ECONOMIC OUTLOOK SPRING 2020

STRENGTHENING THE ECONOMIC RECOVERY

Economic forecast

- The EU, in common with the rest of the global economy, is presently experiencing the deepest recession since the Great Depression of the 1930's.

- Whilst the situation remains very uncertain, **our central forecast is for the EU economy to fall by 7.9% in 2020, and rebound with 5.8% growth in 2021.** This implies that the economy will be operating just slightly below its pre-crisis level towards the end of 2021.

- **The depth of the recession and the strength of the ensuing recovery may also differ considerably between member states**. Our members expect economic activity to have remained above 90% of pre-crisis levels in Germany, compared to below 70% in other member states where lockdowns were also longer. Sectoral differences, including the greater reliance on international tourism in some member states will also impact recovery paths.

- Short-time working schemes has so far largely saved the EU the dramatic unemployment increases seen in the US. **But without strong policy support for businesses and workers, unemployment levels could rise significantly above the 9% level the European Commission has forecasted for the EU in 2020,** and will not return quickly to the 7.9% figure they forecast for 2021.

Key policy issues

- In recent months, we have seen an unprecedented response by the EU and member states alike to rapidly put in place essential measures to protect businesses and workers through this crisis. But further measures are needed to deliver a co-ordinated EU fiscal stimulus of the magnitude seen in other G7 economies. Whilst EU member states have provided relatively large support through loans, equity injections and guarantees, actual direct revenue and expenditure have been relatively small in relation to other G7 economies.

- Whilst in our baseline scenario we expect EU27 GDP to be 2.6% below the 2019-level in 2021, in the event of a stronger, co-ordinated fiscal policy response, we forecast that the gap can be reduced to only 1.4%, setting the scene for a full recovery in 2022.

- BusinessEurope has set out the need for an EU recovery plan focussing on:

    - An ambitious and coordinated fiscal stimulus to support demand, a rapid deployment of EU investment funds as part of an ambitious and co-ordinated EU fiscal stimulus

    - A revitalised and open single market and a strengthened single currency

    - Fair and free trade and investment and support for multilateral solutions

    - Strengthened EU governance to ensure EU financial support increases member states' implementation of growth and employment enhancing structural reforms and upward convergence.

Summary

The EU, in common with the rest of the global economy, is presently experiencing the deepest recession since the Great Depression of the 1930's. The imposition of comprehensive lockdowns has caused national economies and world trade to come to a sudden halt.

Whilst the situation remains very uncertain, our central forecast is for the EU economy to fall by 7.9% in 2020, and rebound with 5.8% growth in 2021. This implies that the economy will be operating just slightly below its pre-crisis level towards the end of 2021.

Both the EU and its member states have responded rapidly with unprecedented measures to support businesses through the crisis, and as a consequence, increases in unemployment in the EU have been much more modest than in the US. But a co-ordinated fiscal stimulus remains essential to strengthening the recovery and minimising the long-term scarring to the EU economy. Our analysis suggests increased fiscal stimulus by member states as part of a co-ordinated EU recovery plan could increase output and reduce the likelihood that the long-term economic impact of the crisis damages long-term EU economic convergence.

Figure 1: BusinessEurope economic forecast, May 2020

	2020	2021
GDP growth (real), %	-7.9	5.8

BusinessEurope spring 2020 economic forecast.

Our forecasting approach during this uncertain period

Developing an economic outlook at present is particularly difficult. Whilst we are able to directly take the views of businesses across Europe, economic prospects will also depend on a number of political and health related factors, in particular:

- The severity of **lockdown measures**, and the length of time in which they are in place
- The **development of the virus**, including our ability to treat and control it, ultimately through a vaccine.
- The **response of consumers**, including their confidence to engage in economic activity such as shopping.
- The strength of the **policy response.**

Our forecast is based on a number of assumptions around these various factors. In particular, we take as our baseline scenario an average **9 weeks lockdown period with no second wave of infections and lockdowns,** although this also takes into account the different intensity and length across EU member state as well as stepwise lifting of measures. It also implies a clear **downside risk to the economic outlook if a second wave of lockdowns** is required.

Alongside a baseline scenario, modelled on existing, announced policy measures, we also model a **scenario that foresees more ambitious policy response nationally at EU-level.**

2020: Pre-lockdown, lockdown and gradually recovery

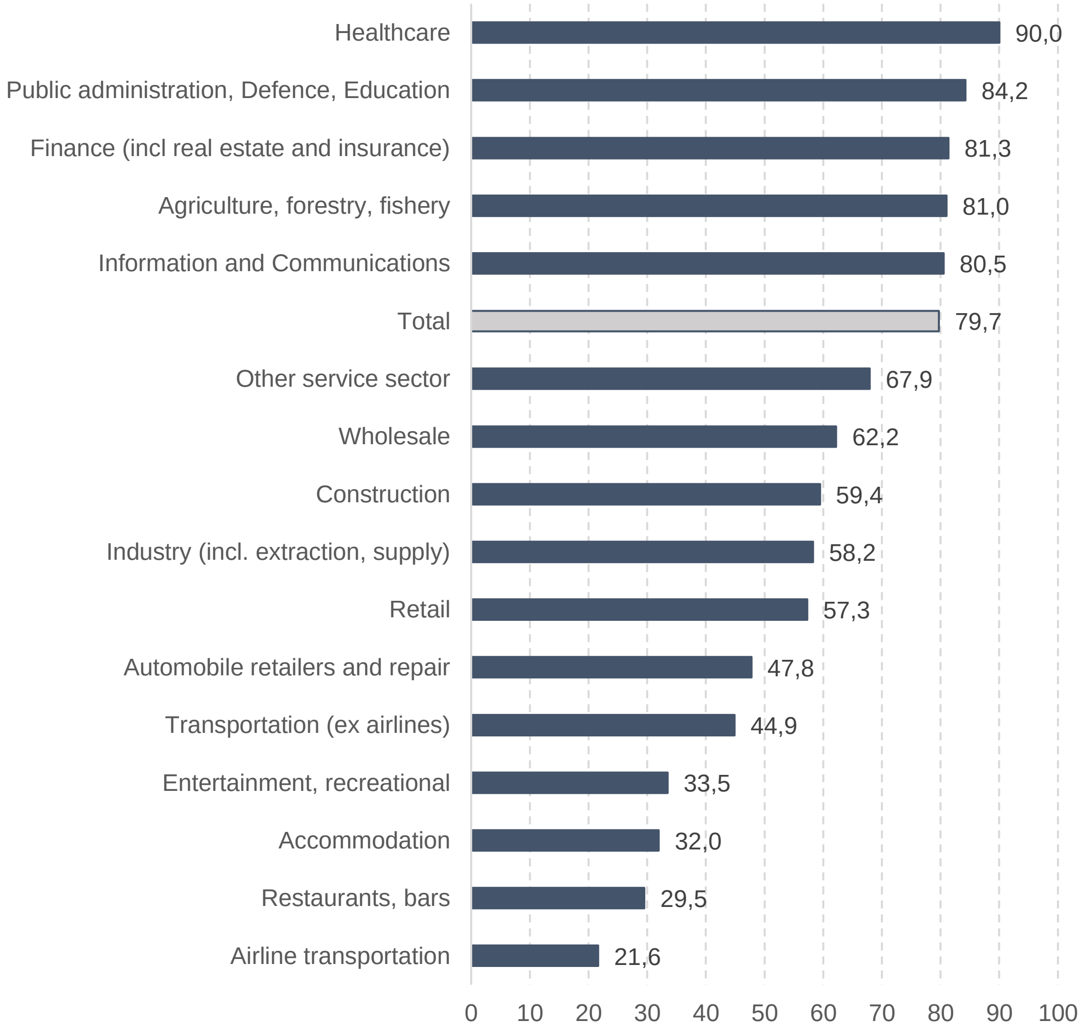
Any forecast for output in 2020 needs to recognise the 3 distinct phases we are likely to see within the EU:

Phase 1, **pre-lockdown** (January to Mid-March): Prior to EU lockdowns starting, we expect EU output to have been similar to the levels achieved in the final months of 2019. Whilst businesses were becoming increasingly concerned with potential supply chain issues from the lockdown in China, and continuing trade tensions were playing on business confidence, the EU economy was still growing.

Phase 2, full lockdown: As the virus spread over the first half of March, member states put in place lockdowns. Figure 2 shows that on average we expect these lockdowns, when in full force, to have reduced economic activity in the EU to around 80% of pre-crisis levels, although this figure will clearly vary between member states.

The lockdowns have caused widespread economic disruptions across all sectors and along supply lines. While the loss of output was unsurprisingly greatest in hospitality sectors (Accommodation, Restaurants, Bars, entertainment and recreative etc.), and in parts of the retail sector, other parts of the economy are also suffering, with Industry for instance operating at around 60% of normal output at the height of the lockdowns.

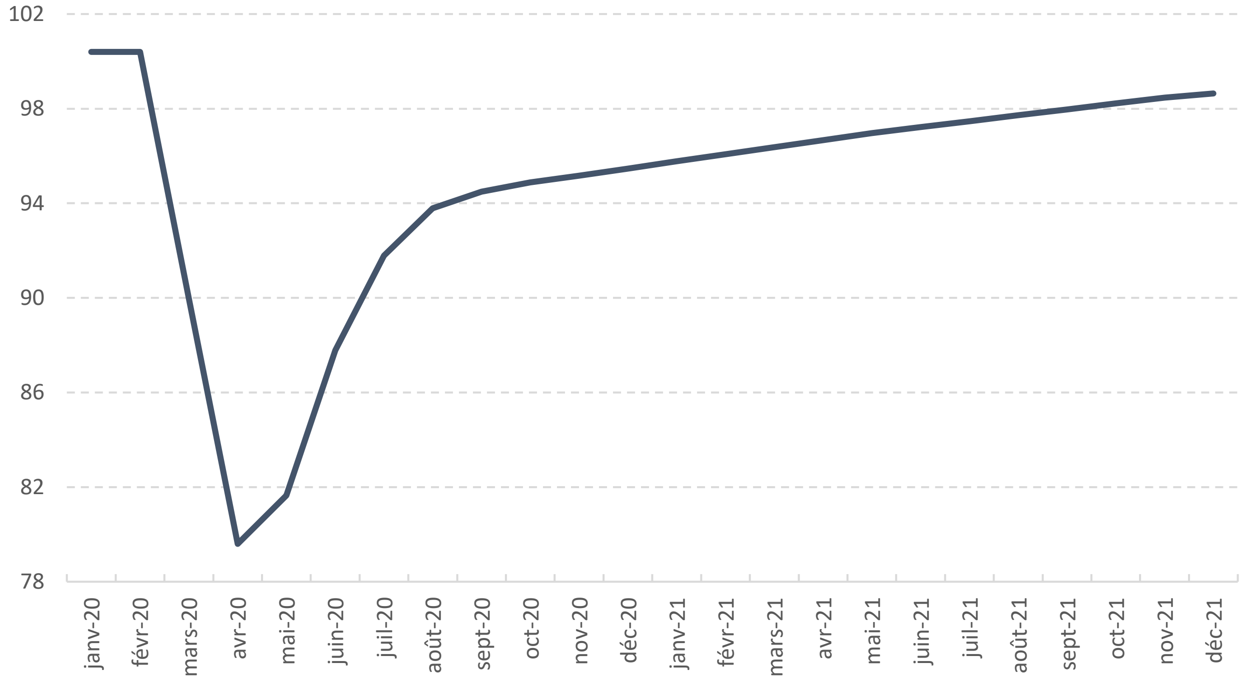
Figure 2: All sectors of the economy negatively affected
EU activity levels by sector during full lockdowns (2019-level=100%)



BusinessEurope Staff estimates, based on various national data and dialogue with national member federations monitoring the situation on the ground in each member state. Seasonally adjusted, GDP-weighted.

Phase 3: Easing of lockdowns and gradual recovery: As we publish this outlook, many member states are starting to slowly reduce the significant restrictions based on staged action plans. As a consequence, we expect economic activity to gradually increase from around 80% of pre-crisis levels to over 90% by the end of the summer (figure 3), and to grow through 2021, almost reaching pre-crisis levels by the end of that year.

Figure 3: The likely path towards a gradual recovery
Level of economic activity, 2019 average = 100 (seasonally adjusted)

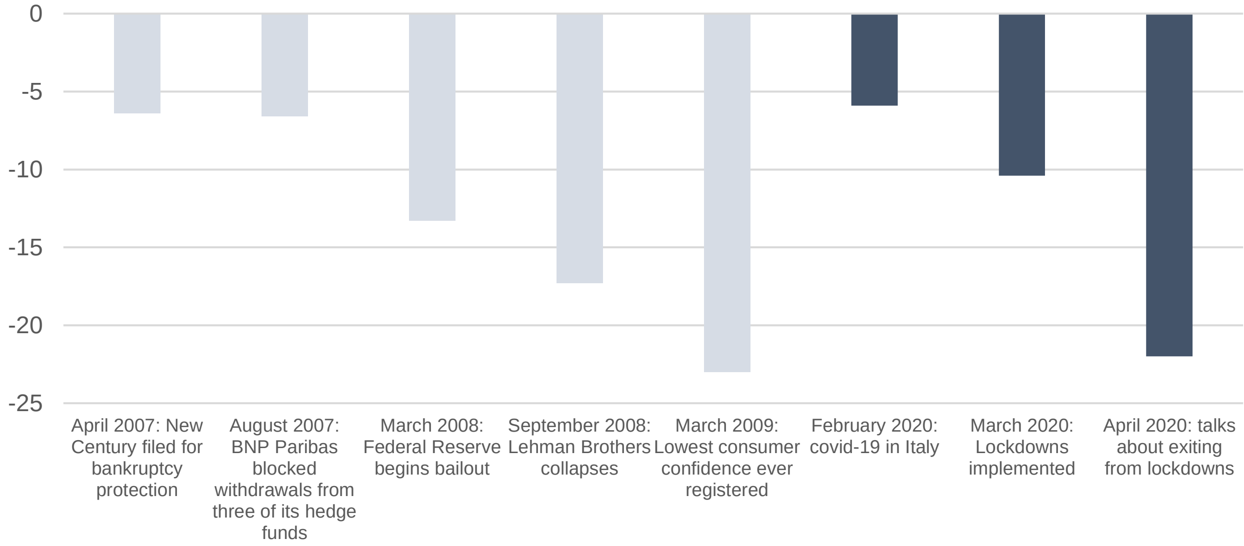


BusinessEurope staff estimates

But as noted above, such a scenario is subject to downside risks either that the increasing rates of transmission may not allow restrictions to be removed as planned, or that as second wave could lead to a re-imposition of some restrictions.

Moreover, even once most restrictions have been removed, it is clear that it will take some time for the economy to return to pre-crisis levels. As figure 4 shows, consumer confidence has fallen more quickly than during the financial crisis over the past two months, in line with people becoming increasingly concerned about their jobs and income, whilst measures of business confidence, such as the Purchasing Managers Composite Index, have seen similar dramatic falls. Looking more broadly, we expect business investment to be strongly reduced even after the summer, given continuing uncertainty and reduced demand, with limited demand impulse from export demand reflecting the global nature of the crisis.

Figure 4: Consumer confidence has fallen faster than during Financial Crisis
EU Consumer confidence levels at selected points in time



BusinessEurope staff based on European Commission data

We therefore expect a fall in output of 7.9% overall in 2020 followed by 5.8% growth in 2021. This corresponds to total EU GDP in 2021 being 2.6% below the total 2019 level.

Employment

Data already released shows only a marginal increase in EU unemployment in March, to 6.6% compared to 6.5% in February, with only a few countries, notably Spain, seeing a significant increase in joblessness. This contrast sharply with the experience of the US where unemployment rose from 3.5% in February to 4.4% in March and an extraordinary 14.7% in April. Such a small rise in the EU is the result of the rapid implementation of short-time work or 'furlough' schemes in many member states, ensuring that whilst people may not actually be at work, they remain under contract and not unemployed. The future path of unemployment will therefore depend on how such short-time works programmes evolve in the coming months, as well as the broader policy environment and overall demand. Ensuring people remain active in the labour market should be a policy priority in the coming months, given the reduced likelihood that people find work after a sustained period of unemployment. We remain concerned that without strong policy support for businesses and workers, unemployment levels could rise significantly above the 9% level the European Commission has forecasted for the EU in 2020, and will not return quickly to the 7.9% figure they forecast for 2021.

Country Differences

The depth of the recession and the strength of the ensuing recovery may also differ considerably between member states. For example, our members expect economic activity to have remained above 90% of pre-crisis levels in Germany, during what was a relatively short lockdown period, in contrast to countries such as France, Italy and Spain, where lockdowns were both lengthier, and where activity in some cases is estimated to have fallen below 70% of pre-crisis levels.

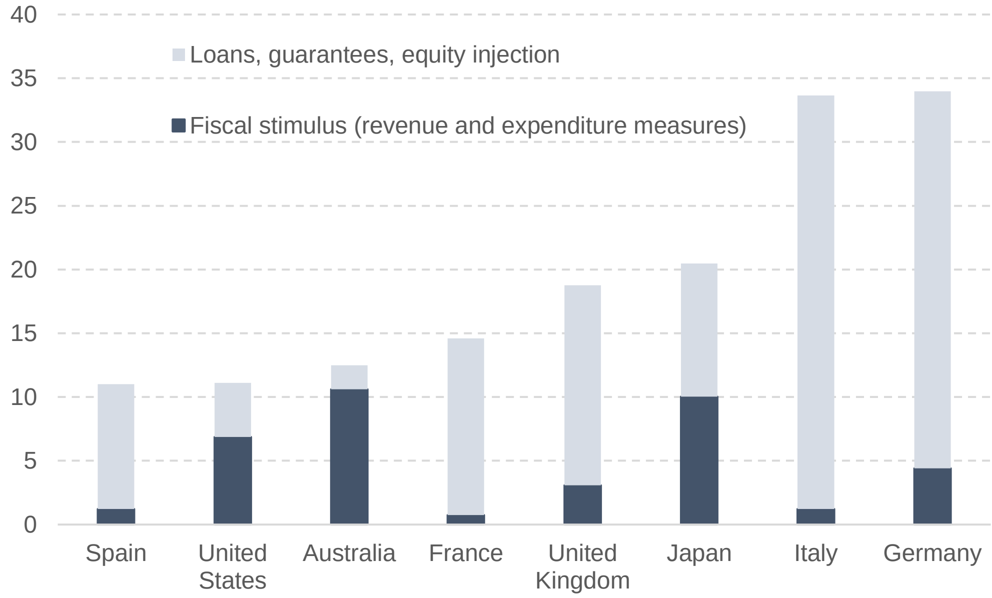
Looking forwards, whilst the restrictions on economic activity as we move into the summer are likely to be reduced, they are likely to become more focussed on sectors such as hospitality, travel and tourism, meaning countries that are traditionally reliant upon these sectors for a large share of output and employment, particularly through international travel, may be hit more strongly, particularly as broader concerns regarding employment and income prospects further reduce domestic consumer expenditure.

As strong and co-ordinated fiscal stimulus is needed to drive recovery

In recent months, we have seen an unprecedented response by the EU and member states alike to rapidly put in place essential measures to protect businesses and workers through this crisis. At member state level, we welcome support to retain workers through short time working schemes, measures to support lending to business, and other measures to offset costs such as tax postponements or reductions.

However, we believe further measures are needed to deliver a co-ordinated EU fiscal stimulus of the magnitude seen in other G7 economies. As figure 5 highlights, whilst EU member states have provided relatively large support through loans, equity injections and guarantees, actual direct revenue and expenditure have been relatively small in relation to out G7 competitors.

Figure 5: Fiscal response to the coronavirus stronger in the G7 than EU countries
Economic response to the downturn in the G7 economies (also showing Spain), % of GDP

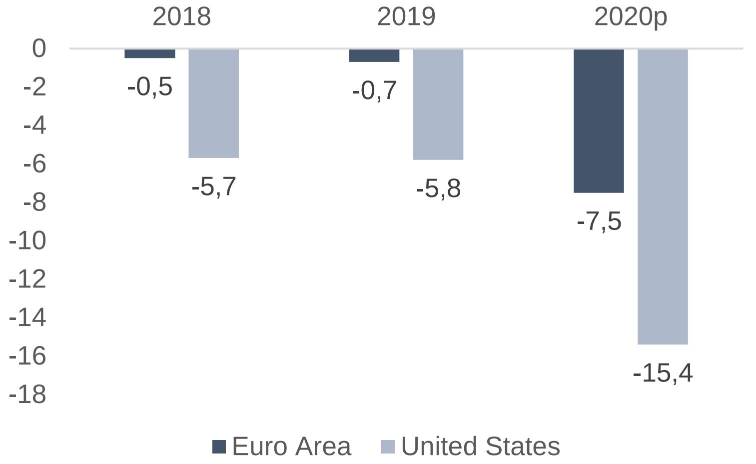


IMF Fiscal Monitor, April 2020. Note that some countries including Japan have passed additional stimulus measures

While discretionary spending fiscal stimulus is presently higher in the US than the EU, it is also the case that the automatic stabilisers of welfare benefits and lower taxes are much stronger in the EU than the US, necessitating a stronger discretionary response. Nevertheless, when we look at projected overall fiscal balances from the IMF (figure 6), which take account of both discretionary and automatic expnditure, the overall fiscal stimulus is likely to be much higher in the US.

Figure 6: The fiscal response has been much more forceful in the US than in the EU

General Government Overall Fiscal Balance, % of GDP

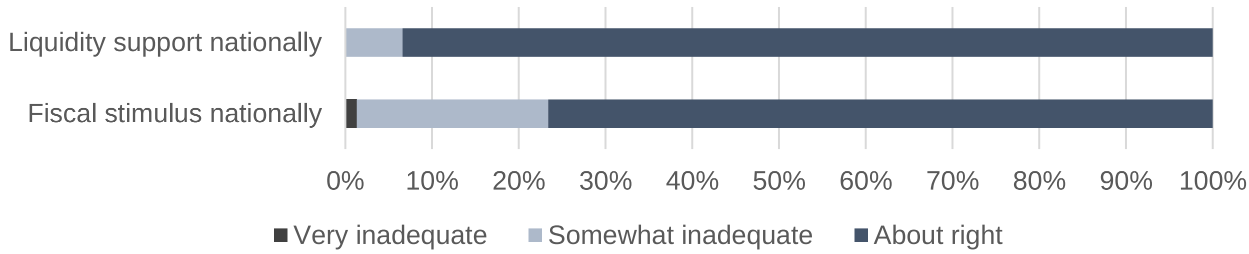


IMF Fiscal Monitor, April 2020, p: projection

This difference is reflected in how European business views the policy responses to the economic downturn that are expected at the national and EU level. As seen in figure 7 below, our member federations are largely satisfied with the liquidity provisions made in their country, but a significant proportion believe there is scope to increase the national fiscal stimulus.

Figure 7: The national response to COVID-19 would benefit from strengthening in large parts of the EU

Member federations' assessment of national policies to address the economic downturn

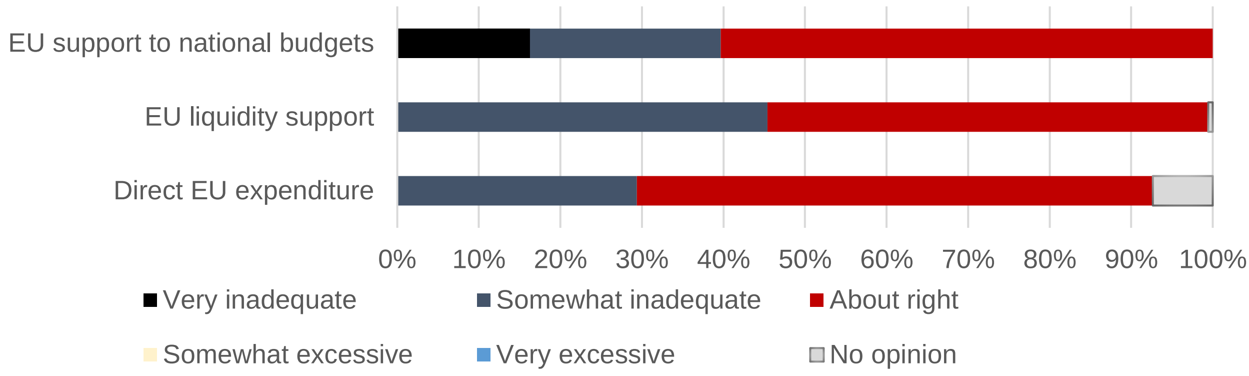


BusinessEurope staff calculations and estimates based on weighted average of policy evaluations from member federations. Only response categories used are shown

Similarly at EU level, we have seen a rapid policy response, both to increase flexibility in the interpretation of rules such as those relating to state aid and the Stability and Growth Pact, and to provide financial support, for example through the Commission €37 billlion Corona Response Investment Initiative, the development of an instrument, SURE, to support short-time working, increased EIB support, and the ECB's emergency fund and broader measures to support financial stability.

Nevertheless, as the figure below indicates, there remains significant scope to strengthen the EU economic response to the crisis. In particular, whilst the majority of our federations are largely satisfied with the EU's regulatory response to the crisis, as well as its plans for direct expenditure, a large number would like to the EU to play a more significant role in providing support to national budgets, through schemes such as the SURE.

Figure 8: European Business believes there remains scope to strengthen EU economic response to the crisis
Member federations' assessment of the EU's response to the economic downturn

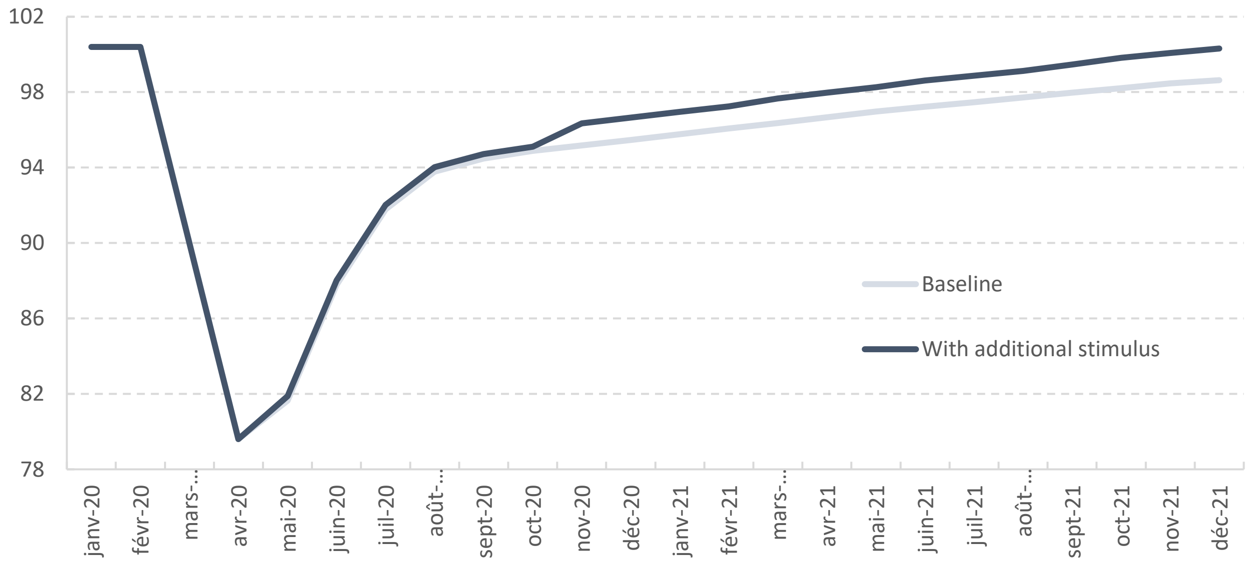


BusinessEurope staff calculations and estimates based on weighted average of policy evaluations from member federations

An increased fiscal stimulus would boost provide long-term benefits

Given the present uncertainty, we have worked with national member federations to also provide alternative growth forecasts in the event of a more significant fiscal stimulus than we are currently seeing, based on the scope ambitious yet not politically unrealistic additional stimulus could feasibly take. This is shown in figure 9.

Figure 9: Baseline forecast and forecast with ambitious additional stimulus
Level of economic activity, 2019=100, adjusting for seasonal variation



BusinessEurope staff estimates

Whilst as noted above, in our baseline scenario we expect EU27 GDP to be 2.6% below the 2019-level in 2021, in the event of a stronger, co-ordinated fiscal policy response, we forecast that the gap can be reduced to only 1.4%, setting the scene for a full recovery in 2022.

Figure 10: Additional fiscal stimulus can speed up the pace of the recovery
BusinessEurope central forecasts, GDP growth (real), %

	2020	2021	With this growth trajectory, 2021-GDP will be…
Baseline scenario	-7.9	5.8	2.6 below 2019-level
With additional stimulus	-7.6	6.7	1.4 below 2019-level

BusinessEurope spring 2020 economic forecast

BusinessEurope's Recovery Plan

It took the European Union six years to escape from the last major economic crisis. We cannot allow a repeat.

In these extraordinary times we must pay attention to the challenges and needs of businesses across the continent. Political ambition and willingness to drive reforms and support our economy is key to emerging from the crisis as unscathed as possible. To help guide political decision-makers to develop and find the right solutions to our predicament BusinessEurope has put forward a proposal for a recovery plan to steer our economy through these troubling times.

BusinessEurope's full proposals for a European Economic Recovery Plan is available online, and our proposals to kickstart the weakened European economy include:

- an ambitious and coordinated fiscal stimulus to support demand, a rapid deployment of EU investment funds as part of an ambitious and co-ordinated EU fiscal stimulus
- a revitalised and open single market and a strengthened single currency
- fair and free trade and investment and support for multilateral solutions
- strengthened EU governance to ensure EU financial support increases member states' implementation of growth and employment enhancing structural reforms and upward convergence.

Read more:

https://www.businesseurope.eu/publications/businesseurope-proposals-european-economic-recovery-plan

About this Outlook

BusinessEurope publishes a biannual Economic Outlook that provides business insight into recent and projected economic developments in Europe.

In producing our economic projections and assessing current challenges and developments in the international and regional economy, BusinessEurope works closely with its member federations and draws on their specialist expertise and detailed knowledge of their national economies and ongoing interactions with business.

In particular, our EU27 and Euro Area forecasting is informed by and reflects (GDP-weighted) economic forecasts, data and estimates the economic research departments of our national member federations. Our economic projections are therefore informed by leading country experts with in-depth knowledge and day-to-day monitoring of the economic situation in every EU member state.

General disclaimer

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BusinessEurope is the leading advocate for growth and competitiveness at the European level, standing up for companies across the continent and campaigning on the issues that most influence their performance. A recognised social partner, we speak for all-sized enterprises in 35 European countries whose national business federations are our direct members.

Austria	Belgium	Bulgaria	Croatia	Cyprus	Czech Republic
Denmark	Denmark	Estonia	Finland	France	Germany
Germany	Greece	Hungary	Iceland	Iceland	Ireland
Italy	Latvia	Lithuania	Luxembourg	Malta	Montenegro
Norway	Poland	Portugal	Rep. of San Marino	Romania	Serbia
Slovak Republic	Slovenia	Spain	Sweden	Switzerland	Switzerland
The Netherlands	Turkey	Turkey	United Kingdom		

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