Vaccine Economics[1]

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ABSTRACT

- **The Covid-19 vaccine will supercharge global growth in 2021, but short-term headwinds, and a complete recovery only by 2022, will create transition risks.**
- **In mid-2021, despite the sizeable hurdles on the demand (vaccination skepticism) and supply sides (production & distribution bottlenecks), we expect the vaccination of vulnerable populations (20-40% of the total) to be completed, setting the stage for a buoyant growth rally in H2 2021.**
- **Policymakers will particularly be under scrutiny, as they will continue to run the show again in 2021-22.**
- **In the real economy, cyclical sectors (including energy, metals, and automotive) to see strong catch-up growth as soon as Q2 2021 as the recovery starts to unfold and economic uncertainty recedes.**

[1] By Allianz and Euler Hermes Research

1. The Covid-19 vaccine will supercharge global growth in H2 2021, allowing for a full revovery by 2022

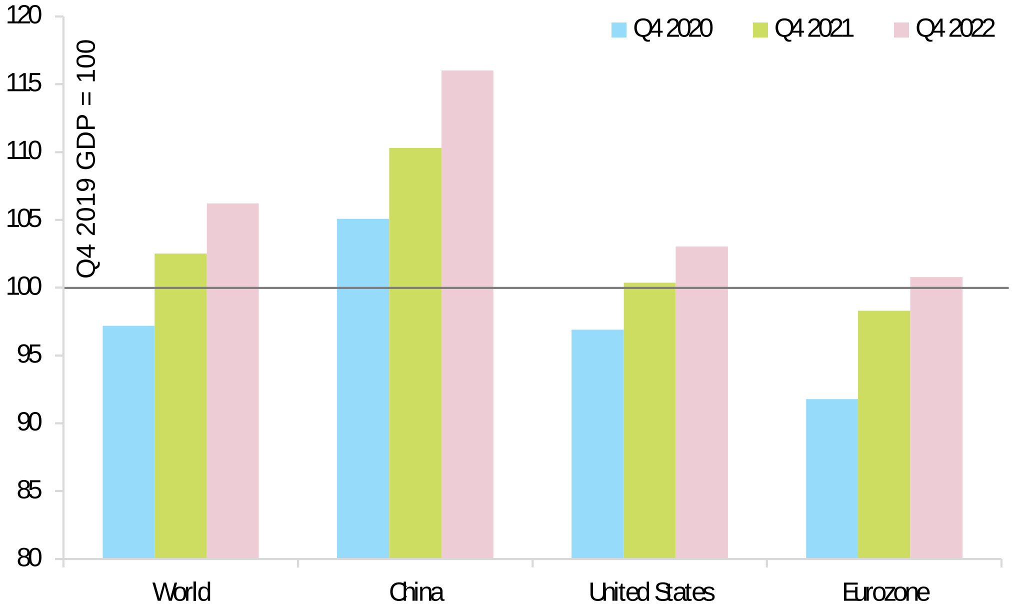
Recent breakthroughs on the vaccine front have led us to revise up our forecast for global economic growth to +4.6% (+0.2pp) in 2021, followed by a sustained recovery in 2022 at +3.8%. Despite sizeable hurdles on the demand (vaccination skepticism) and supply sides (production & distribution bottlenecks, we expect the vaccination rollout to vulnerable populations (20-40% of the total) to be completed by mid-2021 in developed countries and large Emerging Markets. By greatly reducing the pressure on healthcare systems, this will allow for a notable easing of Covid-19 restrictions, in turn setting the stage for a buoyant growth rally in H2 2021.

We expect Belgian GDP to fall by -5% in Q4 and rebound by +1.5% to +2.0% in Q1 2021. Overall, GDP growth is expected at close to -8% in 2020 followed by a rise of +2.5% to +3.5% in 2021 dependent on the confidence effects and fiscal stimulus package.

Expect sectors and countries most impacted by the Covid-19 crisis to outperform in this context, with the return of “social spending” ringing in the re-convergence between manufacturing and services. Meanwhile, economies with delayed or limited vaccine access – notably in the emerging world – will lag behind. A return to pre-crisis GDP levels is expected by Q4 2021 in the US and H1 2022 in Europe. China, meanwhile, will continue its economic normalization. The largely synchronized global economic upswing will also move forward the global trade recovery by a year, with trade in goods back at pre-crisis value levels by end-2020 and services in 2022.

However, the economic outlook risks getting worse before it gets better. Following the sharp Q3 rebound in activity, the economic rollercoaster ride continues at the turn of 2020/21. The resurgence in Covid-19 cases and fresh lockdowns will bring Q4 global economic activity to a standstill, with the quarterly rate slowing to +0.1% q/q after +7.3q/q % in Q3, thanks to a double-dip in Europe and a marked slowdown in the US. An economic resurrection is only on the cards from Easter onwards as warmer temperatures together with progress on the vaccination front will allow for a more marked loosening of restrictions and in turn the unleashing of demand pent up over the winter months.

Figure 1: Real GDP, Q4 2019 = 100



Sources: Euler Hermes, Allianz Research

2. Policymakers need to stay vigilant as the global economy is not out of the woods yet

We expect policymakers to step up support to keep a lid on long-term scarring to the economy and provide a tailwind to the recovery. On the fiscal side, in Europe, safety net measures look set to be extended (short-work schemes, state guaranteed loans & sector support) while in the US stimulus spending will be stepped up by another USD900bn in 2021. Meanwhile, central banks will continue to act as buyers-of-last-resort to the public and the private sectors to ensure favorable refinancing rates, with the Fed and ECB maintaining record-low interest rates until H2 2023. This will be justified by relatively contained inflation dynamics. On the other hand, the accelerating global economic recovery could see Chinese authorities already withdrawing policy support in H1 2021 (rising probability of a first rate hike), with focus shifting to mitigating long-term risks.

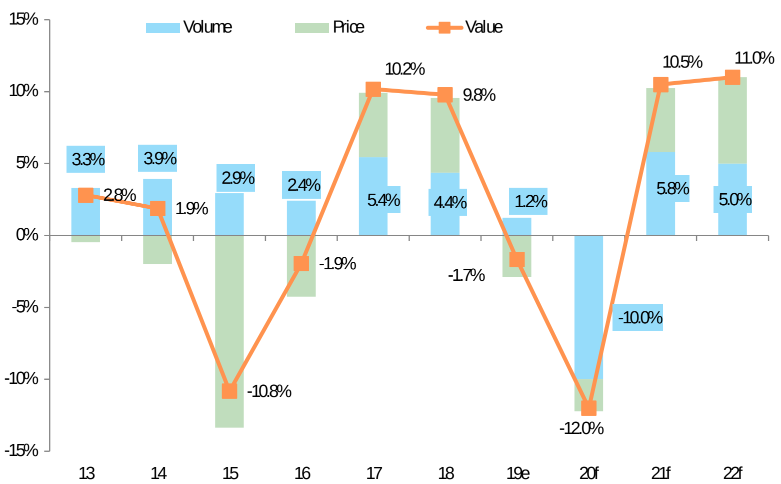
The key risks to our economic outlook center on developments on the vaccine as well as the policy fronts (health & economic), including:

- A short longevity of the vaccine's efficacy (implying the need for much higher resources in terms of frequent vaccination campaigns, which would also be a blow to confidence in the vaccine).

- Mutation risk, which could see researchers having to move back to square one.
- A premature economic re-opening in Q1 in Europe/the US without adequate track & trace procedures in place, which could trigger a triple-dip.
- Inadequate fiscal and/or monetary policy support (including no US fiscal deal as well as a delay of EU recovery fund).
- Debt sustainability concerns flaring up in emerging economies as soon as 2021.
- Unmanaged banking sector weaknesses as solvency risk moves front and center.

Vaccine recovery tailwinds could push forward the global trade recovery by one year, with trade in goods returning to pre-crisis value levels by end-2021 and services by 2022. The stronger recovery of global trade in goods, notably helped by impressive Chinese growth and more targeted lockdowns in Europe, has led us to revise our global trade growth forecasts for goods and services to -10% in 2020 (from -13% previously), +5.8% in 2021 (from 7% previously) and +5% in 2022. We now expect that trade in goods will recover its losses in value terms by the end of 2020 while services would be back to pre-crisis levels in 2022. In 2021, most countries will see export gains (i.e. an increase in exports with respect to 2020), with China (+USD372bn), Germany (+USD192bn) and Italy (+USD139bn) being the main winners. China, Vietnam, Australia and the Netherlands are likely to recover the fastest, with 2021 exports likely to stand at more than 10% above 2019 levels.

Figure 2: Global trade growth, goods and services, volume and USD value (y/y, %)



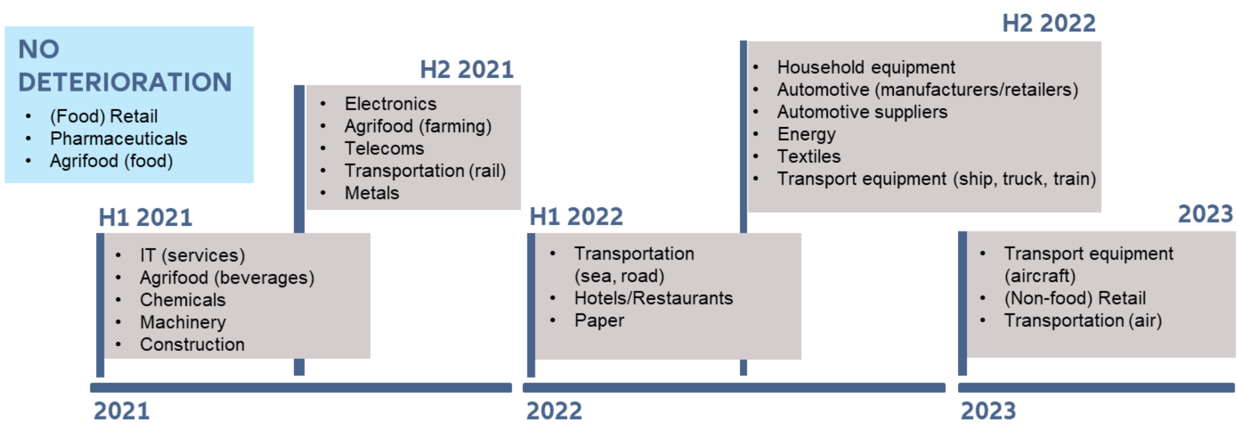
Sources: Euler Hermes, Allianz Research

Even as the recovery of global demand strengthens in 2021, we do not expect the return of the early 2000s globalization trends, nor a complete de-globalization. Instead, we see competing dynamics in global trade. Reshoring talk - for lack of appropriate dynamics to bring production home - will give way to Nearshoring moves i.e. bringing production to a nearby country as our Global Supply Chain Survey pointed out . This is in line with the renewed momentum for multilateralism, especially after the agreement of the RCEP and talks about the return of the US to TPP negotiations. Multishoring or diversification is also on the agenda as companies look for cost-effective supply and production solutions (notably still in China) after an unprecedented shock.

3. What does it mean for sectors?

With the rollout of the vaccine allowing for a return to "business as usual", we expect cyclical sectors (including energy, metals, equipment and automotive) to embark on strong catch-up growth as soon as Q2 2021. Covid-19 sensitive sectors will outperform markedly from H2 2021 onwards as the vaccination of at-risk populations allows for a return of "social spending" (accommodation, food services, transportation etc.). But despite the favorable momentum, the scars from the 2020 hit on turnover and profitability will take time to heal. We expect a majority of sectors to return to pre-crisis levels of turnover and profitability only by early 2022. Air transport (equipment and services) and non-food retail – in which the Covid-19-shock has accentuated powerful structural headwinds – stand out as key laggards that are only likely to recover to pre-crisis activity levels in 2023 and beyond.

Figure 3: Timeline recovery to pre-crisis turnover levels



Sources: Euler Hermes, Allianz Research

4. What does this mean for business insolvencies?

Our Global Insolvency Index posted a -12% y/y drop in Q3 2020, following -13% y/y in Q2, confirming the broad-based and prolonged slump in insolvencies recorded by courts. This despite hints of a timid trend reversal in some economies (Spain, Ireland, South Africa, South Korea, Hong Kong and Denmark) and conversely a downside reversal in China after a surge in Q2. Along with the lockdowns of courts, the paradoxical drop in insolvencies comes from massive support measures implemented and then extended by governments to provide liquidity, extra time and flexibility to companies before they resort to filing for bankruptcy.

The broad-based extension of “temporary” support measures into 2021 is likely to keep insolvencies artificially lower for longer. But their phasing out should start an increase in insolvencies as early as H2 2021, mainly composed of (i) pre Covid-19 “zombies”, i.e. companies that were no longer viable before the crisis but were kept afloat by emergency measures and (ii) Covid-19 “zombies”, i.e. companies weakened by the excess indebtedness resulting from the crisis. As a result, we expect our Global Insolvency Index to rise significantly in 2021 (+25% y/y), thanks to the basis effect created by the sharp drop in 2020 (-10%), as well as 2022 (+13% y/y). All regions would contribute positively to the upturn both in 2021 and 2022, with North America recording the most severe rebound (+57% by end 2022 compared to 2019) compared to Western Europe (+23%) and Asia (+18% or +12% excluding India). Yet, in 2021, one out of two countries in our sample would still register a low number of insolvencies compared to the Great Financial crisis and even the long-term average, notably among advanced economies.

All in all, our Global Insolvency Index for 2021 would be 13% higher than in 2019, prior to the crisis, and 2022 would be 27% higher than in 2019. In Belgium, we expect a 14% insolvency increase in 2021 and in 2022, we forecast an index 22% higher than prior to the crisis.

The phasing out of support measures remains critical and uncertain. Any new extension in terms of timing or magnitude would lead to a modified outlook, with less insolvencies in the short term but more insolvencies in the long term due to the increased ‘zombification’ of companies, notably in the sectors most impacted by the crisis. To this regard, the probability of an additional extension of support measures is higher in countries with larger fiscal and financing room for maneuvering. At a global level, should the support measures be extended for six additional months, the rise in insolvencies would be lower in 2021 (-18 pp to +7%) and higher in 2022 (+6pp to +19%) in a vast majority of countries, with some extra insolvencies in 2023.

Belgian Financial Forum

Figure 4: Business insolvencies by country

As of mid December 2020	in number					annual change in %					2021 vs 2019	2022 vs 2019
	2018	2019	2020f	2021f	2022 f	2018	2019	2020f	2021f	2022 f		
GLOBAL INDEX *	**112**	**122**	**110**	**138**	**155**	**11%**	**9%**	**-10%**	**25%**	**13%**	**13%**	**27%**
North America Index *	60	62	63	86	97	-4%	3%	3%	36%	13%	40%	57%
U.S.	22 158	22 720	23 500	32 000	36 000	-4%	3%	3%	36%	13%	41%	58%
Canada	2 677	2 746	2 250	3 000	3 400	-1%	3%	-18%	33%	13%	9%	24%
Latin America Index *	192	216	217	265	284	38%	13%	1%	22%	7%	23%	31%
Brazil	2 751	2 887	2 450	3 610	3 700	1%	5%	-15%	47%	2%	25%	28%
Colombia	1 243	1 272	1 100	1 400	1 560	53%	2%	-14%	27%	11%	10%	23%
Chile	1 386	1 701	1 880	2 150	2 300	32%	23%	11%	14%	7%	26%	35%
Western Europe Index *	133	134	110	141	164	0%	1%	-18%	28%	17%	5%	23%
Euro zone Index *	146	147	122	156	183	-2%	1%	-17%	29%	17%	6%	24%
Germany	19 302	18 749	16 076	16 900	19 500	-4%	-3%	-14%	5%	15%	-10%	4%
France	54 394	51 413	32 900	50 000	60 500	-1%	-5%	-36%	52%	21%	-3%	18%
United Kingdom	21 161	22 078	15 410	20 250	25 300	10%	4%	-30%	31%	25%	-8%	15%
Italy	11 227	11 106	5 500	9 500	12 500	-7%	-1%	-50%	73%	32%	-14%	13%
Spain	3 915	4 162	4 080	4 900	5 640	0%	6%	-2%	20%	15%	18%	36%
The Netherlands	3 633	3 792	3 290	4 100	4 800	-6%	4%	-13%	25%	17%	8%	27%
Switzerland	4 952	4 923	4 300	5 200	5 500	4%	-1%	-13%	21%	6%	6%	12%
Sweden	7 223	7 358	7 000	7 500	7 900	13%	2%	-5%	7%	5%	2%	7%
Norway	5 010	5 013	3 900	5 500	5 900	10%	0%	-22%	41%	7%	10%	18%
Belgium	9 878	10 598	7 300	12 100	12 900	-1%	7%	-31%	66%	7%	14%	22%
Austria	4 980	5 018	3 300	5 400	6 000	-2%	1%	-34%	64%	11%	8%	20%
Denmark	2 434	2 590	2 250	2 900	3 300	7%	6%	-13%	29%	14%	12%	27%
Finland	2 954	2 989	2 350	2 940	3 450	14%	1%	-21%	25%	17%	-2%	15%
Greece	82	94	85	110	130	-28%	15%	-10%	29%	18%	17%	38%
Portugal	2 694	2 560	2 560	3 150	3 500	-13%	-5%	0%	23%	11%	23%	37%
Ireland	767	568	600	780	900	-12%	-26%	6%	30%	15%	37%	58%
Luxembourg	1 356	1 445	1 330	1 640	1 730	33%	7%	-8%	23%	5%	13%	20%
Central & Eastern Europe Index *	236	243	252	302	315	-16%	3%	4%	20%	4%	24%	30%
Russia	10 282	11 741	10 500	13 400	13 700	-11%	14%	-11%	28%	2%	14%	17%
Turkey	13 593	14 050	15 700	17 850	18 400	-8%	3%	12%	14%	3%	27%	31%
Poland	988	969	1 140	1 330	1 370	10%	-2%	18%	17%	3%	37%	41%
Czech Republic	6 140	8 620	9 300	11 500	11 500	-15%	40%	8%	24%	0%	33%	33%
Romania	8 304	6 524	6 200	7 200	8 000	-9%	-21%	-5%	16%	11%	10%	23%
Hungary	5 692	5 176	4 350	5 200	6 100	-13%	-9%	-16%	20%	17%	0%	18%
Slovakia	1 959	2 447	1 929	2 186	2 452	124%	25%	-21%	13%	12%	-11%	0%
Bulgaria	476	506	535	669	756	9%	6%	6%	25%	13%	32%	49%
Lithuania	2 091	1 610	770	1 600	2 100	-30%	-23%	-52%	108%	31%	-1%	30%
Latvia	593	557	350	610	720	2%	-6%	-37%	74%	18%	10%	29%
Estonia	273	148	120	200	250	-20%	-46%	-19%	67%	25%	35%	69%
Africa & Middle East Index *	148	163	147	174	184	0%	10%	-10%	19%	6%	7%	13%
South Africa	1 845	2 042	2 050	2 550	2 700	-1%	11%	0%	24%	6%	25%	32%
Morocco	7 944	8 439	7 300	8 500	9 000	-1%	6%	-13%	16%	6%	1%	7%
Asia-Pacific Index *	117	139	118	143	163	42%	19%	-15%	22%	14%	3%	17%
China	10 600	11 826	11 850	12 700	13 600	69%	12%	0%	7%	7%	7%	15%
Japan	8 235	8 383	8 200	8 900	9 500	-2%	2%	-2%	9%	7%	6%	13%
India	965	1 895	740	1 600	2 500			-61%	116%	56%	-16%	32%
Australia	6 317	6 405	3 750	7 050	7 050	3%	1%	-41%	88%	0%	10%	10%
South Korea	469	414	400	470	470	-5%	-12%	-3%	18%	0%	14%	14%
Taiwan	217	205	205	220	230	-4%	-6%	0%	7%	5%	7%	12%
Singapore	207	287	217	260	300	23%	39%	-24%	20%	15%	-9%	5%
Hong Kong	255	244	250	300	300	-14%	-4%	2%	20%	0%	23%	23%
New Zealand	2 133	1 907	1 600	2 100	2 100	3%	-11%	-16%	31%	0%	10%	10%

(*) Index 100: 2000

Sources : national figures, Euler Hermes estimations (e) and forecasts (f)

Sources: Euler Hermes, Allianz Research

https://www.eulerhermes.com/en_global/news-insights/economic-insights/2021-22-vaccine-economics.html