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ECONOMIC TALKING POINTS

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2021: A Year of Transition for the Economy and Politics

It has been difficult to shake off the horrific events in Washington last week. The looming question now is whether we will see more violence across the country in the lead up to the Joe Biden's presidential inauguration on January 20th.

Looking back, what remains so hard to comprehend is that the violent mob that stormed their way into the Capitol building and threatened to undo the country's electoral democracy --- did so while the nation was being tormented by the most catastrophic pandemic in more than a century. In fact, on the very day of that assault, the number of deaths from the coronavirus, as well as new cases of infections, approached record levels. The nation was thus devastated by one heinous shock, which piled right on to another terrible shock. And the traumas may not be over for either yet.

We therefore begin the New Year with a fragile economy, a grave national health crisis, and a US Constitution that is struggling to recover from its most severe stress test since the Civil War. But at least one outcome is clear: The Presidency of Donald Trump will shortly end much the same way it began, as a grotesque anomaly in the nation's history.

As Congress and law enforcement now proceed to identify and bring to justice those rioters, a new President is about to enter the White House with a profoundly different style and agenda than his predecessor. As the government resumes its work, we also return to the task of assessing what's next for the economy.

Let's begin with 2021

Many forecasters believe the US economy is poised to take off this year in terms of output and hiring, with several expecting to see GDP growth at 6% or more this year and the unemployment dropping to just above 4%. I'll be frank, that's not quite our expectation, at least not yet. We view 2021 primarily as a year of transition for households and most industries, with the business cycle finally returning to normal in 2022. Until then, though, consumers and employers will likely spend much of this year adapting and adjusting to changes in the economic and business landscape as a result of Covid-19. Our forecast has the economy expanding by 4.8% this year, with the jobless rate slipping to 6% in the final quarter of 2021.

There are four major factors that will determine the course of economic activity in 2021.

1. The speed and effectiveness of the vaccine roll out

The performance of the economy is linked to the effective roll out of the vaccine. Full stop! A slow, confusing, and inefficient roll out will set back the economic recovery. So high on the watch list is the production and distribution of the vaccine across the country, along with the speed Americans are being inoculated. Our projection is that the US will not achieve herd immunity (70% to 80% of the population gets vaccinated) before the fourth quarter of this year.

A similar time frame is projected for the UK and European Union, though for Latin America and Africa such levels of immunity will not be reached until the first half of 2022, at the earliest.

We cannot fix the economy, without fixing the health crisis.

Estimated schedule when countries / regions achieve herd immunity:
(Herd immunity = 70% to 80% of population vaccinated against Covid-19)

US = IVQ 2021
UK = IVQ 2021
EU = IVQ 2021
LATAM = IQ 2022 (90% needed)
AFRICA = IIQ 2022 (90% needed)

But many issues remain:

- Global administration of vaccines appears uneven and could delay world economic recovery.
- New variants of Covid showing up. Will current vaccines remain efficacious?
- Duration of immunity from Covid-19 is unknown.
- Longer term side effects have not been determined.



2. The coming Biden pandemic stimulus package(s)

Additional fiscal stimulus will be needed beyond December's \$900 billion program. That plan will boost GDP growth by 1.5 to 2 percentage points over the next two years. But we do not yet see consumer spending as the main driver of economic activity this year. That is due in part because under the current legislation, the additional \$300 per week in enhanced unemployment assistance and other benefits are set to expire mid-March --- long before the country achieves mass vaccinations.

At a minimum you need to achieve the latter for household spending, business activity and hiring to return to pre-pandemic levels.

Moreover, since the last stimulus program provided little new funding to states and local governments, there is real urgency for the next package to provide those entities with greater resources to help fund the distribution of the vaccine. Without additional monies, we could see mass layoffs of public sector and longer delays in the rollout of the vaccine.

3. Enter the Presidency of Joe Biden

A new Administration is about to take over in Washington. We all hope this sets the stage for the political pendulum to finally swing from one of tribalism and hyper-partisanship, a corrosive trend that deeply divided the country the last four years, and shift over to the side of greater bi-partisanship and cooperation. That would be a positive turn of events.

But there are two challenges here.

First, let's remember a President Biden will not be dealing simply with two parties in Congress, but four distinct and assertive factions (far right conservatives, moderate Republicans, centrist Democrats, and a coalition of progressive Social Democrats and Independents). It won't be easy navigating through these political shoals.

Secondly, the House move to impeach Donald Trump this week for a second time, followed by a lengthier trial in the Senate could put at risk end any chance of a honeymoon between the new Democratic president and GOP members in Congress. It's important to point out that Biden's political and legislative agendas are ambitious for 2021 and 2022 and will likely require support from representatives of both parties.

Among Biden's top domestic and foreign policy goals:

- Accelerate distribution of vaccines and speed-up inoculations
- Pass an additional stimulus program for households, businesses and local governments by February or March.
- A partial rollback of 2017 Tax Act, but implemented in a manner that doesn't undermine the economy's recovery.
- Re-appoint Jerome Powell as head of the Fed when his term expires Feb. 2022.
- Negotiate with the European Union to cancel most tariffs imposed by the Trump Administration.
- Selectively scale back tariffs on \$375 billion worth of imports from China if the Biden Administration determines they do more harm to US manufacturers and consumers than it does to China.
- Increase US naval presence in the South China Sea as a show of force to reject China's annexation of the region and uphold the UN's International Law of the Sea.
- Organize a coalition of democratic countries that will work together to place greater pressure on China to change its illegal business and trading practices.
- Have the US re-engage with international institutions on defense, trade, health care and climate change.

- Demand that Iran restrict its uranium enrichment and end the testing of ballistic missiles for the US to join a JCPOA 2.0.
- Prepare meaningful countermeasure if North Korea resumes ICBM or nuclear tests.
- Retaliate more aggressively against Russia for its extensive cyber attacks on the US and its allies.

4. The unknown: What high probability economic and geopolitical threats could erupt in 2021 and 2022?

Finally, we ask a most difficult but essential question in the aftermath of the pandemic shock. What else can go wrong this year and next? Clearly no one wants to be blindsided by another event that could derail a still wobbly recovery.

Below are the greatest potential hazards lurking ahead:

Domestic:

- A significant escalation in what is already a Cyber World War, one that could disrupt financial activity and America's power grid.
- Problems with the distribution and efficacy of the Covid vaccine: Will enough Americans be inoculated this year? Could more lethal variants of the virus emerge that render current vaccines less effective?
- Is the US sleep walking into a national debt crisis, one that will cause yields on treasury notes and bonds to climb and possibly choke off economic activity?
- Will China continue its retreat from the US government debt market and raise the cost of borrowing for Washington and the private sector?
- Is a price bubble forming in financial assets and, if so, what will be the consequences should it burst this year?

International:

- Will foreign adversaries, like Russia, China, Iran and North Korea, create a geopolitical crisis to test the mettle of a new US President?
- If Iran is determined to enrich uranium toward 20%, what actions will the US and Israel take in response?
- Could the growing presence of US and Chinese military forces in the South China Sea and around Taiwan precipitate an international crisis and disrupt maritime shipping in a critical waterway of the world?

FORECASTS 2021 - 2023

United States

	I 2020	II 2020	III 2020	IV 2020	I 2021	II 2021	III 2021	IV 2021	I 2022	II 2022	III 2022	IV 2022	I 2023	II 2023	III 2023	IV 2023
Real Gross Domestic Product (GDP):																
%	-5.0	-31.4	33.4	2.7	2.6	4.8	5.6	6.3	3.1	5.2	4.7	4.4	2.8	3.8	3.1	2.9
Personal Consumption Expenditures:																
PCE %	-6.9	-33.2	41.0	4.1	2.2	6.8	4.5	5.8	2.4	5.2	4.1	3.9	4.0	4.1	2.8	3.5
Inflation, end of period, year-over-year:																
CPI %	1.5	0.6	1.4	1.4	1.5	2.0	2.3	2.5	2.4	2.5	2.3	2.2	2.5	2.6	2.6	2.7
Unemployment Rate (end of period):																
%	4.4	11.1	7.8	6.7	6.5	6.4	6.1	6.0	6.0	5.8	5.6	5.4	5.4	4.9	4.4	4.1
Non-farm Payrolls, monthly avg. thousand:																
	-303	-4,427	1,322	283	322	385	370	380	270	285	265	240	185	225	235	250
Treasury 10-yr Note Yield % (end of period):																
	0.63	0.65	0.68	0.91	1.17	1.29	1.48	1.70	1.82	2.02	2.11	2.15	2.15	2.20	2.20	2.16
Federal funds rate % (end of period):																
	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.38	0.88	1.13

GDP Growth - Global Economy

Country	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
US	2.6	1.6	2.2	1.8	2.5	3.1	1.7	2.3	3.0	2.2	-2.8	4.8	4.4	3.2
Eurozone	1.7	1.4	-0.9	-0.2	1.4	2.1	1.9	2.5	1.9	1.2	-8.8	3.5	2.5	2.0
United Kingdom	1.7	0.7	0.3	1.8	2.9	2.2	1.9	1.9	1.3	1.5	-10.3	3.9	4.2	3.1
Japan	4.6	-0.4	1.6	1.5	-0.1	1.1	0.5	2.2	0.3	0.7	-5.2	2.4	2.8	2.2
Canada	3.1	3.1	1.8	2.3	2.9	0.7	1.0	3.2	2.0	1.6	-5.8	5.4	3.4	2.9
India	8.4	8.6	6.7	4.9	7.4	8.0	8.1	7.2	6.8	4.8	-8.8	9.9	6.4	5.7
China	10.5	9.5	7.8	7.7	7.3	6.9	6.7	6.8	6.6	6.1	2.1	7.2	6.2	5.7
Brazil	7.5	2.7	0.9	2.3	0.1	-3.5	-3.5	1.2	1.2	1.1	-6.0	2.9	2.7	2.4
Mexico	5.2	4.0	3.9	1.4	2.3	2.7	2.7	2.4	2.1	-0.1	-9.6	3.3	2.8	2.7
Australia	2.8	2.6	3.6	2.4	2.6	2.5	2.4	2.4	2.7	1.8	-3.9	2.5	3.0	2.7
Russia	4.0	4.3	3.4	1.3	0.6	-2.8	-0.2	1.6	2.5	1.2	-4.9	2.4	3.3	2.0
World	4.2	3.1	2.5	2.6	2.8	2.8	2.6	3.4	3.2	2.9	-3.8	4.7	4.2	3.9

Key Currency Values

	End 2008	End 2009	End 2010	End 2011	End 2012	End 2013	End 2014	End 2015	End 2016	End 2017	End 2018	End 2019	End 2020	End 2021	End 2022	End 2023
USD/Yen	91	93	81	77	87	105	119	120	117	113	110	109	103	106	102	100
Euro/USD	1.40	1.43	1.34	1.29	1.32	1.37	1.21	1.09	1.05	1.20	1.14	1.12	1.22	1.19	1.25	1.28

Oil (Brent spot) & Gasoline (Average retail unleaded, \$)

	End 2008	End 2009	End 2010	End 2011	End 2012	End 2013	End 2014	End 2015	End 2016	End 2017	End 2018	End 2019	End 2020	End 2021	End 2022	End 2023
Crude oil per barrel	46	78	95	107	111	111	58	38	49	67	54	67	52	60	50	48
Gasoline	1.61	2.57	3.00	3.27	3.30	3.32	2.26	2.00	2.31	2.47	2.26	2.58	2.25	2.46	2.20	2.17

Economic & Geopolitical Probabilities for 2021 & 2022

- Projections made: January 7, 2021

PROBABILITY	U.S.
HIGH	Pres. Biden and a Democratically-controlled Congress to pass another \$1 trillion stimulus by March 2021.
HIGH	Covid-19 vaccinations will not reach 70% of US population before 4th quarter 2021.
Moderate	Fiscal stimulus plus vaccinations to raise inflation expectations and 10-yr treasury yields throughout 2021.
HIGH	Covid-19 fallout to fundamentally alter the business and economic landscape. Businesses adjust to a new reality.
Moderate	Additional fiscal stimulus will accelerate US growth. Fed likely to scale back asset purchases IVQ 2021.
HIGH	Biden's social compact: Financial lifelines for the economy during Covid-19, followed by higher taxes once recovery takes hold.
	FOREIGN
HIGH	China expands drilling in SCS and ratchets up tensions with both Taiwan and India.
Moderate	Pres. Biden orders larger US naval presence in SCS to defend the International Law of the Sea.
Moderate	President Biden raises sanctions against Russia for its cyber attacks and extrajudicial killings.
HIGH	China and Russia ramp up cyber attacks to undermine the US economic recovery and access biotech secrets.
HIGH	Middle East tensions surge. JCPOA 2.0 proves elusive as Iran enriches uranium toward 20% and blocks IAEA inspections.
Moderate	Vaccinations among emerging countries do not reach herd immunity until 1H 2022.
HIGH	Despite the BREXIT accord in late 2020, talks continue to clarify issues rushed through in final days.

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