Investment Insight

June 2020

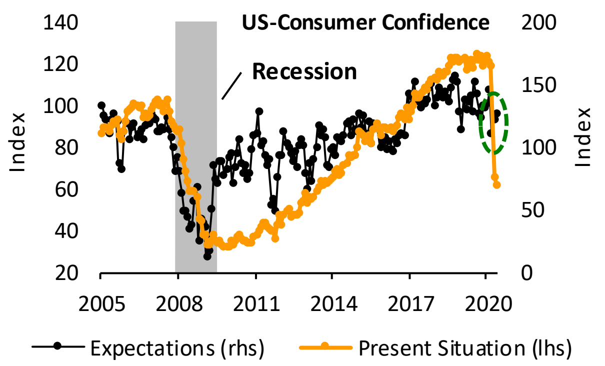
Recovery in sight

The coronavirus crisis is currently giving rise to devastating economic data. But governments and central banks are countering this with extensive support programmes. In addition, the pandemic is developing better than was feared. A recovery is already being anticipated on the stock exchanges.

The economic data makes it increasingly clear that the US economy will suffer an extreme growth slump in the second quarter of 2020. The Bureau of Economic Analysis (BEA) reports a decline of 13.6% in consumer spending for April. Even in the event of a recovery in consumption from May, a decrease of around 45% is likely to result for the quarterly average (annualised compared to Q1). For GDP overall, we maintain our forecast of a decline of a similar magnitude.

However severe the crash might be, a recovery is expected to set in quickly. There is a tailwind primarily from government support in the form of direct payments (cheques) and unemployment benefit. This will only partially offset the financial losses resulting from job losses for many households, whereas others are profiting all the more. This is partly due to the substantial unemployment support that Washington is paying in addition to the regular assistance from the federal states. The lump sum of USD 600 per week means that in particular people on low incomes are now better off than before the crisis despite losing their job. Thanks to this financial tailwind, US citizens are likely to soon make up for the purchases they have put off in the past two months.

USA: Consumers expect only a short economic downturn



Sources: Conference Board, BANTLEON

The government assistance has made the skyrocketing unemployment slightly less frightening. The Bureau of Labor Statistics had already shown a critical picture for April, with 20.5 million jobs lost and a record unemployment rate of 14.7%. The May figures are likely to be even worse. Although increased unemployment is impacting private households, it is putting relatively little pressure on consumer sentiment thanks to government assistance. This is shown by the Conference Board's Consumer Confidence Survey. For instance, the assessment of the labour market environment has already started to improve. This contributes to the consumer outlook also brightening. Contrary to what usually happens in recessions, the

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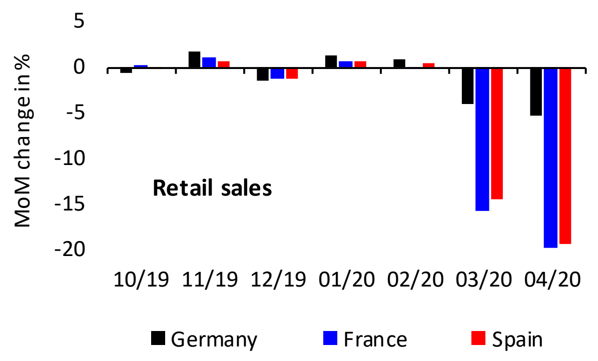
Expectations Index did not decline in step with the current situation in April and May, but instead improved (see figure above).

Private households' confidence is also being expressed in the significant increases in mortgage applications. In addition to private consumption, home construction is also likely to transform from a drag to a driver of growth in the third quarter as a result. All in all, this confirms our view that the US economy will not slip into a downward economic spiral, despite record unemployment. The US economy thus remains on track for a significant recovery in growth in the second half of the year.

In Germany, as expected, the ifo index rebounded in May from the crash of the preceding months, climbing from 74.2 points to 79.5. Although the assessment of the situation has worsened slightly again by 0.5 points to 78.9 due to the weak industrial data, business expectations leapt from 69.4 to 80.1 points because all economic sectors viewed the future less pessimistically. In view of the further easing measures coming into effect in June, we think that business expectations will rise significantly again. Based on our assessment of the current situation, the manufacturing sector is likely to follow the other sectors in June. Unlike in May, the expected increase in the ifo index will then be based on two pillars and therefore probably be even greater. The upward trend is expected to flatten in the following months.

However, the optimistic assessment due to leading indicators does not change the fact that after a decrease of 2.2% in Q1, German GDP will plummet by 10% to 15% in the current quarter. On the other hand, the retail sales reported for April encourage us to think that the decline could be closer to the upper end of the range (see figure right). According to preliminary estimates, sales only fell by 5.3% compared to March. The cumulative decrease in March and April is thus »only« 9%. The picture is very different in France and Spain. Retail sales dropped by around 20% in both countries in April and the decline since February is 33% in France and 31% in Spain.

Retail sales: Germany gets off lightly



Sources: Eurostat, BANTLEON

Medium term economic prospects have brightened with the reconstruction fund proposed by the European Commission. Worth EUR 750 billion, it is significantly more powerful than the Merkel-Macron plan worth EUR 500 billion. Together with April's rescue package, it would constitute at least 9% of EU GDP. The money is to be spread over the years from 2020 to 2024, which would generate an annual effect of an average of 2% of GDP per year and would therefore have a noticeable economic effect.

Confidence recently continued almost uninterrupted on financial markets

Italy and Spain, which were severely affected by the coronavirus crisis, will benefit the most overall from the reconstruction fund, but the eastern EU countries will receive the most money per capita. The lion's share of the cash is to be used for investments. Although this will fire up the economy less powerfully in the short term, it will lead to higher GDP growth rates in the medium and long term. National assistance programmes will take over short-term stimuli anyway. There are thus signs of a positive fiscal impetus of a so far unknown magnitude for Germany and the Eurozone. A similarly strong recovery next year is likely to follow the expected GDP crash of around 6% (Germany) and around 8% (Eurozone) this year. GDP growth in 2022 should also be significantly higher than the long-term potential of around 1.5%.

Confidence has recently continued almost uninterrupted on the financial markets. Risk assets such as equities, high yields, peripheral government bonds and crude oil were in high demand. Conversely, safe havens came under pressure (German government bonds, US Treasuries, USD, Swiss francs, gold). Investors' optimism was fuelled from various sides. For example, companies' business expectations recovered in May from their lows of March/April. At the same time, the steep downward trend in new infection figures continued in Europe. Finally, further impetus is coming from monetary and fiscal policy. Companies' profit prospects are therefore improving.

Political risks are more cause for concern than economic ones at the moment; in particular we would not put anything past *Donald Trump* in the dispute between the USA and China. A setback for the financial markets looks possible. Nevertheless, we expect share prices to be higher at the end of the year than today. For safe havens, by contrast, things are becoming increasingly uncomfortable.

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