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Getting Through the Fog

With COVID-19 vaccines on the way, 'the end is within sight' — but companies and supply chains could be navigating a fundamentally different economic terrain after the pandemic haze clears.

By Dan Zeiger

Throughout a presidency that ends this month and has been unlike any in American history, uncertainty has been a recurring theme on the economy and its potential impact on supply management organizations.

In January 2017, many executives and practitioners were still processing the election of Donald Trump as president, unsure of how the incoming administration would govern. Despite continuing economic expansion, the years that followed brought such X-factors as unprecedented trade turbulence and commodity prices volatility. Last year, many indicators suggested conditions were cooling, sparking fears of an imminent end to the longest period of economic growth in U.S. history.

A once-in-a-century global pandemic ended that 128-month expansion in March. Although many segments of the economy are recovering, the level of apprehension about what lies beyond the coronavirus (COVID-19) is as strong as the uncertainty of past years. The anxiety now is not so much about potential landmines, but what the economic and supply chain landscape will look like after the fog clears.

Joe Biden will be sworn in as president on January 20, bringing the usual questions regarding a transfer of power, as well as — with likely divided government in Washington — the size of COVID-19 relief stimulus. Vaccine distribution must be coordinated. Other landscape-changing dynamics include:

- The deglobalization of supply chains
- A new global trade environment
- Continuing geopolitical tensions
- More e-commerce expansion
- The further intertwining of sustainability and the economy.

“With the vaccines, we know an end is in sight,” says Robert A. Dye, Ph.D., chief economist at Comerica Bank in Dallas, who forecasts 3.9-percent growth in U.S. real gross domestic product (GDP) this year, compared to a 3.7-percent projected decrease for 2020. “With that, financial markets, as well as consumer and business confidence should improve. But there is some choppy water in front of us. It’s an idiosyncratic economy that is being pulled in many directions, and the coronavirus is just one dimension of that. It’s going to take a while before we feel like there’s one direction we’re all moving in at the same time.”

In its October *World Economic Outlook* report, the International Monetary Fund (IMF) projected 3.1-percent growth in the U.S. economy and a 5.2-percent expansion of global GDP. IMF chief economist Gita Gopinath, Ph.D., wrote in the *Outlook*'s foreword that nations' fiscal and regulatory responses "have so far prevented a recurrence of the financial catastrophe of 2008-09. While the global economy is coming back, the ascent will likely be long, uneven, and uncertain."

While the pandemic has been a global tragedy and the healing process will be arduous, it has not rocked foundations like the Great Recession did with banks and financial markets. That should make the recovery easier. However, **Bernard Baumohl, chief global economist at The Economic Outlook Group,** a Princeton, New Jersey-based firm, says that the business and economic worlds have been fundamentally changed by COVID-19.

"We're going to have to live with these changes and adjust to new marketplaces," says **Baumohl**, who projects 3.4-percent U.S. GDP growth in 2021. "That goes for the manufacturing and services sectors. … Once the vaccines are (distributed), economies will bounce back more quickly (than after 2008-09), but there will be scars and changes that will force companies and consumers to reorient their behavior."

Comparisons — and Lessons? — From 2008-09

In recent years featuring an unprecedented mixture of trade turmoil, geopolitical events, natural disasters and economic uncertainty, *Inside Supply Management*® routinely asked procurement professionals and economists if conditions were the worst they've experienced in their careers. The unanimous answer was that the Great Recession was worse.

That is, until the coronavirus pandemic.

The pandemic differs from previous economic crises, says Anthony Nieves, CPSM, C.P.M., A.P.P., CFPM, Chair of the Institute for Supply Management® Services Business Survey Committee, most policy prescriptions have limited efficacy until the virus is controlled.

"If you look at past recessions, coming out of them involved making market corrections," Nieves says. "We changed the way we did business. The tech bubble and the subprime-mortgage crisis were man-made things. Putting aside the conspiracy theories that are out there, this virus is a pathogen that remains incredibly contagious. A vaccine will be critical to getting GDP growth and other business levels back to where they were before the pandemic. But in terms of how this has impacted everyone's way of life, killed many businesses and put so many people in unemployment, this definitely exceeds the 2008 financial crisis."

Adds Dye: "There was significant economic and personal hardships from the events of 2008 and '09, but they didn't kill 285,000 people (the number of COVID-19 deaths in the U.S. in early December). This is a whole new ballgame."

A "financial vaccine," **Baumohl** says, is critical. A divided Washington — Biden, a Democrat, is in the White House and his party controls the House of Representatives, and the Republicans were likely to retain Senate control after the January 5 Georgia runoff elections — is generally considered an ideal scenario for business. Also, there's a blueprint for policy expectations under such a partisan split: From 2011-16, Biden was in the White House as vice president while Republicans controlled at least one house of Congress.

“Businesses do not like uncertainty; they need to be able to plan,” Dye says. “They need to have a good sense of the regulatory environment and other things related to policy. It’s the potentially least disruptive and most certain environment.”

A split Congress is “probably a good thing,” adds Timothy R. Fiore, CPSM, C.P.M., Chair of the Institute for Supply Management® Manufacturing Business Survey Committee. However, it likely limits the scope of a federal coronavirus relief package. In December, Congress was scrambling to pass US$900-million in aid as unemployment benefits and eviction moratoriums, among other protections, were set to expire at the end of the year. However, stimulus checks for Americans and assistance for state and local governments — considered critical by many economists — were sticking points in negotiations.

Another round of stimulus is especially vital to services businesses — especially in the accommodation and food services industry — that employ nearly 90 percent of Americans and have been hit hard by lockdowns and/or capacity restrictions due to public-health mandates, Nieves says. The Paycheck Protection Program (PPP) distributed $522 billion to 5.2 million businesses, helping with payroll and other expenses for up to 24 weeks. The program closed in August, and most businesses’ funding has dried up.

“So, there’s definitely a need for another round to keep that part of the economy open, and the sooner the better,” Nieves says. “It’s tough for a lot of those businesses, and even some major ones have closed. And they’ve been looking at (lawmakers) kicking the can down the road. You can only do that for so long, because for those businesses, it’s all about liquidity and cash flow, which keeps their people working and not laid off or on furlough.”

What **Baumohl** calls a “tale of two economies” in America has been exacerbated by the pandemic, and the insulation limiting the impact on businesses and supply chains continues to thin. “We are going to be stuck for some time with the problem of low-income households and minority communities that have suffered disproportionately from gaps in income and job security,” he says. “It’s a structural issue creating a tear in the fabric of society, and until it’s addressed, the economy might not achieve its full potential.”

A New Chapter on China and Global Trade

The push toward more regionalized supply chains hastened by the trade war was further intensified by COVID-19. While many companies won’t completely untether from China — which boasts the world’s biggest consumer economy, as well as its largest manufacturing workforce and most sophisticated supply chain infrastructure — Fiore says that those that are not dual sourcing should be.

Baumohl adds, “China’s days as a (dominant) manufacturing hub are probably gone soon.” He points out that technologies like artificial intelligence, robotics, 3-D printing and 5G wireless networks are becoming more affordable, which will help shorten supply chains and balance the cost of reshoring or nearshoring production.

The trade environment is expected to undergo a similar change, with Biden’s election expected to quell the unpredictability that defined the Trump era. However, a new president might be less belligerent in dealing with China, but just as stringent, Dye says. “I don’t think a Biden administration is going to give anything away with respect to China,” he says. “They’ll stay tough and do what they can to reduce intellectual-property theft and add as much of a level playing field as possible.”

Since the start of the trade war, the U.S. has slapped tariffs on virtually all Chinese imports, valued at $550 million. A Biden administration figures to relax duties on such allies as Canada, Mexico and the European Union but is expected to demand concessions from Beijing. “The tariffs on our Western and European allies should go away quickly to heal those wounds,” Fiore says. “But China is going to be drawn out. … We’ll deal with that (in part) by rejoining the international community, which I think is good for investment, for people and for trade.”

The U.S. is expected to forego the bilateral trade pacts preferred by Trump in favor of multilateral agreements, and some analysts believe continuing pressure from the U.S. is causing Beijing to be more pliable to opening its markets. China and 14 other Asia-Pacific countries signed the Regional Comprehensive Economic Partnership (RCEP) in November, leading to speculation of a revived Trans-Pacific Partnership (TPP) that could include Beijing. Trump withdrew the U.S. from the original TPP, which China was not part of, in January 2017.

“No one likes a trade war, but when the economy was strong, it was a good time to correct some things,” Nieves said. He feels that the U.S.-Mexico-Canada Agreement, which went into effect this year, is an improvement over the North American Free Trade Agreement (NAFTA). “In my experience, (NAFTA) went only one way,” he says. “With China, bettering those relations might not be the best solution, but lessening some of the (overall trade) tension might keep (the U.S.) from having to fight battles on too many fronts.”

Can a significant reduction in tariff turbulence translate into economic growth? Fiore believes so: “Eliminating tariffs across the globe could probably result in a bump of 0.5 percent in GDP,” he says. “That’s a positive bump. Growth of 1.8 percent is not a good year, but 2.3 percent would be. If you can get some of that by getting rid of the tariffs, that's some juice."

A Global Economy Going Green

In addition to trade deals, the Biden administration is expected to reenter another multilateral pact abandoned by its predecessor: the Paris Agreement on climate change, which has primary goals of reducing greenhouse-gas emissions and keeping global temperate rise below 2 degrees Celsius in this century. The futures of some industries and commodities suggest the global economy will be pulled in a greener direction.

The oil and gas industry might be one. According to the Organization of the Petroleum Exporting Countries (OPEC), worldwide oil demand fell to 9.8 million barrels a day in 2020, a 10-percent decrease, and the oil and gas industry "is not going to recover for a long time," Fiore says. Commercial aviation will likely not lead an oil-demand spike, as Boeing and Moody's Analytics project global air-passenger traffic will not return to pre-pandemic levels for another two to four years.

One county has made green-energy development a national imperative, investing more than $20 billion in wind, solar and other environmentally friendly sources with a goal of generating 60 gigawatts of renewable energy by the end of the decade. That country is Saudi Arabia, the world's biggest oil exporter.

"Saudi Arabia offers an indication of the future," **Baumohl** says. "Energy companies and the auto industry see the writing on the wall and recognize fossil-fuel demand is peaking, so they are going to be investing more capital in renewable energy sources. The world has come to recognize that the days of relying on hydrocarbons are coming to an end."

While the U.S. automotive industry has rebounded after the coronavirus temporarily shuttered plants in Michigan during the spring, electric and especially hybrid vehicles continue to increase their market presence. The United Kingdom, France and Norway are among the countries that have pledged to phase out combustion-engine vehicles by 2050, and in the U.S., California and New Jersey officials have called for banning sales of gasoline-powered cars in their states within 15 years.

Among the Biden administration's sustainability initiatives are a carbon-neutral (or net zero-emissions) U.S. economy by 2050. "Sustainability is not the future (of the economy) — it's today," Dye says.

Hitting 'All the Right Buttons'

In September, Federal Reserve chair Jerome Powell indicated that benchmark short-term interest rates would remain at zero at least through 2023. "That says the Fed doesn't think there will be a full recovery until then, and as I look around, I believe we won't get there any sooner than that," Nieves says.

Among other economic issues to watch in 2021:

The Fed: By keeping interest rates low, pouring money into long-term Treasury bonds and establishing such business-lending vehicles as the Main Street Program, there's little stimulative activity left for the Federal Reserve, **Baumohl** says: "It's hit all the right buttons and done everything it can possibly do. And that's been a lot."

Commodities: The commercial aviation slump limits aircraft production and has a domino effect on such industries as primary metals; fabricated metal products; and computer and electronic products, Fiore says. Meanwhile, copper prices were at their highest level in eight years at the end of 2020, and the manufacturing sector's post-lockdowns rebound has increased steel demand — which could accelerate further if the Biden administration's infrastructure proposals come to fruition.

"Usually, steel prices increase in January and February," Fiore says, "but we saw that in October and November. The homebuilding sector, which is a driver of steel, is doing well. If an infrastructure bill gets passed, the steel market will be pretty healthy."

Labor: Late in 2020, all three editions of the ISM® *Report On Business®* — the Manufacturing PMI®, Services PMI™ and Hospital PMI™ — indicated employment challenges, particularly in attracting returning workers, even to facilities with limited and distanced personnel due to public-health mandates. That impacts production levels and supplier deliveries, which, when coupled with the existing truck driver shortage and the e-commerce surge that shows no signs of slowing, are a continuing concern for companies.

"Until there's a vaccine that everyone is comfortable taking, people are going to keep working (remotely) or not at all," Fiore says.

On the campaign trail, one of Biden's stump lines was: "You can't fix the economy until you control the virus." Dye says that it can be difficult to convey optimism as COVID-19 deaths and hospitalizations continue to escalate, and he fears conditions could worsen for many Americans if additional stimulus and relief are hamstrung by political wrangling.

However, he adds: "When (the economy) gets to the other side of this pandemic, there will be low interest rates and likely a huge amount of pent-up demand. Consumer and business confidence remain at good levels. We still have a huge problem (with COVID-19) today. But when we get to the other side, there's a lot to be optimistic about."

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