

Covid-19 remains a threat for the economic recovery in both the US and Europe

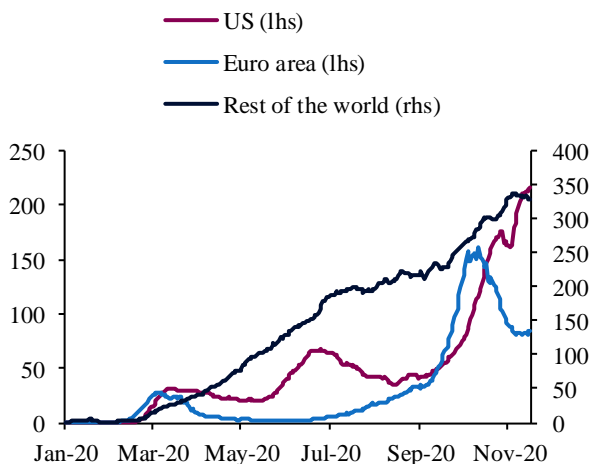
This year was one of the most dramatic on record when it comes to global economic conditions. As the Covid-19 pandemic wrought havoc across continents, the positive momentum of accelerating global demand from late 2019 and early 2020 quickly reversed into a severe economic recession. But aggressive policy stimulus and the temporary containment of the pandemic led to a rebound last quarter, with global activity stabilizing. In addition, the rapid development of several effective vaccines against Covid-19 are offering the promise of a durable solution to the pandemic. Vaccine development and mass immunization programs are necessary conditions for a sustained global economic recovery next year. However, developments in previous weeks are clouding the picture for a quick recovery at the beginning of 2021.

Covid-19 still poses a significant threat to the recovery. New waves of Covid-19 cases continue to emerge, particularly in the US and Europe. The epidemic is now worsening there, just ahead of the peak of their flu season. A new variant of the virus in Europe is also considered to be more transmissible than other streams of Covid-19.

mitigation strategies, including hard social distancing measures such as quarantines, curfews and lockdowns on both a domestic and cross country level. The objective is to lengthen the time through which the virus spreads over the winter, flattening the curve of infections before hospitals get overloaded by a bigger surge of severe cases. This is still needed as vaccine deployment will be gradual, requiring months before key countries reach immunization levels that would grant “herd immunity.”

This piece dives into three main points about the new wave of cases in the US and Europe, highlighting their economic consequences.

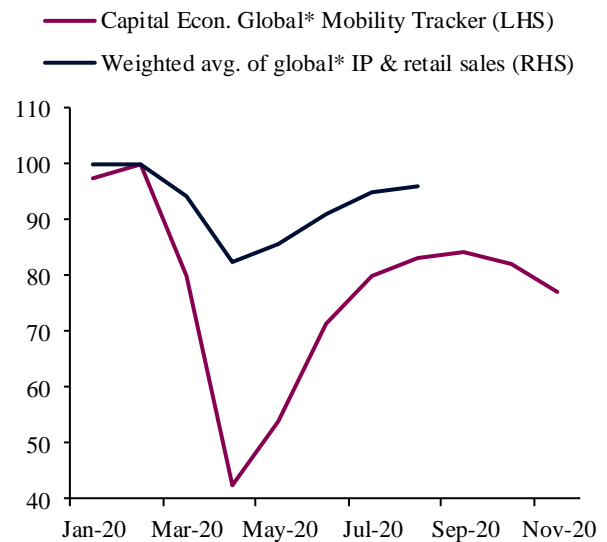
New Covid-19 infections
 (thousand daily cases, 7-day average)



Sources: John Hopkins University, QNB analysis

In response to that, several European countries and US states are re-imposing more aggressive

Global industrial production (IP) and mobility
 (January 1st = 100)



Sources: Capital Economics, QNB analysis

First, the new wave of Covid-19 cases, along with the mitigation strategies to contain its spread, are already slowing down the pace of the recovery in the US and Europe. This puts additional pressure on the global economy, as the US and Europe account for about 43% of the world’s GDP. High frequency mobility indicators, a proxy for overall economic activity, show that the recovery peaked in September 2020,

before additional restrictions and lockdowns led to a new contraction.

Second, the economic shock of the new wave of Covid-19 cases will be more moderate than previous shocks. There is less uncertainty about the virus itself and how to handle it, despite all the natural mutations and the new variants of the virus. Irrespective of the vaccines, Covid-19 treatments have also improved across the board. Moreover, supply side effects are expected to be smaller than in Q2 2020. Corporates and households are now more adapted to social distancing mandates and there is already a work-from-home infrastructure in place. To a certain extent, large parts of the US and European economies are adjusted to functioning under the “new normal” with the pandemic. Nevertheless, the picture is uncertain and risks are tilted to the downside.

Third, additional policy stimulus will be needed to support vulnerable households and corporates in the US and Europe. Employment figures are still not back to pre-pandemic levels and social distancing measures disproportionately affect low-skilled workers and small and medium businesses. Moreover, any additional policy stimulus will only serve to maintain the status quo. A healthy economic recovery requires even more financial support to these segments of the population

All in all, despite vaccine optimism, Covid-19 is still expected to cause economic turbulence in 2021. Indeed, given the volatility of events and the potential for additional headwinds, the economic picture for 2021 remains blurred.

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