

First quarter 2021

## Key messages

- Asia is taking the lead in the recovery process, while the gap to pre-crisis levels in Latin America remains large
- COVID-19 infections to remain an issue, as emerging markets are at the back of the queue in hunt for vaccines
- China: amid strong recovery monetary and fiscal stimulus to be gradually phased out in 2021

## Number in focus

6.7%

Turkey's economy experienced a sharp rebound in the third quarter this year, growing by 6.7% from a year ago - the highest growth rate reported among major economies. While a strong stimulus campaign - including a government-led credit push - boosted consumption and investments, it also exacerbated economic vulnerabilities, which led to a slump in the Turkish lira and higher inflation. Consequently, the new central bank governor raised interest rates by 475bps to 15% in November, but more hikes might be needed to stabilise the currency and bring inflation down.

## Chart in focus



For a fifth month in a row, the Emerging Markets Manufacturing Purchasing Managers' Index remained in expansionary territory above the 50-point mark, reflecting an ongoing gradual recovery after the sharp economic contraction induced by the pandemic in spring. More recently, also export orders crossed the 50-point mark, showing that global demand remains solid. Stricter containment measures, especially in the western world, to tackle the second coronavirus wave have been more targeted compared to spring and mainly impact the services sector, while industrial activity keeps running.

## North Asia leading the recovery

Third quarter GDP growth rates across emerging countries showed that, after an unprecedented economic slump in spring, the worst is now over. Economies across the board pursued a significant economic recovery as they eased mobility restrictions, leading to a resumption of industrial activity and consumption. Nevertheless, divergences among countries prevail (see Chart 1). Despite a considerable rebound in the third quarter, Latin American economies', such as Mexico's or Colombia's GDP remains well below pre-crisis levels. While in some Latin American countries such as Peru a high share of the population working in the informal sector made social distancing impossible, other countries such as Brazil or Mexico suffered from a lack of an efficient nationwide strategy to contain the virus spread. Consequently, a persistently worrisome health situation keeps weighing on consumer confidence and hampers a further substantial unwinding of social distancing measures. On the other hand, countries in the Asian continent performed relatively well. Besides China, that reached pre-crisis levels already in the first half this year, Taiwan surpassed its pre-crisis levels in the third quarter 2020. Also, South Korea and Indonesia recovered a large part of their losses, standing at only less than three percent below their pre-crisis levels by the end of September. Moreover, indicators in the North Asian economies, show that the recovery continues to gain steam into the fourth quarter. November manufacturing PMI indices continued to move up the 50-points mark that separates expansion from contraction and export data showed strong growth figures compared to a year ago in China, Taiwan as well as in South Korea. Robust external demand continues to support North Asia's economic performance, since

governments take more targeted approaches to contain the virus spread compared to the first COVID-19 wave in spring. Moreover, under the current circumstances, pandemic related goods produced in Asia, such as smartphones, computers as well as medical equipment remain in high demand. Finally, also a relatively better management to contain the virus spread allowed these countries to get back to normal life – although a recent flare-up in South Korea meant that some containment measures had to be implemented once again.

## Emerging countries at the back of the queue in hunt for vaccines

Strict lockdown measures in the Czech Republic and Poland introduced early November to tackle the second coronavirus wave that overwhelmed the countries' healthcare systems proved to be successful, leading to a steep decline of new daily infections. Meanwhile, new COVID-19 cases flare up in other major emerging countries, such as Turkey, Russia, South Africa, Mexico and Brazil, asking for harsher social distancing measures once again. While the measures will have a denting impact on the services sector, the more targeted approach during this second wave will likely have a lesser impact on overall economic activity compared to the slump in spring. Still, COVID-19 infections and lockdown necessities will remain a key topic in 2021 for the emerging world. Other than developed countries, emerging markets will be at the back of the queue when it comes to vaccinations. On the one hand, many emerging countries have not concluded vaccine agreements to the same extent as their developed counterparts. Hence, the majority of vaccine doses that are

Chart 1: Asian economies are taking the lead in the economic recovery process

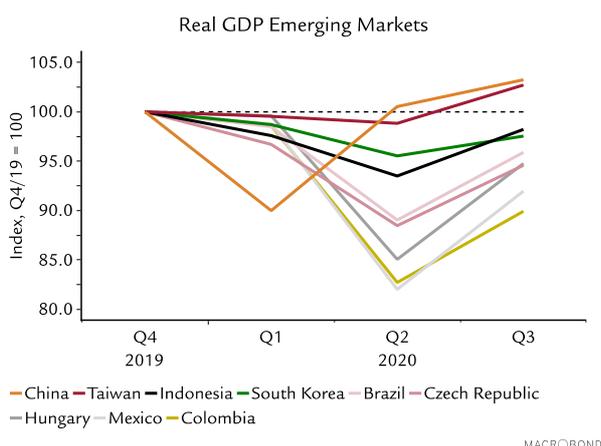
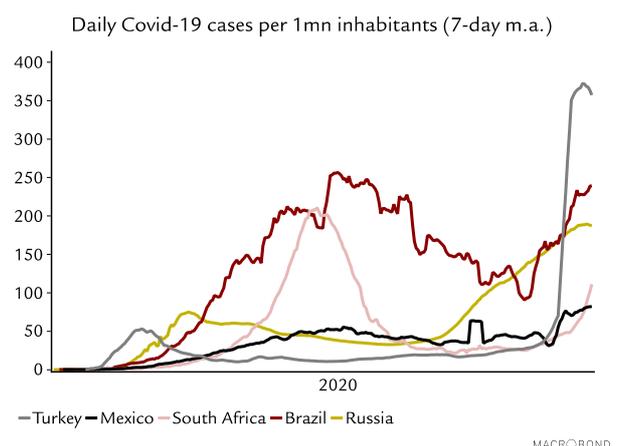


Chart 2: Second COVID-19 wave hits emerging markets

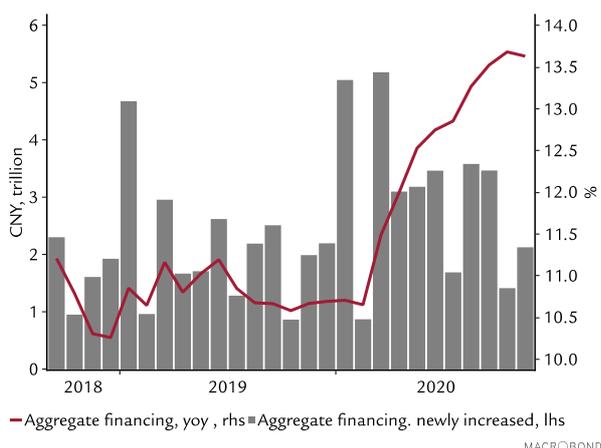


currently in the pipeline will first go to the developed world. On the other hand, distribution and infrastructure constraints will impede a fast vaccination rollout - particularly for those vaccines that require freezing for longer-term storage, such as the ones from Moderna or Pfizer-BioNTech. On the positive, there are still over 200 vaccine candidates in development and if a greater number of these candidates proves to be successful, it is to be hoped that vaccines will reach also the emerging world rather sooner than later.

## China to move to policy normalisation

China's economy surpassed its pre-crisis level by more than three percent in the third quarter 2020 and economic indicators for the fourth quarter point to an ongoing economic expansion. As factories reopened swiftly after the lockdown implemented in February, while restrictions on individual mobility were relaxed only gradually, industrial production recovered earlier and stronger compared to consumption. Nevertheless, November retail sales grew by 5% compared to a year ago, showing that consumers are swiftly catching up. China's successful containment of the pandemic throughout 2020, that helped avoiding a second wave of contagion, has been key for the country's strong economic performance. Heading into 2021, the country will, however, have to prove that it is able to manage the contagion risk during the Chinese New Year festivities that will take place in February, during which hundreds of millions of people leave their cities in order to meet their families in the more rural part of the country. Moreover, since China's economy has recovered strongly from the pandemic-induced crisis, fiscal

Chart 3: Growth of China's broad credit measure to decelerate amid phasing-out of stimulus measures

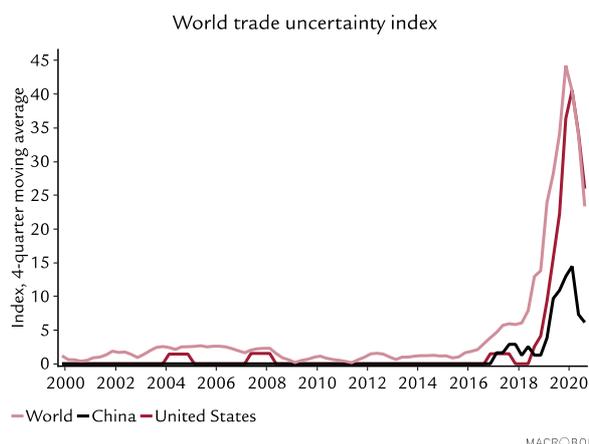


and monetary stimulus measures will be gradually phased-out in order to slow down the credit acceleration and refocus on reducing the country's debt pile. The deleveraging effort will likely lead to an increase in default rates, particularly among non-profitable state-owned companies, and authorities will have to be vigilant to find the right balance between necessary defaults and prevention of systemic risks.

## Economic policy uncertainty to decelerate under Joe Biden

Biden's win in the US presidential elections, will not lead to a revamp of US-China relations. However, the approach to deal with China will likely change - moving towards more predictable and multilateral policies, likely reducing the economic policy uncertainty that spiked during Donald Trump's presidency, especially over trade (see Chart 4). Particularly, under Biden the likelihood of improvement in various areas that have been negatively impacted has increased. On trade, tariffs already in place will most likely not be removed in the short-term, but a partial removal of tariffs has become more likely, if China meets demands concerning intellectual property protection, market openness, etc. On technology, Biden might listen more to US industry concerns, as many US companies depend heavily on China sales and might therefore be less aggressive in putting additional Chinese companies on the so-called "US entity list" that bans US exports to enlisted companies. Nevertheless, as Biden puts greater priority towards human rights and democracy issues - topics that will be difficult to handle - negotiations or concessions on the above-mentioned areas will be complicated. Hence, US-China relations will likely remain tensed.

Chart 4: Economic policy uncertainty over trade to decrease as Biden pursues more predictable policies



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