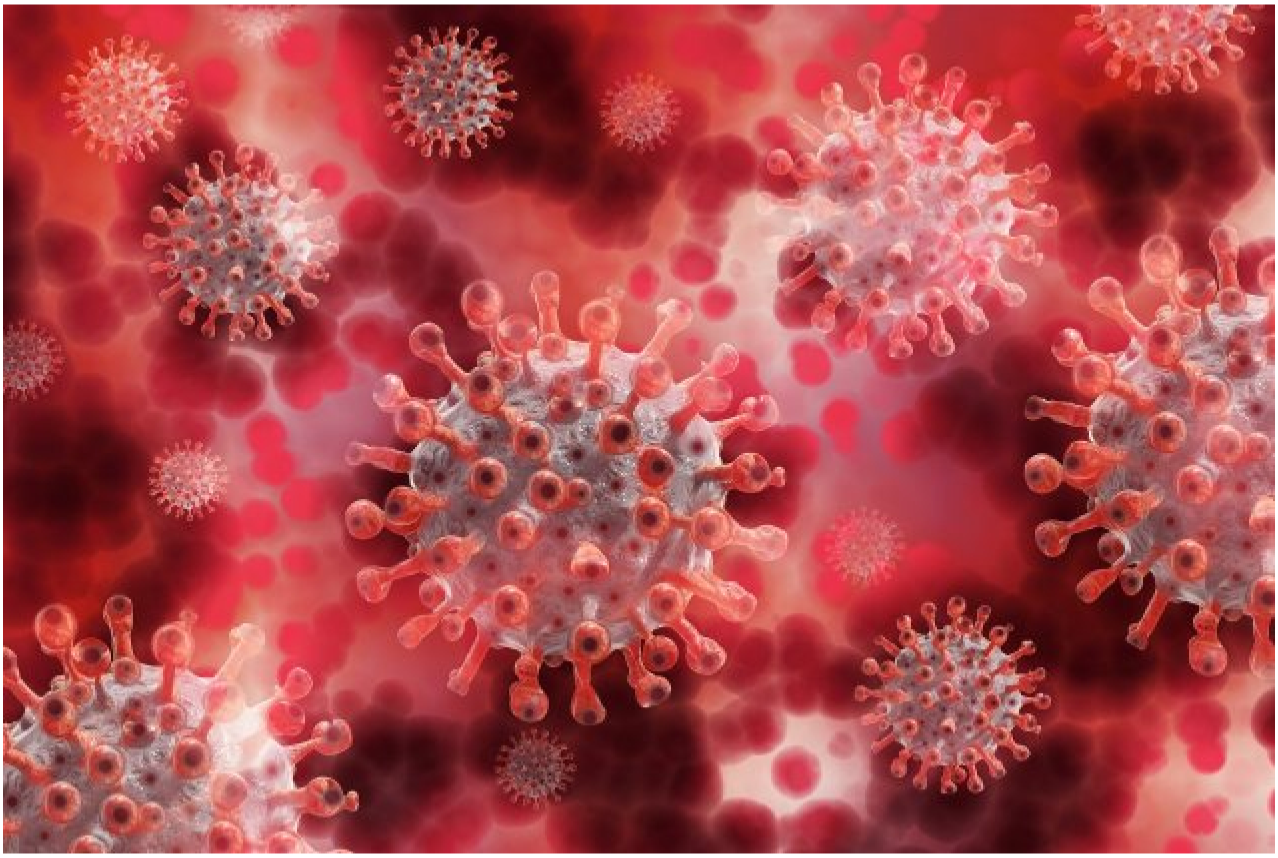
Q2 GDP fell off a cliff. Yet months of shocking headlines has made record declines feel somewhat “normal”. They’re not. What is creating a stir is the rising number of hotspots locally as well as globally. The battle with the virus is going to be long, drawn out, and fraught with unpalatable trade-offs, especially between lives and livelihood.



Cash pile. Whether through lack of opportunity or a conscious choice, UK households and non-financial firms continue to build deposits. Net deposits rose by £18bn in June, down from May’s mammoth £53bn. Since March, banks have boosted net deposits worth £175bn. Firms continue to borrow though the lockdown. Larger ones are opting to borrow via financial markets (£10.6bn) and repay banks (£16.7bn). SMEs rely on bank funding, borrowing £10.2bn in June, an annual growth rate of 17.4%. Much of this is survival. But we need to ensure that borrowing now leaves room for investment-led lending later.

Rainy day fund. What did you do earlier this summer? Well UK households spent June saving. Our collective deposits jumped by £11.6bn – more than twice the monthly average pre-Covid – and are 7.5% higher than a year ago. With normal life on pause, many were simply unable to spend as much as usual: outstanding credit card balances fell for the fourth straight month. Others, no doubt, were motivated to save more by the threat of redundancy later in the year. Not everyone is as cautious though: 40,000 had mortgages approved, compared to just 9,300 in May. If the outlook does improve then households will certainly have plenty in the bank.

Furlough for longer. Restrictions lifting on most consumer-services businesses ignited hopes of many employees restarting work. But the proportion of UK workers still on the Job Retention Scheme fell only to 25% in the first half of July (29% in June-end) and just 7% of all firms were still not actively trading. It surely takes longer than a week to restart fully. Worryingly however, accommodation & food services and entertainment & recreation sectors furloughed half of their workers in early July. Firms will find it harder to retain employees if things don't pick up soon as, starting August, they need to start paying insurance and pensions contributions.

Painfully weak. Eurozone GDP fell 12% in Q2, in line with market expectations. While details of the expenditure side are not available, split by member-states point towards weak consumption spending and anaemic business investments as the main culprits. Different sectoral mixes across the countries results in uneven impacts. Germany for instance escaped with a less severe fall of 10%, while the southern economies took a bigger hit due to greater reliance on tourism. Given the sizeable initial damage alongside resurgence of virus spread, the road to recovery is going to be rather long.

Sticky. The eurozone unemployment rate for June rose only marginally to 7.8%. Although the labour market was artificially supported by government schemes during lockdown it's still good news. Households with incomes relatively unscathed can help drive a quicker recovery. The figures reveal the issues with how unemployment is measured though; it only considers those looking for jobs and many weren’t doing so during lockdown! More importantly, expect a steady rise in unemployment over the coming months as firms shed jobs due to the post-lockdown economic weakness.

Nadir. The US economy shrank at an annualised rate of 32.9% in Q2, recording the largest contraction since the post-war era. The fall was mainly driven by a 35% plunge in consumption, as the lockdown prevented households from spending especially on high personal contact services, such as health care, recreation and eating out. But on the bright side, real disposable income surged by 50%, underpinning the importance of the fiscal support. Looking ahead, Q3 is likely to experience a rebound in economic activity thanks to favourable base effect as well as partial return to the ‘new normal’.

Sobering. The Federal Reserve held steady in its July meeting. That said, the Fed Chairman, Jay Powell was downbeat about growth outlook, in contrast to the bullish mood on Wall Street. He reiterated that the path to recovery would “depend significantly on the future course of the virus” as well as fiscal policy support. Republicans and Democrats are at odds over the details of the next fiscal stimulus, which is crucial to supporting activity. The recent temporary rise in unemployment benefits ceased at the end of July, removing a key support for households’ incomes and consumer spending.

Strength to strength. China’s official composite PMI edged down only marginally to 54.1 in July from its two-year high seen last month. Overall, it reflects a continuation of the strong recovery that set in Q2. The breakdown by sectors reveals that both manufacturing and non-manufacturing PMIs did well. Construction has been a key beneficiary of the ramp up in government’s infrastructure spending, a key pillar of the over stimulus delivered so far. What’s even better is the upbeat performance of the labour market sub-index which will support future consumer spending.

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