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SG Economics & Sector Studies

Fast restart, slow recovery

- One year on from the outbreak of the Covid19 pandemic, the global economic environment continues to be shaped by an unprecedented modern-day crisis. Vaccine rollout offers hope of being able to reopen economies over the course of 2021, and this, coupled with large scale policy stimulus and pent up savings, offers the prospect of a fast restart.

- Uncertainty on the health crisis remains high, however, and we present both a Central and Extended scenario reflecting this. Our Central scenario assumes that social distancing measures are effectively lifted by 1Q22. In the Extended, we assume the health crisis runs for an additional year.

- The open of 2021 saw an unexpectedly sharp move up on long bond yields in the US as markets discounted reflation at a faster than expected pace, and we have revised our bond yield outlook higher on both sides of the Atlantic, albeit to a significantly lesser extent for Europe. Reflecting the market confidence in the new Draghi government, we have also lowered our view of Italian spreads over Germany, and notably this side of the next general election due by June 2023. We nonetheless expect major central banks to be cautious and lean against unwarranted tightening of financial conditions.

- Recovery in commodity prices, frictions due to supply-chain dislocations coupled with a demand restart and various base effects are expected to translate into punctual price spikes, not least in the US. However, the surge in inflation is likely to be temporary with still significant excess capacity in labour markets keeping any self-sustained demand-driven inflationary process at bay. With central banks set to be more tolerant of near-term inflation overshoot, market risk premia on inflation could track higher.

- While we see potential for the restart to be fast, the recovery is likely to be slow due to scarring effects. Beyond the economic rebound expected in 2021, the Covid19 crisis will most likely leave behind permanent damage to the world economy via loss of human capital and large public and corporate debt, which absent more determined structural reform are set to weigh on long-term trend potential.

THE FUTURE IS YOU SOCIETE GENERALE

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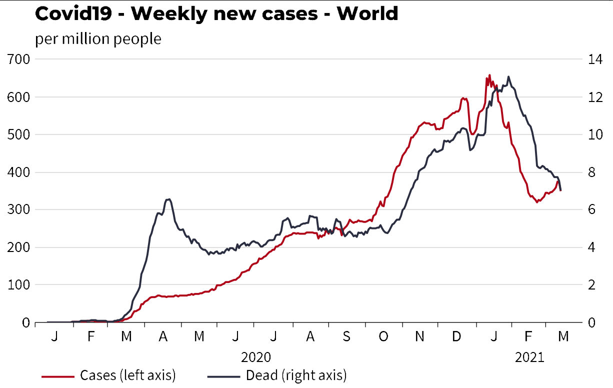
EXECUTIVE SUMMARY

WORLD ECONOMY RESTARTING

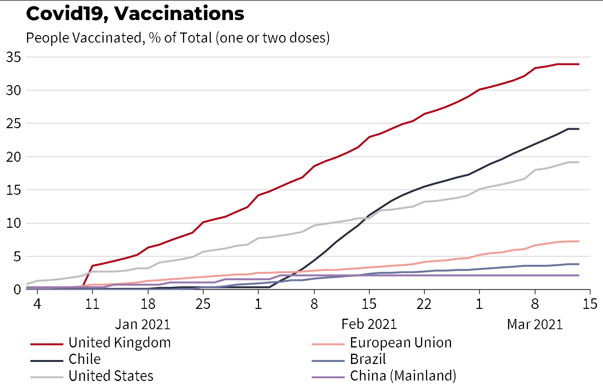
One year on from the outbreak of the Covid19 pandemic, the global economic environment continues to be shaped by a modern-day crisis that is unprecedented in terms of cause, suddenness, depth and heterogeneity. Despite significant scientific advances in the fight against Covid19, the outlook as to health outcomes and the approximate date of return to normality remains uncertain. Vaccine roll-out, although uneven, is gaining momentum, and the Covid19 death toll is slowing (*cf.* chart below). Yet, the circulation of the virus remains active, with new variants raising concerns. Economic activity remains under pressure from social distancing measures including lockdowns and reduced inter-country movement.

The pandemic persists but is slowing down



Source: CSSE at Johns Hopkins University.

Vaccination progressing at different speeds



Source: Official data collected by Our World in Data

Yet, hopes of a turnaround in the pandemic this year with vaccine roll-out and strong government stimulus in a few large economies (especially the $1.9 trillion US fiscal package) have improved the global economic outlook in recent months and lifted investor optimism. At the beginning of 2021, the resurgence of trade and industry has been noticeable, especially in Asia, and international trade in goods is now above pre-pandemic levels. In addition, many sectors, including even hard food services, have shown adaptability to pandemic restrictions.

Our global growth outlook for 2021 has been revised up compared to our previous scenario (in December 2020) reflecting upward revisions for the US, Japan and China. Note also, that many economies in Europe surprised with better-than -expected performance in 4Q20. Assuming that health restrictions can be gradually lifted, our central scenario forecasts that the world economy will rebound by 5.5% in 2021 (a +0.5pp revision from our last economic scenario), recovering from a -3.6% contraction in 2020. The strength of the recovery is set to vary significantly across countries, with the restart expected to be fastest in the US. The outlook also improved for China and India, which will in turn support growth in emerging Asia.

Covid19 remains the dominant driver of the world economic outlook in the short term. Given the high uncertainty regarding the evolution of the pandemic, we continue to accompany our Central scenario – based on a gradual exit from restrictions over the course of 2021 – with an alternative, Extended health crisis scenario that assumes it could be a year longer before normal life returns and that the restrictive measures are not lifted until 1Q23.

Reflation trade and bonds yields

The prospect of a restarting the global economy after the from the pandemic along with massive fiscal and monetary stimulus in developed countries is sparking a lively debate about a possible upcoming risk of inflation. This debate is being further fuelled by the ongoing shift in the major central bank policies, with the expectation of greater central bank tolerance for higher inflation after a period of undershoot.

Accumulated delays in deliveries and unfilled orders have already triggered punctual price increases in international markets, notably in industrial metals (copper, lead, nickel, tin and zinc), fertilisers and agricultural products (tea, rice, soybeans, wheat, sugar). The oil price, moreover, is now back at pre-pandemic levels, after OPEC+ decided to keep output largely unchanged amid higher demand.

The more positive market sentiment regarding growth and rising inflationary expectations have driven a rise in long-term interest rates since the beginning of 2021, and not least in the US. The 10y US Treasury, which started the year below 1%, broke above 1.6% mid-March, an upward movement also explained largely by an increase in market implied inflation expectations, albeit that real yields have also seen some gains. The 10y German Bund also headed up in early 2021, from -0.6% early January to -0.3% in mid-March.

Bottlenecks and shortages due to supply-chain Covid19-related dislocations coupled with a demand restart and various base effects are expected to translate into punctual price spikes in our central scenario in 2021, not least in the US. However, we expect much of this surge to prove temporary as persistent excess supply on labour markets are keeping the prospects of any self-sustained demand-driven inflationary process at bay. In the euro area, China, Japan and the US, recent CPI releases do not point to any price pressure up to now. Scarring from the Covid19 is indeed significant with an accumulation of debt on public and private balance sheets and job destruction.

Reflecting this reality, the Fed has expressed that it does not envisage a start to a rate normalisation as long as the labour market remains fragile. The unemployment rate, even if it is falling, is still at its highest level since 2014. Turning to the euro area, the ECB announced increased asset purchases to prevent any tightening of financing conditions. The Bank of Japan and the Bank of Australia also expressed willingness to intervene to curb long term rates if needed. Although we have made significant revisions to our interest rate outlook, and not least in the US, our overall narrative is still one of a prolonged period of low rates, engineered by central banks. This, in turn, should moderate potential snowball effects of higher public debt (which has reached historical levels), albeit that low rates are not a sufficient condition to reduce public debt burdens, most import is economic growth and here structural reform matters.

It cannot be ruled out that the adoption of ultra-accommodative fiscal and monetary policies for long periods of time could at some point damage the credibility of central banks, which have managed to anchor the public's inflation expectations at around 2% over the past 25 years. Yet, the role of "credibility" is not to be overstated as other structural factors are also influencing the inflation regime. Globalisation, coupled with technological advances, has in the past decades contained the price of many consumer products worldwide, helping central banks build their reputation regardless of their independency mandate. Policy error, be it protectionism, unproductive fiscal spending, failure to deliver structural reform or central banks acting too late, could see inflation expectations become unanchored with the risk of see the misery index summing high inflation and high unemployment return.

A SLOW RECOVERY WITH SCARRING EFFECTS

The restart can be fast, but the recovery is likely to be slow due to scarring effects. After the rebound in 2021 (+5.5%), global growth is expected to gradually slow, and we expect global GDP to increase 3.3% in 2022 and 2.9% in 2023 (Central scenario). Beyond the economic rebound, the Covid19 crisis will most likely leave permanent damage to the world economy via damage to human capital and large public and corporate debt. Low profitability in sectors damaged by the pandemic also weakens growth potential. Against this backdrop, there is a risk of a vicious circle arising between high indebtedness, lower growth potential, and firm bankruptcies, which could seriously weaken economic growth. Beyond monetary support, government policies regarding upgrading existing infra-structure and the reskilling of labour will be crucial in order to sustain the recovery post-Covid19. Accelerating green and digital transitions will also be critical.

In our Central scenario, the time to catch up to the 4Q19 GDP levels will be relatively fast for the US, where the economy will reach pre-crisis income by 2Q21, but rather slower for the euro area (1Q23) and the UK (1Q24). Regarding emerging market economies (EME), China and a few other countries (Egypt, Turkey) already recovered pre pandemic income levels and posted positive GDP figures in 2020, and most others – including Brazil, India and Russia – should retrieve their 2019 GDP level in 2022. Asia is likely to benefit from the rebound of the Chinese economy and the recovery in international trade. Questions remain regarding the capacity of EME to grow on the basis of their domestic markets despite high levels of debt. The situation looks challenging in Latin America and Africa, where (with a few exceptions) room for policy manoeuvre is smaller – amid higher government debt ratios– and fragilities are higher regarding potential reversals in international capital flows.

ECONOMIC FORECASTS

Real GDP Growth, %

	2019	2020f	2021f		2022f		2023f	
	Actual	Actual	Central	Extended	Central	Extended	Central	Extended
Developed Markets	**1.6**	**-5.3**	**4.8**	**2.1**	**2.8**	**2.8**	**1.7**	**2.7**
United States	2.2	-3.5	5.3	2.5	3.8	4.1	2.2	3.0
Japan	0.3	-4.9	3.4	0.3	1.7	2.0	0.6	1.1
United Kingdom	1.4	-9.9	5.0	2.0	3.0	3.0	2.0	2.5
Euro area	1.3	-6.8	4.9	1.6	2.0	1.1	1.4	3.8
Germany	0.6	-5.3	3.0	0.5	2.5	1.0	1.3	3.5
France	1.5	-8.2	6.5	3.5	1.7	1.0	1.5	4.0
Italy	0.3	-8.9	6.3	2.0	1.5	1.0	1.1	3.0
Spain	2.0	-11.0	7.2	2.0	3.0	1.2	1.8	5.2
Emerging Markets	**3.5**	**-2.6**	**5.9**	**3.6**	**3.6**	**3.7**	**3.7**	**4.0**
Asia	4.9	-1.0	7.4	5.1	4.6	4.8	4.6	4.9
China	6.0	2.3	8.0	6.0	4.9	5.0	4.6	5.0
India	4.9	-8.0	10.0	6.5	5.8	7.0	4.7	5.2
CEE	2.1	-4.1	3.7	1.4	2.1	2.3	2.5	2.6
Russian Federation	1.2	-2.9	2.0	-0.5	1.5	2.5	1.5	1.5
Latin America	0.1	-7.4	4.4	2.0	1.8	2.0	1.9	2.1
Brazil	1.1	-4.8	4.1	1.0	2.2	3.2	2.2	2.2
Middle East & Cent. Asia	0.3	-5.6	2.6	0.6	1.9	1.6	2.1	2.3
Africa	3.3	-2.4	3.3	1.3	2.7	2.4	3.4	3.6
World (PPP weighted)	**2.8**	**-3.6**	**5.5**	**3.0**	**3.3**	**3.4**	**2.9**	**3.5**

Market variables

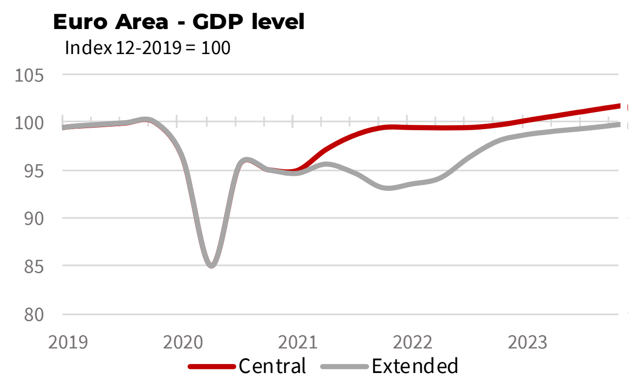
		Central			Extended		
end of period, %	**15.3.21**	**2021f**	**2022f**	**2023f**	**2021f**	**2022f**	**2023f**
Fed Funds target (high)	0.25	0.25	0.25	0.50	0.25	0.25	0.25
Gov 10Y, United States	1.60	1.80	2.00	2.25	0.75	0.75	1.00
ECB Refinancing rate	0.00	0.00	0.00	0.00	0.00	0.00	0.00
ECB Deposit facility rate	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
Gov 10Y, Germany	-0.33	-0.10	0.00	0.20	-0.60	-0.60	-0.50
Gov 10Y, France	-0.09	0.20	0.50	0.60	-0.20	0.10	0.10
Gov 10Y, Italy	0.60	0.90	1.50	1.70	0.65	1.15	1.25
Gov 10Y, Spain	0.30	0.70	1.10	1.20	0.35	0.65	0.75
BoE, Bank rate	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Gov 10Y, United Kingdom	0.80	0.90	1.00	1.20	0.40	0.60	0.60
BoJ rate	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
10y government bond	0.11	0.00	0.00	0.00	0.00	0.00	0.00
EUR / USD	1.19	1.15	1.15	1.20	1.10	1.10	1.10
EUR / GBP	0.86	0.95	0.95	0.95	1.00	1.00	1.00
USD / JPY	109	110	110	105	105	105	105
USD / CNY	6.49	6.50	6.50	6.50	6.50	6.50	6.50
Brent ($/b)	69	55	55	55	48	50	50

EURO AREA

- **The convergence of GDP to its pre-crisis level will be slow and growth paths will diverge from one economy to another.**
- **Monetary policy will remain very accommodative and interest rates are set to stay low over the forecast horizon.**
- **There are several downside risks; notably financial instability or a surge in political tensions.**

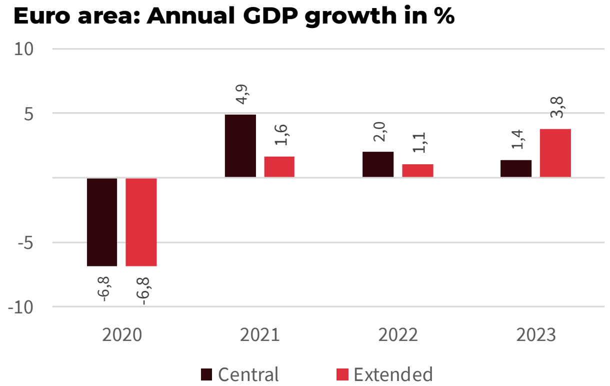
The intensification of non-pharmaceutical interventions (NPIs) in late 2020 did not exacerbated the recession as much as expected. However, the latter remains more severe than the recession recorded by the euro area during the previous financial and sovereign debt crises. In 2021, vaccination campaigns and the gradual unwinding of NPIs will support the rebound in activity, especially in the second half of the year. Catching up will continue in 2022, but at a more moderate pace. In the wake of the 2020 shock, rising unemployment will slow the absorption of accumulated savings by households, while weaker corporate balance sheets will weigh on the investment cycle. Against this backdrop, GDP is expected to return to its pre-crisis level in 2023 only in our Central scenario. If the pandemic risk were to last longer, delaying the withdrawal of NPIs for one year (to early 2023 instead of early 2022), GDP convergence would also be delayed for one year.

Recovery is set to be very progressive



Source: SG Economic and Sector Studies

Growth will be very moderate in 2022-2023



Source: SG Economic and Sector Studies

The European Recovery Plan (calibrated according to income losses of each country) will help to ease divergence in the growth trajectories of the different economies. However, a certain degree of divergence seems inevitable as some economies are more exposed than others to the pandemic through the sector channel[1].

In 2021, world trade is set to rebound a little more strongly than initially expected, in the wake of better-than-expected growth in China and the US. Longer term, the

[1] For example, the sectors hardest hit by health measures, such as the arts, entertainment and recreation, wholesale and retail trade, accommodation and food services, and air transport represent 21.4% of GDP in Spain compared to only 13.0% in Germany (Eurostat data from 2019).

recovery will, nonetheless, remain very gradual, reflecting a different pace of the pandemic's ebb on a global scale and scarring. In addition, certain factors that drove the recovery after the great financial crisis will not be present this time. For instance, the absence of a major fiscal stimulus in China, and the weakening of many emerging economies by the pandemic, rule out the scenario of a marked and lasting rebound in external demand. Euro area exports are therefore expected to show moderate growth on average over the forecast horizon.

In the wake of the shock recorded in 2020, the rebound in domestic demand will be modest in the medium term. With the support of various national public guarantee mechanisms, companies have increased debt to compensate for the losses linked to lockdowns and various other social distancing measures. In this context, the deterioration in debt ratios, already high in some countries before the crisis, is set to weigh on investment recovery. In addition, some increase of defaults will likely see tightening of bank lending conditions, albeit much less marked than during the crises of 2008-2013.

On the household side, the rise in unemployment and wage moderation is set to weigh on consumption. The "forced" savings accumulated during the confinement period will certainly not be entirely spent, as precautionary behaviour prevails in an uncertain economic environment. The loss of income and tighter lending conditions will also weigh on residential investment.

Public demand will be stronger. However, despite the low financing costs of governments, some countries' public debt ratios already high before the crisis limit fiscal room. The grants that will benefit Member States as part of the European Recovery Plan in 2021-2023 will finance part of the support measures, which will help to rule out the scenario of a strong divergence in growth trajectories (which will nevertheless be observable).

In the Committee of 11 March, the ECB maintained the total envelope of the Pandemic Emergency Purchasing Programme (PEPP). In the short run, the ECB's strategy will continue to be dictated by managing the direct repercussions of the crisis (ample supply of liquidity to banks and massive asset purchases). Longer term, normalisation of monetary policy appears difficult and the risk will remain tilted towards additional easing measures. The ECB's upcoming strategy review of the monetary policy will offer more insight on how the institution will manage its future QE policy and the eventual exit from the PEPP.

In 2021, the rebound in inflation will mainly reflect base effects, which will dissipate from 2022. Beyond that, price dynamics will remain modest.

The moderation of labour costs and weak demand will dissuade companies from raising their prices, while at the same time the rise in oil prices will remain moderate. Thus, the mobilization of TLTROs and asset purchases (via extending the duration and increasing the size of their envelope) will remain at the heart of the ECB's strategy.

The risk of further trade tensions ebbing with the new US Administration offers a slight improvement in the balance of risks surrounding our scenario. However, the list of downside risks remains long, and not least the risk of a longer health crisis. Likewise, the downgrading of the sovereign rating of the most fragile states or too strong and too early fiscal consolidation threatening the recovery could feed tensions in the sovereign debt market. Finally, a new surge in euroscepticism and political risk ahead of elections in key Member States cannot be ruled out.

Euro Area	2019	2020	2021f		2022f		2023f	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	1.3	-6.8	4.9	1.6	2.0	1.1	1.4	3.8
Inflation, %	1.2	0.3	2.0	1.9	1.1	1.2	1.3	1.4
Unemployment, %	7.6	8.0	8.7	9.2	9.1	9.9	8.8	9.6
Fiscal balance, % GDP	-0.9	-8.3	-5.9	-7.6	-5.2	-7.5	-4.9	-6.0
Public debt, % GDP	89	105	106	112	109	117	111	117

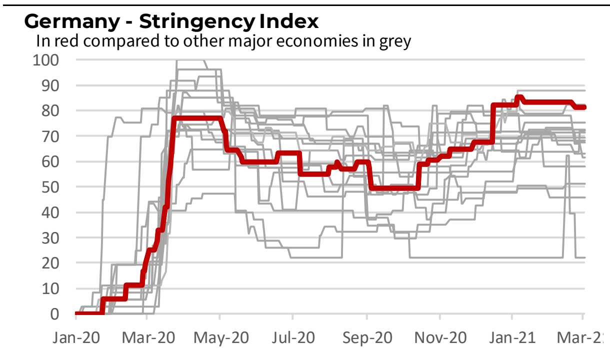
Base = Central scenario
Ext. = Extended health crisis scenario

GERMANY

- **Convergence of the economy towards its pre-crisis level will be faster than elsewhere in the euro area but will remain gradual.**
- **Once past the technical rebound in 2021, inflation remains moderate over the forecast horizon.**
- **Despite the deterioration of public and private debt ratios, the risks to financial stability are limited.**

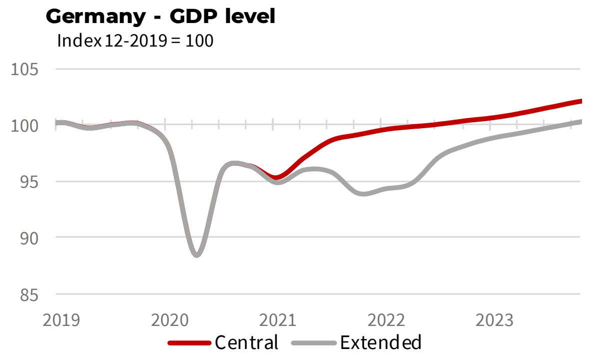
The German economy held up well against tighter non-pharmaceutical interventions (NPIs) at the end of last year. In contrast to the other major economies in the euro area, the scale of the recession in 2020 was no greater than in 2009. In 2021, the maintenance of strict NPIs in the first quarter will initially hamper any rebound in activity, before it picks up again in the second half of the year with the ramp-up of the vaccination campaign. The rebound is expected to continue in 2022, allowing the economy to return to its pre-crisis level during the year, faster than its counterparts in the rest of the euro area. The lagged effects of the crisis on employment, investment, and external demand (especially from the rest of the euro area) will cap the scenario of faster recovery.

The ever-present health crisis…



Source: University of Oxford

… But growth will pick up from 2Q-20



Source: SG Economics & Sector Studies

On the external demand side, normalisation is likely to be more moderate than observed in the wake of the Great Financial Crisis. In the short term, the rebound in exports will remain strong, supported by the reopening of the European economies and the stronger than expected recovery of activity in the United States and China. Longer term, however, it will be more difficult for German companies to compensate for the moderation in demand in Europe by redirecting sales to emerging markets as was the case a decade ago. Indeed, the scale of the fiscal stimulus will be more modest in China, while emerging economies will emerge from the health crisis weaker overall.

The subsidies granted and the equity provided by the public authorities have pushed at bay the scenario of an excessive deterioration in the balance sheet of companies.

Debt ratios will, however, have increased with the interruption of activity in 2020. This factor, together with the relative weakness of expected demand, will weigh on the rebound in investment medium term. On the household side, the rise in unemployment and the decline in per capita income will weigh on consumption in 2021-2022 beyond an initial restart. Growth in housing investment will also be modest for the same reasons, suffering in addition from a likely tightening of lending conditions by banks. One positive could, however, come from climate related real-estate renovations and upgrades.

Emergency "Above the line" fiscal measures	**EUR/bn**
Enhancement of health care provisions	58.5
Economic Stabilisation Fund	100.0
Grants to small and individual businesses	50.0
Total	208.5
% GDP	6.1%
Measures of the recovery plan	
Temporary VAT rate cut (2S-2020)	20.0
Temporary energy tax cut	11.0
Exceptional social benefit (400 EUR per child)	4.0
Stronger incentives to buy electric vehicles	2.2
Tax deferrals for companies	25.0
Exceptional credits to local administrations	13.0
Other spending measures	54.8
Total	130.0
% GDP	3.8%

The increase in public demand recorded in 2020 as part of the emergency measures and the recovery plan will continue to have positive effects on activity. The budgetary measures taken in response to the health crisis and the stimulus plan represent around 10% of GDP. Public debt is expected to increase by around 15 percentage points of GDP over the forecast horizon, to around 75% of GDP in 2023.

Inflation will rise punctually in 2021 due to positive base effects on energy prices and on the prices of goods and services that had benefited from the temporary VAT cut in the second half of 2020. Once these effects have dissipated, inflation is set to slow from 2022 onwards to reflect an environment of high unemployment and moderate labour costs.

Despite the deterioration in public and private debt ratios, the risks to financial stability appear to be limited. The new US Administration, and the easing of trade tensions which should result, reduce the downside risk on the dynamics of foreign trade. But at the same time, the downside risks remain numerous. In particular, too slow a roll-out of the vaccination campaign would delay the convergence of the economy towards its pre-crisis level.

Germany	2019	2020	2021f		2022f		2023f	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	0.6	-5.3	3.0	0.5	2.5	1.0	1.3	3.5
Inflation, %	1.4	0.4	2.1	1.6	1.2	1.0	1.4	1.5
Unemployment, %	5.0	5.9	6.6	7.0	6.7	7.4	6.5	7.2
Fiscal balance, % GDP	1.5	-5.3	-4.3	-5.6	-3.5	-5.5	-3.3	-4.3
Public debt, % GDP	60	72	73	76	74	80	75	80

Base = Central scenario
Ext. = Extended health crisis scenario

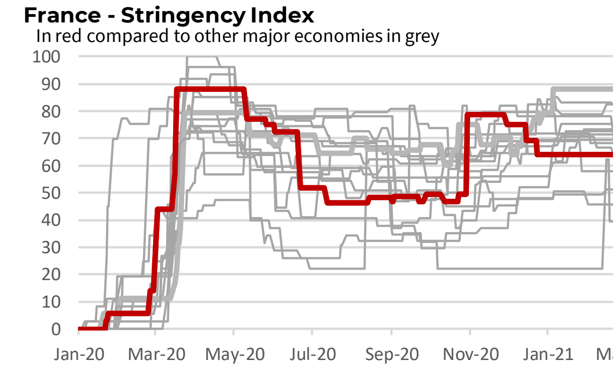
FRANCE

- **The health crisis legacy on employment and debt will weigh on growth in the medium term.**
- **Favourable base effects will support inflation this year, but it is set to moderate in the medium term.**
- **Public debt is expected to increase by 30pp of GDP over the forecast horizon, exceeding 130% of GDP in 2023.**

The economy withstood the second lockdown late last year better than expected. Nevertheless, the recession in 2020remains historic, with GDP falling by 8.2% over the year. In 2021, growth will rebound fairly strongly in the wake of the gradual unwinding of non-pharmaceutical measures (NPIs), which would be completely lifted at the beginning of 2022 in our Central scenario. Longer term, the withdrawal of support measures and the legacy of the crisis in terms of job destruction and both public sector and corporate indebtedness will weigh on growth. While fiscal stimulus will boost activity in 2021-22, it will not fully compensate the loss of income in 2020.

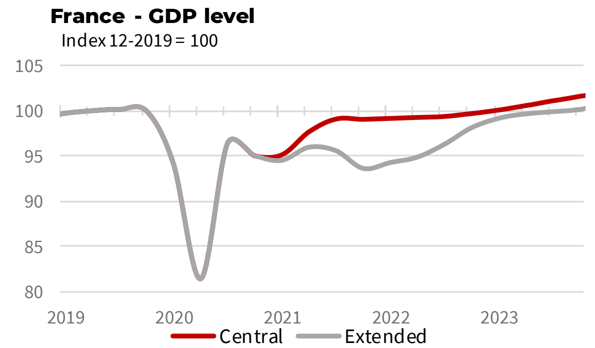
In this context, the convergence of GDP towards its pre-crisis level will be long. Our Central scenario does not see this before 2023, with an unemployment rate reaching 10% at its peak. In the scenario of an Extended health crisis, where NPIs would not be completely lifted before 1Q23, GDP convergence to pre-crisis levels would also be delayed by one year to 2024.

The second lockdown was less strict



Source: University of Oxford

Towards a very progressive recovery



Source: SG Economic and Sector Research

The pandemic will continue to weigh on the dynamics of foreign trade. Indeed, French exports are heavily dependent on the prospects in aeronautics and tourism, two sectors particularly vulnerable to the evolution of the pandemic. With the uneven and choppy ebb of the pandemic on a global scale, the rebound in exports is therefore set to be progressive.

Budgetary measures adopted in response to the health crisis	Size EUR bn
▪ **First emergency plan (PLFR I, II and III) - 2020**	**64.5**
Including:	
▪ Enhancement of short time working schemes	30.8
▪ Solidarity Fund (subsidies for the smallest companies)	8.5
▪ Exceptional funds for health administrations	9.8
▪ Offset of social security contribution exemption	5.2
▪ Extension of income replacement and postponement of the reform of unemployment insurance	1.6
▪ **2020-2025 recovery plan (including EUR 37 billion of Maastrichtian measures[2] included in the 2021 PLF)**	**100**
Demand-driven measures:	**41**
▪ Public investment (including energy renovation of buildings, green infrastructure and mobility)	23
▪ Support for households (including support to the purchase of clean vehicles and increase in the back-to-school allowance)	10
▪ Other public expenditure (including digitalisation of public services and companies)	8
Supply-driven measures:	**44**
▪ Tax cuts on production	20
▪ Innovation (including Future Investment Programs)	16
▪ Employment and training (including youth plan, short time working and investment in skills)	8
Autres mesures	**15**
▪ **First emergency plan (PLFR IV) - 2020**	**20**
Including:	
▪ Enhancement of the Solidarity Fund	10.9
▪ Extension of the most favourable short time working scheme until December 2020	3.2
▪ Exceptional poverty allowance	2.1
▪ Other measures (including advancement to 2020 of the second Ségur health pact component)	4,3
Total du plan	**184.5**
% du PIB 2019	7.8

Source: DG Trésor, PLFR I, II, III & IV, PLF 2021, SG Economic and Sector Research

Productive investment has so far withstood the crisis well but is expected to show modest growth in medium term. Businesses have been weakened by the forced shutdown of entire sectors of the economy in 2020. The liquidity impact of operating losses has been largely offset by heavy borrowing and debt ratios, already high before the crisis, and have deteriorated. In this context, as the crisis also has severely affected the value of collateral, investment may suffer from less and more selective financing. In addition, in the absence of a sustained and lasting rebound in demand, the most indebted companies will be forced to postpone part of their investments in order to increase their financing capacity and stabilise debt ratios. In the long term,

[2] Part of the stimulus plan spending will not be accounted in the budget balance. Indeed, some of them will not be executed by entities identified as public administrations within the meaning of Maastrichtian accounting. In addition, others are financial transactions and will be recorded directly in the public debt ratio and not in the budget balance.

this expected moderation in investment is likely to affect the growth potential of the French economy.

On the household side, job destruction and wage moderation will weigh on spending in the medium term. The absorption of "forced" savings accumulated during the lockdowns will drive consumption in 2021 as the pandemic recedes. But with rising unemployment, households will retain precautionary savings, ruling out the scenario of consumption rapidly converging to its pre-crisis level. Residential investment, which has resisted the crisis rather well, will slow down under the effect of the moderate tightening of credit conditions by the banks.

Favourable base effects on energy prices will bring inflation back to its 2019 level this year. But in the longer term, moderate labour costs and weak demand expectations rule out a stronger rebound in inflation.

The contraction of activity and the government's emergency measures in response to the health crisis will have seriously deteriorated the fiscal position in 2020. The unwinding of certain exceptional measures and the subsidies earmarked to France as part of the European recovery plan will contribute to improving the public balance in 2021. But with the execution of the recovery plan and the slow convergence of the economy towards its pre-crisis level, public debt ratios will deteriorate over the forecast horizon, the public debt reaching 130% of GDP in 2023.

The balance of risks surrounding our scenario has improved with the new US Administration and the risk of trade tensions ebbing accordingly. On the upside risks, a more active government policy on strengthening corporate equity would help accelerate the investment cycle and bring the economy to its pre-crisis level at a faster pace. But the list of downside risks remains long, from a delay in the vaccination campaign and new social movements.

France	2019	2020	2021f		2022f		2023f	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	1.5	-8.2	6.5	3.5	1.7	1.0	1.5	4.0
Inflation, %	1.3	0.5	1.3	1.1	1.1	1.2	1.3	1.3
Unemployment, %	8.1	7.8	9.3	10.0	9.9	10.4	9.5	10.0
Fiscal balance, % GDP	-3.0	-10.2	-6.2	-7.8	-5.7	-7.6	-5.0	-5.6
Public debt, % GDP	98	116	120	124.5	123	130	126	130

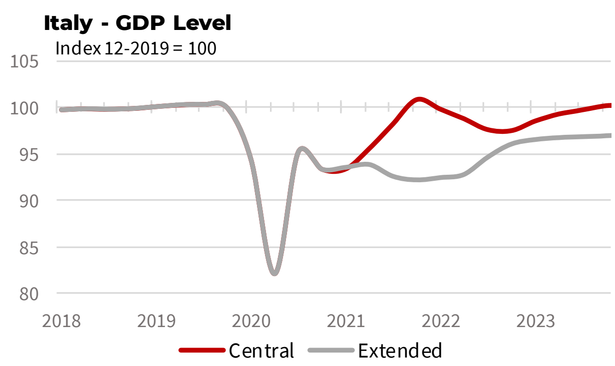
Base = Central scenario
Ext. = Extended health crisis scenario

ITALY

- **Policy support to underpin fast restart.**
- **Economic scarring and structural headwinds spell slow recovery.**
- **A narrow window of opportunity for reform.**

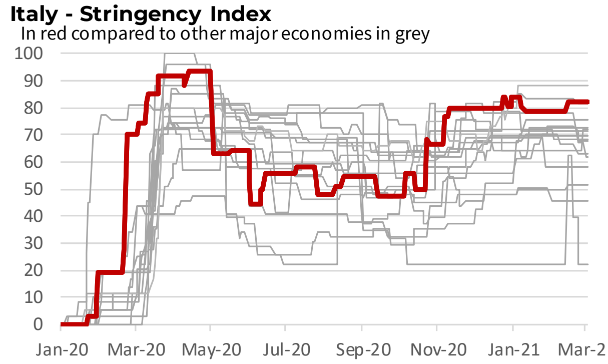
2021 opens with an economy still under pressure from social distancing measures, but the ongoing rollout of the vaccine programme and further fiscal support in the pipeline hold out the prospect of fast restart over the summer, albeit that uncertainty on the health crisis remains significant. Market confidence was boosted as Mario Draghi was sworn in as Prime Minister on 13 February 2021 and the coming weeks will deliver details on Italy's recovery plan. The present national unity government has the advantage of implementing fiscal stimulus rather than austerity, which offers a better chance of reform. Our central scenario assumes some progress, but we still see many remaining structural headwinds, which coupled with the economic scarring from the Covid19 crisis, spell a slow underlying recovery.

Quick start on reopen, slow recovery



Source: SG Economic and Sector Research

Tough social distancing remains



Source: University of Oxford

As we head to press, the first support package of Mario Draghi's national unity government of a reported €32bn (2% of GDP) is being readied with the aim to extend further temporary support measures to the hardest hit sectors, assist families and accelerate the vaccine programme. These support measures come as Italy, like many of its European neighbours, has set new social distancing measures under pressure from the spread of new coronavirus variants.

The coming weeks will, moreover, see a flurry of activity as the Draghi government finalises the national recovery and resilience plan to be submitted to the European Commission by end-April and then assessed by the Commission, with the hope that the European Council then approve before the summer recess, allowing Next Generation EU (NGEU) and national funds to start rolling out in the latter half of 2021. Setting Italy on a path to structurally higher growth is a first prerequisite to also tackle the country's burgeoning public debt.

2020/21 "Above the line" fiscal measures	EUR/bn
Autumn packages	**5.4**
August decree	**25.0**
Relaunch Decree (15 May), of which:	**55.0**
Wage supplementation schemes (employment support)	15.0
Support for small businesses (cancellation of corporate tax - IRAP, grants for hardest hit SMEs…)	12.0
Guarantee income and decent living conditions for Italian households and self-employed	6.5
Extra spending for the Civil Protection and the healthcare sector	4.5
Subsidies for tourism and leisure (tax reductions, vouchers...)	4.0
"Cura Italia" decree (17 March), of which:	**25.0**
Keeping people employed and supporting the unemployed	2.4
Additional healthcare related spending	10.4
Reduced taxes and contributions for small firms	3.2
Total	**110.4**
% of GDP	7.0%

One dimension that will be of importance further down the road is how the EU fiscal rules may evolve and also how the NGEU funds are included in these calculations. Near-term, the Commission has recommended that the "general escape clause" be applied again in 2022 and urged that full use of the flexibility within the Stability and Growth Pact is made when the rules reapply as of 2023. The real question medium-term is just how demanding the EU fiscal rules will prove for the Italian economy; should NGEU funds be at least partly excluded, then this would offer some respite. If, furthermore, a revamped set of EU rules were to place emphasis, as Prime Minister Draghi has done, on good debt-bad debt, with good debt being that financing productive investment, then that would be a further positive and could help also align national incentives, further helping to lift trend GDP and win public acceptance for the necessary structural reforms.

The debate on the new EU fiscal rules is unlikely to advance much ahead of the German election in September, but once the discussion gains momentum, it will be a focal point for markets. Finally, developments in the discussion of bank holdings of national government bonds within the framework of Banking Union also merit attention as Italian banks have once increased holdings.

Italian bond spreads first narrowed on the back of the ECB's PEPP, due to run until at least the end of March 2022, and received a further boost on the back of Prime Minister Draghi's appointment, pushing the 10-year yield spread over Germany below 100bp for the first time since 2016. Keeping bond yields in check is the second leg of durably reducing the general government debt burden, that we expect to clock in at just over 165% of GDP in 2023. The first is sustainable economic growth.

National liquidity support measures have bought space for firms hard hit by the pandemic and concern remains that once the economy reopens and temporary support is lifted, that insolvencies could result, also adding potential pressure to bank balance sheets with the risk of seeing credit conditions to viable companies tighten. Expansionary fiscal policy couple with favourable overall financial markets conditions should, however, should keep NPL levels well below previous peaks, and not least is, as we expected, the lifting of temporary support measures once the health crisis abates will be carefully managed.

Italy next faces general elections by June 2023 at the latest, leaving Draghi a fairly short window of time to deliver. Hope is that he can use this window to convince Italy's European partners of the need for better fiscal governance within the EU and perhaps even some permanent joint fiscal tools, and at the same time convince the Italian electorate of the merits of what historically has often proved unpopular structural reform. While we are confident that Draghi will make some progress, our concern is that the span of reform he can realistically achieve will not give a large enough boost to Italy's trend GDP and see the risk that reforms be watered down by future governments as significant.

Italy	**2019**	**2020**	**2021f**		**2022f**		**2023f**	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	0.3	-8.9	6.3	2.0	1.5	1.0	1.1	3.0
Inflation, %	0.6	-0.1	0.9	0.6	1.0	1.0	1.2	1.2
Unemployment, %	9.9	9.4	11.8	12.7	11.4	12.4	10.9	12.1
Fiscal balance, % GDP	-1.6	-10.4	-7.7	-9.9	-7.2	-9.8	-6.9	-8.6
Public debt, % GDP	135	157	159	166	163	173	166	174

Base = Central scenario
Ext. = Extended health crisis scenario

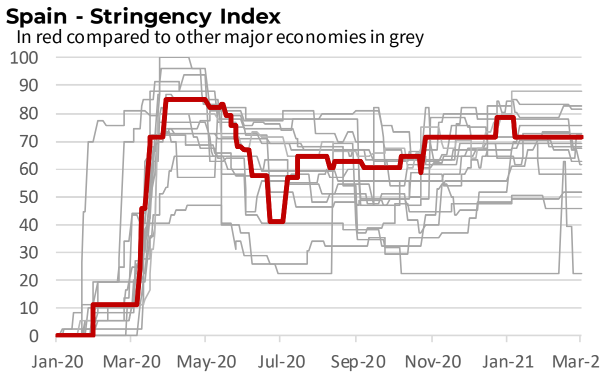
SPAIN

- **Activity slowed in 4Q20; the intensity of the rebound in 2021 will depend on the evolution of the health crisis.**
- **Spain's emergency and recovery plan total 11.1% of GDP.**
- **Public debt is set to climb higher as of 2022.**

Of all the major G20 economies Spain recorded the largest GDP contraction in 2020. GDP finished 11% below its 2019 level. The country, which is particularly exposed to the hotel and restaurant services sector, saw its domestic and external demand deteriorate sharply in 2020.

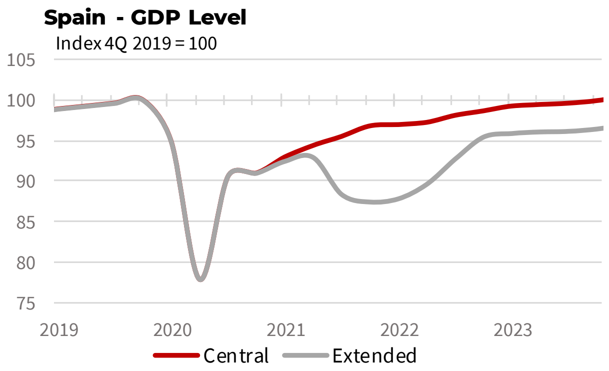
The new restrictions, although more targeted than those deployed in the spring, will have a negative impact on activity in the coming months, particularly in the service sector since this sector requires a high degree of social interaction. Prime Minister Pedro Sanchez announced in early February that Spain would not welcome massive arrivals of foreign tourists until 70% of the population is vaccinated, i.e. by the end of summer 2021. This will have a negative impact on the tourism sector, which accounts for 12% of GDP, a higher share than the European average (around 5% of GDP).

More targeted restrictions



Source: University of Oxford

Return to pre-crisis GDP level in 2023



Source: SG Economic and Sector Research

The impact of the health crisis on employment will also weigh on growth in the medium term. The massive job losses to be expected in tourism-related sectors, which began in January as a result of the Filomena storm that paralyzed central Spain, will increase unemployment rate and further penalize growth.

Investment prospects will also be limited. Credit standards are set to tighten further in 2021 both for households and businesses. In addition, the eventual removal of moratoria on medium-term debt could jeopardize the repayment capacity of the most vulnerable agents, exacerbating the tightening of financing conditions. Finally, many investment decisions could be delayed due to the high degree of uncertainty about future sales, the declining level of capacity utilization and the reduced availability of funds for such spending.

Emergency and recovery measures	Size EUR bn
▪ **Emergency plan (2020-2021)**	**66.7**
▪ Aid and subsidies for businesses	0.26
▪ Fiscal measures to support businesses	6.35
▪ Public expenditure on health	13.28
▪ Household income support measures	16.05
▪ Measures to stimulate household consumption and investment	0.25
▪ Other appropriations and public expenditure	3.3
▪ Aid to VSE-SMEs, the self-employed and the liberal professions	9.4
▪ Partial activity devices (ERTE)	17.8
▪ **Recovery Plan (2021-2023)**	**71.9**
▪ National Care and Employment Plan	4.1
▪ Promotion of culture and sport	0.8
▪ Urban and Rural Agenda	11.2
▪ Resilience of infrastructures and ecosystems	8.9
▪ Investments related to energy transition	6.4
▪ Modernization of public administration	3.6
▪ Modernization of the industrial fabric and SMEs	12.3
▪ Agreement for Science, Innovation and the Strengthening of the Health System	11.9
▪ Investment in the education system and continuous training	12.7
Total	**138.6**
% of GDP	11.2

Source: DG Trésor, comparative note of 27 November 2020, SG Economic and Sector Research

In this context, *the Next Generation EU* (NGEU) plan will be crucial for reviving economic activity in 2021.These funds will total €72bn in non-refundable transfers between 2021 and 2023, or 5.8% of GDP. The government plans to use €27bn of NGEU grants this year in anticipation of the budgeted funds.

The intensity of the rebound will above all depend on the progress of the vaccination campaign by this summer. Beyond 2021, the tourism recovery is expected to gain momentum, with most impediments to activity being fully lifted, while domestic demand growth will likely moderate once pent-up demand is reabsorbed. This would result in a growth path stabilizing around 2% in 2022/2023.

Spain	2019	2020	2021f		2022f		2023f	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	2.0	-11.0	7.2	2.0	3.0	1.2	1.8	5.2
Inflation, %	0.8	-0.3	1.0	0.5	1.8	1.7	1.3	1.3
Unemployment, %	14.1	15.6	17.4	18.6	17.0	18.9	16.4	18.2
Fiscal balance, % GDP	-2.9	-12.0	-8.7	-11.8	-7.6	-11.7	-7.1	-9.7
Public debt, % GDP	96	118	117	127	119	136	122	137

Base = Central scenario
Ext. = Extended health crisis scenario

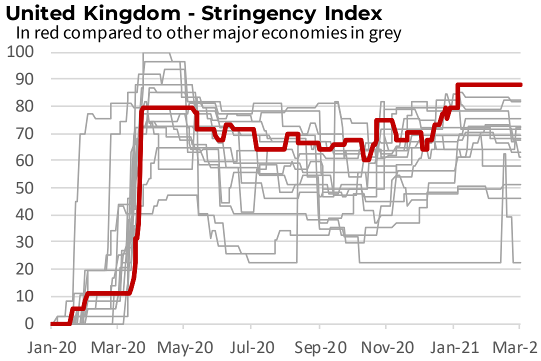
UNITED KINGDOM

- **The swift vaccine rollout feeds hope of a sharp rebound in 2021.**
- **However, we expect the economic scarring of the crisis and the consequences of Brexit to weigh on underlying trend potential.**
- **Bold fiscal and monetary policy have helped cushion the blow. Build Back Better not enough to offset Brexit and scarring headwinds.**

UK economic growth in 4Q20 (+1%) surprised on the upside but leaves output far below pre-pandemic levels (-7.8% as compared to 4Q19). This larger gap between pre-pandemic levels and actual levels, as compared to similar countries, continues to reflect lockdowns that have been longer in the UK, and the Brexit uncertainty effect. In the short run, recovery is threatened by the tough lockdown restrictions that have been in place throughout the first quarter of 2021, and by the very progressive unlocking recently announced by the Prime Minister - the lifting of the last social restrictions are planned no sooner than the end of June.

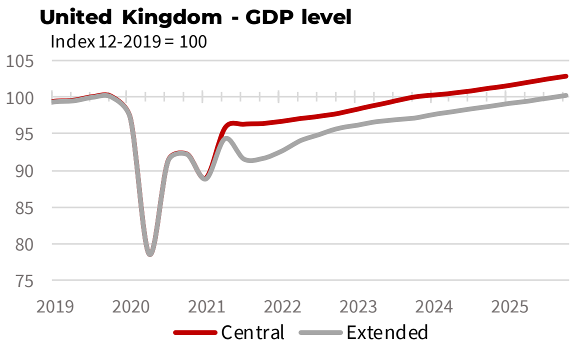
The swift vaccine rollout, however, feeds hope of a sharp rebound driven by consumption from 2Q21 onwards. Despite this rebound, in our central scenario we do not expect the UK economy to recover to the pre-pandemic level of activity before the end of 2023. This is due to the economic scarring of the crisis, notably on the labour market, and the damages to the trade balance caused by the new post-Brexit relationship between the UK and the EU27.

A high average stringency index in 2020



Source: University of Oxford

The full recovery will take time



Source: SG Economic and Sector Research

To mitigate the effect of this outbreak on the economy, the UK authorities will continue to update their support package for households, business, and public services to protect jobs and help businesses through months of further disruption.

On the fiscal side (cf. table below), the response since the beginning of the crisis encompasses: i/ new additional funding for the NHS, public services, charities and culture (GBP 127bn); ii/ the strengthening of the social safety net, notably by increasing payments under the Universal Credit scheme as well as expanding other benefits (GBP 8bn); iii/ measures to directly support businesses, like property tax holidays, grants for small firms and firms in the most-affected sectors – notably cash grants of up to £3,000 per month for businesses which are closed - and compensation for sick pay leave (GBP 66bn). With the second lockdown at the end of 2020, the government has fully reactivated the Self-Employment Income Support Scheme (SEISS) and the Coronavirus Job Retention Scheme (CJRS), that pays 80% of the earnings (to a maximum of GBP 2,500 per employee per month) of self-employed workers and furloughed employees. The combined cost of the measures is now expected to be around GBP 73bn.

Chancellor Sunak announced a new GBP65bn budget plan on 3 March 2021. Top of the list, the plan extended and adapted various pandemic support measures to both businesses and households. The plan also offered further means for the vaccine rollout. In a bid to stimulate employment, the plan announced various support measures to low income groups. With an eye to strengthen public finaces further down the road, the Chancellor announced a increase of the corporate tax rate to 25%, still amongst the lowest in the major advanced economies. Finally, the new Budget coincided with the release of the government's Build Back Better plan. The aim is to give a boost to infrastructure, skills and innovation. Welcome as this plan is, we remain concerned that it will not suffice to offset the headwinds from Brexit and economic scarring.

"Above the line" fiscal measures	**Size GBP/bn**
Public services spending: Health Services, local authorities, measures to support vulnerable individuals, supporting rail services and funding for the devolved administrations	127
Employment support: Coronavirus job retention scheme and self-employed income support scheme as well as job retention bonuses (which we will redeploy at the appropriate time)	73
Welfare package: Universal credit (minimum income floor) and increased weekly universal credit by 20gbp. Employment and support allowance to remove 7 day wait. Local housing allowance measures	8
Business support: Small business grant schemes and business rate packages	66
Draft budget 2021: *Extension of the job protection scheme from April to September 2021* *Extension of the suspension of the real estate transaction tax* *Extension of VAT cuts*	
Total	274
Total including budget draft 2021	344

Despite the unprecedented size of public support, it is worth noting that the announced packages interact with the pre-existing benefit system. In this respect, the UK tends to stand out by offering a relatively low level of income support to employees who become unemployed, notably when compared to other European countries whose insurance-based systems already provided a much greater level of insurance. The latest data showed unemployment at about 1.7 mn in Dec. 2020 — or 5.1%, the highest figure in five years. The figure would no doubt be much higher without the government's furlough scheme now covering an estimated 6.4 mn jobs. In our central scenario we expect the unemployment rate to peak at 7.8% in 3Q21.

The UK economy is also supported by accommodative monetary policies aimed at preserving firms' and households' access to financing and insuring market liquidity. In March 2020, the Bank of England (BoE) reduced the main rate by 65 bps to 0.1%. The central bank also expanded its holding of UK government bonds and non-financial corporate bonds by GBP 300bn in March and June 2020. An additional increase of the target stock of government bonds by GBP 150 bn was announced in November 2020 taking the total stock to GBP 875bn. This is a cumulated increase of 100% since March 2020. The BoE also introduced a new Term Funding Scheme for the commercial banks to reinforce the transmission of the rate cut, with additional incentives for lending to the real economy, and especially SMEs. The Treasury and the BoE launched the Covid Corporate Financing Facility which, together with the above-mentioned Coronavirus Business Interruption schemes, makes GBP 330bn of loans and guarantees available to businesses. The Treasury and the BoE also agreed to temporarily extend the use of the government's overdraft account at the BoE to provide a short-term source of additional liquidity to the government if needed.

These policies have effectively supported corporates' access to liquidity. The latest figures indicate that UK private sector businesses raised a total of GBP 75bn from banks and financial markets from March to December in debt instruments, causing the amount of outstanding debt to grow by 9.5% over the past 12 months at the end of December. Equity financing has also been dynamic since March, with GBP 23bn raised at the end of December. This equity funding tends to alleviate the financial stability concerns resulting from the crisis.

The agreement negotiated between the UK and the EU27 on their relationship from 2021 reached at the end of December, avoids the introduction of customs duties and quotas on trade in goods but does not provide for the UK to remain in the customs union. Trade in goods is henceforth subject to customs declarations and other administrative formalities, which are a hindrance to trade between the UK and the EU27. The agreement is extremely piecemeal on services (50% of UK exports to the EU27) where it is limited to a non-discrimination agreement. For UK service providers, the end of the transition period implies compliance with the rules of the host country of each Member State, as they will no longer benefit from the "country of origin" principle, mutual recognition or "passporting". The EU27 has only granted the UK regulatory standards equivalence status on a temporary basis and in specific areas of financial services, such as derivatives clearing, for financial stability issues. The extension and continuation of this equivalence status to a wide range of financial services is unlikely to happen, despite the UK's willingness to continue negotiations on this issue.

The agreement does not close the discussions between the parties which will continue. In addition, discussions on financial services and data transfer which is currently allowed by a temporary six-month agreement will also prevail. In the medium and long term, we still consider that Brexit will reduce the growth potential by 0.8 percentage points compared to the growth potential prior to the Brexit referendum, bringing the figure down to 1.0%.

United Kingdom	2019	2020	2021f		2022f		2023f	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	1.4	-9.9	5.0	2.0	3.0	3.0	2.0	2.5
Inflation, %	1.8	0.9	1.7	1.2	2.1	1.9	2.0	1.9
Unemployment, %	3.8	4.5	7.1	8.2	6.4	7.3	5.3	5.8
Fiscal balance, % GDP	-2.3	-13.1	-10.2	-14.2	-6.1	-7.4	-4.8	-6.2
Public debt, % GDP	85	102	105	112	106	114	106	115

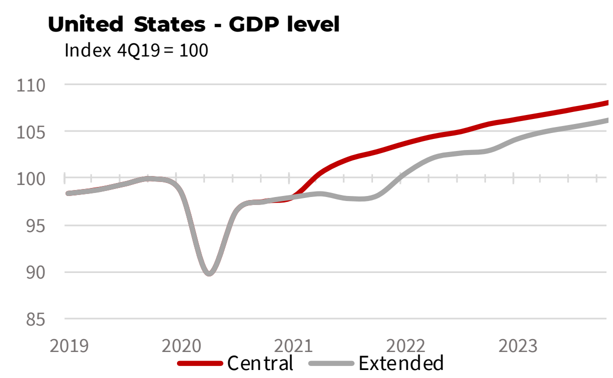
Base = Central scenario
Ext. = Extended health crisis scenario

UNITED STATES

- **Growth is expected to accelerate sharply in a context of strong budgetary support and a recovery in consumption and investment.**
- **The Fed is expected to maintain favorable financial conditions in 2021 despite the expected increase of inflation.**
- **The main risks for the economy are a marked deterioration in the health crisis and a tightening of financial conditions in the event of a persistent increase of inflation or merely inflation fears.**

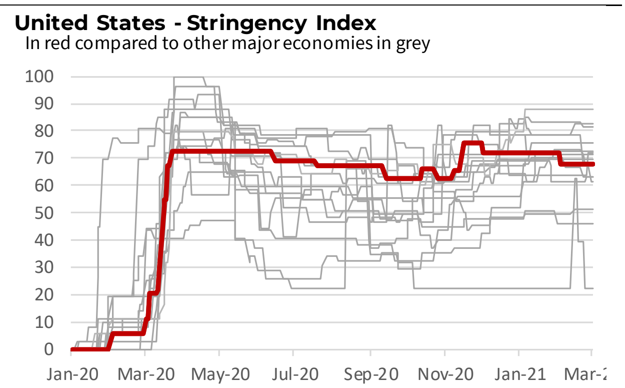
The recovery of activity in the United States is expected to accelerate significantly in the coming quarters. GDP grew at an annualized rate of 4% in 4Q20, reflecting the recovery in private consumption and business investment following the Covid19 shock, as well as strong momentum in residential investment. Residential investment has proved resilient (6% in 2020) supported by favorable financial conditions and strong growth in household income. Indeed, household disposable income increased by 7% in 2020, despite the contraction of the economy, thanks to various government transfers implemented in 2020 as part of support plans.

Return to pre-crisis level seen in 2Q21



Source: SG Economic and Sector Research

Stringency level are still relatively high



Source: University of Oxford

The economy is expected to accelerate sharply and return to its pre-crisis level by 2Q21 as the vaccine rollout plan moves forward and the various support measures are implemented, allowing for a significant rebound in domestic demand. Indeed, households and businesses are emerging from this crisis with relatively strong balance sheets. The household savings surplus, resulting from the rise in income and consumption restrictions related to health measures, is estimated at $1,600bn (8% of GDP). This savings surplus should continue to grow thanks to the new Biden administration's support plan, which provides $1,000bnn in transfers to households in the form of unemployment benefits, family allowances and household checks.

On the corporate side, the corporate profit margin rate has remained stable thanks to government subsidies ($600bn in guaranteed loans), while the new support plan provides $150bn in additional assistance to companies and $450bn to local authorities for investment needs among others. The gradual lifting of health restrictions should result in a strong catch-up in consumption and investment, enabling the economy to return to its pre-crisis level by the second quarter of 2021. Overall, GDP should grow by 5.3% in 2021 and 3.8% in 2022. In the event of an extension of the health crisis, the recovery would be more modest in 2021 with 2.5% growth and a stronger rebound in 2022.

Inflation remains moderate (1.5% in January) but is expected to rise above the "classic target" of 2% in the coming months. On the one hand, energy inflation is expected to rise significantly due to base effects related to the low energy prices last year, weather-related vagaries in Texas that resulted in a significant drop in production, and a surge in electricity prices as well as the recovery of oil prices. Moreover, the lifting of health restrictions and the resumption of consumption of services should enable a rebound in service prices, which have been decelerating since the beginning of the crisis. However, once these base effects have passed, inflation should return to the classic "target" level of 2%. Indeed, even though the stimulus plan will place GDP above its potential level according to the CBO, it will not be accompanied by persistent overheating, since most of these measures are temporary in nature and are income substitutes while the crisis lasts. In addition, the labor market is expected to continue to improve gradually, with the participation rate recovering later than activity, which will moderate inflationary pressures. Finally, the more structural elements that have contributed to the moderation of inflation, such as robotization, are still present.

In this environment and in the context of the new objectives (core inflation averaging 2% over time and maximizing employment levels), the Fed is expected to maintain the range of its monetary policy rate at 0%-0.25%, as well as purchases of government securities in 2021. The Fed would stop its purchases of securities in 2022, once the recovery of the economy and employment is well underway, and the first rate increase would take place in 2023.

Main measures of Covid-19 relief packages (USD bn)

	CARES act (2020)	CRRSA act (2021)	ARP act (2021)
Aid to firms	**611**	**325**	**150**
PPP	600	284	150
Other	11	41	
Aid to households	**832**	**337**	**1000**
Unemployment benefits	500	120	400
One time checks & child tax credit	290	166	600
Other	42	51	
Education	**32**	**82**	
Healthcare related	**180**	**63**	**400**
Transportation	**72**	**45**	
Support for airline industry	58	18	
Support for other sectors (Amtrack, highway)	14	27	
Tax cuts	**300**	**30**	
Other spending	**25**	**29**	
Capital for Fed programs	510		
Financial aid to local government	150		350
FEMA	45		
Total	**2 757**	**911**	**1 900**

The main risks for the US economy are a prolongation of the health crisis and a sharp correction on financial markets. The health crisis has eased since the beginning of the year with a decrease in the number of cases and hospitalizations and an increasing rate of vaccination. Nevertheless, in the event of a further significant increase in the number of cases and hospitalizations or the spread of a new strain, it is likely that the new administration will impose more restrictive measures, delaying the resumption of activity. The second risk would be a sharp correction in the bond market. As a result of the announcement of the size of Biden's support plan and the strong recovery in energy prices, long-term bond rates rose rapidly, as markets were betting on a strong return of inflation that would force the Fed to tighten financial conditions. This correction in the bond markets was also transmitted to the equity markets. Thus, a continuation of this trend is tightening financial conditions while the recovery in employment has not yet begun.

United States	**2019**	**2020**	**2021f**		**2022f**		**2023f**	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	2.2	-3.5	5.3	2.5	3.8	4.1	2.2	3.0
Inflation, %	1.8	1.3	3.0	2.1	2.5	3.0	2.5	2.3
Unemployment, %	3.6	6.8	4.3	6.6	3.8	5.0	3.6	4.5
Fiscal balance, % GDP	-6.7	-13.1	-10.5	-17.0	-8.0	-13.0	-5.5	-10.0
Public debt, % GDP	80	103	106	112	109	116	111	120

Base = Central scenario
Ext. = Extended health crisis scenario

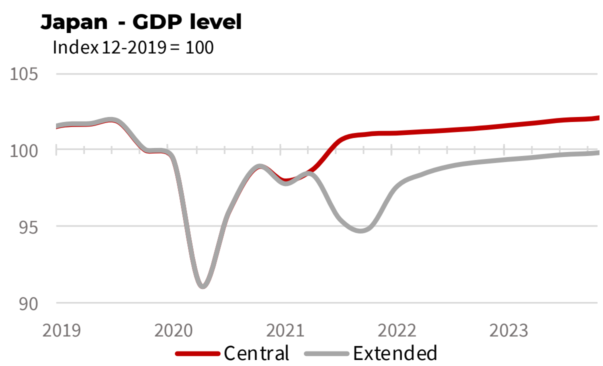
JAPAN

- **Quarterly GDP is expected to return to pre-Covid19 level during 2H21.**
- **New measures have been put in place to counter the risk of deflation.**
- **The considerable fiscal stimulus will have a phased impact over time, and public debt is increasing**

The economic recovery will continue, but at a more moderate pace. The quarterly GDP will return to its pre-Covid19 level in the second half of 2021, in particular due to the strong rebound recorded in Q3 and Q4 2020.

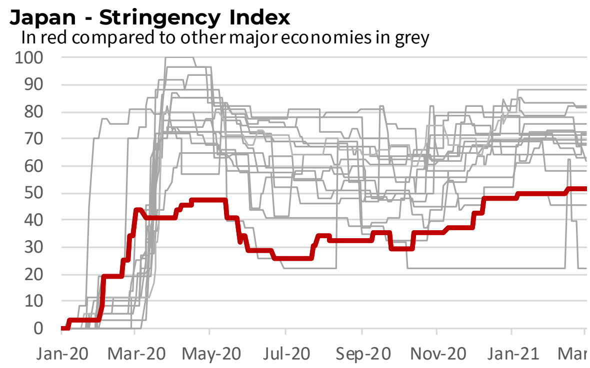
A third wave of Covid19 took place in January, necessitating the reinstatement of the state of emergency in 10 prefectures for two months. Added to this, the late start of the vaccination campaign (17 February), and the health uncertainties will leave their mark on the strength of the recovery.

Gradual recovery of GDP



Source: SG Economic and Sector Research

Higher stringency due to the third wave

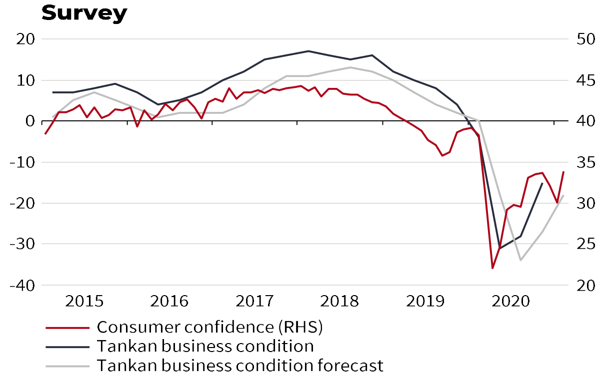


Source: University of Oxford

Household confidence has fallen accordingly. Until a critical threshold of herd immunity is reached, there is little prospect of an unhindered rise in confidence. Consumption, although on the rise compared to 2020, will continue to follow a winding recovery.

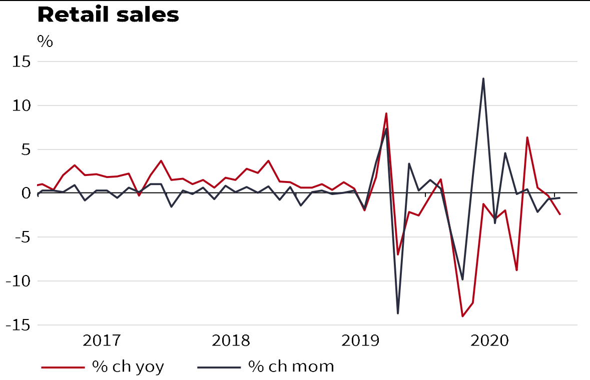
On the business side, the Tankan survey reveals some improvement in the perception of the economy. But the indices remain well below zero - indicating that the economic environment is perceived as more unfavourable by businesses.

Low confidence of economic actors



Source: BoJ, Ministry of Finance, SG Economic and Sector Studies

Hesitating recovery in retail sales



Source: Cabinet office, SG Economic and Sector Studies

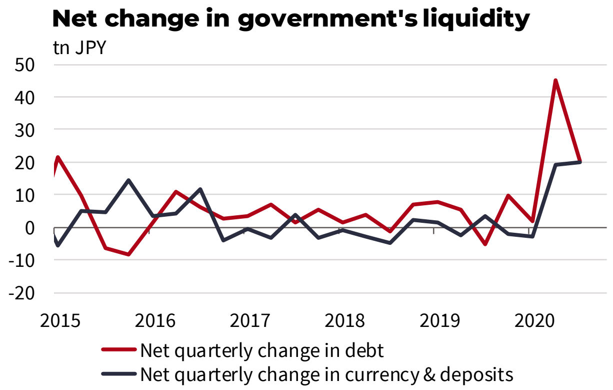
The risk of a deflationary spiral is all the more present in such a context of low morale. The ageing Japanese society has already experienced a deflationary past. If household perceptions do not improve because of a prolonged health crisis, this implies a very slow return to normal of their consumption levels. Investment will then be impacted, and the objective of reflation becomes even more difficult to achieve. Indeed, inflation has sunk back into the negative zone. Inflation excluding fresh produce has been negative since July 2020, whereas the BoJ's target is 2%.

"Above the line" fiscal measures	**Size JPY/tn**
Cash payment for SMEs, self-employed individuals and furloughed employee	7.1
Cash payment for households (JPY 100,000 for all residents)	12.8
Rental subsidies for corporates	2.0
Spending on medical system	7.3
Spending on public facilities	4.7
Miscellaneous spending on structural improvement	10.7
Lending facility for corporates	11.6
Go-to campaign which will subsidize people's travel expenses and tickets for entertainment events	2.7
Reserves for future prevention of virus outbreak	10.0
Program of digitalisation and carbon neutrality	2.8
Measures to improve productivity (help to SMEs, securing supply chains, etc)	2.4
Help to employment and well-being	5.4
Spending on disaster prevention and security	3.1
Total	82.5
%GDP	14.8%

Faced with such a risk, the fiscal stimulus effort is considerable despite a public debt/GDP ratio already close to 240%. While the Japanese government did not hesitate to announce an additional stimulus package of JPY73,600bn (13% of GDP) in December 2020, and the "mamizu" - the actual spending - of all the announced plans could be as high as 15% of GDP, implementation will take time. The ambitious fiscal policy is slow to be fully realised. Indeed, the government finds itself with a massive surplus of liquidity, the result of unspent fundraising. This additional liquidity will be used in a staggered manner and will contribute to the further growth that the initial budget, which ends in March 2021, will provide.

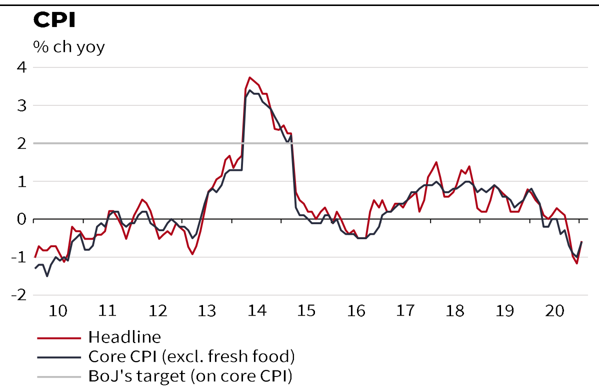
On the monetary side, no major changes are expected. The conduct of monetary policy should continue to target the short (-0.1%) and long (0%) rates, allowing for some stability of extremely favourable financing conditions. In 2020, the BoJ's balance sheet increased by 23 percentage points of GDP, reaching 125%. The rate of purchase of government securities should slow down markedly in 2021.

Additional liquidities to be used later



Source: BoJ, Ministry of Finance, SG Economic and Sector Studies

Inflation far away from the target



Source: BoJ, SG Economic and Sector Studies

Finally, with the debt to GDP ratio approaching 250% of GDP, the question of debt sustainability will arise if the period of deflation is prolonged. Even if the cost of financing public debt is kept extremely low with the vast majority (90%) of debt held by domestic investors including the BoJ, the repeated slippage in the fiscal consolidation schedule could ultimately affect investors' perception of risk.

Japan	2019	2020	2021f		2022f		2023f	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	0.3	-4.9	3.4	0.3	1.7	2.0	0.6	1.1
Inflation, %	0.5	0.0	0.0	-0.4	0.7	0.0	0.5	0.6
Unemployment, %	2.3	2.8	2.8	3.0	2.6	2.8	2.6	2.7
Fiscal balance, % GDP	-3.3	-13.8	-6.5	-11.0	-3.3	-5.0	-3.0	-3.0
Public debt, % GDP	238	252	258	264	260	269	262	270

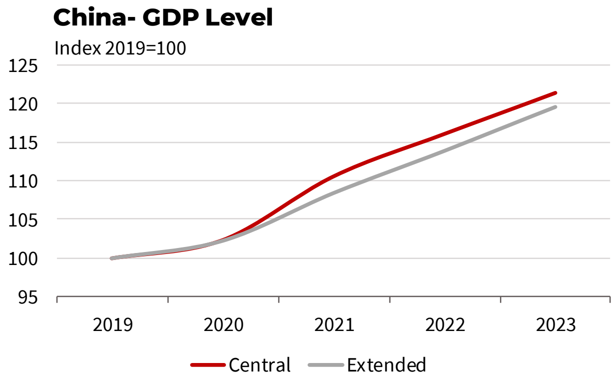
Base = Central scenario
Ext. = Extended health crisis scenario

CHINA

- **Slowed recovery is expected to regain momentum.**
- **The policy mix is less accommodating and focuses on de-risking.**
- **A balance must be struck between increased credit risk and the financing needs of the economy.**

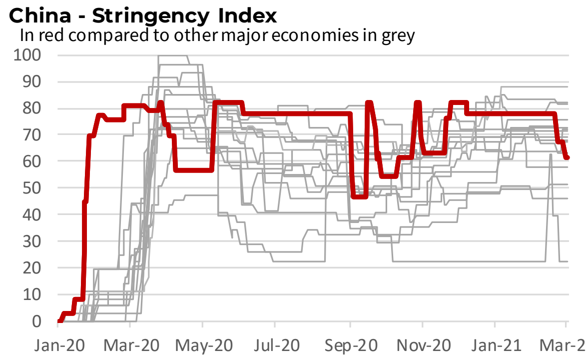
The economic recovery in China will continue with a strong rebound despite the slowdown observed in late 2020 and early 2021. Momentum will be maintained during the first quarters of 2021 before gradually returning to its long-term trend in the following years.

Deeper loss in GDP in extended crisis would require more stimulus



Source: SG Economic and Sector Research

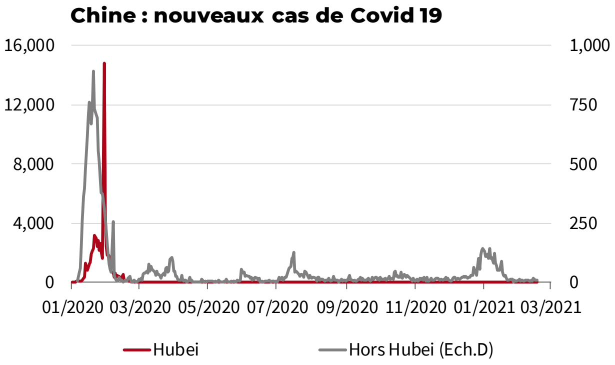
Little impact on social and economic life despite high stringency index



Source: University of Oxford

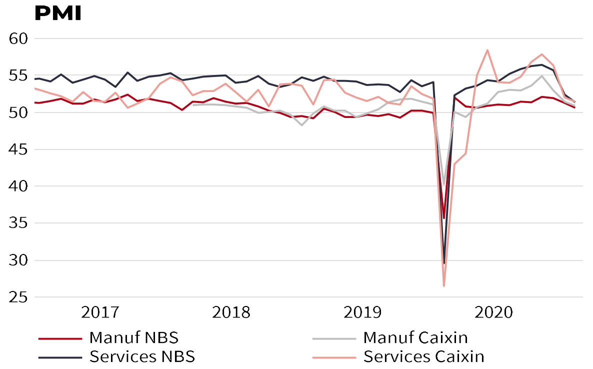
The resurgence of Covid19 contaminations last December and January led to the reinforcement of sanitary measures and, thus, a deceleration of activity, especially in the consumption of services. The impact should be temporary, given the way the health crisis is being managed, which allows the contamination curve to drop as soon as the first signs of an upturn appear. Even if vaccination is slower than in the most advanced countries in this area, China is pursuing a policy based on eliminating sources of contamination, which maintains economic and social activity, while waiting to achieve collective immunity. Therefore, if slight disruptions in economic recovery are possible due to the temporary increase in Covid19 cases, activity will quickly resume.

Temporary rise in infections



Source: NHC, SG Economic and Sector Studies

Slowed recovery



Source: NBS, Caixin, SG Economic and Sector Studies

Fiscal measures	**Size CNY/bn**
Special local government bonds	3750
Special central government bonds	1000
Increases in general government spending and social security outlays*	750
Reduction in social security charges and tax*	2500
Total	**8000**
%GDP	**8%**

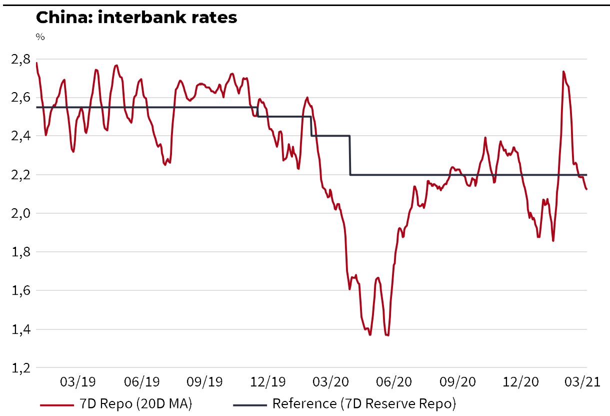
* estimated by SG Economic and Sector Studies, net from automatic stabilisers

Policy support has become less accommodating but, on the one hand, they continue to have a positive impact on the economic situation, and on the other hand, its normalisation is favourable to better growth sustainability.

Indeed, the central bank raised the interbank financing rate very early on, as early as in June. It then reiterated its policy by withdrawing liquidity at the end of January as China prepared for the year's biggest celebration. The result was a deceleration in credit growth, which peaked in October/November 2020. However, the credit cycle usually has a lagged effect of 2 or 3 quarters on the real economy cycle. The credit stimulus will then continue during the first quarters of 2021.

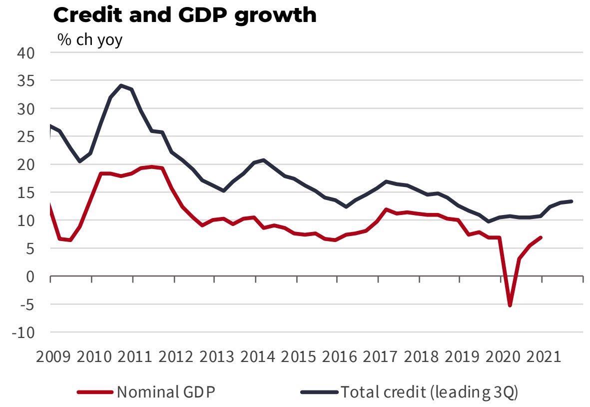
On the fiscal side, not only is the widened public deficit in 2020 proving smaller than expected (CNY -8,720bn vs. -11,700bn), spending under the tax fund (to which Special Local Government Bonds - SLGB - contribute) has not been in line with the budget (CNY 11,800bn vs. 12,600bn). The fact that local governments did not issue as many SLGBs as the amount allocated to them as part of the stimulus (CNY 3,480bn vs. 3,750bn) corroborates the previous observation. Indeed, a more cautious application at the end of the year, with the virtual absence of net issuance of SLGBs, is a harbinger of fiscal normalisation and an economic policy that now aims to reduce the risk associated with debt.

Recent correction in interbank rates



Source: PBoC, SG Economic and Sector Studies

Credit cycle still favourable



Source: NBS, PBoC, SG Economic and Sector Studies

The latter, having become the economic policy priority, has several components: avoiding over-stimulating activity; tolerating credit defaults; limiting and strengthening regulation on real estate credit, the development of credit in Fintech and local government indebtedness; and finally recapitalising the banking sector. Such a shift in priority, which leaves growth in the background and which takes place well before economic activity in the rest of the world returns to its pre-crisis level, has the direct consequence of a faster convergence of growth towards its long-term trend, but it is favourable to better sustainability given the already high level of debt (280% of GDP).

In a phase of normalisation of the stimulus, credit risk will re-emerge all the more as greater tolerance is given to it. A delicate balance must therefore be struck between allowing a reasonable increase in such a risk and continuing to meet the financing needs of the economy.

China	2019	2020	2021f		2022f		2023f	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	6.0	2.3	8.0	6.0	4.9	5.0	4.6	5.0
Inflation, %	2.9	2.5	1.7	1.5	2.3	2.2	2.3	2.3
Current account, % GDP	1.0	2.4	2.1	2.1	2.1	2.0	1.9	1.8
Fiscal balance, % GDP	-3.1	-3.6	-2.8	-3.0	-2.8	-2.9	-2.8	-2.8
Public debt, % GDP	38.6	46	44	45	44	45	44	45

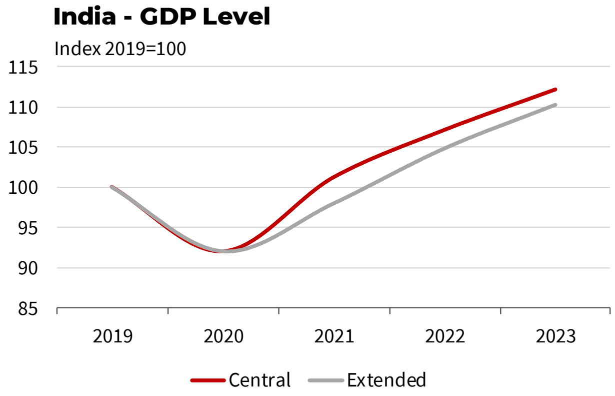
Base = Central scenario
Ext. = Extended health crisis scenario

SOCIETE GENERALE

INDIA

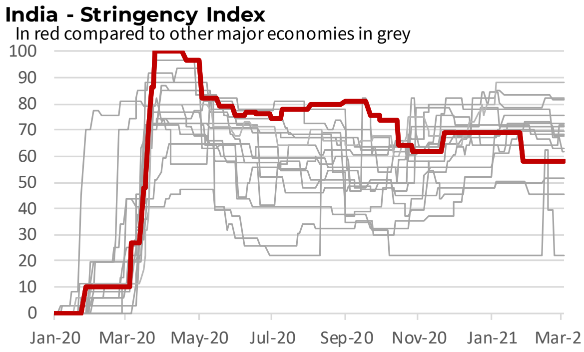
- **The recovery will be stronger than expected but some weaknesses remain.**
- **Fiscal room for manoeuvre is limited, the transmission of monetary policy is partial.**
- **The financial system remains vulnerable despite the respite provided by the moratorium.**

Growth expected to weaken after recovery



Source: SG Economic and Sector Research

Fewer infections, lower stringency



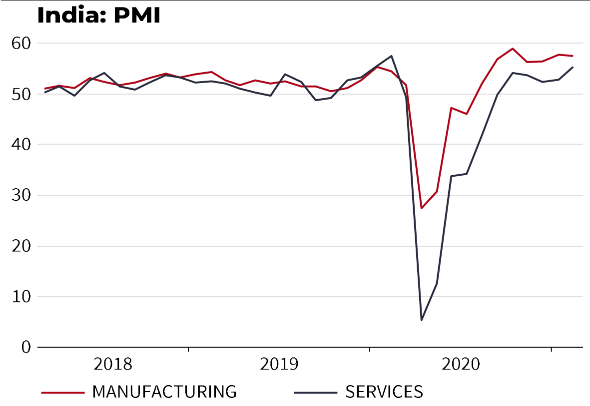
Source: University of Oxford

The recovery of activity is on course, thanks to an improving epidemic situation. Growth is expected to rebound on the basis of a sharp contraction in 2020. Then, it will converge towards its long-term trend, weakened by structural problems.

As the daily cases have not regained, the incidence rate (5.6 per million inhabitants) is among the lowest in Asia. In addition, a vaccination campaign began in January. Despite the delay in the vaccination programme, India is one of the first emerging countries to have started it. The pandemic situation has become much milder than in 4Q20, and part of the demand restricted by the pandemic is now expected to be released. The recovery will then be stronger than expected.

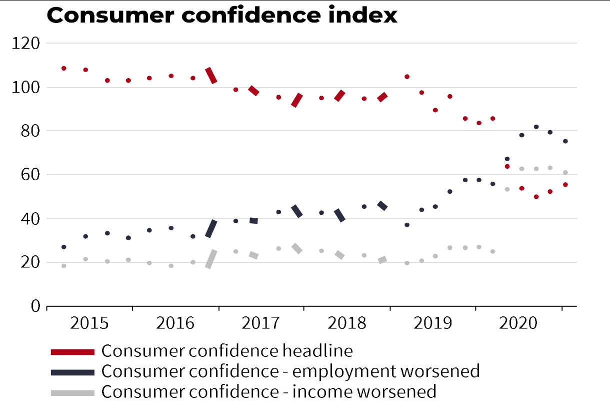
However, vulnerabilities remain, exerting a pull-back force on growth that would quickly cause it to fall back to lower levels. Firstly, household confidence is struggling to recover. This probably reflects a sluggish labour market. 75% of respondents to the RBI confidence survey for the month of January 2021 still believe that their employment situation is deteriorating and 60% say their income is lower. Hence a brake on a full recovery in consumption.

The recovery is going on...



Source: RBI, SG Economic and Sector Studies

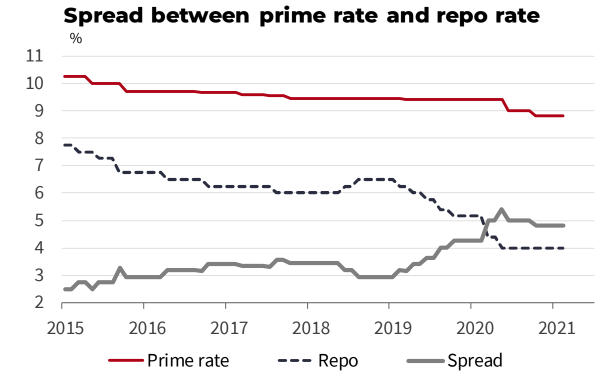
... consumer confidence remains weak



Source: RBI, Central Statistics Office, SG Economic and Sector Studies

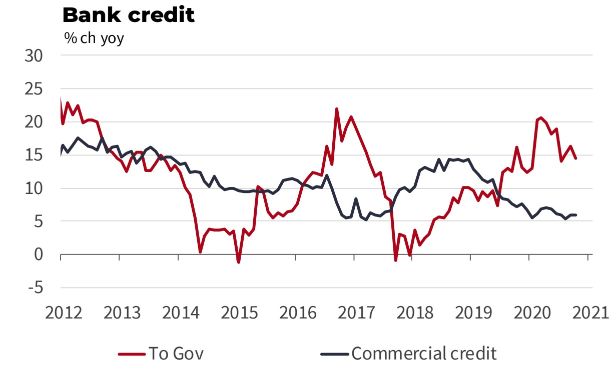
Moreover, structural problems remain. Firstly, the high public debt ratio (close to 90% of GDP) constrains the government's ability to support growth. The 2020 recovery plan is, in fact, only slightly ambitious (less than 2% of GDP in real expenditure), while GDP contracted by 24% in Q2 2020. The budget for the fiscal year 2021-2022 foresees only 1% growth in spending but a 15% increase in revenues. Moreover, the government has even drastically reduced (-40%) the expenditure intended to support the rural economy, i.e. subsidies for food, fertilisers and support for rural employment. These three items now account for only 11.6% of the 2021-2022 budget, instead of 19.4% in the previous fiscal year.

Very partial transmission of monetary policy



Source: RBI, SG Economic and Sector Research

Weak growth in credit



Source: RBI, SG Economic and Sector Research

"Above the line" fiscal measures	Size* INR/bn
March Stimulus mainly based on Pradhan Mantri Garib Kalyan Package (support to low-income households, e.g. in-kind or cash payment)	910
EPF (Employment Provident Fund) liquidity relief (paid by the government for 6 months) and statutory contribution rate reduction	93
A reduction of 25% of existing rates of Tax Deducted at Source (TDS) & Tax Collection at Sources (TCS)	500
Food distribution for migrants (benefiting 80mn migrants)	35
Proposal under Compensatory Afforestation Fund Management and Planning Authority (CAMPA) funds to provide employment to tribal people	60
Investment in agriculture	150
Investment in 8 critical sectors (coal, mineral production, defence, airspace, social infrastructure, power distribution, space and atomic energy)	481
Additional public investment	370
Production linked incentive scheme targeting 13 priority sectors (spending over 5 years)	1479
Higher fertilizer subsidy allocation	555
Support for urban housing construction	185
Total	4818
%GDP	2.6%

*estimated actual fiscal spending

Secondly, the vulnerability of the financial system is at the root of a very partial transmission of monetary easing. The country had already experienced a series of failures of financial institutions before the health crisis. Indian banks have a non-performing loan ratio (NPL) of 8% in Q2 2020. This ratio is set to increase as a moratorium on loan repayments was in place between March and August 2020. State-owned banks, representing 60% of the country's banking assets, would have an even higher NPL ratio. Non-performing assets are weighing on the banks' ability to lend to the economy, not only in terms of price with interest rate inertia as the policy rate has fallen, but also in terms of quantity with growth in credit to the non-government sector slowing down since 2019. In 2021, in a context of lower inflation, the RBI would have the possibility of lowering its key rate, but this would only have a partial impact on credit growth and therefore on activity.

India	2019	2020	2021f		2022f		2023f	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	4.9	-8.0	10.0	6.5	5.8	7.0	4.7	5.2
Inflation, %	4.5	6.6	5.0	6.3	5.0	5.5	5.0	5.2
Current account, % GDP	-1.1	0.6	-1.0	0.2	-1.2	-1.0	-1.2	-1.0
Fiscal balance, % GDP	-7.4	-13.0	-10.0	-13.0	-9.0	-8.0	-7.0	-7.5
Public debt, % GDP	72	86	85	90	86	88	85	87

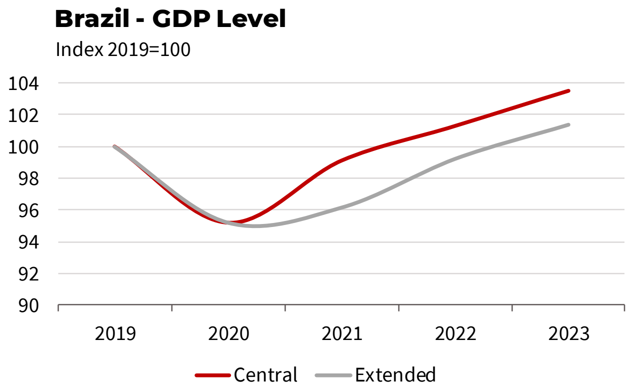
Base = Central scenario
Ext. = Extended health crisis scenario

BRAZIL

- **Activity quickly picked up again, supported by large budget transfers and sustained external demand.**
- **The BCB is ready to maintain flexible financial conditions in a context of modest inflationary pressures.**
- **The main risk is a disorderly fiscal adjustment because the debt parameters have deteriorated significantly.**

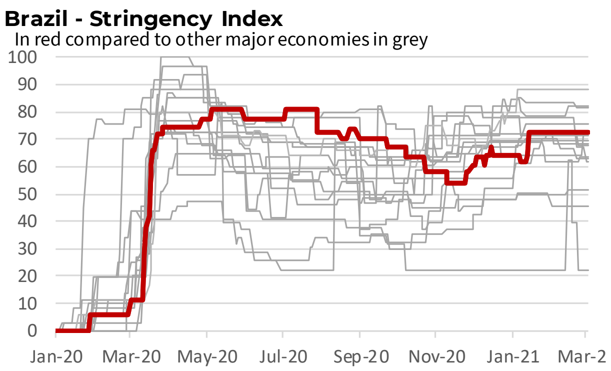
The economy is continuing it's recovery after the spring shock thanks to strong fiscal support and resilient external demand. Real GDP grew by 3.2% QoQ (-1.2% YoY) in 4Q20 with a very strong rebound in investment. Indeed, the latter increased by 20% QoQ (13% YoY) thanks to the import of offshore oil drilling platforms. Excluding this element, investment increased by 12% QoQ. Overall, investment should remain dynamic over the next few months in a context of strong improvement in the terms of trade and favourable financial conditions. However, the recovery in investment, excluding the commodities sector, should be more moderate in an environment of significant overcapacity in certain sectors and high political and regulatory uncertainties. Private consumption continues to recover, but at a more moderate pace (3.4% q/q), supported by government transfers.

Return to its pre-crisis level by end 2021



Source: SG Economic and Sector Research

Stringency level are still relatively high



Source: University of Oxford

After a contraction of 4.1% in 2020, the economy is expected to grow by 3.5% in 2021 and 2.3% in 2022. Private consumption should gradually converge throughout 2021 to its pre-crisis level as fiscal transfers fade and the labor market gradually recovers. External demand is likely to continue to support growth, benefiting from strong demand for primary goods in Asia. In the event of a prolonged health crisis, it is likely that the government will not adopt containment measures. Despite being one of the countries most affected by the Covid19 crisis, the federal government has not implemented major social distancing measures and has announced that its main health policy is vaccination. In this regard, the worsening health crisis is expected to affect the Brazilian economy through external and financial channels: major containment measures in Europe and the United States would likely weigh on the country's exports, while the tightening of international financial conditions would also weigh on investment prospects. In the case of a prolonged health crisis, GDP growth would only reach 1% in 2021 and 3.2% in 2022.

The inflation outlook has deteriorated over the past three months, but inflation is expected to remain around the BCB's 4% target. Inflation accelerated from 2.3% in July to 3.9% in October, as food prices rose 14% yoy. Nevertheless, the less volatile components of the consumer basket and services continue to show stability. Indeed, services inflation is still at low levels (1.5% in January) while inflation of non-tradable goods is at 3.1%. Demand pressures are expected to remain moderate in the coming months (the unemployment rate is very high while real wage growth has stagnated over the last five years), and the pass-through of the exchange rate to prices is now low, supporting the low inflation environment. The BCB kept the SELIC rate at 2% in August - its lowest level since the introduction of inflation targeting in 1999, but it is likely to raise rates in the event of a sharp rise in inflation or high volatility of financial variables. Congress has approved an asset purchase program, but the BCB has not yet made significant purchases of BRL government securities and has stated that it will intervene only when traditional tools are exhausted.

"Above the line" fiscal measures	**Size R$/bn**
Health expenditures	2
Transfers to unemployed or informal workers of BRL 600 per month until July	45
13th salary for retirees	46
Salary bonus allowance	12.8
Withdrawals from mandatory saving (FGTS)	41.5
Increase of Bolsa Familia	2
Temporary increase of unemployment insurance	10
Continuous cash benefits	5
Tax deferrals for companies	36
Transfers to states	80
Credit guarantees	319
Total	599.3

The main risk to the outlook is a disorderly fiscal adjustment. Given the depth of the recession and the size of the fiscal stimulus measures implemented, public debt increased from 74% of GDP in 2019 to 90% of GDP at end 2020 and is projected to reach 100% in 2022. Interest rates on the public debt in RBL remain contained and the currency depreciation had little effect on public debt, as most loans are issued in local currency. In addition, the measures that have been taken are expected to expire in early 2021, and the "golden fiscal rule" (primary expenditure growth cannot exceed the previous year's inflation) is expected to be more restrictive in 2021.

The authorities have issued shorter-term debt securities to finance the fiscal stimulus, which has lowered the maturity of the debt. A return of inflation could trigger a rise in local currency rates, which would tighten credit conditions and force the government to adopt a more significant fiscal adjustment. In addition, the expansionary fiscal policy has allowed the government to increase its popularity in 2020 despite the recession and the health crisis. As a result, there is a risk that President Bolsonaro may not comply with the fiscal rule in 2021 in the run-up to the 2022 general elections, which would imply a further deterioration of the fiscal accounts. Finally, the persistence of the climate of political crisis that has led to the departure of "pro-market" members of the federal cabinet could also lead to greater uncertainty in the financial markets.

Brazil	**2019**	**2020**	**2021f**		**2022f**		**2023f**	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	1.1	-4.8	4.1	1.0	2.2	3.2	2.2	2.2
Inflation, %	3.6	3.2	3.8	3.4	3.4	3.4	3.3	3.3
Current account, % GDP	-2.6	-0.9	-1.8	-0.8	-2.2	-1.5	-2.2	-2.0
Fiscal balance, % GDP	-6.0	-13.7	-8.6	-10.0	-7.2	-8.0	-6.0	-5.5
Public debt, % GDP	77	89	92	100	96	107	110	111

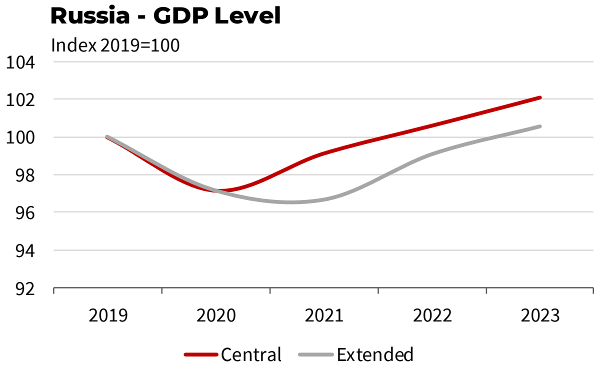
Base = Central scenario
Ext. = Extended health crisis scenario

RUSSIA

- **The economy was less affected than expected by the pandemic thanks to strong macroeconomic conditions at the time the country entered the crisis.**
- **Inflationary pressures are expected to persist in 2021, limiting the central bank's ability to pursue an expansionary monetary policy.**
- **The prospects for fiscal consolidation could weigh on the economy's ability to rebound. Medium term, the major "national projects" announced at the end of 2018 provides hope for the growth potential**

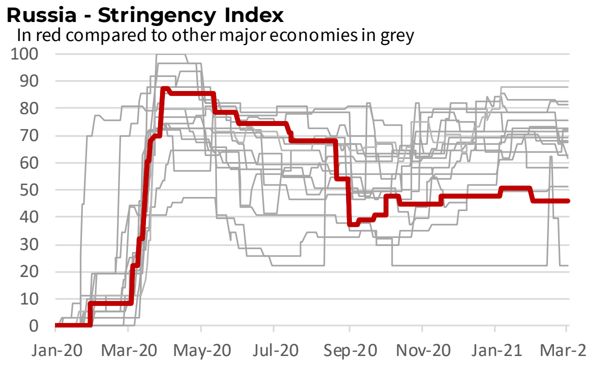
The economy contracted less than expected in 2020 at -3.1%. This is the third largest contraction in Russian GDP since the 1998 sovereign default. It should be noted that the Russian economy entered the crisis in a paradoxical situation. On the one hand, macroeconomic fundamentals were strong (low public debt, comfortable external financial position, low inflation and a well-capitalized banking system). This allowed the implementation of appropriate countercyclical measures. On the other hand, the question remains about the capacity of the economy to rebound in the coming quarters. This is under the assumption (of our central scenario) of a successful completion of the vaccination programs. These would allow for a normalization of the functioning of the economy that should be complete between the end of 2021 and early 2022.

Growth was less affected than in other major emerging economies…



Source: SG Economic and Sector Research

…and confinement measures have been considerably relaxed



Source: University of Oxford

The pre-crisis GDP growth rate already raised questions about the economy's growth potential. Indeed, after the drop in oil prices in 2014-2015, GDP could only grow at an average rate of 1.5% between 2016 and 2019. This trajectory remains insufficient to ensure the convergence of the Russian economy towards the most developed economies. Structural reasons (low investment, institutional weaknesses, etc.) are regularly put forward to explain the Russian economy's difficulty in really taking off.

Demand is expected to rebound, albeit to a limited extent, in 2021 thanks to the gradual reopening of the economy. This rebound should be moderate given the acceleration of inflation in recent months, which at 5.7% in February is well above the Central Bank of Russia's target of 4%. This will limit the ability of the monetary authority to maintain an expansionary monetary policy in the long term. Inflationary pressures are driven by rising input prices, food prices, and lagged effects of the ruble's depreciation in 2020. However, prices are expected to decelerate in the second half of 2021 as the ruble and commodity prices are expected to stabilize.

After a support package amounting to more than 4% of GDP in 2020, fiscal policy is expected to undergo a gradual consolidation phase starting this year. The authorities have made it clear that they are ready to act in the event of a deterioration of the situation, but the long-term objective is to limit any recourse to debt or the use of sovereign wealth funds as much as possible. It should be noted that Russia has the lowest public debt ratio of the G20 countries at nearly 20% of GDP.

Medium term, the government continues to rely on the major projects that were announced in 2018. This is a strategic plan targeting thirteen different sectors (including health, education, infrastructure, ecology, demography ...) to increase the country's growth potential. This represents public investments of about 20% over a period of six years. Since their announcement, however, implementation has been very limited.

Budgetary measures in 2021	
Subsidies to households with children	
Subsidized real estate loans	
Recapitalization schemes of SOEs under consideration	
Total	
% of GDP (2020)	1.5%

Russia	**2019**	**2020**	**2021f**		**2022f**		**2023f**	
	Actual	Actual	Base	Ext.	Base	Ext.	Base	Ext.
Real GDP, % YoY	1.2	-2.9	2.0	-0.5	1.5	2.5	1.5	1.5
Inflation, %	4.5	3.5	4.5	6.0	4.0	4.0	4.0	4.0
Current account, % GDP	3.8	2.0	2.0	1.5	2.5	2.0	2.5	2.0
Fiscal balance, % GDP	1.9	-4.1	-2.0	-3.5	-1.5	-3.0	-1.5	-2.5
Public debt, % GDP	14	19	19	22.0	19	23.0	18	23.0

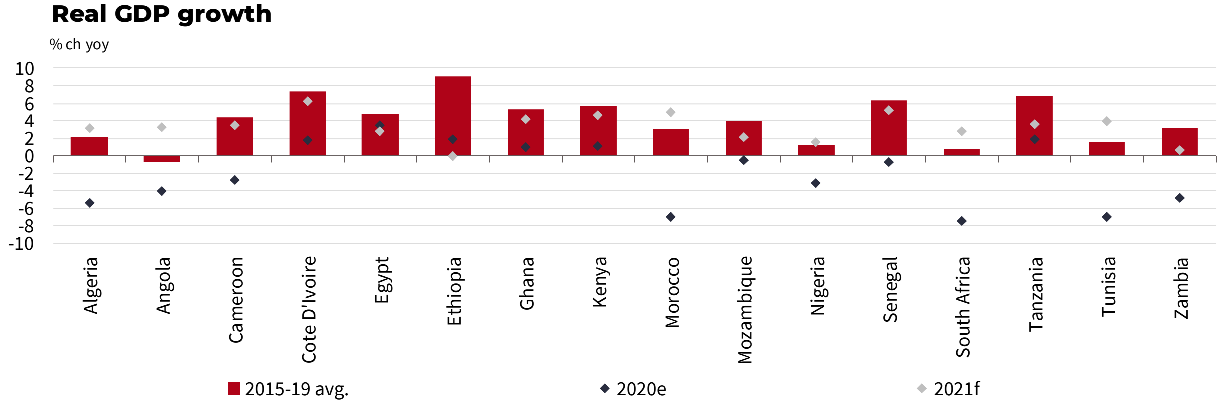
Base = Central scenario
Ext. = Extended health crisis scenario

AFRICA

- **Although the health situation remains less alarming than initially expected, vaccinations continue to pose a real problem.**
- **Despite an economic slowdown that is less pronounced than elsewhere, the social cost of Covid19 will be higher in Africa.**
- **A new wave of public debt restructuring in some countries cannot be excluded.**

Despite a 2nd wave (stronger than the 1st in terms of contaminations and deaths) recorded in December 2020 / January 2021, the health situation in Africa continues to be less alarming than initially expected. In relation to the total population of the continent (1.3 billion inhabitants), the cumulative figures of contaminations (< 3 / 1000) and deaths (< 1 / 1000) remain lower than those of other regions. Moreover, preliminary studies carried out on the 1st wave seem to indicate that there was no significant underestimation of death figures in the region. Even in this relatively optimistic picture, the lack of vaccination remains problematic. Hampered by poorly developed health systems and already strained public finances, the vast majority of African countries have not been able to pre-order vaccines, and therefore find themselves dependent on "donations" granted by some producing countries (China and Russia, in particular) and on the COVAX initiative (created by the WHO). While some national campaigns have only just begun (South Africa, Morocco, etc.), the very optimistic objectives of COVAX (3% of Africans vaccinated mid-2021, 20% at the end of the year) already seem insufficient to guarantee a "return to normal" this year.

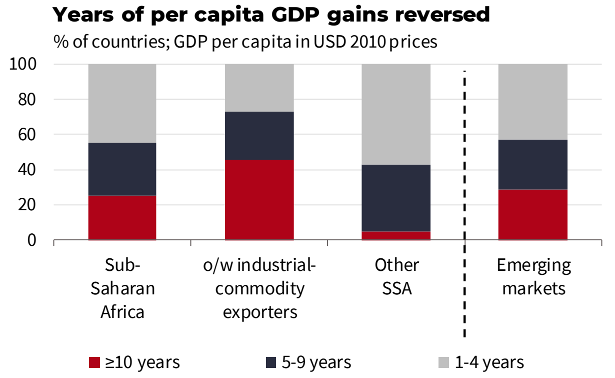
A strong heterogeneity of economic performances



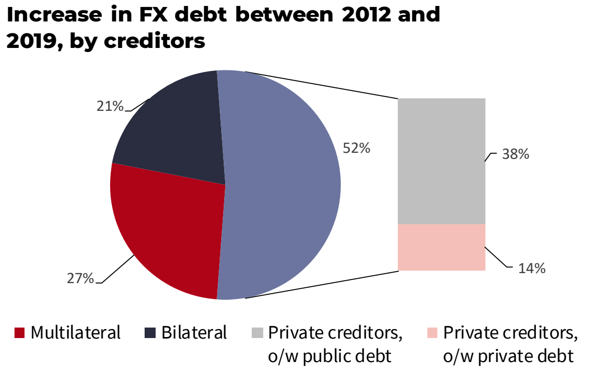
Source: SG Economics & Sector Studies, IMF

If Africa in 2020 recorded the first recession in its modern history, the economic impact of Covid19 was on average less pronounced than in other regions, with real GDP growth losing about 6 to 7 percentage points between 2019 and 2020. Nonetheless, this observation first masks a strong heterogeneity of economic performances, between diversified economies (Côte d'Ivoire, Egypt, Ethiopia, Ghana, Kenya, Senegal, Tanzania) which recorded positive or very slight negative growth in 2020; and economies dependent on oil (Algeria, Nigeria, Angola), tourism (Morocco, Tunisia), and/or the most connected to the world economy (South Africa) recording historical recessions (of the order of 5 to 8%). Second, the social impact of the Covid19 crisis is more significant in Africa than elsewhere, given (i) lower GDP per capita levels before the crisis, (ii) the lack of social safety nets on the continent, and (iii) a still strong demographic growth (of the order of 2.5% per year) which makes a regular increase in GDP mandatory. Thus, the World Bank estimates average living standards are back by a decade or more in 25% of Sub-Saharan African economies.

A significant decline in living standards



A growing share of private creditors



Source: SG Economics & Sector Studies, IMF, World Bank

In addition, and as discussed previously, the Covid19 crisis has significantly accelerated the trend of deterioration in public finances which begun in 2014-15. While the significant international financial support (record financing lines from the IMF, Debt Service Suspension Initiative – DSSI, etc.) granted to Africa has so far helped avoid a liquidity crisis, the continent's more structural solvency problems could lead to a new wave of public debt restructurings in the most fragile countries. Thus, in February, Chad and Ethiopia officially expressed their willingness to restructure their public debt in foreign currency under the " Common Framework for Debt Treatments" (CFDT) defined by the Paris Club and the G20 in November 2020. This framework, which is intended to be an extension of the DSSI, has as its founding principle a "comparability of treatment among all creditors", and therefore calls again for the participation of private creditors (capital markets, banks, etc.), Africa's main sources of financing since 2015. All in all, whether Africa's public debts are restructured or not, it is difficult to imagine that the continent could in the coming years go into massive debt to finance public investment programs as it was the case between 2012 and 2019. This will inevitably (at least partially) overshadow regional growth prospects, which are already relatively weak and uncertain (4% in 2021 and 2022).

EMERGING ASIA

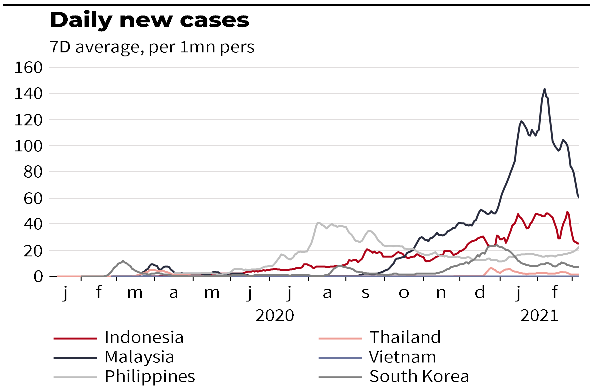
- **The disparity in intra-regional growth mainly reflects the disparity in the management of the epidemic.**
- **There is still some room for manoeuvring in the policy mix.**
- **Improved external fundamentals help build resilience to volatile capital flows.**

There continues to be growth in the region, but intra-regional disparity remains high. The heterogeneity of the health situation is the main cause. The region maintains its relative performance compared to the rest of the world.

First, some economies have experienced a less pronounced shock and are emerging from the health crisis more rapidly. The spread of the virus is more limited or controlled in economies such as South Korea, Taiwan, Thailand and Vietnam. Their economic activity is generally more dynamic. In Taiwan and Vietnam, GDP has even increased by 3.1% and 2.6% respectively in 2020. In South Korea, the GDP only recorded a slight contraction of 1% over the same period. Thailand is an exception with a GDP contraction of 6.1%, due to a domestic political crisis and a heavy dependence on international tourism.

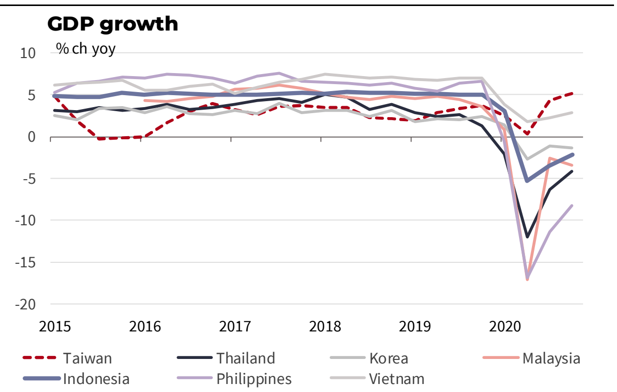
The countries that still have an uncontrolled incidence rate are Malaysia, Indonesia and to a lesser extent the Philippines. Activity there declined by 5.6%, 2.1% and 9.5% last year.

The Covid19 not totally under control...



Source: Datastream Refinitiv, SG Economic and Sector Studies

... leaving marks on growth

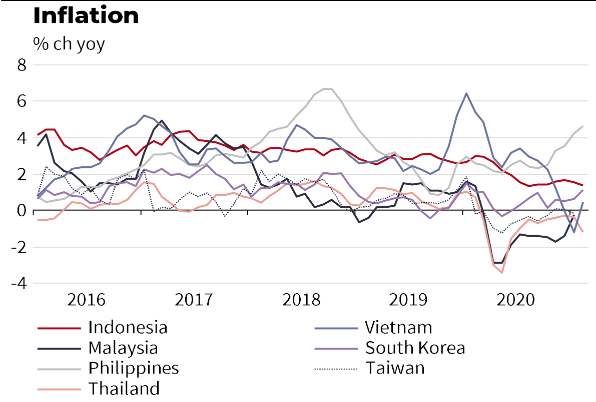


Source: IMF, SG Economic and Sector Studies

The region as a whole has some policy room, and the external fundamentals are strong. This allows the region to recover more quickly than other emerging countries in this time of health crisis, and to be more resilient even in the event of a more prolonged crisis.

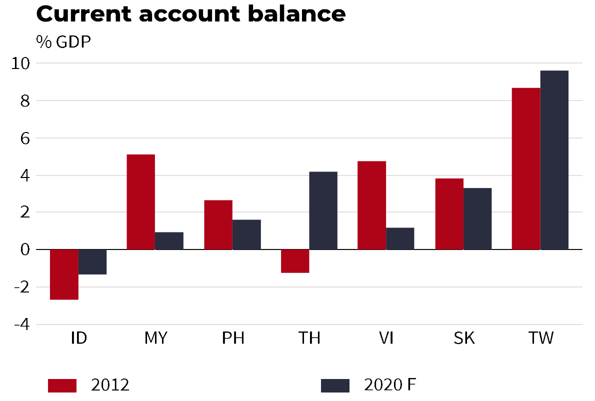
In terms of public finances, all countries will have seen their public debt-to-GDP ratio increase. As the scope for additional stimulus has eroded, it is still possible, especially if fiscal tools with a sufficiently high multiplier are used. Only Malaysia would have public debts approaching 70% of GDP by the end of 2020, while those of the other countries should not, or only slightly, exceed 50%. On the monetary side, as the risk of inflation is low, the central banks would have the possibility of further monetary easing. Only the Philippines has recently recorded an inflation rate above the central bank's target, which constrains the use of short-term monetary tools.

Weak inflation risk



Source: Refinitiv, SG Economic and Sector Studies.

Better external position than in 2012



Source: IMF, SG Economic and Sector Studies

Moreover, the region's exports have outperformed the rest of the world, thanks in particular to the specialisation in semiconductors and better control of the epidemic having preserved value chains. With the exception of the Philippines and Thailand, the countries' exports returned to double-digit growth in December 2020. The trade balance of surplus countries has increased and it has decreased for those with a negative balanc. Countries have seen their foreign exchange reserves increase substantially. While Taiwan and South Korea have traditionally built up abundant foreign exchange reserves, those of Indonesia - often considered sensitive to fluctuations in foreign capital - have risen by 14% since March 2020; those of the Philippines, due in part to the transfer of remittences, have rebounded by 22% since the epidemic.

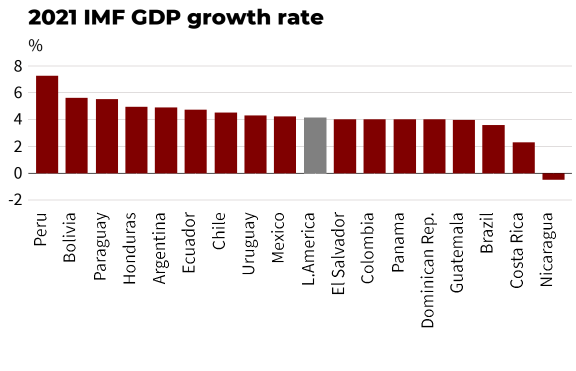
This improvement in external fundamentals enables countries in the region to better cope with the next risk of foreign capital reversal, such as the risk of tapering. The Indonesian rupee depreciated by 11%, the Thai baht by 9%, the Philippine peso by 8.4% and the Malaysian ringgit by 5.8% in the six months following the Fed's first communication on the possibility of reducing its purchase programme in 2013.

LATIN AMERICA

- **Regional growth is expected to recover only partially from the Covid19 shock, driven mainly by external factors.**
- **Central banks should maintain flexible monetary conditions in an environment of moderately rising inflation. The fiscal response should remain limited.**
- **The risk remains high as the pandemic continues and the region has entered this crisis after a period of weak growth.**

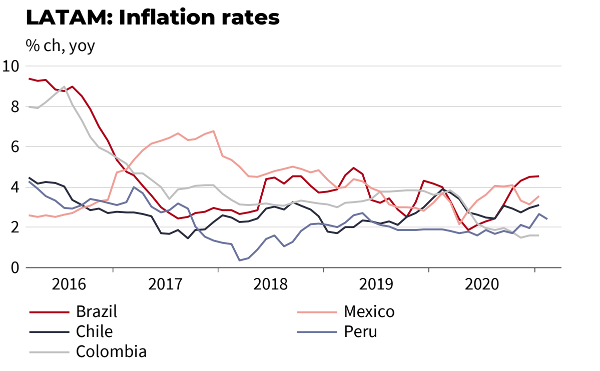
After having been significantly affected by the economic and health crisis of Covid19, regional growth is expected to recover only gradually. The number of infections and victims is slowly decreasing in most countries of the region and, except for Chile, vaccination campaigns are slow. Thus, the continuation of the health crisis is expected to constrain the recovery of private consumption. In addition, most governments in the region have low tax margins as a result of the crisis, which is also expected to limit the recovery of domestic demand. In this context, external demand should be the main driver of the recovery. Indeed, the recovery in commodity prices (oil, energy, agricultural) should support investment and exports from South American countries. In addition, the very strong recovery of the US economy should benefit the region via the trade channel but also via the channel of remittances from migrants. Finally, despite the recent volatility of regional currencies linked to the volatility of U.S. interest rates, risk premiums on sovereign foreign currency debt remain at low levels.

Latin America: moderate recovery after a sharp drop.



Source: SG Economic and Sector Research, IMF

Inflation is on an upward trend but remains in the tolerance range of Central banks



Source: SG Economic and Sector Research, Refinitiv

In Brazil, where the health crisis remains acute, the contraction of the economy was finally less severe than the regional average (-4%) thanks to the significant fiscal support in 2020 (8% of GDP) and should return to its pre-crisis level by the end of the year. The central bank has kept its key rate at 2%, its lowest level since the beginning of the implementation of the anti-inflation regime, but it could start an upward cycle if inflationary pressures (4.5% in January) remain persistent. Congress also authorized the Central Bank to engage in quantitative easing operations with government debt securities and some corporate securities. The recovery in 2021 is expected to be supported in part by improved terms of trade, and doubts persist about extending budget support. Overall, the health crisis is expected to prolong the country's period of sluggish growth (1% on average since 2015).

In Mexico, the health and economic crisis are also acute, resulting in an 8.5% contraction in activity. As is the case in Brazil, the Mexican government has not implemented a strict lockdown. The Central Bank has gradually reduced interest rates from 7% to 4% since the beginning of the crisis. Given the slowdown of inflation, with core CPI reaching 3.8% in Janury, it is expected that the monetary authority will keep ease financial conditions. Mexico did not implement any fiscal stimulus plan and managed to maintain a primary fiscal surplus (0.6% in the third quarter), which also explains the sharp contraction of the economy. In 2021, growth is expected to be driven mainly by the strong recovery of the U.S. economy. On the one hand, more than 80% of the country's exports go to the United States, which should benefit from the recovery of the Mexican industrial sector. On the other, Mexico also benefits from migrant remittances (3.5% of GDP in 2020) which should remain significant in 2021. In total, the Mexican economy is expected to grow by 4% in 2021 and not return to its pre-crisis level until the end of 2022.

CENTRAL AND EASTERN EUROPE

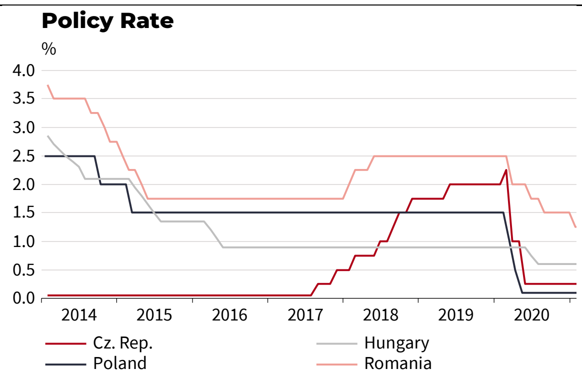
- **The rebound in 2021 will be limited by a first quarter still marked by health uncertainties, but also by persistent inflation, which should weigh on demand.**
- **Beyond 2021, growth will continue to be driven by the economic catch-up. The region should benefit from productivity gains as well as from structural funds and the European recovery fund.**

As in the other regions, economic activity was less severely affected in the fourth quarter of 2020. While the region had largely escaped the first wave of March-April 2020, however, it was hit hard by the second wave from October. Contrary to the majority of neighbouring countries, Central and Eastern Europe is once again standing out with a very noticeable resurgence of the epidemic since January, particularly in the Czech Republic, Slovakia, Hungary and Bulgaria. New cases are also on the rise in Romania and Serbia. Poland remains the only major economy in the region that is coping fairly well with the health situation.

The region has benefited from the strength of international trade in recent quarters, thanks to an export sector that is well integrated into global value chains. Nevertheless, beyond this recovery, the dynamics of domestic demand remain constrained by the persistence of the pandemic. Several factors are expected to contribute to the relatively weak rebound in 2021.

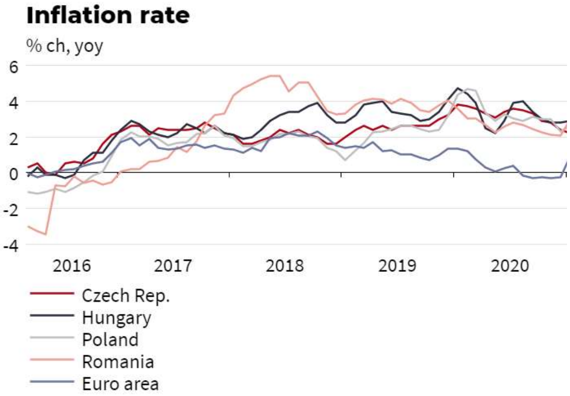
The persistence or acceleration of inflation in some countries will limit the ability of central banks to push for further cuts in key rates. In addition, the rise in long-term bond yields in most countries could weigh on the costs and therefore the borrowing capacity of companies and households. Inflation should naturally affect real disposable household income, the increase in which is likely to be limited in 2021 in a context where firms are reviewing their wage policies.

Generalized decrease in rates in the region



Source: SG Economic and Sector Studies, Refinitiv

Inflation limits ability to lower rates further



Source: SG Economic and Sector Studies, Refinitiv

However, medium term, the process of economic catch-up that has been underway for several years is expected to continue. This process should benefit from the proximity of the countries in the region to the euro area, which favours their productive integration. In addition, these countries will continue to receive funds from the EU in several forms. Thus, the combination of the European Recovery Fund (Next Generation EU), the Employment Support Fund (SURE), and the European Structural Funds themselves are expected to constitute aid of around 20 to 30% of GDP by 2025, depending on the country. The first wave of this European aid comes from the SURE fund. Loans from the European recovery fund should also arrive during the year. The various estimates are based on a reduction of almost 25% of the need to resort to debt for the year 2021 thanks to these funds. Part of the European recovery plan includes a grant component, but this is expected to be implemented at the end of the year.

With the normalization of health conditions, as expected in our central scenario, the region could benefit from more dynamic growth from 2022 onwards. In contrast to the major developed economies, the countries of Central and Eastern Europe are expected to suffer less from the stigma of the crisis. In fact, companies in the region have entered the crisis with a reasonable level of debt. The labour market remains structurally tight, resulting in low structural unemployment and steadily rising real wages. Finally, public debt levels in the region remain well below the debt levels of its euro area neighbours.

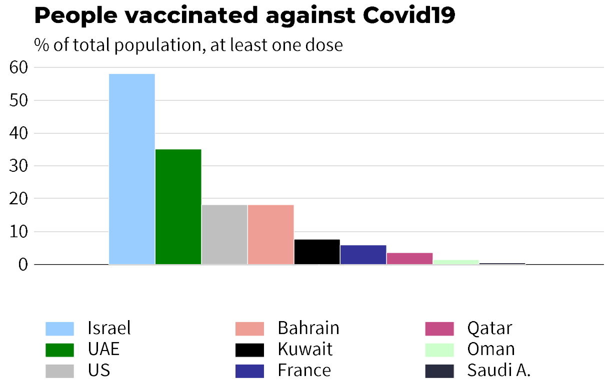
GULF STATES

- **Higher oil prices improve the outlook of fiscal accounts.**
- **Debt ratios are still expected to rise.**
- **The blockade imposed on Qatar since 2017 was lifted early January.**

Higher oil prices are now easing the blow to the Gulf countries, but the economic fallouts from Covid19 related restrictions remain very present. The speed of recovery in 2021 is subject to a high degree of uncertainty. Despite external demand increasing, business and travel hubs such as the UAE, continue to experience the consequences to hit the aviation and hospitality sectors, whilst all over the region, the lower employment associated with the exodus of migrant workers has a strong impact on total domestic spending, hurting the retail sector and real estate occupation. The rollout of vaccination programmes is quite rapid in the UAE and Bahrain, but the region is still facing significant virus circulation.

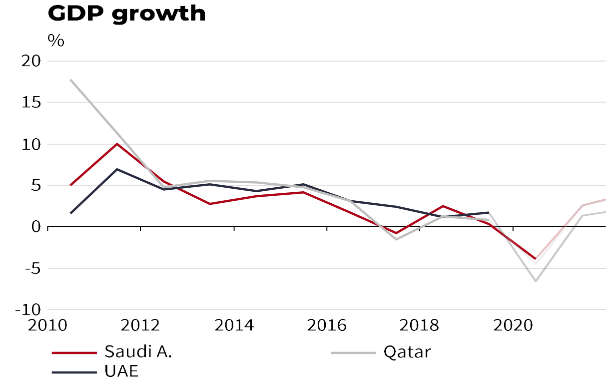
The biggest factor of uncertainty still relates to oil price volatility. Brent traded at $70/b into mid-March, the highest price since the end of 2019 and 60% above the 2020 average. However, oil futures (and our forecasts) point to lower oil prices ahead and a risk of non-compliance with production agreements.

The Emirates' rapid vaccination campaign



Source: COVID-19 Data Repository by the Center for Systems Science and Engineering (CSSE) at Johns Hopkins University

Steep drop of activity in 2020



Source: FMI, World Economic Outlook

Breakeven oil prices have generally fallen since 2014 with governments trying to diversify fiscal revenues away from oil (through, for example, the introduction of VAT in Saudi Arabia, the United Arab Emirates, and Bahrain) and cutting spending (social transfers and government subsidies). Yet, except for in Qatar (which intends to buy back part of its public debt in 2021) and Kuwait, national budgets are likely to remain out of balance over the medium term. Againt this backdrop, the region will stil have to turn to debt markets. This is likely to be on a smaller scale than in 2020, when international sovereign bond issuance reached a record high of USD 66 billion.

With oil prices increasing, the balance of payments is due to shift as well. The experienced decline in FX reserves over 2020 is similarly set to rebalance. The current account balance will remain negative in Oman and Bahrain, with Kuwait and Saudi Arabia moving into positive territory should the higher trading values of oil prices be confirmed.

The region has long been preparing for medium-term challenges, which the Covid19 crisis renders even more relevant. The various national economic development plans envisaged by the Gulf monarchies focus on economic modernization, renewable energy development, and reforms to isolate public income from oil price volatility. However, this transition is not an obstacle-free path, as considerable challenges in the labour market (different treatment of national vs foreign works, higher salaries in the public than in the private sector) and market regulation (favouring national companies) are often seen as an obstacle to private sector involvement. Furthermore, the volatility in the oil rent weighs on the ability to self-finance infrastructure projects.

The geopolitical landscape also remains a source of uncertainty. President Biden's administration appears to be setting some distance from Saudi Arabia, in sharp contrast to the close relationship President Trump sought. The UAE and Bahrain agreed to the full normalisation of relations with Israel in 2020, and talks seem to be underway for similar improvements with Saudi Arabia. The blockade imposed on Qatar since 2017 by its neighbours was lifted on 5 January 2021, against the backdrop of improving diplomatic relations between Qatar and Saudi Arabia. Nevertheless, the UAE and Egypt remain sceptical of Qatar, who has allowed for Turkey to establish a military presence in their country, and thereby increasing its presence in the region. Finally, Qatar may act as a mediator for a new nuclear deal between the US and Iran, a deal which faces opposition from Saudi Arabia and the UAE.

MACRO FORECASTS

Real GDP Growth, %

	2019	2020f	2021f		2022f		2023f	
	Actual	Actual	Central	Extended	Central	Extended	Central	Extended
Developed Markets	**1.6**	**-5.3**	**4.8**	**2.1**	**2.8**	**2.8**	**1.7**	**2.7**
United States	2.2	-3.5	5.3	2.5	3.8	4.1	2.2	3.0
Japan	0.3	-4.9	3.4	0.3	1.7	2.0	0.6	1.1
United Kingdom	1.4	-9.9	5.0	2.0	3.0	3.0	2.0	2.5
Euro area	1.3	-6.8	4.9	1.6	2.0	1.1	1.4	3.8
Germany	0.6	-5.3	3.0	0.5	2.5	1.0	1.3	3.5
France	1.5	-8.2	6.5	3.5	1.7	1.0	1.5	4.0
Italy	0.3	-8.9	6.3	2.0	1.5	1.0	1.0	3.0
Spain	2.0	-11.0	7.2	2.0	3.0	1.2	1.8	5.2
Emerging Markets	**3.5**	**-2.6**	**5.9**	**3.6**	**3.6**	**3.7**	**3.7**	**4.0**
Asia	4.9	-1.0	7.4	5.1	4.6	4.8	4.6	4.9
China	6.0	2.3	8.0	6.0	4.9	5.0	4.6	5.0
India	4.9	-8.0	10.0	6.5	5.8	7.0	4.7	5.2
CEE	2.1	-4.1	3.7	1.4	2.1	2.3	2.5	2.6
Russian Federation	1.2	-2.9	2.0	-0.5	1.5	2.5	1.5	1.5
Latin America	0.1	-7.4	4.4	2.0	1.8	2.0	1.9	2.1
Brazil	1.1	-4.8	4.1	1.0	2.2	3.2	2.2	2.2
Middle East & C.Asia	0.3	-5.6	2.6	0.6	1.9	1.6	2.1	2.3
Africa	3.3	-2.4	3.3	1.3	2.7	2.4	3.4	3.6
World (PPP weighted)	**2.8**	**-3.6**	**5.5**	**3.0**	**3.3**	**3.4**	**2.9**	**3.5**

Inflation, %

	2019	2020f	2021f		2022f		2023f	
	Actual	Actual	Central	Extended	Central	Extended	Central	Extended
Developed Markets								
United States	1.8	1.3	3.0	2.1	2.5	3.0	2.5	2.3
Japan	0.5	0.0	0.0	-0.4	0.7	0.0	0.5	0.6
United Kingdom	1.8	0.9	1.7	1.2	2.1	1.9	2.0	1.9
Euro area	1.2	0.3	1.6	1.3	1.2	1.1	1.3	1.3
Germany	1.4	0.4	2.1	1.6	1.2	1.0	1.4	1.5
France	1.3	0.5	1.3	1.1	1.1	1.2	1.3	1.3
Italy	0.6	-0.1	0.9	0.6	1.0	1.0	1.2	1.2
Spain	0.8	-0.3	1.0	0.5	1.8	1.7	1.3	1.3
Emerging Markets								
China	2.9	2.5	1.7	1.5	2.3	2.2	2.3	2.3
India	3.7	6.6	5.0	6.3	5.0	5.5	5.0	5.2
Russian Federation	4.5	3.5	4.5	6.0	4.0	4.0	4.0	4.0
Brazil	3.7	3.2	3.8	3.4	3.4	3.4	3.3	3.3

Unemployment, %

	2019	2020f	2021f		2022f		2023f	
	Actual	Central	Central	Extended	Central	Extended	Central	Extended
Developed Markets								
United States	3.6	6.8	4.3	6.6	3.8	5.0	3.6	4.5
Japan	2.3	2.8	2.8	3.0	2.6	2.8	2.6	2.7
United Kingdom	3.8	4.5	7.1	8.2	6.4	7.3	5.3	5.8
Euro area	7.6	8.0	8.7	9.2	9.1	9.9	8.8	9.6
Germany	5.0	5.9	6.6	7.0	6.7	7.4	6.5	7.2
France	8.1	7.8	9.3	10.0	9.9	10.4	9.5	10.0
Italy	9.9	9.4	11.8	12.7	11.4	12.4	10.9	12.1
Spain	14.1	15.6	17.4	18.6	17.0	18.9	16.4	18.2
Emerging Markets								
China	5.1	5.6	5.1	5.9	4.9	5.1	4.9	5.0

Fiscal deficit, % GDP

	2019	2020f	2021f		2022f		2023f	
	Actual	Central	Central	Extended	Central	Extended	Central	Extended
Developed Markets								
United States	-6.7	-13.1	-10.5	-17.0	-8.0	-13.0	-5.5	-10.0
Japan	-3.3	-13.8	-6.5	-11.0	-3.3	-5.0	-3.0	-3.0
United Kingdom	-2.3	-13.1	-10.2	-14.2	-6.1	-7.4	-4.8	-6.2
Euro area	-0.9	-8.3	-5.9	-7.6	-5.3	-7.5	-4.9	-6.0
Germany	1.5	-5.3	-4.3	-5.6	-3.5	-5.5	-3.3	-4.3
France	-3.0	-10.2	-6.2	-7.8	-5.7	-7.6	-5.0	-5.6
Italy	-1.6	-10.4	-7.7	-9.9	-7.3	-9.8	-7.0	-8.6
Spain	-2.9	-12.0	-8.7	-11.8	-7.6	-11.7	-7.1	-9.7
Emerging Markets								
China	-3.1	-3.6	-2.8	-3.0	-2.8	-2.9	-2.8	-2.8
India	-7.4	-13.0	-10.0	-13.0	-9.0	-8.0	-7.0	-7.5
Russian Federation	0.8	-0.3	1.0	-3.5	1.8	-3.0	1.3	-2.5
Brazil	-5.9	-13.7	-8.6	-11.8	-7.2	-11.7	-6.5	-9.7

Public debt, % GDP

	2019	2020f	2021f		2022f		2023f	
	Actual	Central	Central	Extended	Central	Extended	Central	Extended
Developed Markets								
United States	80	103	106	112	109	116	111	120
Japan	238	252	258	264	260	269	262	270
United Kingdom	85	102	105	112	106	114	106	115
Euro area	89	105	106	112	109	117	111	117
Germany	60	72	73	76	74	80	75	80
France	98	116	120	125	123	130	126	130
Italy	135	157	159	166	162	173	165	174
Spain	96	118	117	127	119	136	122	137
Emerging Markets								
China	39	46	44	45	44	45	44	45
India	72	86	85	90	86	88	85	87
Russian Federation	14	19	19	22	19	23	18	23
Brazil	74	89	92	100	96	107	100	111

Current account balance, % GDP

	2019	2020f	2021f		2022f		2023f	
	Actual	Central	Central	Extended	Central	Extended	Central	Extended
Developed Markets								
United States	-2.2	-2.4	-3.0	-2.6	-3.0	-2.8	-2.5	-2.5
Japan	3.6	3.2	3.4	2.9	3.7	3.1	3.6	3.4
United Kingdom	-3.1	-3.9	-7.3	-7.1	-7.0	-6.9	-6.4	-6.3
Euro area	2.3	2.2	3.2	3.2	3.0	3.4	3.1	3.5
Germany	7.2	6.6	7.5	7.6	7.4	7.9	7.5	7.9
France	-0.7	-2.3	-1.1	-0.9	-0.5	0.0	-0.7	-0.4
Italy	3.0	3.6	4.0	3.8	2.6	4.1	3.0	4.1
Spain	2.1	0.3	0.8	0.2	1.1	0.4	1.1	1.8
Emerging Markets								
China	1.0	2.4	2.1	2.1	2.1	2.0	1.9	1.8
India	-1.1	0.6	-1.0	0.2	-1.2	-1.0	-1.2	-1.0
Russian Federation	3.8	2.0	2.0	1.5	2.5	2.0	2.5	2.0
Brazil	-2.7	-0.9	-1.8	-0.8	-2.2	-1.5	-2.2	-2.0

CONTACTS

Michala MARCUSSEN
Group Chief Economist
+33 1 42 13 00 34
michala.marcussen@socgen.com

Olivier de BOYSSON
Emerging Markets Chief Economist
+33 1 42 14 41 46
olivier.de-boysson@socgen.com

Marie-Hélène DUPRAT
Senior Advisor to the Chief Economist
+33 1 42 14 16 04
marie-helene.duprat@socgen.com

Ariel EMIRIAN
Macroeconomic analysis
+33 1 42 13 08 49
ariel.emirian@socgen.com

François LETONDU
Macro-sector and macro-finance analysis
+33 1 57 29 18 43
francois.letondu@socgen.com

Constance BOUBLIL-GROH
Central & Eastern Europe, Russia
+33 1 58 98 98 69
constance.boublil-groh@socgen.com

Olivier DENAGISCARDE
Macro-sector analysis
+33 1 58 98 74 22
olivier.denagiscarde@socgen.com

Juan Carlos DIAZ MENDOZA
Americas
+33 1 57 29 61 77
juan-carlos.diaz-mendoza@socgen.com

Clément GILLET
Africa
+33 1 42 14 31 43
clement.gillet@socgen.com

Erwan JAIN
Macro-sector analysis
+33 1 58 98 05 35
erwan.jain@socgen.com

Alan LEMANGNEN
Euro area, France, Germany
+33 1 42 14 72 88
alan.lemangnen@socgen.com

Simon RAY
Macro-finance analysis, UK
+33 1 4213 70 80
simon.ray@socgen.com

Valérie RIZK
Macro-sector analysis
+33 1 58 98 82 85
valerie.rizk@socgen.com

Danielle SCHWEISGUTH
Western Europe
+33 1 57 29 63 99
danielle.schweisguth@socgen.com

Edgardo TORIJA ZANE
Global economic forecasting
Middle East, Turkey and Central Asia
+33 1 42 14 92 87
edgardo.torija-zane@socgen.com

Bei XU
Asia
+33 1 58 98 23 14
bei.xu@socgen.com

Yolande NARJOU
Assistant
+33 1 42 14 83 29
yolande.narjou@socgen.com

Société Générale | SG Economics and Sector Studies | 75886 PARIS CEDEX 18

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