RBC Economics

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Overview

Managing COVID outbreaks key for the path to economic recovery

The equity market rally that extended from late-March to early-June—pushing the S&P 500 within 5% of February's record high—faded over the past month as investors balanced improving economic data with concerns about a resurgence in COVID-19 infections. Oil prices, too, haven't been able to break out of their recent range with WTI hovering around US$40 per barrel, $20 less than at the start of the year. Equity market volatility remains elevated compared with recent years, and demand for the safety of gold has pushed prices to a nine-year high.

To be sure, recent data have signaled a stronger than expected rebound in activity in many advanced economies. Significant government support underpinned plenty of pent up demand as restrictions have been relaxed. But the path forward remains fraught with risks. Look no further than the United States, where easing of physical distancing measures resulted in the number of infections accelerating in many states. Even countries that better controlled the pandemic, like Australia, have had to re-impose lockdown measures in some areas. Many European countries, and Canada, have kept their case curves flat. But that doesn't mean easing of restrictions, and the nascent economic recovery, can continue apace.

It's also worth keeping in mind that these economies have a deep hole to climb out of. Even with declines in activity generally contained to March and April, the IMF expects the global economy will contract by 5% this year (global growth only slowed to zero in 2009). The OECD's forecast was a bit more pessimistic, and highlighted that a potential second wave of outbreaks would cause an even deeper contraction this year, and a limited recovery in 2021. Monetary policy is set to provide significant support in any case, but a return to widespread lockdowns would test the capacity of fiscal authorities.

Central bank near-term bias

New BoC Governor Macklem is sounding less optimistic than his predecessor, noting the recovery will be "prolonged and bumpy". Low rates are locked in, and QE will continue well into the recovery.

The Fed's dot plot suggests rates will remain close to zero at least through 2022. Asset purchases have slowed from crisis levels but continue at a relatively brisk pace, and are likely to remain in place for an extended period.

The BoE expanded its QE program by less than we expected in June, but we still see scope for a further increase later this year. We also think the BoE will cut its policy rate below zero by year end.

ECB President Lagarde signaled the central bank will pause to see how the pandemic and recovery progresses before making further monetary policy changes. Asset purchases and negative rates continue.

The RBA sounded more uncertain in July as worries about coronavirus resurgence offset generally firmer economic data. The central bank once again noted that accommodation can be scaled up if necessary.

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Highlights

▲ US consumers are leading the rebound, with help from government transfers.

▲ Growth in coronavirus cases is accelerating in many states, with some starting to re-impose restrictions.

▲ Job gains in May and June were impressive, but hiring momentum appears to have slowed and layoffs continue.

▲ The Fed's dot plot showed 15 of 17 members don't see a rate hike by the end of 2022.

US recovery getting underway…

Recent data confirm the US economy's sharp contraction only extended through April. After a surprising 2.7 million jobs were added in May, payroll employment increased by a further 4.8 million in June (in total retracing about 1/3 of the jobs lost in the prior two months). Consumers have been a key driver of the early rebound—retail sales surged by 18% in May, and core sales were actually higher than in February. That likely reflects the release of some pent up demand as retailers were allowed to re-open and Americans had more opportunities to spend some of the government handouts (including cash payments in April and a generous top up to state unemployment insurance) that have supported household incomes during the pandemic.

That said, consumer confidence remains subdued and big ticket purchases like autos were well below pre-pandemic levels in June. And some activities continue to be restricted by physical distancing. Sales at food service and drinking establishments were still 40% below pre-pandemic levels in May and restaurant reservations were less than half of last year's levels as of late June.

…but fresh outbreaks pose a threat

The resurgence in coronavirus cases is putting this early recovery at risk. Average daily case growth over the past week is now in excess of 50,000, well above the 32,000 daily peak in early-April. While renewed outbreaks in large states like Florida, Texas and California are drawing attention, fully 3/4 of US states were seeing an acceleration in weekly case growth as of early-July and nearly 40% saw an uptick in deaths. Having reopened before the virus was under control, some states are beginning to re-impose restrictions on economic activity. That's likely to reduce re-hiring momentum, and will create challenges for businesses that have already run through much of their Paycheck Protection Program loans (generally worth about 2.5 months' payroll).

High-frequency tracking of employment at small service sector businesses already suggests the rebound in jobs and hours worked started to stall in late-June. Weekly initial jobless claims remain stubbornly high at more than 1.3 million, indicating businesses continue to cut jobs even as others are re-hiring. The federal top up for UI benefits is set to expire at the end of July, which will mean an income hit for the millions of Americans that remain unemployed. Congress is working toward another stimulus package in the $1 trillion range that will likely provide some further support to those out of work. Nonetheless, we think challenging labour market conditions over the second half of the year will make for a slow recovery. And while we're penciling in a 20% annualized rebound in Q3 GDP (after an expected 35% drop in Q2), risks are skewed to the downside if more states need to re-impose restrictions.

Monetary policy to remain accommodative for years

The Fed held its policy rate just above zero in June, and according to the committee's dot plot, it's likely to remain there for years to come. 15 of 17 FOMC members don't expect to raise interest rates through the end of 2022. That reflects a concern that ongoing economic slack—the Fed's median forecast doesn't see GDP reaching end of 2019 levels until 2022—will keep core PCE inflation below the Fed's 2% objective, a mark it had difficulty achieving even in good economic times.

Other stimulus measures aren't going away anytime soon. With financial conditions having improved, some of the Fed's lending programs have seen less uptake. But other liquidity facilities are just getting underway and could be worth hundreds of billions of dollars. While the Fed has slowed the pace of asset purchases since the height of the crisis, it will continue buying roughly $80 billion of Treasuries and $40 billion of agency mortgage-backed securities per month. For reference, the Fed's monthly Treasury purchases were $45 billion at the height of its 'QE3' program in 2013. The Fed didn't provide specific guidance on how long QE will continue, though minutes of the June meeting suggest some form of outcome-based forward guidance (a commitment to keep policies in place until specified unemployment or inflation objectives are achieved) might eventually be used to provide additional clarity on the likely path for fed funds and asset purchases. Yield curve targeting (currently being used by central banks in Japan and Australia) was discussed but most of the committee appeared skeptical.

Canada's economy returned to growth in May…

Canada's economic output shrank by an unprecedented 18% between February and April, nearly four times the peak to trough decline during the 2008-09 recession. But the economy started to claw its way back in May (GDP rose 3% according to StatCan's preliminary estimate) and recent activity indicators point to further improvement in June. Retail sales reportedly increased by 19% in May (retracing about 40% of the previous two months' declines) and our own consumer spending tracker suggests card spending nearly returned to year ago levels by mid-June. Auto sales have also rebounded sharply, with June's unit sales more than tripling from April's low. New cars aren't the only big ticket purchase Canadians were more willing to commit to—home resales started to pick up in May and were at or above year-ago levels in some major markets in June.

A quick start to the recovery, particularly on the household side, reflects some pent up demand after health restrictions limited Canadians' ability to go out and buy anything but essentials (online sales have unsurprisingly flourished). Government support for households—$53.5 billion in CERB payments through the end of June, and billions more in tax credits and child benefits—has also helped shore up income in the face of significant job losses. CERB payments were recently extended by 8 weeks, meaning those that started making claims in mid-March will continue to receive benefits until the end of August.

…but don't extrapolate that trend

While the early recovery has been swift, we think demand will remain soft over the second half of the year due to low business and consumer confidence and ongoing physical distancing. That will mean still-challenging labour market conditions, and reliance on less generous EI payments for those whose CERB benefits have run out. And while some consumer-facing sectors have seen a solid rebound, business confidence generally remains subdued. The Bank of Canada's Business Outlook Survey showed a sharp downturn in overall sentiment in Q2, with many firms cutting capex plans, and hiring intentions remaining muted. In a separate CFIB survey, more than 40% of small business respondents still characterized their general business situation as "bad". Nearly as many expect to reduce full time employment in the next 3-4 months. Exporters are feeling the pinch, too—EDC's trade confidence index fell to a record low in Q2 with both sales and new business opportunities slowing sharply.

Fiscal support comes at a cost

Fiscal support measures have prevented a more severe economic downturn—the government estimates GDP would have fallen by more than 10% in 2020 without its interventions—by providing a helping hand in the early stages of the recovery. The price tag has been substantial, though. Finance Minister Morneau announced the federal budget deficit is expected to come in at $343 billion, or 16% of GDP, in 2020-21. That largely reflects nearly $230 billion in stimulus measures (including an expanded wage subsidy program) and a $71 billion revenue hit, the majority of which is due to lower tax receipts. The unprecedented shortfall will push federal debt above $1 trillion, or 49% of GDP.

Citing the pandemic's heavy toll on government finances (both federal and provincial), Fitch downgraded Canada's credit rating to AA+ from AAA in June. Other ratings agencies still give the country's debt a top-tier rating, though we expect further downgrades will follow. Market reaction to the downgrade was muted with GoC yields remaining at all-time lows. The Bank of Canada's QE program is helping to contain borrowing costs—at its current pace, the bank's purchases (including regular purchases at auction) will equate to more than 85% of bond issuance this year. Lower public debt charges were about the only positive news in the government's fiscal update.

New BoC governor sounding less optimistic

Outgoing BoC Governor Poloz ended his term with relative optimism, noting that the economy was still tracking the "best-case scenario" laid out in the bank's April MPR. But his successor, Tiff Macklem, isn't sounding as cheery. In his first speech as governor, Macklem warned "the recovery will likely be prolonged and bumpy, with the potential for setbacks along the way." While re-opening should support near term job growth, and consumer spending will be boosted by pent up demand in the "recovery" phase, Macklem noted that not all jobs will come back and lingering uncertainty will

Highlights

▲ Our spending tracker suggests the consumer sector continued to recover through June.

▲ Government income support is helping the millions of Canadians still out of work…

▲ …though the tab for such support is pushing the deficit to a post-war high, resulting in a ratings downgrade.

▲ The BoC expects a near term "recovery" phase will be followed a more gradual and prolonged "recuperation" phase.

Highlights

▲ The UK economy has started to bounce back from a sharp 25% contraction through April…

▲ …but a more gradual trajectory from here will keep the BoE in stimulus mode, with further QE and lower rates to come.

▲ Euro area economies have bounced back as health restrictions have eased.

▲ The ECB has put significant stimulus in place and is waiting to see what fiscal authorities can muster.

result in weak demand over a more gradual "recuperation" phase. With demand expected to recover more slowly than supply, excess capacity in the economy is likely to keep inflation below the Bank of Canada's 2% target. Our forecast assumes CPI ex food and energy, which fell to just 0.6% year-over-year in May, will only reach 1.6% by the end of 2021.

The upshot is that some of the monetary policy support launched by the BoC since March will need to remain in place for an extended period. While improved market functioning means liquidity providing programs are seeing less demand, government bond purchases are continuing at a steady pace. The central bank's guidance remains that large scale asset purchases will continue "until the economic recovery is well underway"—a commitment that we think will see QE extending well into next year. Rate hikes remain off the table throughout our forecast horizon.

UK recovery surprisingly strong, but it's early days

UK GDP fell by a staggering 25% between February and April with all private industries seeing a decline in output. But as in many other countries, it looks like the economy returned to growth as physical distancing measures were eased. Retail sales came back to life in May, unwinding about 40% of the previous two months' decline. PMIs rose sharply in both May and June, with the manufacturing index rising back above 50 (signaling expansion) and the services reading only modestly lower. It looks like the initial phase of the recovery is moving at a brisk pace. However, indicators of new orders and employment continue to point to soft demand going forward, and there is potential for greater job losses once the government's furlough scheme (currently supporting 9.4 million jobs) runs out. The government just announced a fresh stimulus package worth nearly £30 billion that includes payments for employers that bring workers off furlough by the end of January 2021. But we still expect weak demand will weigh on the labour market's recovery.

Fiscal stimulus isn't the only game in town. At its June meeting, the BoE announced a £100 billion expansion of its asset purchase program (to £745 billion) while holding its policy rate just above zero. But the increase in QE was half the size we were expecting, and means weekly asset purchases will slow over the second half of the year. The decision to reduce the pace of purchases may have reflected a bit of optimism on the BoE's part—policymakers noted Q2 GDP would likely decline by less than the 25% projected in May (our own forecast is -19%) and that the early recovery in consumer spending is looking stronger than anticipated. That said, the BoE expressed some concern about the medium term outlook, particularly regarding the health of the labour market. As noted above, we share those concerns, and still see scope for a further increase in the asset purchase target later this year to ensure government borrowing costs remain low. There was little discussion of negative rates in June, though markets continue to price in a move below zero, and our own forecast looks for the bank rate to be cut by a further 25 basis points by year end.

Euro area back to growth, but easing in restrictions will slow

Euro area economies also look to have staged a decent rebound beginning in May. Retail sales rose sharply, retracing nearly 2/3 of the previous two months' declines. PMIs picked up in May and June, with countries that eased lockdown measures most significantly seeing the greatest improvement in business sentiment. Given a faster than expected recovery, we're now expecting a less significant decline in Q2 GDP (-11.2% non-annualized vs. -26% previously). But with the removal of health restrictions set to slow—Germany, for example, is set to maintain social distancing rules until October at the earliest—we don't think the sharp, early improvement in economic indicators should be extrapolated. We are penciling in a moderate rebound in Q3, but see risks later in the year when government support starts to fade and labour market conditions remain challenging.

Having nearly doubled the size of its Pandemic Emergency Purchase Program in June and added significant liquidity through another TLTRO operation, we don't expect any major policy changes from the ECB over the summer. Indeed, President Lagarde said the central bank has done so much that it has "quite a bit of time to assess" incoming data. The ECB will be closely watching fiscal developments, with some board members noting that successful implementation of the proposed rescue fund (which European leaders will continue to hammer out at a mid-July summit) might mean the central bank doesn't need to make full use of its PEPP purchase envelope.

Interest rate outlook

%, end of period

	Actuals						Forecast					
	19Q1	19Q2	19Q3	19Q4	20Q1	20Q2	20Q3	20Q4	21Q1	21Q2	21Q3	21Q4
Canada												
Overnight	1.75	1.75	1.75	1.75	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Three-month	1.67	1.66	1.65	1.66	0.21	0.20	0.20	0.20	0.20	0.25	0.25	0.25
Two-year	1.55	1.47	1.58	1.70	0.42	0.29	0.30	0.30	0.30	0.30	0.35	0.35
Five-year	1.52	1.39	1.40	1.69	0.59	0.37	0.40	0.40	0.45	0.50	0.60	0.65
10-year	1.62	1.47	1.36	1.70	0.70	0.53	0.55	0.60	0.65	0.70	0.80	0.90
30-year	1.89	1.69	1.53	1.76	1.31	0.99	1.05	1.15	1.25	1.30	1.35	1.40
United States												
Fed funds**	2.50	2.50	2.00	1.75	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Three-month	2.40	2.12	1.88	1.55	0.11	0.16	0.15	0.15	0.15	0.15	0.15	0.15
Two-year	2.27	1.75	1.63	1.58	0.23	0.16	0.30	0.35	0.40	0.45	0.55	0.65
Five-year	2.23	1.76	1.55	1.69	0.37	0.29	0.50	0.60	0.70	0.75	0.90	1.00
10-year	2.41	2.00	1.68	1.92	0.70	0.66	0.75	0.90	1.00	1.10	1.25	1.35
30-year	2.81	2.52	2.12	2.39	1.35	1.41	1.40	1.50	1.55	1.60	1.65	1.70
United Kingdom												
Bank rate	0.75	0.75	0.75	0.75	0.10	0.10	0.10	-0.15	-0.15	-0.15	-0.15	-0.15
Two-year	0.63	0.62	0.37	0.54	0.13	-0.08	-0.10	-0.25	-0.25	-0.15	-0.10	-0.10
10-year	0.99	0.84	0.49	0.83	0.34	0.17	0.25	0.10	0.15	0.20	0.25	0.30
Euro area												
Deposit Rate	-0.40	-0.40	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
Two-year	-0.60	-0.73	-0.74	-0.59	-0.69	-0.69	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60
10-year	-0.07	-0.33	-0.58	-0.19	-0.48	-0.45	-0.50	-0.40	-0.35	-0.30	-0.25	-0.20
Australia												
Cash target rate	1.50	1.25	1.00	0.75	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Two-year	1.47	0.98	0.76	0.92	0.24	0.25	0.20	0.20	0.20	0.20	0.20	0.20
10-year	1.78	1.32	1.01	1.37	0.77	0.87	0.85	0.90	0.95	1.00	1.10	1.10
New Zealand												
Cash target rate	1.75	1.50	1.00	1.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Two-year swap	1.62	1.35	0.92	1.25	0.52	0.19	0.40	0.40	0.40	0.40	0.40	0.40
10-year swap	2.15	1.78	1.20	1.78	0.92	0.72	0.90	0.90	0.90	0.90	1.00	1.10
Yield curve*												
Canada	7	0	-22	0	28	24	25	30	35	40	45	55
United States	14	25	5	34	47	50	45	55	60	65	70	70
United Kingdom	36	22	12	29	21	25	35	35	40	35	35	40
Eurozone	53	40	16	40	21	24	10	20	25	30	35	40
Australia	31	34	25	45	53	62	65	70	75	80	90	90
New Zealand	53	43	28	53	40	53	50	50	50	50	60	70

* Two-year/10-year spread in basis points, **Top of 25 basis point range

Source: Reuters, RBC Economics Research

Central bank policy rate

%, end of period

		Current	Last				Current	Last	
United States	Fed funds	0-0.25	1.00-1.25	March 15, 2020	Eurozone	Deposit rate	-0.50	-0.40	September 18, 2019
Canada	Overnight rate	0.25	0.75	March 27, 2020	Australia	Cash rate	0.25	0.50	March 19, 2020
United Kingdom	Bank rate	0.10	0.25	March 19, 2020	New Zealand	Cash rate	0.25	1.00	March 16, 2020

Source: Bloomberg, Reuters, RBC Economics Research

Economic outlook

Growth outlook

% change, quarter-over-quarter in real GDP

	19Q1	19Q2	19Q3	19Q4	20Q1	20Q2	20Q3	20Q4	21Q1	21Q2	21Q3	21Q4	2018	2019	2020F	2021F
Canada*	1.2	3.2	1.1	0.6	-8.2	-35.0	30.0	4.0	4.0	4.0	5.0	5.0	2.0	1.7	-6.0	4.0
United States*	3.1	2.0	2.1	2.1	-5.0	-35.0	20.0	10.0	7.0	5.0	4.0	4.0	2.9	2.3	-5.5	4.8
United Kingdom	0.7	-0.1	0.5	0.0	-2.2	-18.7	20.4	1.2	1.6	1.2	0.3	0.4	1.3	1.5	-7.3	7.6
Euro area	0.5	0.1	0.3	0.1	-3.6	-11.2	8.1	-2.8	1.8	3.8	3.0	0.4	1.9	1.2	-8.7	5.0
Australia	0.5	0.6	0.6	0.5	-0.3	-7.4	2.6	0.6	1.0	1.1	0.8	0.7	2.8	1.8	-3.7	2.3

*annualized

Inflation outlook

% change, year-over-year

	19Q1	19Q2	19Q3	19Q4	20Q1	20Q2	20Q3	20Q4	21Q1	21Q2	21Q3	21Q4	2018	2019	2020F	2021F
Canada*	1.6	2.1	1.9	2.1	1.8	-0.1	0.0	-0.1	0.0	1.2	1.2	1.5	2.3	1.9	0.4	1.0
United States*	1.6	1.8	1.8	2.0	2.1	0.4	0.0	-0.2	0.1	1.6	2.1	2.3	2.4	1.8	0.6	1.5
United Kingdom	1.8	2.0	1.9	1.4	1.7	0.6	0.5	0.8	0.7	1.3	1.4	1.5	2.5	1.8	0.9	1.2
Euro area	1.4	1.4	1.0	1.0	1.1	0.2	0.2	0.3	0.3	1.3	1.3	1.4	1.8	1.2	0.4	1.0
Australia	1.3	1.6	1.7	1.8	2.2	0.9	1.0	0.9	1.1	2.3	2.2	2.2	1.9	1.6	1.3	2.0

Source: Statistics Canada, Bureau of Economic Analysis, Bureau of Labor Statistics, Office for National Statistics, Statistical Office of the European Communities, Australian Bureau of Statistics, Statistics New Zealand, RBC Economics Research

Inflation tracking

Inflation Watch

	Measure	Current period	Period ago	Year ago	hree-month tren	Six-month trend
Canada	CPI ex food & energy[1]	May	-0.2	0.6	0.2	1.0
United States	Core PCE[1,2]	May	0.1	1.0	-0.6	1.1
United Kingdo	All-items CPI	May	0.0	0.5	0.4	0.4
Euro area	All-items CPI[1]	Jun	0.2	0.3	-1.3	0.2
Australia	Trimmed mean CPI[1]	Q1	0.5	1.8	N/A	N/A
New Zealand	All-items CPI	Q1	0.8	2.5	N/A	N/A

1 Seasonally adjusted measurement.
2 Personal consumption expenditures less food and energy price indices.

Source: Statistics Canada, Bureau of Labor Statistics, Office for National Statistics, Statistical Office of the European Communities, Australian Bureau of Statistics, Statistics New Zealand, RBC Economics Research

Currency outlook

Level, end of period

	Actuals						Forecast					
	19Q1	19Q2	19Q3	19Q4	20Q1	20Q2	20Q3	20Q4	21Q1	21Q2	21Q3	21Q4
Canadian dollar	1.33	1.31	1.32	1.30	1.41	1.36	1.38	1.40	1.38	1.37	1.36	1.35
Euro	1.12	1.14	1.09	1.12	1.10	1.12	1.14	1.15	1.14	1.13	1.12	1.11
U.K. pound sterling	1.30	1.27	1.23	1.33	1.24	1.24	1.24	1.22	1.20	1.18	1.17	1.16
Japanese yen	110.9	107.9	108.1	108.6	108	108	100	95	97	99	101	103
Australian dollar	0.71	0.70	0.68	0.70	0.61	0.69	0.65	0.64	0.63	0.63	0.63	0.63

Canadian dollar cross-rates

	19Q1	19Q2	19Q3	19Q4	20Q1	20Q2	20Q3	20Q4	21Q1	21Q2	21Q3	21Q4
EUR/CAD	1.50	1.49	1.44	1.46	1.55	1.53	1.57	1.61	1.57	1.55	1.52	1.50
GBP/CAD	1.74	1.66	1.63	1.72	1.75	1.68	1.71	1.71	1.66	1.61	1.59	1.56
CAD/JPY	83.0	82.4	81.6	83.6	76.5	79.5	72.5	67.9	70.3	72.3	74.3	76.3
AUD/CAD	0.95	0.92	0.89	0.91	0.86	0.94	0.90	0.90	0.87	0.86	0.86	0.85

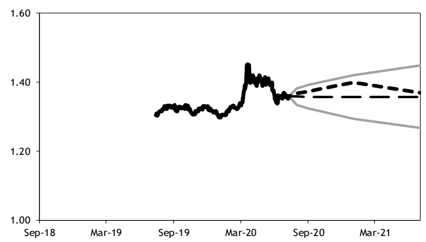
Rates are expressed in currency units per US dollar and currency units per Canadian dollar, except the euro, UK pound, Australian dollar, and New Zealand dollar, which are expressed in US dollars per currency unit and Canadian dollars per currency unit.

Source: Bloomberg, RBC Economics Research

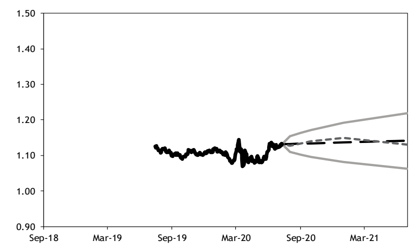
RBC Economics outlook compared to the market

The following charts track historical exchange rates plus the forward rate (dashed line) compared to the RBC Economics forecast (dotted line) out one year. The cone for the forecast period frames the forward rate with confidence bounds using implied option volatilities as of the date of publication.

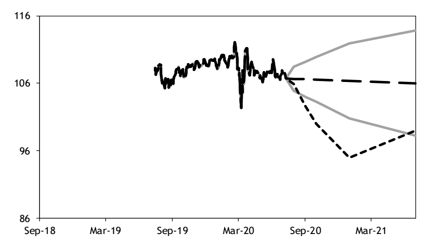
Canadian dollar



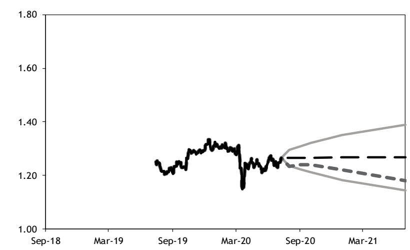
Euro



Japanese yen



U.K. pound

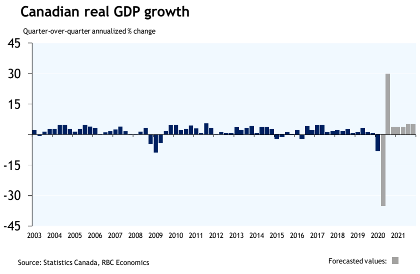


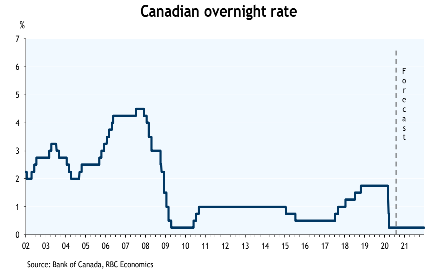
Central bank watch

Bank of Canada

The BoC will finally provide a full forecast update in July, and based on comments from Governor Macklem, it's likely to show a prolonged recovery and inflation persistently below 2%.

The BoC's forward guidance on asset purchases remains vague, though updated forecasts might give some indication of when the bank thinks the recovery will be "well underway".

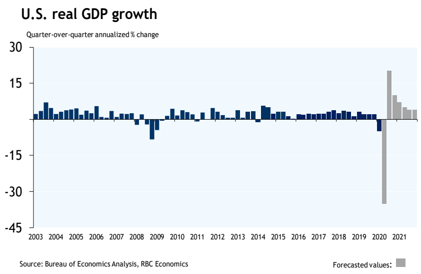


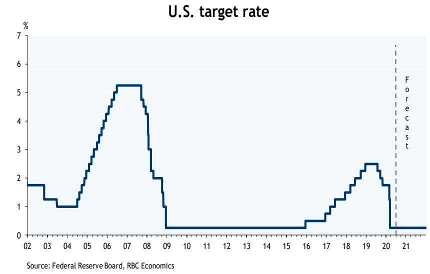


Federal Reserve

The Fed's economic projections are a bit more pessimistic than our own. There's no shortage of uncertainty as many states are dealing with COVID-19 outbreaks that could jeopardize the H2/20 recovery.

FOMC members see persistently low inflation calling for near zero rates through at least 2022. Asset purchases will help keep a cap on longer-term rates, while other programs are providing ample liquidity.

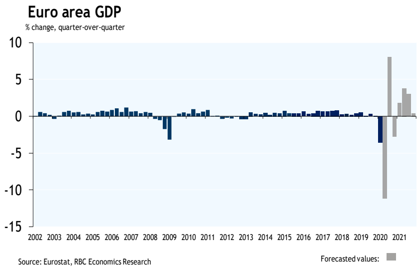


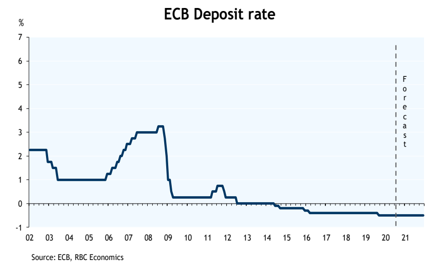


European Central Bank

A downward revision to expected inflation pushed the ECB into action in June, but early signs of recovery leave the central bank in no rush to provide further stimulus at this stage.

ECB actions have helped reduce peripheral sovereign spreads, and a rescue fund deal that facilitates transfers to economically weaker countries would also help in that regard.

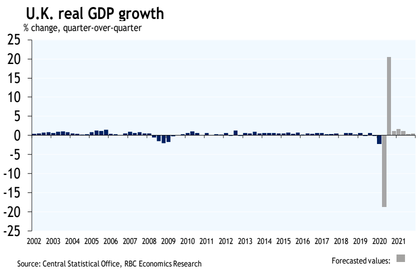


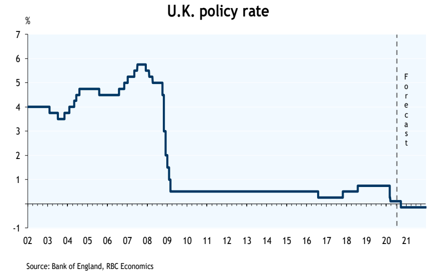


Bank of England

The BoE sounded slightly optimistic in June, noting Q2 GDP likely contracted by less than expected. However, medium term risks remain, particularly as fiscal support begins to fade.

The BoE is slowing the pace of its asset purchases but we still see scope for another increase in QE. Markets continue to price in negative rates, and we think the BoE will follow through in November.

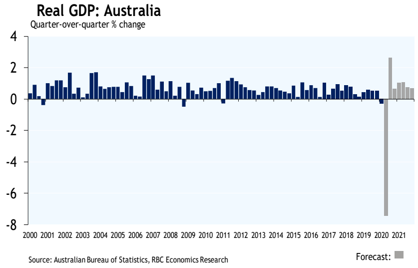


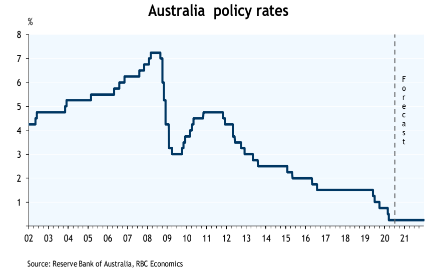


Reserve Bank of Australia

Australian employment fell further in May, but other economic indicators have started to firm. Improving data will run up against fresh lockdown measures in the country's second largest city.

With coronavirus cases once again on the rise, the RBA sounded more cautious in July. It remained on the sidelines, though, keeping 3-year yields anchored around 0.25%.



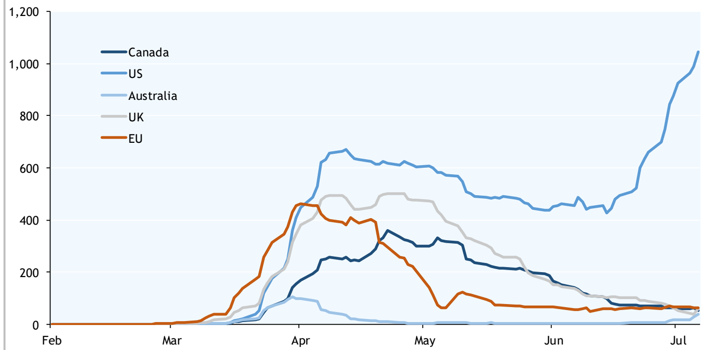


Lifting lockdowns leads to consumer comeback… for now

Many advanced economies have had success controlling coronavirus cases since May. But the US outbreak never really got under control, and easing restrictions has resulted in a sharp acceleration in case growth. Australia's renewed outbreak pales in comparison.

Confirmed COVID-19 cases per million population

7-day increase in cases per million population

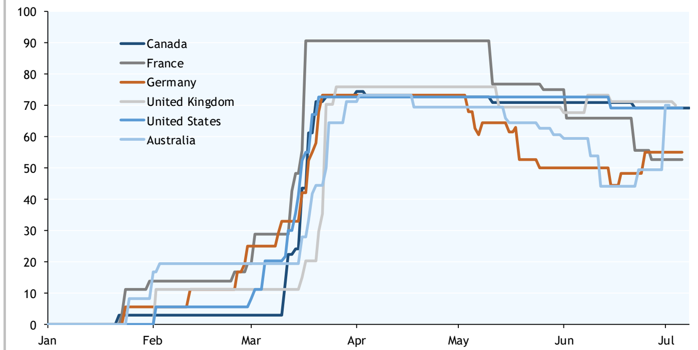


Source: Johns Hopkins University, RBC Economics

Countries have generally been able to let up on some restrictions, though areas of Australia and the US have had to re-impose measures to varying degrees. Even where the virus is relatively controlled, the recent easing in restrictions—and thus the pace of economic recovery—is likely to slow.

Oxford COVID-19 Stringency Index

stringency of lockdown and social distancing polices (0-100 index, higher=more stringent)

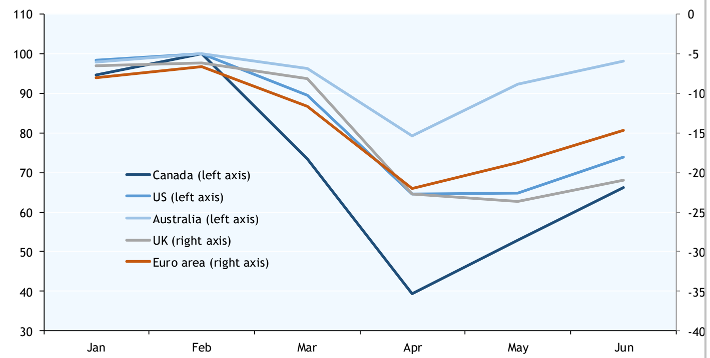


Source: Oxford COVID-19 Government Response Tracker, RBC Economics

Consumer confidence has started to improve as restrictions have been eased and some jobs have returned. But sentiment generally remains subdued, and renewed virus outbreaks in some countries could reverse some of the recent improvement.

Consumer confidence

Feb/2020=100 (left axis), % balance (right axis)

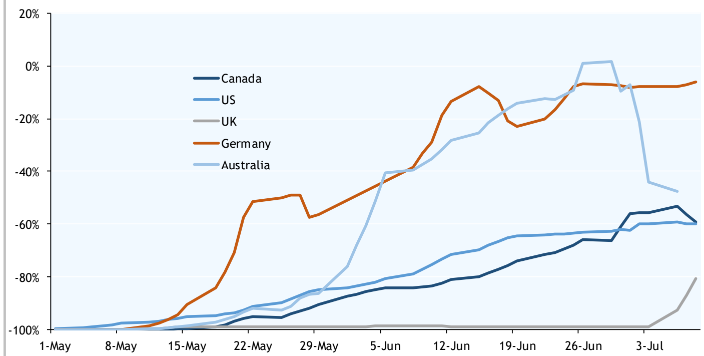


Source: Conference Board of Canada, The Conference Board, EC, Westpac-Melbourne Institute, RBC Economics

With physical distancing measures easing, retail sales have staged a decent rebound and some other hard-hit services sectors (like restaurants) are beginning to recover. But as Australia shows, that recovery depends on health restrictions, which won't always move in one direction.

Restaurant reservations

year-over-year % change in seated diners, 7-day average



Source: OpenTable, RBC Economics