



**RESEARCH &  
INSIGHTS**

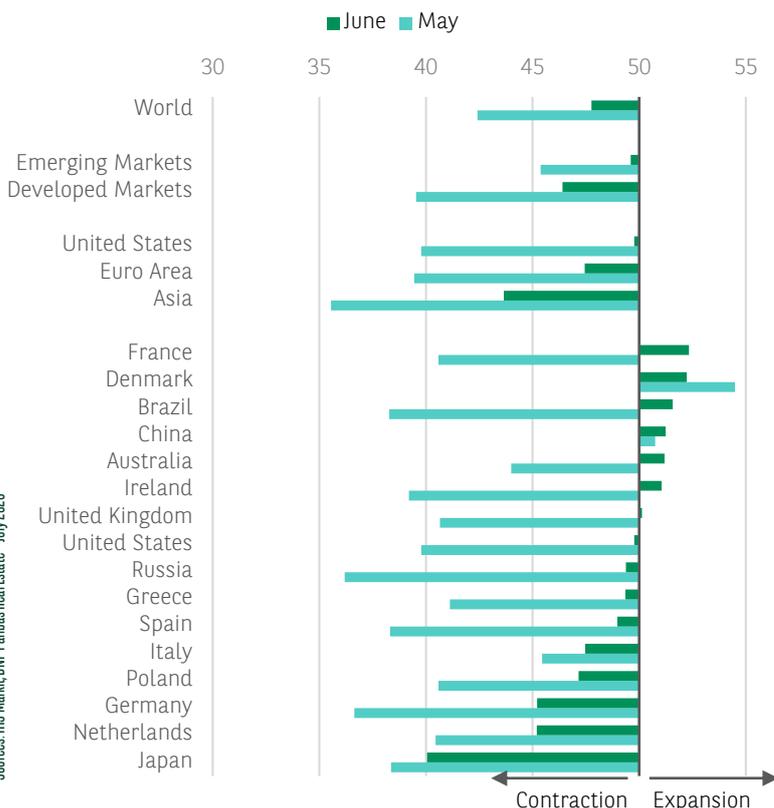
**COVID-19: A SUMMER LIKE NO OTHER**

As of 09th July 2020

The global economy is now gradually reopening. The leading indicators are positive and suggest that a V-shaped recovery is still on the table. However, after three months of lockdown these indicators may only signal a technical rebound (rather than expansionary growth) with the relaunch of production and some 'revenge consumption'.

The coming months will be crucial for the global economy, and household confidence will be one of the key drivers. With the holiday season approaching and an implied decrease in business activity, household consumption will be one of the main indicators to look at in the short term. Encouraging people to spend money will be important to sustaining a recovery, although household expenditure is now being decided against a backdrop of unemployment worries. In the mid-term, the impact of the crisis on the job market may determine future economic development and whether we see a quick and short rebound, or a protracted path back to growth.

**Figure 1: PMI indices in the main economies**



Sources: IHS Markit, BNP Paribas Real Estate - July 2020

**Nascent recovery in economic activity**

As an increasing number of countries scale back or remove their lockdown measures, economic activity is resuming slowly across the world. Firms emerging from lockdown are restarting production, increasing again the overall supply of goods and services.

As a result, PMI indices showed a record gain in June for both the manufacturing and services sectors. The world manufacturing PMI was even above its February level, indicating that business sentiment is now improving significantly.

Of the major countries (Figure 1), seven recorded an expansion in their manufacturing output with France logging the strongest gain. Indeed, the situation in France is quite positive as both supply and demand have picked up as life returns to some kind of normality.

In China, the first country hit by the pandemic, the strong recovery of its manufacturing sector has also been encouraging, as has the Chinese government's handling of the virus's second wave. Facing new cases in Beijing and in some surrounding cities in June, China was able to quickly bring the situation under control with targeted measures. This proved that a resurgence in the pandemic could be managed without the need for a complete lockdown that could have compromised recent economic gains.

Interestingly, in a contrasting trend, the manufacturing sector is still contracting in Germany despite no complete lockdown and a death toll way below other European countries. Poor external demand is holding back Germany's recovery as the export market continues to struggle; however, the lifting of restrictions across Europe should support an improvement in demand levels.

While the PMI indices seem to suggest a strong V-shaped recovery as manufacturers regain confidence, recessionary factors may still play a big role and be a drag on a rebound.

Importantly, the positive trend of the recovery will continue only if the underlying demand remains vigorous after this initial rebound. However, new orders were still in contraction in June, despite a material gain (Figure 2), and reduced consumption and lower requirements are still dampening the recovery. This indicates that demand continues to be subdued and may not be able to support the ongoing economic expansion.

**Figure 2: New orders and exports in the world**



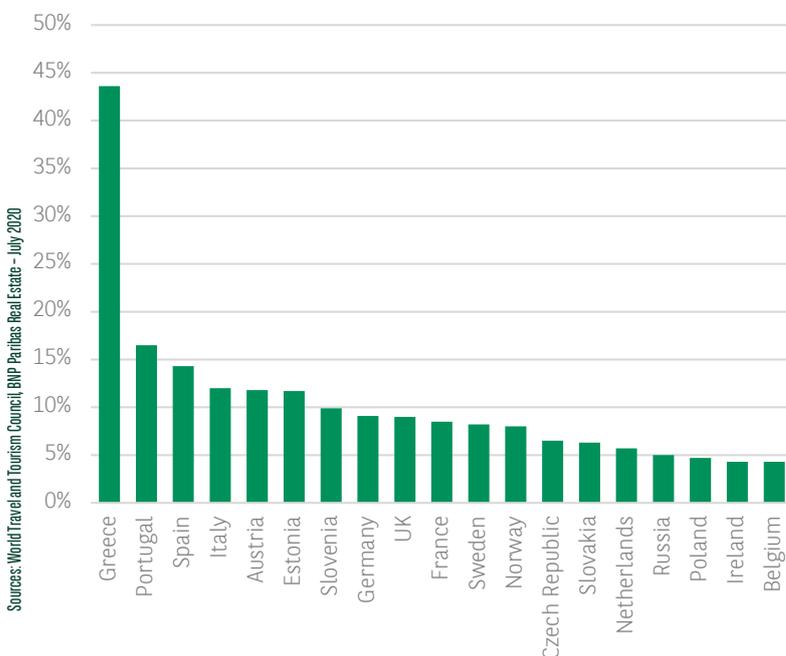
Another key factor is the lower level of trade following the fall in global demand for imports, and export-oriented economies such as China, the U.S. and even Germany may experience protracted impacts from the slowdown. Moreover, the tariff war that began in 2018 had already weakened global trade and the COVID-19 crisis will probably accelerate this trend. The atmosphere of mistrust among countries and the apparent willingness to reshore manufacturing and consumption, for example, may not vanish quickly.

Consequently, business sentiment remains a concern as it is still below its pre-pandemic level. Nevertheless, the indicator is beginning to move and increasing fastest in countries that are easing their lockdowns, and we will eventually see consumer sentiment indicators match it. The next few months will be very informative as to the final shape of the recovery. As with the outbreak itself, country recovery outcomes will show similarities, but will also differ in a variety of ways that reflect the individual structure of each country’s domestic demand.

**How will the summer be for Europeans?**

The holiday season is now starting. With the easing of lockdowns across Europe, people may have hoped for a normal summer, but the gradual and partial reopenings of borders will keep that from happening, leading to weaker consumption. Those countries which are highly dependent on foreign tourism will struggle to attract the visitor volumes seen in 2019 to support their economies.

**Figure 3: Weight of the Tourism and Travel sector (as % of GDP)**



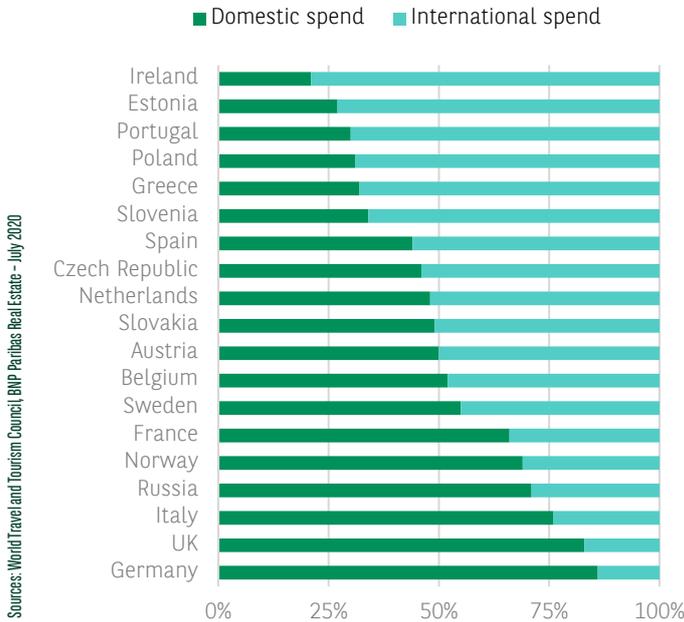
In the European Union (including the UK), the travel and tourism (T&T) sector accounts for around 9.5% of the total GDP (or USD 1,470 billion in 2019) and employs 22.6 million people. Greece is the most tourist-dependent country, far ahead of Spain and Italy (Figure 3). The reopening of borders for these countries was crucial ahead of the holiday season, but a lack of confidence from tourists may still be a worry. Although the surge in cases in Portugal, Spain and Germany raises some concerns, the major issue for tourists is flight safety and ease of travel. This is illustrated by recent data which show that there has been an increase in travel to tourist destinations within driving distances. For example, Germans are travelling more than usual to Eastern France and Northern Italy this year, as opposed to the Greek islands or the Algarve (Portugal).

Due to some borders still being closed and the lack of confidence, we may see a relative absence of cross-border tourists and a rise of domestic holidays and ‘staycations’ during this summer. Even though countries inside the EU bloc have opened their borders to each other, we are not expecting a surge in outbound tourism this year as confidence stays very low. Moreover, as the EU has recommended opening its external borders to only 15 countries, tourists coming from outside the EU will be clearly missing. Their absence could mean a potential loss of 37% of the total spend by visitors in the T&T sector.

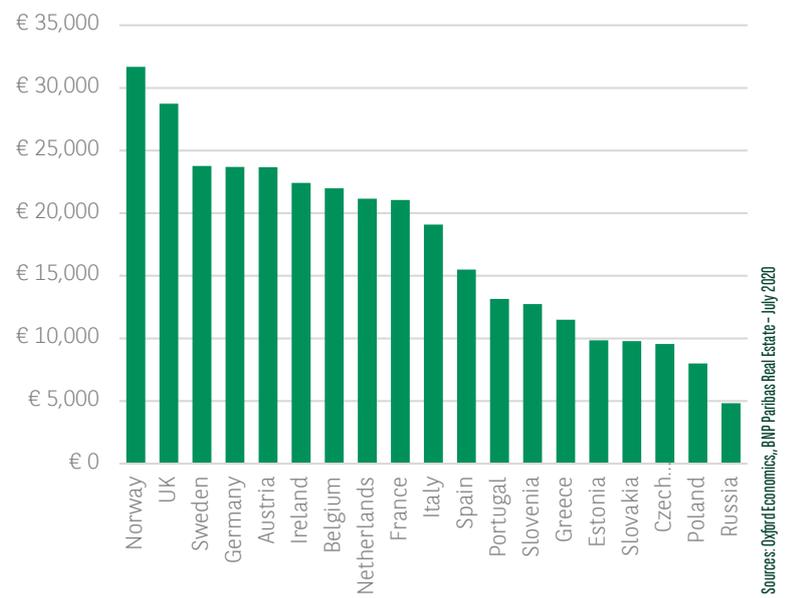
Some countries may suffer more than others for two reasons: their reliance on international spending (Figure 4) and their average income per capita (Figure 5). Countries highly dependent on international spending (such as Greece, Spain and Poland) will still need to attract foreign tourists, while others may expect that an increase in domestic demand will compensate their potential losses. Some touristic retail destinations will also face a significant downturn in business as international tourists are their main consumers (such as the Champs-Élysées in Paris, Regent Street in London, and Las Ramblas in Barcelona).

The increase in domestic tourism will also reflect the difference in average income per inhabitants across countries. The richest countries may want to retain their people's spending during the summer and encourage domestic holidays to benefit local economies. On the other hand, the supply structure of tourism in Southern European countries is much larger than the domestic audience can support, hence their dependence on foreign consumption is high. With fewer domestic tourists and lower purchasing power in general, the tourism industry in these countries faces considerable difficulties.

**Figure 4: Reliance on domestic vs international spending**

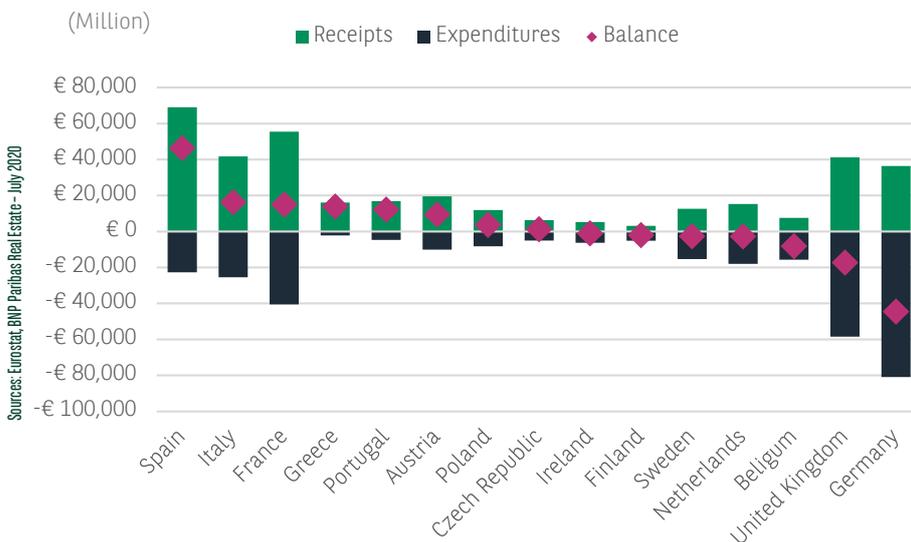


**Figure 5: Average income per inhabitants in Europe (in €)**



Finally, the balance between travel receipts (earned by countries in the case of inbound tourism) and expenditure (spent by residents in the case of outbound tourism) shows the potential winners from the surge in domestic tourism (Figure 6). Germany and the UK, the two main countries with a deficit in travel expenses (spending more abroad than at home), could be the main beneficiaries. Indeed, as a greater part of their population will not go abroad for the summer, their potential expenditure might be directed internally and benefit domestic consumption. France should also be one of the winners; its tourism sector is well-developed and seems to be attracting some of the few international tourists that are travelling. As traveller confidence will be paramount in driving international tourism, it is certain that those countries with low infection rates, or who are seen to be managing the crisis efficiently, will be top of the list for outbound travel.

**Figure 6: Travel receipts and expenditure by countries in Europe (in million of €)**



The holiday season will be key for a recovery, and perhaps also for consumer confidence given the well-known positive effects on human psychology that vacations have. This is not a measurable item in economics but still important to economies given the stress of the lockdown on populations.

Nonetheless, the spectre of a receding job market looms over European households. Undoubtedly, the impact of the COVID-19 crisis on employment will drive big-ticket expense decisions in the immediate future. A lasting increase in the unemployment rate will mean not only a direct loss in consumption in the medium term, but also constrained consumer confidence in a recovery. Therefore, the ability of European countries to mitigate the expected rise in unemployment over the remainder of 2020 will play a key role in helping to shape their recoveries.

## Towards a depressed labour market?

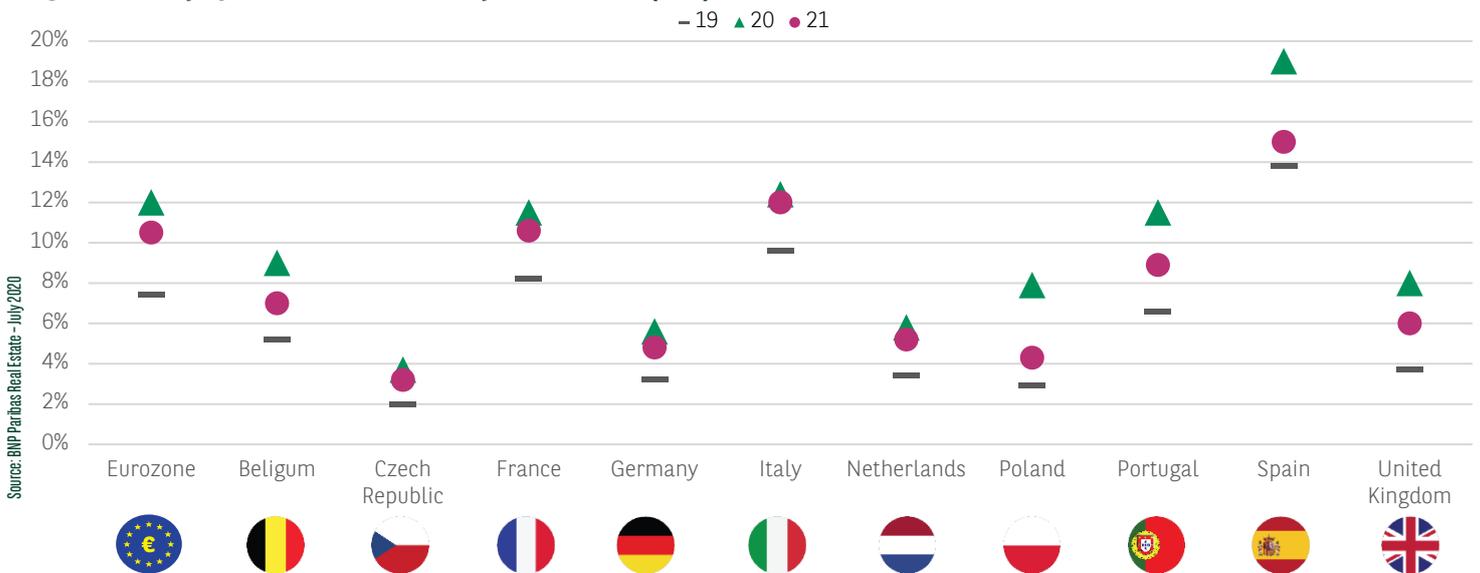
The recovery of the job market remains one of the big uncertainties with regards to the ongoing crisis. The short-term impact on the labour market seems inevitable and quite predictable, with bankruptcies and lay-offs in almost every sector, yet the longer-term picture is still unclear.

The rebound of the employment market will have some major implications for the sustainability of the recovery. Up to this point, governments have protected jobs through national employment support schemes across Europe, but policymakers are now recalibrating their support. In effect this will reveal that many companies are employing people that the current level of demand may not be able to support.

By the end of the summer, the main schemes will cease or will be restructured, and unemployment rates could increase dramatically across Europe. The support schemes are moving from short and generous policies to longer and industry-specific support (particularly for those sectors most affected by the pandemic, such as arts, tourism, retail and transportation). As a result, these sectors will avoid mass unemployment through external policies, and not through sustainable demand, with governments directly supporting workers to postpone job losses. However, the main risk is that governments will end up supporting 'zombie' companies that ought to have ceased operations.

This will result in structural interference in the job market, where people do not move to sectors with job shortages, preferring to stay in their protected jobs financed by the government. The final cost of these schemes could be high for the governments, increasing the level of debt and preventing necessary expenditure in other areas of society.

Figure 7: Unemployment rates across European countries (in %)



However, and on a positive note, if demand starts to increase strongly, business confidence will begin to be restored and some bankruptcies and lay-offs may be avoided. As a result, there will be less need for job retention schemes as demand will meet the supply.

The pace of the recovery will also be important. Countries with the biggest impact from COVID-19 in terms of GDP (such as those in Southern Europe) or with strict regulations on their labour market (such as France) may have a slower recovery than others (Figure 7). The longer the impact on employment lasts, the longer the time to gain confidence and return consumption to its pre-COVID level.

## Summer's End

The first economic data available since the easing of lockdown are very positive. We saw a strong rebound from the supply side and the beginning of momentum on the demand side. However, the V-shaped recovery is not yet secured and will depend on the sustainability of the demand. To this end, the holiday season will be critical to simultaneously rebuild confidence and increase consumption in the short term. In the longer term, the ability of countries to absorb the expected rise in unemployment through sustainable demand, job creation or even incentives to accelerate sectorial mobility will drive the recovery.

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## A 360° vision

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