V” shaped recovery.

### Author

**James Knightley**

Chief International Economist, US

[james.knightley@ing.com](mailto:james.knightley@ing.com)

---

Article | 6 August 2020

## Eurozone: Better, but the fear factor remains

After the historic GDP contraction in 2Q, Eurozone economic figures have improved, though the flare-up of Covid-19 infections has placed a burden on the recovery



Source: Shutterstock

A view of a deserted beach in Benidorm, Spain, one of Spain's hotspots for tourism.

### Historic GDP contraction

So we now have official figures that we can in the future refer to as the worst in history.

In the second quarter of 2020, Eurozone GDP contracted by 12.1%, with Spain even printing an 18.5% contraction. The good news is that as lockdown measures are eased, the European Commission's economic sentiment indicator has now risen three months in a row, with July's 87 point level firmly above the second quarter's average of 71.1.

---

*We maintain our -8.0% GDP forecast for this year, while slightly lifting our 2021 outlook to 4.8%*

---

While for the third quarter, the v-shaped recovery is still in place, the flaring up of Covid-19 infections clearly signals that until an effective vaccine is available, life will not return to normal.

The disappointing Spanish tourism season shows how vulnerable a great number of service sectors remain to the pandemic's vagaries. The health risk and targeted confinement measures are keeping consumers hesitant, leading to a higher propensity to save. On the plus side, the European Union has now decided on a recovery fund, which will provide about 0.8% of GDP fiscal stimulus, both in 2021 and 2022. We maintain our -8.0% GDP forecast for this year, while slightly lifting our 2021 outlook to 4.8%.

## Inflation quirk

Notwithstanding the VAT rate cut in Germany, eurozone core inflation actually increased from 0.8% to 1.2% in July.

However, this is probably a statistical quirk, since the sales period has been delayed until August in a number of countries, rendering the year-on-year comparison less favourable in July. That said, 2021 could see somewhat higher inflation as the German VAT rate will increase again and energy price inflation becomes positive.

But even then, we are only pencilling in 1.4% headline inflation.

## Euro trouble

Meanwhile, the euro's effective exchange rate has gained around 6% since February and it is not that far away from an all-time high.

While it might be too soon for the European Central Bank to counteract, it is definitely a factor that will contribute to low inflation, soliciting dovish comments from the ECB. And even if the tightening of spreads on sovereign bond yields could incite the central bank to slow down its bond purchases, the stronger common currency leads us to believe that an additional €400bn of PEPP (Pandemic Emergency Purchase Programme) remains feasible.

## Author

### **Peter Vanden Houte**

Chief Economist, Belgium, Luxembourg, Eurozone

[peter.vandenhoute@ing.com](mailto:peter.vandenhoute@ing.com)

## China's tech war with the US has made us revise our yuan forecast

The persistence of the technology war is hurting long term Chinese growth and the yuan's strength. Although we're revising our yuan forecast, it isn't much stronger from the current spot



Source: Shutterstock

In this photo illustration, a TikTok logo is seen displayed on a smartphone with the Chinese and American flag in the background

### New challenges to economic growth

The Chinese economy is recovering. GDP grew by 3.2% year-on-year in 2Q20 but there are new challenges ahead.

- The first-in-first-out from Covid-19 has been China's advantage compared to other economies. There have been some small clusters recently, but the government has acted swiftly to impose very tight social distancing measures, limiting the impact on the economy.
- There has been widespread flooding affecting agriculture as well as infrastructure construction. The typhoon season has also arrived, bringing more uncertainty to the flood damage.

These two challenges hurt short-term economic growth, and the government has offered help to offset some of the damage, so we are not too worried that these will hit GDP growth significantly in

2H20.

The longer-term challenge to the economy is the US becoming increasingly aggressive towards Chinese tech companies. US companies are banned from doing business with more Chinese companies and there were renewed threats on Huawei in May. Recently, the US administration has forced TikTok, whose parent company is a Chinese corporate, to be sold to US companies or stop operating in the US.

This hurts China's long term growth in technology exports.

## The yuan strengthens but only slightly

This technology war has put yuan strength at risk.

Even though China has fought against Covid-19 quite successfully, the yuan depreciated against the dollar to 7.1680 per dollar in May, which was the peak in 2020, as a result of the renewed threats to Chinese telecommunications group Huawei.

But in June, economic indicators improved and since then the Chinese economy has started to recover. From its peak, USD/CNY at 7.1680 to 6.9809 on 3 August, the yuan has appreciated by 2.61%.

If we measure the yuan's performance from the beginning of 2020, then it is still 0.25% weaker against the USD. This is in contrast with the dollar index's 2.95% depreciation over the same period. Some of the yuan appreciation that should have reflected in the USD/CNY exchange rate has been offset by the technology war.

We expect the technology war to persist for the rest of the year, which will continue to affect the yuan's performance.

We have revised our USD/CNY forecast to 6.97 from the previous 7.05 by the end of 2020.

We expect a stronger yuan from the previous forecast but the strength of the yuan from now to the end of 2020 is likely to be hit by negative news from the tech war.

### Author

#### Iris Pang

Chief Economist, Greater China

[iris.pang@asia.ing.com](mailto:iris.pang@asia.ing.com)

## FX: King dollar loses its crown

The dollar's four percent decline in July marked its largest monthly drop since 2010. Driving this decline is both a re-rating of the European project, but also the dollar's loss of its growth and yield advantage. The latter leaves the dollar vulnerable into November's contentious presidential elections



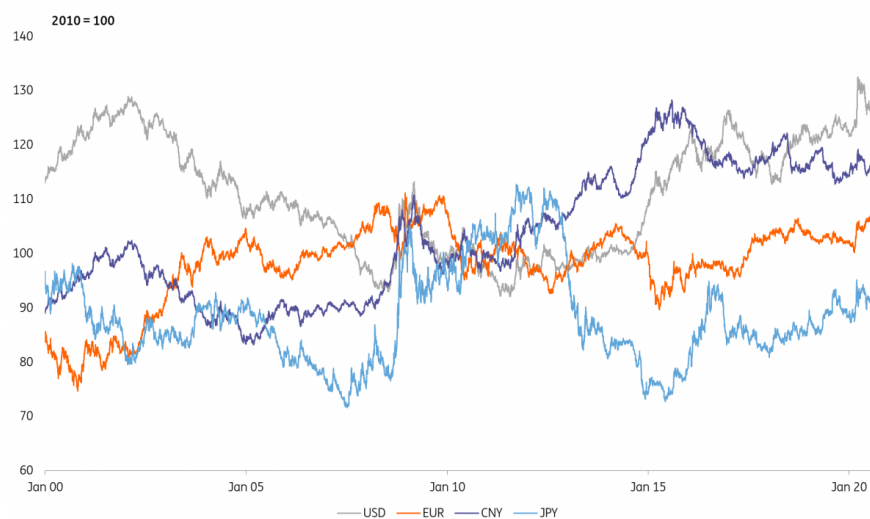
### Dollar: We don't need you any more

The myriad of factors which propelled the dollar around eighteen percent higher between March 2018 and March 2020 have faded. The dollar rally in 2018 and 2019 was all about large US fiscal stimulus and then US protectionism. These drove a growth and interest rate wedge between the US and the beleaguered overseas economies.

The dollar rally in March 2020 was all about liquidity needs. The fact that foreign central banks are now only drawing down around US\$100bn from the Fed's dollar swap lines – versus a peak of US\$450bn in May – suggests the need for emergency dollar liquidity or [hoarding](#) has reversed.

In other words, dollar demand from both the investor and commercial community is in decline and the dollar is no longer the only game in town.

## Trade weighted exchange rate indices: USD retreats from highs



Source: BIS

### Euro: A reluctant alternative

Progress on the EU recovery fund has prompted a re-assessment of the European project and the euro. Investor surveys show the fund management community are still overweight US equities but inclined to move into Europe. Depending on the path and handling of Covid-19 second wave, a re-allocation of funds towards Europe should be the theme for 2H20.

We expect EUR/USD to maintain its bullish momentum into an uncertain US presidential election in November. That means pressing 1.20, with outside risk to 1.25. This environment should also favour the liquid, defensive currencies of JPY and CHF – as the market seeks dollar alternatives.

### Author

#### Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

[chris.turner@ing.com](mailto:chris.turner@ing.com)

## Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. (“ING”) solely for information purposes without regard to any particular user’s investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit [www.ing.com](http://www.ing.com).