The Economic Outlook: The Recovery Gets Harder from Here

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The global recovery is underway but its pace will vary across countries

Evolution of real GDP, 2018–2021 (index, 2019 = 100)

**World**
- global recovery underway

**US**
- strong start to recovery, but it gets harder from here

**Euro area**
- outlook uneven given virus resurgence in some countries

**Japan**
- good disease control is not enough

**UK**
- hit by delayed, worse Brexit

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<tr>
<th>‘18</th>
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<th>‘20</th>
<th>‘21</th>
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**Note:** Purchasing power parity weights used to calculate global GDP.

**Source:** Author’s calculations using GDP growth rates from OECD for 2019 and PIIE for 2020-2021.
The global recovery is underway but its pace will vary across countries

Evolution of real GDP, 2018–2021 (index, 2019 = 100)

- **China**
  - 2018: 94.3
  - 2019: 103.0
  - 2020: 109.2
  - 2021:
  - *Note:* recovery is strengthening and looks more sustainable

- **India**
  - 2018: 96.0
  - 2019: 98.9
  - 2020: 92.0
  - 2021:
  - *Note:* India struggling to contain virus and policy space limited

- **Russia**
  - 2018: 100
  - 2019: 98.6
  - 2020: 96.8
  - 2021:
  - *Note:* hit hard by lower oil prices

- **Brazil**
  - 2018: 100
  - 2019: 98.9
  - 2020: 92.0
  - 2021: 92.5
  - *Note:* underlying economic weakness and potential social unrest drag

*Note:* Purchasing power parity weights used to calculate global GDP.

*Source:* Author’s calculations using GDP growth rates from OECD for 2019 and PIIE for 2020-2021.
The early stages of the US recovery showed a sharp rebound in aggregate demand.

Gains in wealth and income left the fortunate consumers with great wherewithal to spend.

Source: S&P Dow Jones Indices; FRED

Source: US Bureau of Economic Analysis; FRED
Pent-up demand and low interest rates are powering spending on big-ticket items

New Single-Family Home Sales

- Thousands
- Years: 2000 to 2020

New Light Vehicle Sales

- Millions
- Years: 2000 to 2020

Source: US Census Bureau; FRED

Source: US Bureau of Economic Analysis; FRED
Demand has been sufficient to boost some aspects of business confidence

Firms are replenishing inventories, and, while some businesses have failed, applications to start new businesses are running high.

**Core Durable Goods Orders**

- Note: Nondefense capital goods excluding aircraft.
- Source: US Census Bureau; FRED

**Business Applications Filed By Likely Employers**

- Note: Four-week moving average data are as of week 39 of each year.
- Source: US Census Bureau; FRED
Inflation and inflation expectations have recovered to (low) pre-pandemic levels

Core PCE Prices
Percent change from year earlier

5-Year Breakeven Inflation Rate Implied by Treasury-Indexed Securities
Percent

Source: US Bureau of Economic Analysis; FRED
Source: Federal Reserve Bank of St. Louis; FRED
BUT: The US recovery is only partial and the pace of improvement is slowing

Nonfarm Payrolls

<table>
<thead>
<tr>
<th>Year</th>
<th>Change in Nonfarm Payrolls (Thousands)</th>
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<tbody>
<tr>
<td>Jun</td>
<td>4781</td>
</tr>
<tr>
<td>Jul</td>
<td>1761</td>
</tr>
<tr>
<td>Aug</td>
<td>1489</td>
</tr>
<tr>
<td>Sep</td>
<td>661</td>
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Source: US Bureau of Labor Statistics; FRED

Still down 10.7M from Feb. level
AND:
While the timing is similar across geographies, the recovery is very uneven

Change in Consumer Spending since January 2020
Percent

Change in Nonfarm Payrolls since January
Percent

Source: https://tracktherecovery.org/

Note: Data for profession and business services exclude temporary workers.
Source: US Bureau of Labor Statistics; FRED
Baseline US forecast calls for growth to follow more typical recovery path going forward

U.S. Real GDP Growth

Source: US Bureau of Economic Analysis; Fred; author’s forecast
The baseline forecast leaves the US economy 3 percent below where it would have been in 2021:Q4 in the absence of a pandemic.

**US Real GDP**

Extrapolating 2019:Q4 forward with 1.8% growth rate

Source: US Bureau of Economic Analysis; author’s forecast
Some of the gap is a shortfall relative to potential but some is a reduction in potential.

*Pandemic-affected potential GDP includes forces reducing aggregate supply over the short term and beyond.

Source: US Bureau of Economic Analysis; author’s forecast
## Potential forces weighing on the supply side of the economy

<table>
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<tr>
<th>Short-term</th>
<th>Medium-term</th>
<th>And beyond</th>
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<tbody>
<tr>
<td>Reduced ability to conduct business in sectors where virus containment is</td>
<td>Structural unemployment (and skill mismatch) as workers reallocate from</td>
<td>Lower level of private capital stock because of reduced business</td>
</tr>
<tr>
<td>difficult</td>
<td>sectors that do not revive</td>
<td>investment</td>
</tr>
<tr>
<td></td>
<td>Reduced “organizational capital” as firms fail and get replaced by new ones</td>
<td></td>
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<tr>
<td></td>
<td>Debt overhang in business sector (and possibly in household sector)</td>
<td>Lower level of public capital stock as budget gaps force states to tighten</td>
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<tr>
<td></td>
<td></td>
<td>belts</td>
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<td></td>
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<td>Less skill development due to remote education</td>
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Outcomes highly dependent on health and policy, so important to look at scenarios

All of the major economies had strong fiscal and monetary policy responses, but different health policies and different economic outcomes so far

Therefore, it is important in forecasting to consider alternative scenarios

Macroeconomic policy, health policy, and the extent of long-term damage will all matter
What might produce a stronger recovery?

Early vaccine is effective and has high take-up

Significant fiscal stimulus ($2+ trillion) is passed in early 2021

Economic scarring is limited and that which occurs does not significantly suppress economic activity
Upside scenario

Unemployment Rate

Source: US Bureau of Labor Statistics; author’s forecast
What might produce a weaker recovery?

Vaccine progress is slower than currently expected (partially effective and limited take-up)

Future fiscal stimulus is limited (modest package by February, nothing further)

Replacement of failed small businesses is slow

Household sector suffers wave of financial distress
Downside scenario

Unemployment Rate

Source: US Bureau of Labor Statistics; author’s forecast
# Addendum: Real GDP Growth Rates

<table>
<thead>
<tr>
<th>Real GDP Growth (Y/Y)</th>
<th>2019</th>
<th>2020</th>
<th>2021</th>
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<tbody>
<tr>
<td>Global Output Growth</td>
<td>2.9</td>
<td>-4.4</td>
<td>4.7</td>
</tr>
<tr>
<td>United States</td>
<td>2.2</td>
<td>-3.8</td>
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<tr>
<td>Euro Area</td>
<td>1.3</td>
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<td>United Kingdom</td>
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<td>China</td>
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