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## Article

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# Global economy: USA and China leading the way, Europe lagging behind

By Claus Michelsen, Guido Baldi, Paul Berenberg-Gossler, Geraldine Dany-Knedlik, and Hella Engerer

## ABSTRACT

The resurgence of the pandemic and renewed lockdowns have slowed the recovery of the global economy, but the overall losses will be less severe than after the first coronavirus wave in spring 2020. Industry in particular continues to develop well. In contrast, retail trade and personal services have been heavily affected, especially in hard-hit regions such as Europe. However, the fiscal stimulus cushions much of the distortions. With increasing levels of immunity, most economic restrictions will be lifted beginning in the second half of 2021, which should boost private consumption. Due to strong growth in the US and China, DIW Berlin is increasing its forecast by 0.4 percentage points for both 2021 and 2022 and expects growth of 6.7 and 4.8 percent for each year, respectively. Global production should first be able to reach its long-term growth path by the end of 2022. Although the Brexit Deal and the end of Donald Trump's presidency have eased some global uncertainties, risks still remain, especially from new waves of coronavirus infections and sharp increases in insolvencies.

A second wave of the coronavirus pandemic has been thwarting economic recovery since the fourth quarter of 2020. After recovering strongly in the third quarter of 2020 by 7.9 percent compared to the second quarter, the global economy only grew by 1.8 percent in the fourth quarter (Figure 1).

Stricter lockdown measures in Europe and North America have led to economic setbacks. Production in the euro area shrank by 0.7 percent in the fourth quarter of 2020, and with growth of only around one percent, recovery slowed down in the United Kingdom and the US. In light of low infection rates, economies in Asia—led by China—continued to recover strongly at the end of 2020. However, at the end of 2020, the economic performance of most countries was just below or already at the pre-crisis level. Nevertheless, production growth has to increase by a third until the long-term growth path is reached again.

In Europe and North America, the pandemic will continue to dampen the global recovery process despite increased levels of immunity. Following a continuous decline of new coronavirus cases at the beginning of 2021, cases have been increasing in many European countries since the end of February 2021. A third wave and a return of stricter lockdown measures in this region is likely over the first half of 2021. In the US, too, the number of new cases is not currently declining; rather, it is remaining at a constant, but still high, level. In addition, the spread of virus mutations is causing an increase in case numbers in other regions, especially South America.

In many countries, vaccination programs have already begun but are off to a slow start, mainly due to vaccine shortages. Therefore, effective herd immunity will not be reached in major economies before the end of the first half of 2021. Until then, the pandemic and the lockdown measures will continue to negatively impact retail and personal services. Initially, this will dampen the global economic upswing.

Nevertheless, economic losses due to the current wave of coronavirus are likely to be markedly lower than in spring 2020. On the one hand, current heavy caseloads have been concentrated in two regions, North America and Europe. On

the other, industrial value added in these regions is markedly increasing and appears to barely be affected by the pandemic. Correspondingly, corporate investment and trade in industrial goods are also developing solidly in many places; in particular, the continuing upswing in Asian countries is likely to further support industrial production, especially in the manufacturing sector, and strengthen international trade.

With adequate immunity, the upturn in the major economies is likely to pick up significant speed by summer 2021. However, this forecast assumes that the current economic restrictions to control the coronavirus will only be marginally reduced by summer 2021. With sufficient immunity, the infection prevention and control measures can begin to be gradually reduced in the second half of 2021, so that by the end of the year only a few legal requirements and voluntary behavioral changes will affect the economy. In 2022, restrictions will be limited to a few sectoral and regional measures in most countries.

Additional fiscal stimuli as well as a very accommodating monetary policy are likely to support the recovery over the coming years. Many governments passed further fiscal aid packages. For example, since December 2020, the US government has passed two relief packages totaling around 2.8 trillion USD, which is around 13 percent of the US's 2020 GDP. These relief packages will significantly strengthen the US's growth prospects. Some European countries also topped up existing stimulus packages, albeit to a lesser extent than the US. Additional direct fiscal measures should partially offset current corporate and household income losses and thus prevent longer-term distortions.

Many stimulus packages that have been passed also contain investment-enhancing funds to boost the recovery process over the coming years. In Japan, for example, half of the stimulus packages passed—around three percent of Japanese GDP—is earmarked for investments in digitalization and decarbonization. Much of the EU's recovery fund (NextGenerationEU), which accounts for about six percent of the EU's economic output, is also geared toward promoting corporate investment. In addition to fiscal policy, the further favorable financing conditions and a robust development of industrial production will support corporate investments in many places.

In contrast, private consumption will remain dampened initially. This is in part due to high infection rates in economically important regions, but also due to household income losses and their continuing uncertainty about future economic development. This is reflected in the high savings rates in many places. The loosening of economic restrictions in regions currently hit hard by the coronavirus should significantly boost household consumption, as some consumption is likely to catch up. Sufficient immunity and less fear of new waves should give private consumption additional momentum and decrease the savings rate.

The labor market is likely to only recover sluggishly in many places. By the end of 2020, only about half of the employment



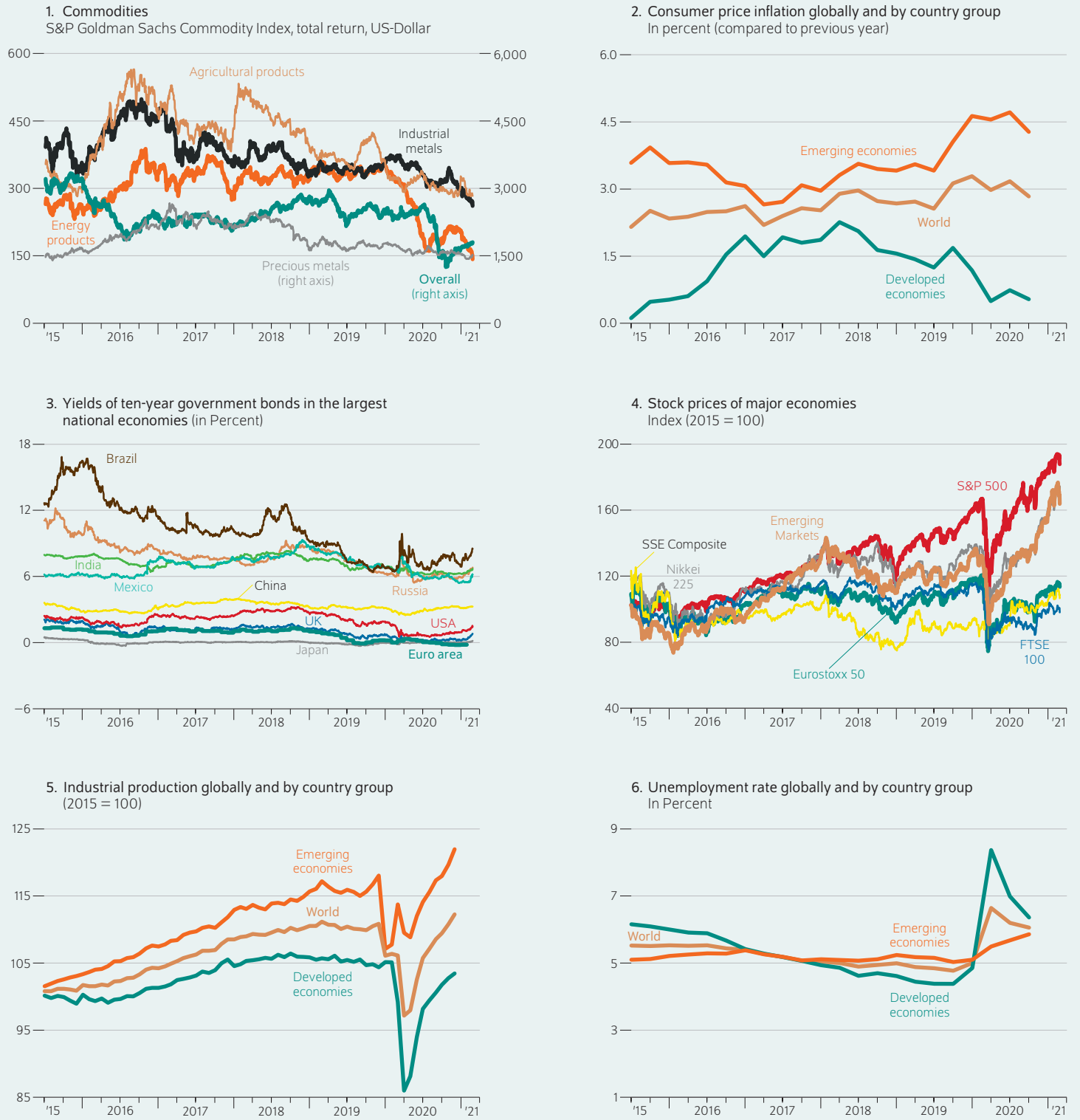
losses from the spring of 2020 had been made up in most countries. The unemployment rate in advanced economies continues to sink, but most are still significantly above the pre-crisis level (Figure 2). If emergency aid for businesses, such as short-time work allowance, is ended at short-notice, unemployment will be expected to rise again. The gradual recovery on the labor markets is also likely to weigh on wage developments in many economies. Thus, consumer price inflation in most economic areas should only moderately increase despite recent increases in energy prices.

In 2020, the coronavirus pandemic caused the global economy to shrink by around 2.7 percent. Due to a strong recovery in Asia, especially of the Chinese economy, the overall decline is around 0.7 percentage points less than DIW Berlin previously expected (Table). An increase in the new infection rate in Europe and the US slowed further recovery, but the upturn will likely continue with strong growth rates in the second half of 2021. Thus, global production will likely only be able to reach its long-term growth path by the end of the forecast period. Due to the unexpected and powerful upswing in China and the improved growth outlook for the US, DIW Berlin is increasing its forecast by 0.4 percentage points for both 2021 and 2022. Thus, DIW Berlin expects growth rates of 6.7 percent for 2021 and 4.8 percent for 2022.

Downward uncertainties have been eased somewhat by the trade agreement concluded between the EU and the UK and Joe Biden's inauguration as US President in January 2021. However, the forecast overall remains tainted with predominantly negative risks, especially due to the continuing uncertainties about the course of the pandemic, new virus mutations, and the effectiveness of available vaccines.

Figure 2

Global economic indicators



Note: Last observations on February 26, 2021 (parts 1,3, and 4), third quarter of 2020 (parts 2 and 6) and December 2020 (part 5).

Sources: National statistical offices; IMF; Macrobond; Eurostat; CPB World Trade Monitor, S&P Dow Jones Indices, STOXX, Nikkei Inc.; Shanghai Stock Exchange, FTSE; authors' own calculations.

Table

**Real GDP, consumer prices, and unemployment rate in the global economy**  
In percent

	GDP				Consumer prices				Unemployment rate in percent			
	Change over previous year in percent											
	2019	2020	2021	2022	2019	2020	2021	2022	2019	2020	2021	2022
Euro area	1.3	-6.8	3.4	4.2	1.3	0.1	1.6	1.2	7.5	8.1	9.2	8.1
without Germany	1.6	-7.5	3.6	4.4	1.2	-0.1	1.3	1.1	9.5	9.8	11.4	10.1
France	1.5	-8.3	4.4	4.4	1.1	0.5	1.2	1.1	8.5	8.2	9.8	8.5
Italy	0.3	-8.9	3.0	3.9	0.7	-0.2	1.0	0.9	9.9	8.9	10.3	9.7
Spain	2.0	-11.0	5.1	5.8	0.7	-0.3	1.0	1.1	14.0	16.2	18.6	16.0
Netherlands	1.6	-3.8	2.2	3.0	2.6	1.1	1.6	1.6	3.4	3.8	5.7	5.3
United Kingdom	1.4	-9.9	4.7	6.5	1.7	1.0	1.8	2.4	3.8	4.5	6.5	6.1
USA	2.2	-3.5	6.7	3.5	1.9	1.2	2.6	2.1	3.6	7.5	5.3	4.0
Japan	0.3	-4.9	2.9	1.8	0.5	-0.1	-0.3	0.9	2.4	2.8	3.0	2.6
South Korea	2.0	-0.9	3.3	3.1	0.4	0.5	1.2	1.4	3.8	4.0	4.1	3.7
East-Central Europe	4.1	-3.7	4.0	4.7	2.7	3.1	3.3	3.1	3.3	3.7	4.2	3.7
Turkey	1.0	1.6	4.9	3.0	15.2	12.3	13.1	11.0	13.7	14.0	14.3	13.3
Russia	1.3	-3.1	2.9	2.9	4.5	3.4	4.3	4.1	4.6	5.8	5.6	4.9
China	6.2	2.5	8.9	5.8	2.4	3.4	2.1	3.0	4.1	4.1	4.1	4.1
India	4.7	-8.2	8.9	7.4	3.7	6.6	3.8	3.6				
Brazil	1.4	-5.0	3.0	2.0	3.8	3.3	4.7	3.5	11.9	13.8	14.1	13.3
Mexico	0.0	-8.7	3.5	2.0	3.4	3.4	3.6	3.2	3.5	4.6	5.9	4.5
Developed economies	1.7	-4.8	5.1	3.7	1.5	0.7	1.9	1.7	4.5	6.6	6.0	5.0
Emerging economies	4.6	-1.5	7.6	5.5	3.6	4.5	3.6	3.8	5.2	5.5	5.7	5.4
World	3.5	-2.7	6.7	4.8	2.8	3.1	2.9	3.0	4.9	6.0	5.8	5.2

Sources: National statistical offices; DIW Berlin Economic Outlook Spring 2021.

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Despite lockdown measures and vaccination campaigns, further uncontrolled increases in regional and global infection rates could occur, especially if virus mutations spread rapidly. This, in turn, would make stricter lockdown measures necessary and would likely further delay an economic upswing. Additionally, slow vaccine rollouts could dampen the hope of a relatively quick end to the pandemic and weaken public trust. Another risk is that corporate and personal

insolvencies will rise sharply, in particular as a result of the continuing (partial) lockdowns. This could lead to significant loan defaults and, as a result, destabilize the financial markets, which could also jeopardize the solvency of a number of countries. Global recovery, on the other hand, would be strengthened by faster vaccine distribution and more effective treatments for COVID-19.

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