ECB Signals More Stimulus Coming in December; Second Lockdowns across Europe as Second Wave Worsens

**EUROZONE:** The European Central Bank’s Governing Council signaled at their October 29 decision that they will increase monetary stimulus at the next scheduled meeting on December 10, or before if necessary. Their monetary policy statement reads that “the Governing Council will recalibrate its instruments” at the December decision. President Lagarde implied at the October press conference that this “recalibration” would likely include an increase in asset purchases (a.k.a. QE) made through the Pandemic Emergency Purchase Programme and an extension of the program’s end date; the ECB currently commits to keep the program active at least until June 2021. President Lagarde also said the ECB could adjust other monetary policy instruments, including the types of assets their QE programs buy, or make further cuts to benchmark interest rates. The ECB is expecting to ease primarily in reaction to the pandemic, which is worsening across the Eurozone and European Union. New coronavirus cases in the E.U. continued to record new record highs in the last week of October. In response, Germany will impose a lockdown beginning November 2, France began a four-week lockdown on October 30, Italy ordered closed congregate businesses beginning October 26, and Spain imposed a curfew October 25. These lockdowns are so far more targeted than those of the spring, but will nevertheless weigh on the recovery in the fourth quarter of 2020.

**UNITED KINGDOM:** The United Kingdom also will re-enter national lockdown, beginning November 5. Congregate businesses will close, including non-essential retailers and dine-in restaurants; however, unlike the initial lockdown, daycares and schools will remain open. Financial markets price in roughly two in five odds of the Bank of England cutting the bank rate to a negative level by the third quarter of 2021. Bloomberg reports that the U.K. and E.U. are nearing a deal on post-Brexit trade relations, which could be finished by mid-November.

**UNITED STATES:** U.S. real GDP partially recovered to 3.5 percent below its pre-downturn level in the advance or first estimate for the third quarter of 2020; its peak was in the fourth quarter of 2019. In the seasonally-adjusted and annualized quarterly terms typically used to report real GDP, it rose 33 percent after a 31 percent fall in the second quarter; those are the largest respective increases and declines on record. To put the third quarter’s partial recovery in context, a recession in which real GDP declines a cumulative 3.5 percent would still be the third worst recession since the end of the Second World War. The economy’s recovery in the third quarter was led by consumer spending, with very strong growth of spending on durable goods, which was higher in the third quarter than before the crisis struck; by contrast, consumer spending on services also rose in the third quarter but was well below its pre-crisis level—consumers spend roughly twice as much on services as goods in the U.S. Residential fixed investment jumped, and business spending on equipment rose, while investment in structures remained depressed. Trade was a net drag in the third quarter as imports grew faster than exports, reflecting American businesses adding to inventories to insure against supply chain disruptions in the winter months.

Personal income and expenditures both continued to recover in September in data released after the first estimate of third quarter GDP. Personal income rose 0.9 percent on the month, and was 3.6 percent higher than its level in February; personal income spiked Sharply in April as tax credits and unemployment insurance payments temporarily boosted incomes, the fell through August as transfer payments slowed. Personal income excluding transfers plunged 9.1 percent from February to April, and was still 1.6 percent below its February
level in September. Personal consumption expenditures rose 1.4 percent in the month, with spending on durable goods up 3.0 percent, spending on nondurable goods up 1.5 percent, and spending on services up 1.1 percent. Consumer spending was still 2 percent below its February level in September; spending on services was down 6.3 percent, while spending on goods was 7.7 percent higher. New single family home sales dipped 3.5 percent in September; while September was down from July and August, the last three months were the three strongest since 2006.

Weekly activity indicators continued to improve in the week ended October 24. Initial claims for state unemployment insurance fell 4 percent on the week to 732,000 before seasonal adjustment or 751,000 after seasonal adjustment; initial claims for Pandemic Unemployment Assistance rose 4 percent to 360,000. Continuing claims fell 8 percent on the week ended October 17 to 7.422 million before seasonal adjustment or 7.756 after seasonal adjustment. The number of claimants for all UI programs fell 2 percent in the week ended October 10, and the prior week’s level was revised down slightly. The Federal Reserve Bank of New York’s Weekly Economic Index improved again in the week ended October 24 with a 3.3 percent year-over-year decline in the second estimate, following a 4.0 percent decline in the prior week. PNC forecasts that the November 6 release of the October Bureau of Labor Statistics jobs report will show 900,000 nonfarm payroll jobs added from September with the unemployment rate down to 7.5 percent from 7.9 percent.

These data are encouraging signs that the economic recovery continued in the beginning of the fourth quarter. At the same time, the uptrend in new coronavirus cases, hospitalizations, and deaths in recent weeks increases the risk that the U.S. like Europe could enter a second lockdown in the winter.

CHINA: The CFLP manufacturing PMI edged down to 51.4 in October from 51.5 in September, while the nonmanufacturing PMI rose to 56.2 and was the strongest since 2013; the Caixin general manufacturing PMI for China rose to 53.6 from 53.0 and was the strongest since 2011.

JAPAN: As expected, the Bank of Japan held its monetary stance unchanged at its October 28 monetary policy decision. The negative short-term policy rate is set at -0.1 percent, the target for the ten-year government bond remains “around zero percent” (a target range of -0.2 percent to 0.2 percent), and purchases of exchange-traded funds, real estate investment trusts, commercial paper, and corporate bonds will continue at their prior rates. The BoJ’s Policy Board members downgraded their forecasts for real GDP growth in the 2020 fiscal year (April 2020 to March 2021), with the median forecast lowered to a -5.5 percent contraction from -4.7 percent in their July forecasts. Policy Board members forecast CPI inflation excluding fresh food to be negative in the current fiscal year, and to be under 1 percent in the 2021 and 2022 fiscal years, well short of the BoJ’s 2 percent target.

CANADA: Matching PNC’s and consensus expectations, the Bank of Canada (BoC) held unchanged its target for the policy overnight rate at 0.25 percent at the October 28 monetary policy decision; the BoC considers 0.25 percent to be their policy rate’s effective lower bound. The BoC maintained its forward guidance, stating that central bankers will “hold the policy interest rate at the effective lower bound until economic slack is absorbed so that the 2.0 percent inflation target is substantially achieved.” The BoC updated its 2020 real GDP forecast to a 5.5 percent contraction in its October Monetary Policy Report, better than the 7.8 percent contraction predicted in the July Report. Real GDP grew a cool 1.2 percent in August from July, the fourth consecutive monthly gain following an upwardly revised 3.1 percent increase in July. The details of the August GDP report were lukewarm. Output of goods-producing industries rose 0.5 percent while that of services-providing industries grew 1.5 percent. Growth was broad-based with every sector expanding from July to August except mining, utilities and transportation. The economy contracted 3.8 percent in the twelve months to August following a 5.0 percent decline in July and a record 16.9 percent contraction in April. Building permits rose 17.0 percent in September from August following a downwardly revised 1.4 percent increase in August; residential building permits increased 6.9 percent in September, while non-residential building permits increased 40.6 percent.

MEXICO: Real GDP rose 12.0 percent in the third quarter of 2020 after a 17.1 percent contraction in the second quarter. These growth rates are not annualized—Mexico’s real GDP grew nearly 60 percent in the third quarter using the annualized terms in which U.S. GDP is reported. Mexican real GDP was still down 8.6
percent from a year earlier in the third quarter, an improvement from the 18.7 percent drop in the second quarter but still indicating a long, long way to go for Mexico to regain full employment. In the third quarter, agricultural output grew 7.4 percent from a quarter earlier as well as from a year earlier; industrial output rose 22 percent on the quarter but fell 8.9 percent on the year; and services output rose 8.6 percent on the quarter and fell 8.8 percent on the year.

**BRAZIL:** As expected, the Central Bank of Brazil’s (BCB’s) Monetary Policy Committee unanimously voted to hold the benchmark Selic rate at a record-low 2.0 percent when central bankers met on October 27. Central bankers signaled the possibility of an additional cut ahead, stating that “current economic conditions continue to recommend an unusually strong monetary stimulus but the Monetary Policy Committee recognizes that, due to prudential and financial stability reasons, the remaining space for monetary policy stimulus, if it exists, should be small.” Financial markets are currently pricing a Selic rate of 5.0 percent in November 2021 while the central bank’s October 23rd weekly survey of professional forecasters shows a median estimate for the Selic rate of 2.75 percent in November 2021. The BCB raised its inflation forecast for 2020 to 3.1 percent from 2.1 percent at the previous meeting in September, consistent with a pickup in economic activity and the translation of the weaker real into higher prices for imported goods and services.

A record-high 313,600 formal jobs were added in September following four straight months of job losses between March and June according to the government’s survey of employers. The manufacturing and service sectors had the strongest gains in September, with the manufacturing sector contributing over a third of the month’s net gain. The recovery looks less impressive by the household survey, though; the unemployment rate rose for an eighth straight month to a record-high 14.4 percent in the three months to August according to a survey of households; it was 13.8 percent in the three months to July. The details of the August employment report were equally weak. The number of employed people dropped to an all-time low 81.7 million, down 12.8 percent from August last year. The employment ratio (people in work as a share of the working-age population) in the three months to August fell to a new record-low 46.8 percent from 47.1 percent in the three months to July and 54.8 percent in the three months to January. The labor force participation rate remained unchanged at a record-low 54.7 percent in August, well below the 61.7 percent rate in January.

Brazil’s outlook is cloudy as the country grapples with the coronavirus pandemic, weak economic fundamentals and fiscal fragility; the government in September proposed that a Renda Cidada (Citizen Income) social welfare program replace the Bolsa Familia (Family Allowance) come 2021, but President Jair Bolsonaro is constrained by the “spending cap rule” which limits growth in government spending to the previous year’s rate of inflation.