



# ECONOMIC OVERVIEW MONTHLY

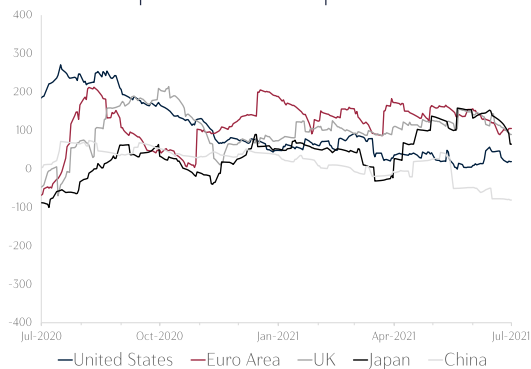
June 2021

- As the global economy emerges from the pandemic, it is experiencing an exceptional phase of accelerating economic growth.
- The US will lead growth in 2021, managing to close the pandemic-induced gap and return to pre-pandemic output and spending levels.
- The rising inflation observed in the US and, to a lesser extent, in Europe is driven by both supply-side bottlenecks as well as vigorous demand.

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- ❖ The world economy is now in a phase of exceptional and accelerating economic growth, led by the United States where the business cycle indicator puts the country in an overheating phase.
- ❖ The recovery remains asynchronous among major economies and it is influenced by the evolution of the pandemic, the vaccination campaign and fiscal policies in each country.
- ❖ Strong economic growth will require central banks to communicate properly, any potential paradigm shift, in order to preserve accommodative financial conditions necessary for keeping the actual recovery pace.

Fig. 1  
Growth Expectations - Surprise index



Source: Citi

Fig. 2  
OECD leading indicators

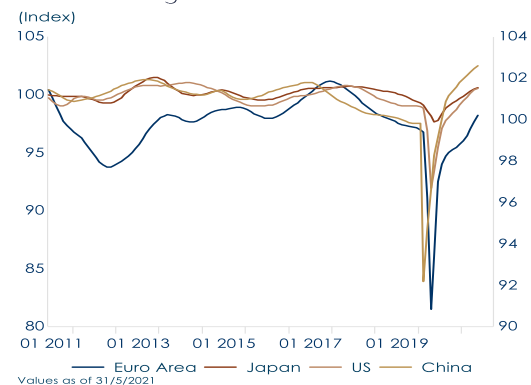
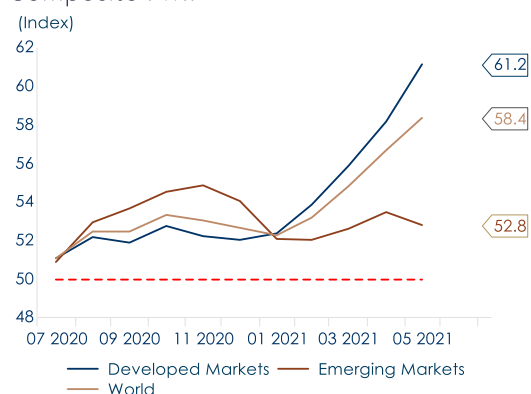


Fig. 3  
Composite PMI



## MACROECONOMIC BACKGROUND

**Global growth:** As the global economy emerges from the pandemic, it is experiencing an exceptional phase of accelerating economic growth. In the wake of the successful vaccination campaigns and the consequent lifting of the containment measures which restricted economic activity, Growth appears robust on both sides of the Atlantic, as well as in China and Asian countries connected through the supply chain. Despite the largely accommodating and coordinated monetary and fiscal policies implemented since the onset of the pandemic, the different rates and efficiency at which the vaccination campaigns are being rolled out are negatively affecting the synchronization of countries' economic cycles. China, which came out of the pandemic first, likely saw its growth peak already at the end of 2020 and will continue to grow at its potential of between 5% and 6% this year. The US will lead growth in 2021, managing to close the pandemic-induced gap and return to pre-pandemic levels. On the other hand, the Euro Area is lagging behind. After a weak first quarter due to the continuous closures, its economic recovery is taking hold in this second part of the year, bolstered by the international recovery and the rollout of Next Generation EU fund.

Inflation indicators in the flash PMIs for June reached new record highs and supplier delivery times lengthened still further. However, outside the US at least, there are few signs that goods shortages and higher costs have held back the recovery in manufacturing output. More generally, the PMIs suggest that lockdown easing continues to propel recoveries in the US and Europe, where restrictions have eased.

Manufacturing output indices stayed at high levels other than in Japan, where it fell below 50 for the first time since January, as the latest restrictions seemed to take their toll on production. However, since state of emergencies were lifted almost everywhere in Japan on Sunday, output should recover quickly from July onward.

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Fig. 4  
US PMI Indices

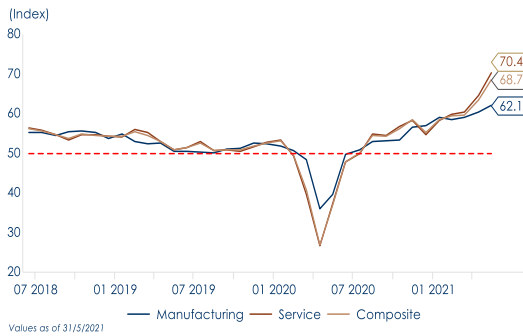


Fig. 5  
Euro Area PMI Indices

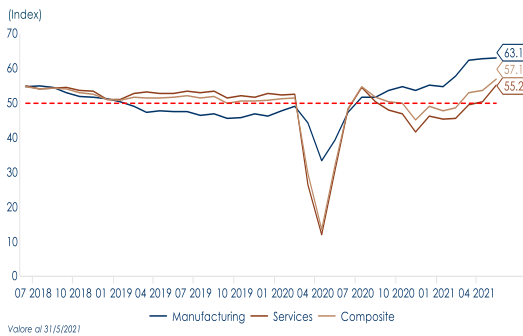
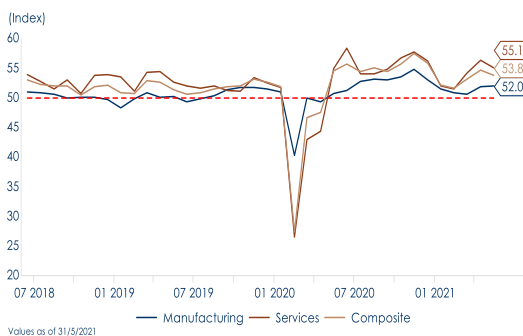


Fig. 6  
China PMI Indices



**United States:** The US will lead global growth in 2021. The business cycle indicator puts the country in an overheating phase. Economic activity will continue to gain strength in the coming months thanks to the Covid vaccines, while further fiscal stimulus will act as a reflationary bridge to support the more cyclical sectors of the economy. GDP growth for 2021 is expected to be the strongest in decades. However, the economy is suffering from pandemic-induced anomalies. The Beige Book prepared for the June FOMC meeting reiterates the presence of excess demand for goods and labour, bottlenecks in supply and a transfer of part of the inflationary pressure to prices.

**Euro Area:** Economic activity in the Euro Area was affected by the evolution of the pandemic and the slow vaccination programme, showing negative growth in the first quarter of the year, but should catch up with global growth from the second quarter onwards. Manufacturing remains strong in all countries in the Area. Surveys indicate a sustained recovery, while the increase in industrial production in April suggests that the sector continues to rebound. Supply disruptions seem like they will weigh on production for a while longer, limiting the industry's recovery, but business surveys indicate strong underlying demand. Business and consumer confidence is rising. This should be followed by a consumption-led rebound starting mid-year, as warmer weather allows for a gradual reopening. At its June meeting, the ECB revised its projections on the economic outlook for the Euro Area significantly upwards, but stated that it considered any change in monetary policy parameters and, in particular, a reduction in the purchases under the pandemic emergency purchase program (PEPP), premature and unnecessary. In the second part of 2021, the NGEU fund will provide further support by stimulating investment. However, the recovery continues. Fiscal support remains strong.

**China:** GDP growth jumped from 6.5% y/y in Q42020 to 18.3% y/y in Q12021, supported by a strong favorable base effect. The country's economy remains positive beyond the base effect. Industrial production rose 35% y/y in February and 14% y/y in March, exports and imports of goods in yuan grew 58.6% and 18.8% respectively in Q12021, while infrastructure investment rose 33% on average in February and March. Private consumption also rebounded, recording a positive contribution to GDP growth in Q12021 (11.6 pp of 18.3% y/y GDP growth), after a negative contribution in all four quarters of 2020. Soft data for April offers the same positive picture. The PPI is showing price pressure.

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Fig. 7  
The infection curve seems to be under control and steadily declining

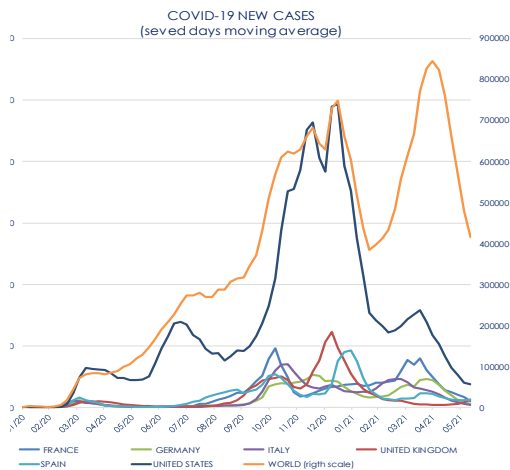


Fig. 8  
The vaccination campaign in the Euro Area is accelerating swiftly

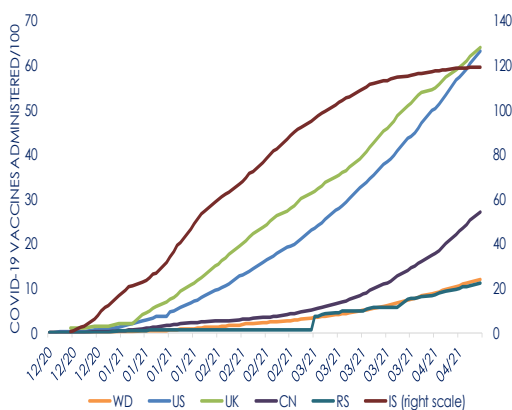
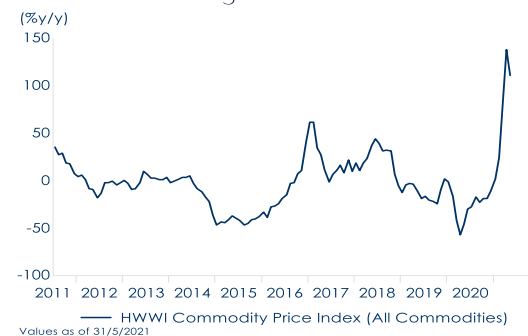


Fig. 9  
HWWI Commodity Price Index



## DISCUSSION POINTS

### Evolution of the pandemic

Global daily new infections have continued to decline, reaching their lowest level since early March at the start of June. Daily infections are now the lowest since the pandemic began in the US and euro-zone, although there has been a worrying uptick in the UK due to the new Delta variant. Most economies have seen an improvement, with the most dramatic change in India after its recent third wave. Infection rates are still high in parts of Latin America, South and Southeast Asia

### Economic recovery continues...

Almost all of the countries we analyzed are gaining momentum. The recovery remains asynchronous and is influenced by the evolution of the pandemic, the vaccination campaign and fiscal policies in the countries. That is why China, the United States and Europe are at different points in the business cycle. The Euro Area should accelerate in the second half of 2021.

### Will the rise in inflation be temporary? Will it be uniform between countries?

The rising inflation observed in the US and, to a lesser extent, in Europe is driven by both supply-side bottlenecks as well as vigorous demand. Rising commodity prices, difficulties in international trade and shortages of cargo in the face of imbalances between supply and demand have led to higher producer prices. This inflationary drive began to be felt in April in the prices of consumer goods. The key variable in understanding whether the rise in inflation will be transitory or not, remains the labour market, where there are wide differences between several countries.

### How soon will central banks prepare to normalize monetary policy?

Monetary policy will continue to be accommodating on a global scale. However, central banks of major developed countries are now grappling with a reshaping of their monetary policies, which are still largely expansionary. It is imperative for them to properly communicate the transition to the new phase without jeopardizing the ongoing economic recovery and triggering a sudden tightening of financial conditions.

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Fig. 10  
The recovery in global trade is ongoing and global trade in volume is accelerating (YoY volume increase and 3 months MA)  
(CPB World Trade Volumes y/y, %)

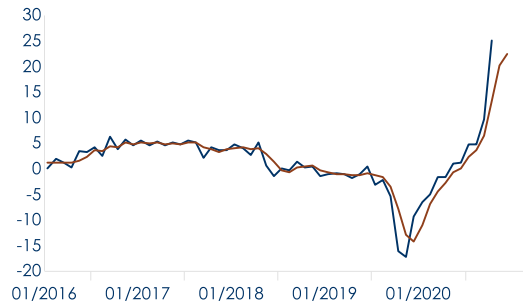


Fig. 11  
Dispersion among global economic activity clocks, China is leading...

**The aggregate figure masked the difference between Asia and the rest of the world**  
(CPB Real Goods Exports\* (Dec. 2019 = 100))

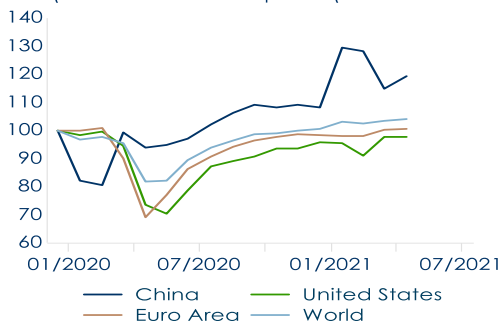


Fig. 12  
Global maritime transportation costs index (y/y, %)

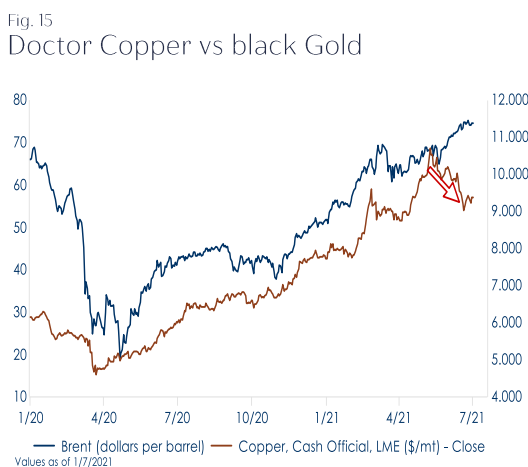
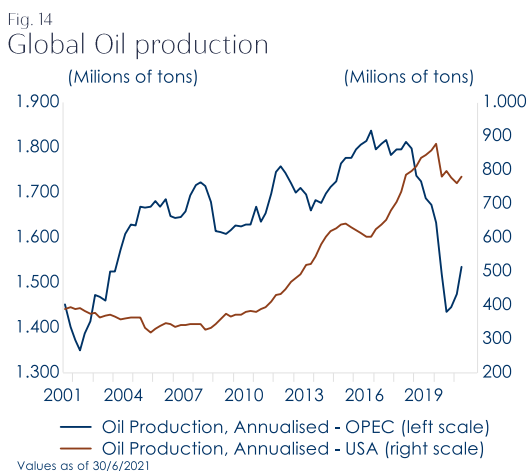
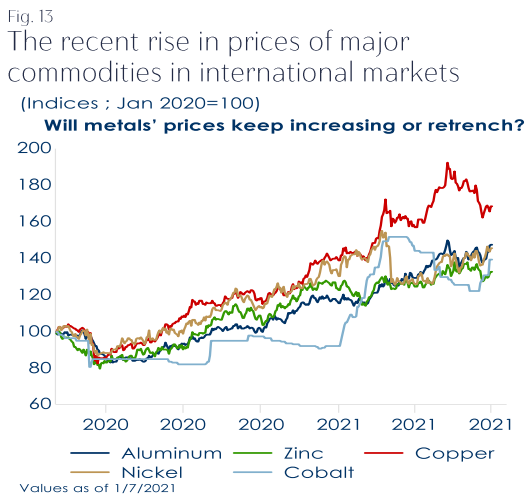


## FOCUS OF THE MONTH - 1/2 INTERNATIONAL TRADE

- ❖ The April's data revealed that world trade flows have enjoyed virtually uninterrupted growth for 12 months now, with world trade remaining well above its pre-virus level. However, between the quintupling of shipping costs over the past year, supply disruptions, and a potential cool down in the demand for traded goods as economies re-open, there is no shortage of impediments to a continued robust recover.
- ❖ According to data from the CPB Netherlands Bureau, after jumping by 2.3% m/m in March, real world goods trade rose by a further 0.5% in April. The annual growth rate leapt from 9.9% to 25.3%, although this was primarily due to the very weak base for comparison a year ago when trade flows collapsed during the early stages of the pandemic. Base effects will continue to render annual growth rates meaningless in the months ahead. Nonetheless, looking through the technical base effect, real world goods trade was still about 6% higher than its level in December 2019.
- ❖ Since April, a further rise in port congestion and an accompanying surge in container shipping costs suggests that shipping traffic has remained resilient in recent weeks. Having been fairly flat in the two years prior to the pandemic, global sea freight rates for container shipping are now 4.5 times their level from the start of 2020, with even bigger increases for shipping routes from Asia to Europe. The latest rise in costs coincided with congestion at global ports and anchorages returning to its 2020 peak with Chinese ports, in particular, seemingly struggling to keep up with demand.

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## FOCUS OF THE MONTH - 2/2 PRICE OF INDUSTRIAL METALS



The pandemic, by causing supply-side bottlenecks, has accelerated the recent rise in prices of major commodities in international markets. The rise is also the result of greater demand for key materials for the manufacture of products related to the major technological transformations underway, starting with the digital and energy sectors. Four factors have driven the increase in the price of industrial metals:

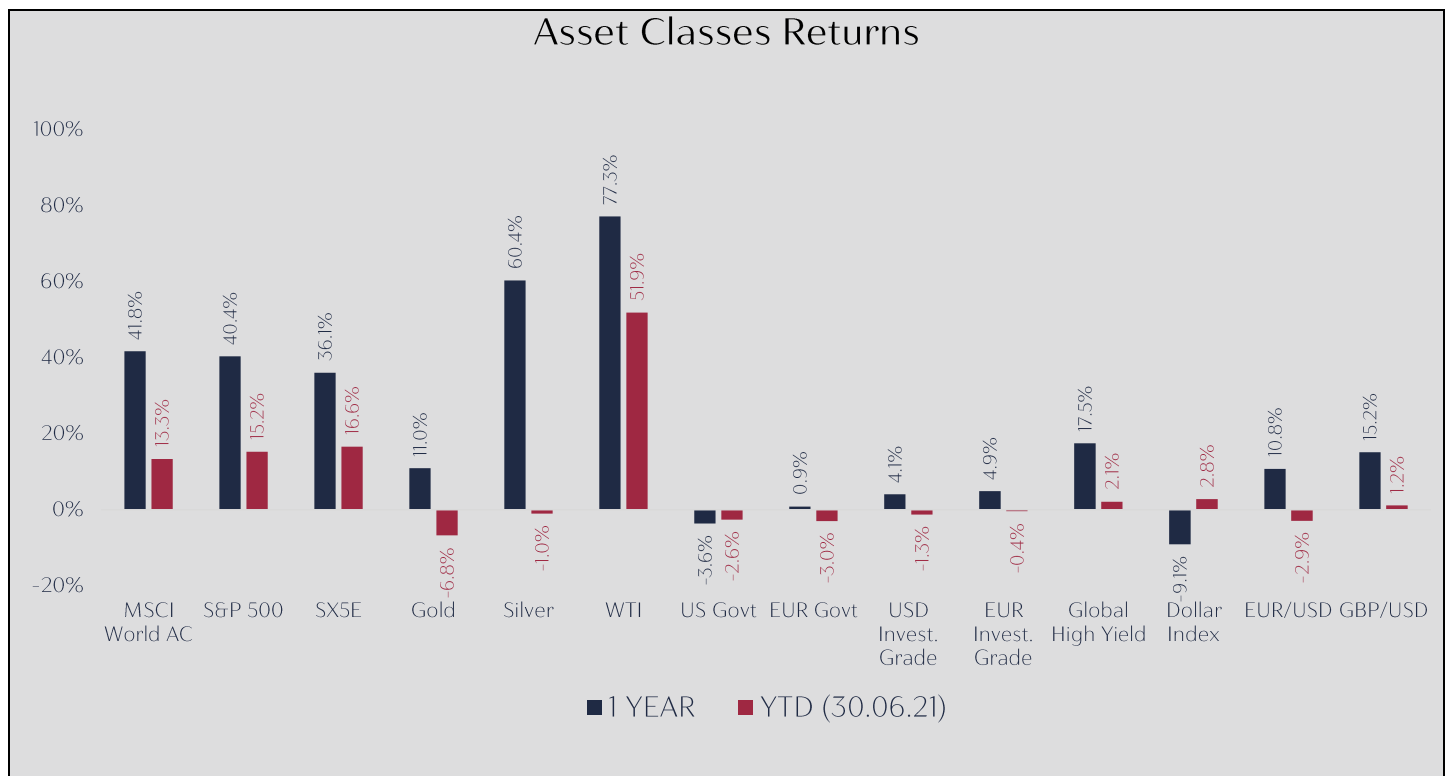
- ❖ **An economic recovery based on the manufacturing sector:** Manufacturing was able to adapt to the pandemic and recovered faster than services, especially in China, which is the largest user of metals.
- ❖ **Supply-side factors:** Many mining operations have been temporarily disrupted by Covid-19, while the cost of freight rates for the transport of materials has reached a 10-year high due to congestion at key ports, quarantine restrictions, continued shipping staffing issues and a rebound in fuel prices from the deep troughs of spring 2020. All this has increased the cost of metals.
- ❖ **Expectations for faster energy transition and infrastructure spending:** Positive expectations about the pace of the transition to a greener economy and ambitious infrastructure programs gave metals prices a further boost. Both would increase the global economy's "metal intensity". For example, a rapid energy transition could require a 40-fold increase in the consumption of lithium for electric cars and renewable energy, while the consumption of graphite, cobalt and nickel for these purposes could increase by about 20-25 times, according to the International Energy Agency. Ambitious infrastructure programs in the European Union and the United States would increase demand for copper, iron ore and other industrial metals.
- ❖ **Metal storage:** Metals are easier to store than oil or some agricultural commodities. This makes their price more forward looking and, therefore, more sensitive to changes in interest rates and market expectations.

Now, futures markets are suggesting a 50% increase in industrial metals prices in 2021 (year-over-year), but a 4% decline in 2022, showing that we might be close to the peak. However, prices are expected to remain high and could rise further, especially if demand for the energy transition accelerates. On the other hand, prices could fall more than expected if legislative approval and government actions required for energy transition and infrastructure programs do not materialize as expected.

# ECONOMIC OVERVIEW MONTHLY

## MARKET UPDATE

As the global economy emerges from the pandemic, it is experiencing an exceptional phase of accelerating growth. Following successful vaccination campaigns, growth appears robust on both sides of the Atlantic, as well as in China and Asian countries connected to it through the supply chain. Despite broadly accommodative and coordinated monetary and fiscal policies since the start of the pandemic and the different rates at which the vaccination campaigns are being rolled out are causing the cycles in the various countries to be somewhat less synchronous. China, which came out of the pandemic first, likely already, saw its growth peak at the end of 2020 and the US will drive growth in 2021. While the Euro Area is lagging behind major economies, after having posted a weak first quarter, and is seeing an upswing in the economic recovery in this second part of the year, bolstered by the international recovery and the rollout of Next Generation EU. Over the coming months, we expect reflation to materialize in the outperformance of equity markets and the more cyclical sectors (Europe, Japan, EM; Financials, Energy, respectively), and of the Value versus Growth style. The dollar is set to weaken in this initial phase, weighed down by the public deficit, reduced private savings and increased (deficit) investment, which will produce a marked deterioration in external balances.



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## RISKS OF SCENARIO

	Main Risks	Risk Evaluation		
		Impact	Probability	Development
ECONOMIC	<b>World:</b> The pandemic will continue to be the main obstacle to economic recovery. An uncontrolled spread of infection in some emerging countries could postpone the end of the global health crisis.	HIGH	HIGH	↓
	<b>World:</b> US-China relations are likely to remain tense, although the Biden election could lead to a multilateralism return.	HIGH	MEDIUM	=
	<b>World:</b> After the increase in inflation due to base effects and supply-demand imbalances produced by the pandemic, an inflationary spiral could be triggered on the back of a structural change in the Phillips, influenced both by the new tax regime of the Biden administration and by an reshoring phenomena intensification after the Covid interrupted long stretches of "low cost" supply from East to West.	MEDIUM	MEDIUM	↑
	<b>United States:</b> Covid-19 has deeply affected the U.S. labor market and consequently the consumption component, which could remain depressed for a long time if faced with an increase in precautionary savings in the presence of persistent uncertainty about the evolution of the epidemic.	HIGH	MEDIUM	↓
	<b>United States:</b> Government bond yield curve steepening.	HIGH	MEDIUM	↑
	<b>United States:</b> Fed exit too early on easy monetary policy in the event of a sudden rise in inflation.	HIGH	LOW	↑
	<b>Eurozone:</b> Eurozone countries economic asymmetry is increasing. The COVID-19 has asymmetrically affected the Eurozone countries, which have been able to implement different fiscal measures and, above all, will have to face different financing conditions on the markets.	HIGH	MEDIUM	↑
	<b>Euro Area:</b> Euro Area Inflation remained in negative territory. The area risks slipping into deflation.	HIGH	HIGH	=
POLICY	<b>Emerging countries:</b> The main scenario risk is that of a sudden slowdown in capital flows to emerging economies, which amplifies their degree of vulnerability and brakes their growth.	HIGH	LOW	↓
	<b>Euro Area:</b> Credit standard tightening on the back of phasing-out of state guarantees.	HIGH	LOW	=
POLITICAL	<b>Euro Area:</b> There is a risk of execution of the Next Generation EU tax plan.	HIGH	MEDIUM	↓
	<b>World:</b> There is a progressive loosening of global cooperation.	HIGH	HIGH	=
	<b>World:</b> Geopolitical issues (e.g. Hong Kong, Latin America...) continue to present many unresolved elements. The results could spark a new screwiness in the world economy and weigh on the recovery.	MEDIUM	MEDIUM	=



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## POSITIONING

In this scenario:

- ∨ we are taking a **negative view** of core European government bonds. We remain neutral on US government bonds. Emerging market debt scores favourably on the source of higher carry;
- ∨ the **corporate bond market** is not yet offering attractive valuations, although the support provided by the purchases of central banks, especially the IG component, remains significant;
- ∨ we are maintaining our **positive view of equities**. Even after the recent recovery, we see forecast 12-month returns on equities as more attractive than those in the fixed income space, in line with an economic cycle that, according to our base scenario, will rebound with the support of policy makers, returning confidence and increased capex. We continue to favor emerging market equities and the Chinese stock market in particular, assuming the country's higher relative growth. The Euro Area stands to benefit from the change of pace in fiscal policy, while Italy should benefit from the authority, stability and competence of Prime Minister Draghi.

	NEGATIVE	NEUTRAL	POSITIVE
<b>FIXED INCOME</b>		●	
Sovereign EUR	●		
Sovereign USD		●	
Corporate IG		●	
High Yield		●	
Emerging Market Sovereign		●	
<b>EQUITY</b>			●
USA		●	
EMU			●
JAPAN			●
Emerging Market			●

Source: CMB Monaco, Mediobanca SGR

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