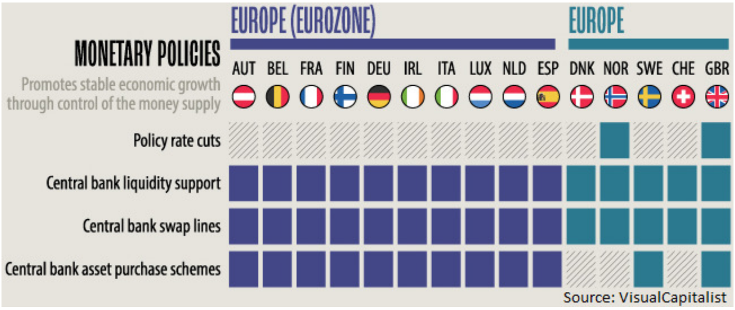
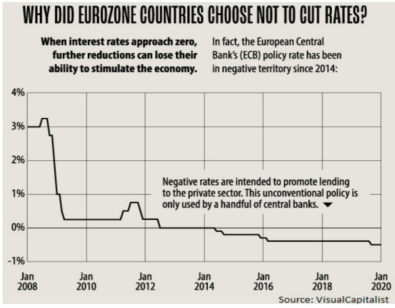
Renewed European Response

Emergency Support

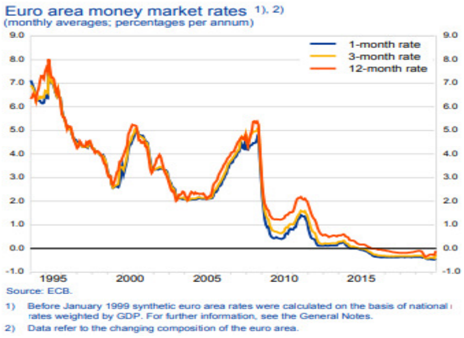
The euro area is facing an economic contraction of a magnitude and speed that are unprecedented in peacetime. Measures to contain the spread of the coronavirus (COVID-19) have largely halted economic activity in virtually all the countries of the euro area and across the globe. The collapse in activity is initially the strongest for services, particularly those related to travel and recreational activities. This has already been indicated by some of the available survey evidence. However, the lockdown measures and the ensuing supply bottlenecks reduced production dramatically across large segments of the industry.

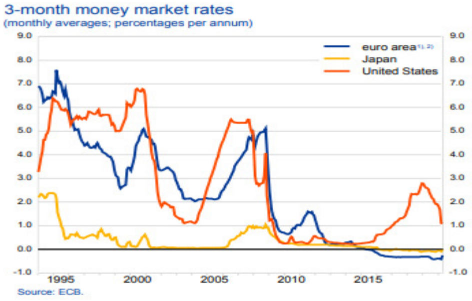
ECB President Christine Lagarde created the 750 billion euro Pandemic Emergency Purchase Program (PEPP) in March that, unlike vehicles created during the debt crisis in 2012, provides unlimited and unconditional support to member states to purchase private and public securities and will include all the asset categories eligible under the existing asset purchase programme. This program will expand the range of eligible assets under the corporate sector purchase programme (CSPP) and to ease the collateral standards. These measures are aimed at ensuring that all sectors of the economy can benefit from supportive financing conditions that enable them to absorb the Covid-19 shock. Thus, the ECB is supporting Italy's massive borrowing without conditions, thereby avoiding political turmoil. The purchase of assets under PEPP will be terminated once the Governing council judges that the corona virus crisis is over, but in no case before the end of the year.





In early March, when ECB announced a 120 billion euro to expand its asset purchase, it was widely expected that the bank would reduce lending rates by at least 10 basis points. However, with the rates already reduced to -0.5% in September of 2019, there was little room to do further. "Contrary to expectations, the ECB did not cut its deposit rate more deeply into negative territory. Instead, the ECB will buy more assets with a focus on private sector bonds and inject even more liquidity at even more favorable terms into the banking system," Holger Schmieding, economist at Berenberg, said in an email to CNBC. Experts have also argued that in comparison with other central banks, the ECB's toolkit is more constrained given that its rates are already in negative territory. Although, ECB announced in early March that European banks would be able to borrow money with an interest rate of -0.75%. This is meant to incentivize banks to lend money from the central bank and lend it to businesses and people.



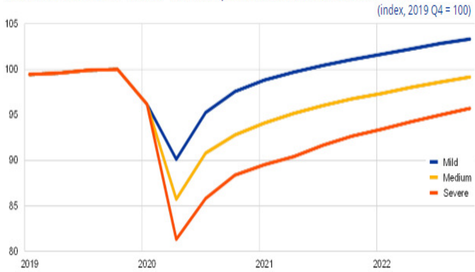


A study by the Peterson Institute says, "ECB purchases and bond holdings become the expression of a euro area fiscal solidarity, a shared fight against a common enemy that the ECB and European political leaders could not otherwise have contemplated out of fear of overstepping national sovereignty of member states." Thus, Christine Lagarde might be a modern-day Alexander Hamilton.

Gut Wrenching Recession

Christine Lagarde, President of the European Central Bank, said Wednesday that the euro zone economy could shrink up to 12% in the worst-case scenario. The decline will be at least 8%, Lagarde said, cautioning that "the mild scenario (5% decline) is out of date." According to ECB, overall, the containment measures are assumed to cause a relatively larger loss of value addition in retail trade, transport, accommodation and food service activities compared to manufacturing, construction and other sectors. Under the assumptions used for these illustrative scenarios, the marginal impact of an additional month of lockdown measures on the annual GDP level is initially, approximately, between 2 and 2½ percent according to ECB estimates. Given the high uncertainty surrounding the ultimate extent of the economic fallout, growth scenarios produced by ECB staff in April estimated that euro area GDP could fall by between 5% and 12% this year, depending crucially on the duration of the containment measures and the success of policies to mitigate the economic consequences for businesses and workers. As the containment measures are gradually lifted, these scenarios foresee a recovery in economic activity, although its speed and scale remain highly uncertain.

Euro area real GDP under the mild, medium and severe scenarios
(index, 2019 Q4 = 100)



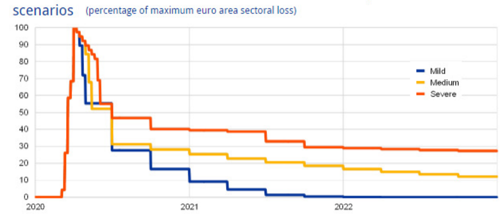
Source: ECB calculations.

Initial sectoral losses due to strict lockdown measures (percentage of gross value added)

Sector	Loss
Agriculture	10
Industry (excl. manufacturing and construction)	40
Manufacturing	40
Construction	40
Retail trade, transport, accommodation, food service activities	60
Information, communication	10
Financial and insurance activities	10
Real estate activities	20
Professional, scientific, administrative and technical activities	30
Public administration	10
Arts, entertainment, recreation and other activities	30

Source: ECB staff.
Note: Under these scenarios, the lockdown is assumed to have a softer sectoral impact (by around 20-30%) in the course of the second quarter of 2020 on account of agents' reaction (behavioural response) to minimise economic disruptions.

Time profile of indicative losses in gross value added implied by containment measures in the euro area under the mild, medium and severe scenarios (percentage of maximum euro area sectoral loss)



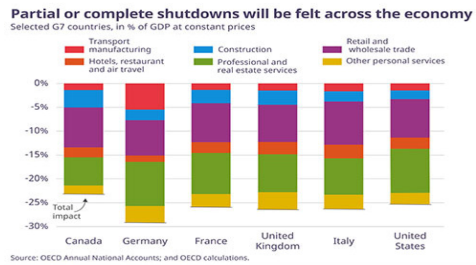
Source: ECB calculations.
Note: Losses are measured relative to the maximum sectoral losses for the euro area, computed as a weighted average of the losses for the largest five euro area countries.

As a result of the pandemic, the global economy is projected to contract sharply by 3 percent in 2020 according to IMF estimates released in April, much worse than during the 2008–09 financial crisis. In a baseline scenario, which assumes that the pandemic fades in the second half of 2020 and containment efforts can be gradually unwound, IMF expects the Euro Area economy to grow by 4.7 percent in 2021 after a steep decline of 7.5% in 2020 as economic activity normalizes, helped by policy support.

Many countries face a multi-layered crisis comprising a health shock, domestic economic disruptions and plummeting external demand. Necessary measures to reduce contagion and protect lives will take a short-term toll on economic activity but should also be seen as an important investment in long-term human and economic health. Because the economic fallout reflects particularly acute shocks in specific sectors, policymakers will need to implement substantial targeted fiscal, monetary, and financial market measures to support affected households and businesses the report added. Such actions will help maintain economic relationships throughout the shutdown and are essential to enable activity to gradually normalize once the pandemic abates and containment measures are lifted.

Overview of the *World Economic Outlook* Projections		Projections		Difference from January 2020 WEO *Update*[1]		Difference from October 2019 WEO[1]	
	2019	2020	2021	2020	2021	2020	2021
World Output	**2.9**	**–3.0**	**5.8**	**–6.3**	**2.4**	**–6.4**	**2.2**
Advanced Economies	**1.7**	**–6.1**	**4.5**	**–7.7**	**2.9**	**–7.8**	**2.9**
United States	2.3	–5.9	4.7	–7.9	3.0	–8.0	3.0
Euro Area	1.2	–7.5	4.7	–8.8	3.3	–8.9	3.3
Germany	0.6	–7.0	5.2	–8.1	3.8	–8.2	3.8
France	1.3	–7.2	4.5	–8.5	3.2	–8.5	3.2
Italy	0.3	–9.1	4.8	–9.6	4.1	–9.6	4.0
Spain	2.0	–8.0	4.3	–9.6	2.7	–9.8	2.6
Japan	0.7	–5.2	3.0	–5.9	2.5	–5.7	2.5
United Kingdom	1.4	–6.5	4.0	–7.9	2.5	–7.9	2.5
Canada	1.6	–6.2	4.2	–8.0	2.4	–8.0	2.4
Other Advanced Economies[2]	1.7	–4.6	4.5	–6.5	2.1	–6.6	2.2
Emerging Market and Developing Economies	**3.7**	**–1.0**	**6.6**	**–5.4**	**2.0**	**–5.6**	**1.8**

Source: IMF

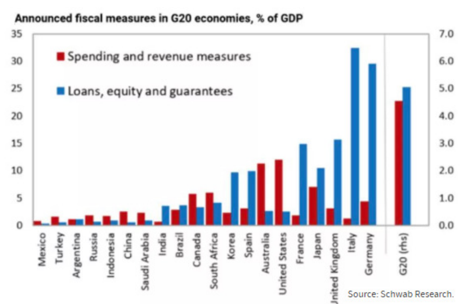


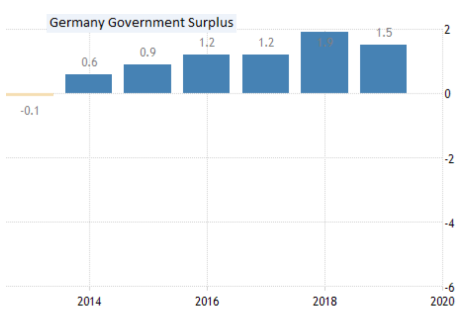
Source: OECD

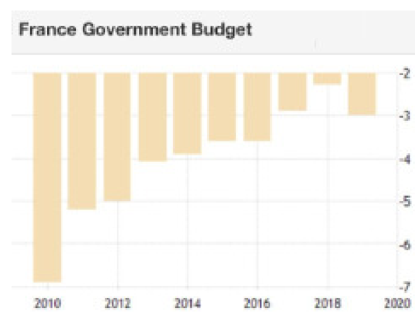
For each month of containment, there will be a loss of 2 percentage points in annual GDP growth according to revised OECD estimates released on March 27. The tourism sector alone faces an output decrease as high as 70%. OECD reckons, many economies will fall into recession - this is unavoidable, as we need to continue fighting the pandemic, while at the same time putting all the efforts to be able to restore economic normality as fast as possible. There will also be some variation in the timing of the initial impact on output across economies, reflecting differences in the timing and degree of containment measures.

Acting in Unison

The European Union on Wednesday unveiled a €750 billion economic recovery program with the objective of protecting the lives and livelihoods, repair the market as well as to build a lasting and prosperous recovery as the region attempts to claw its way back from its worst economic crisis in decades; if negotiations between all 27 member economies are successful, the plan could represent a major step toward unifying the bloc's financial systems. Under the new plan, the EU will borrow €750 billion by issuing long-term government bonds on international markets which it will then distribute via €500 billion in grants to every member state and €250 billion available for loans (member countries must apply individually to be eligible for the loans, which will carry conditions and restrictions). Talking about taking a new bold step together toward collective recovery, President of the European Commission Ursula Von Der Leyen in her speech emphasized on unity and said a struggling economy in one part of Europe weakens an economy in the other part.







Source: Trading Economics

Source: Trading Economics

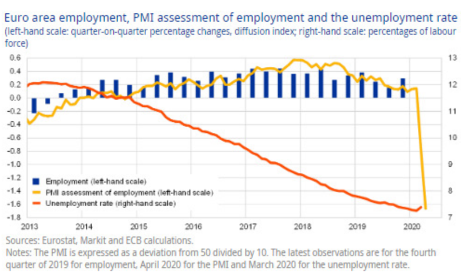
The grants are likely to be a sticking point in negotiations for the EU's wealthier nations like the Netherlands and Sweden, the New York Times reported. Germany and France, the two powerhouses, however, are in favor of the grants—those two nations issued a proposal for a similarly structured relief package last week. It was a historic step for Germany, who have in the past opposed the idea of jointly issued debt between EU economies. The EU's member states will meet on June 18, 2020, to begin hashing out the details of the recovery plan. One senior Dutch official told CNBC that negotiations aren't likely to be easy: "The positions are far apart and this is a unanimity file, so negotiations will take time. It's difficult to imagine this proposal will be the end-state of those negotiations."

Curbing Unemployment

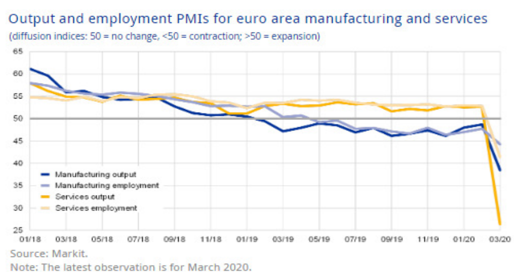
For enhanced cooperation, the EU finance ministers agreed a €500bn rescue package to guarantee spending by indebted countries and national short time working schemes in the second week of April for European countries badly impacted by the corona virus crisis. However, EU ministers chose not to back a demand from France and Italy to create so called "coronabonds", after continued resistance from some countries towards the idea of sharing out the cost of the crisis. The half trillion euro package agreed was less than the 1.5 trillion euro which the European Central Bank suggested the bloc might need to tackle the crisis.

Like never before, European countries are relying on programs that encourage struggling companies to retain employees but reduce their working hours. The state then subsidizes a portion of their pay, in some countries paying as much as 80% of average wages. Job programs are keeping hard hit businesses across Europe afloat, preventing millions of workers from losing their jobs and income for now, and thousands of bosses from seeing their trained staff scatter.

In Europe, much of the fiscal ammunition has been spent on directly supporting businesses that have kept workers formally "employed" in their original jobs, even if they are no longer working full time. For example, in Germany, the short-time working scheme - or Kurzarbeit - has already replaced up to 60 per cent of earnings for 10m employees (data as on May 17, Financial Times) who might otherwise have lost their jobs. This scheme worked well after the 2008 financial crisis and is now being copied by other European countries. In the UK, the coronavirus job retention scheme has replaced 80 per cent of lost earnings for 7.5m employees, up to a maximum of £2,500 a month. Chancellor Rishi Sunak has sensibly announced that a version of this scheme will remain in place at least until the end of October. Without such schemes, lay-offs and redundancies in Europe would already have been vastly greater.

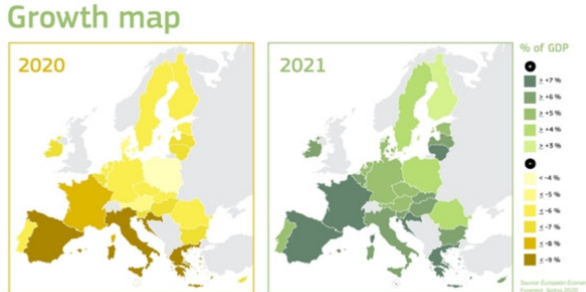


Source: Eurostat



Source: Markit

Some 11.3 million workers in France are getting up to 84% of net salary. The government estimates the cost at 24 billion euros ($26 billion), with half of all private sector employees expected to take part (figures as reported by Associated Press, April 30). In Germany, some 10 million workers are being supported, with the government paying up to 60% of their net salary if they are temporarily put on shorter or zero hours. Those with children get 67%, and many companies such as Volkswagen add more. The impact of the pandemic and the cushioning provided by such short-work programs were underlined in reports released in late April showing the unemployment rate in the 19-country eurozone edged up only by a tenth of a point to 7.4% in March despite a record economic contraction. CNN reported earlier this month, nearly 39 million people are being paid by governments to work part time or not at all – a record level of support that will shape the way the economy comes out of the pandemic.

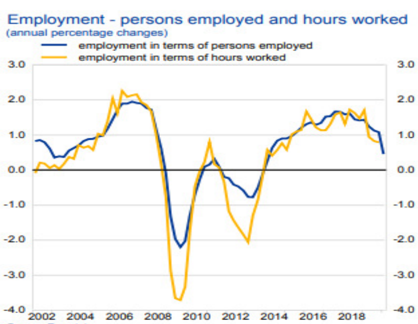


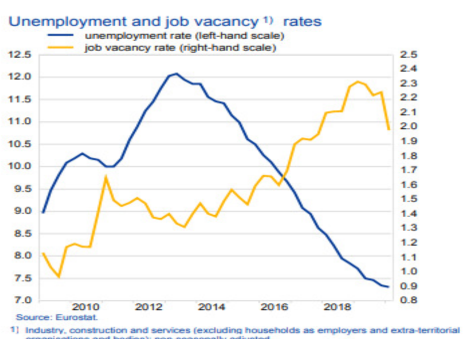
Source: Moody's, FT

Source: European Commission

The work support programs are different from jobless benefits. They are only for temporary shutdowns that are due to no fault of the business itself. Such programs can't save jobs that disappear due to long-term slowdowns in customer demand or to technological changes. But it gives workers and bosses breathing space and hope, preventing the unnecessary destruction of viable businesses. This could give Europe a leg up in its recovery, allowing economies in the region to restart quickly and efficiently as demand rebounds. Yet problems could arise if activity isn't as resilient as expected. People may need convincing to leave their homes to go shopping regularly, and working from home is expected to continue for some time.

Employment data for the second quarter of 2020 are not yet available. The unemployment rate declined to 7.3% in February, a similar rate to that observed before the financial crisis. However, it just increased tepidly to 7.4% in March, the first month affected by the spread of COVID-19 and the subsequent implementation of containment measures across the euro area. The muted reaction of unemployment may be related to measures to ease access to short-time work schemes. Preliminary estimates show an unprecedented number of employees in these schemes across the five largest euro area countries. While the situation has worsened for all major regional groups, estimates indicate that Europe and Central Asia will experience the greatest loss in working hours (11.8 percent) second only to Americas (12.4 percent) according to the latest ILO estimates released in April.



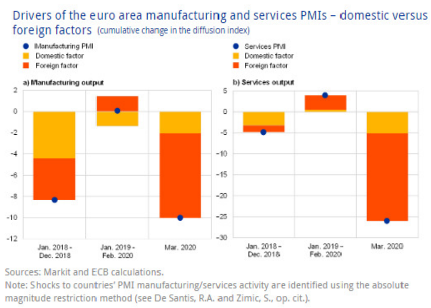


'May' Modest Recovery

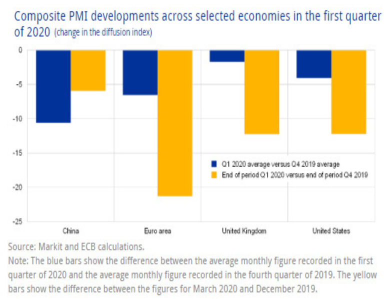
Although services are less trade-intensive, they have become strongly correlated globally owing to the pandemic and the common measures which have been taken to contain it. The econometric model of ECB attributes a large fraction of the collapse in the manufacturing and services output PMIs for the euro area in March to the foreign factor, which is likely to reflect the fall in global trade and the lagged impact of the global slowdown given the sharp drop in economic activity in China in February. It is worth pointing out, however, that the euro area domestic factors also account for a significant part of the decline in both sectors in March 2020.

The flash IHS Markit Eurozone Composite PMI rose from an all-time low of 13.6 in April to 30.5 in May, highest since February. By remaining well below 50 (no-change level), the PMI registered a third successive monthly fall in output and continued to indicate a rate of contraction in excess of anything seen prior to the COVID-19 outbreak. The prior low of 36.2

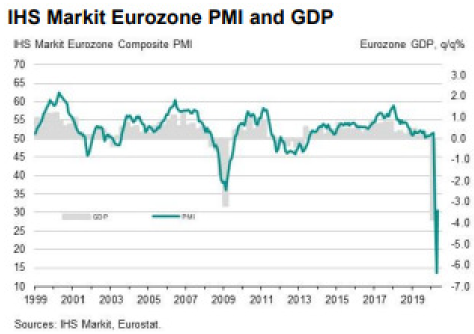
was seen during the peak of the global financial crisis in February 2009. The rise in the PMI in May nevertheless indicated a markedly slower pace of contraction compared to April's record collapse. Rates of decline eased in manufacturing and services, reflecting both a reduction in the number of companies reporting lower activity and an increase in the number of firms reporting an improvement.



Source: Market and ECB Calculations

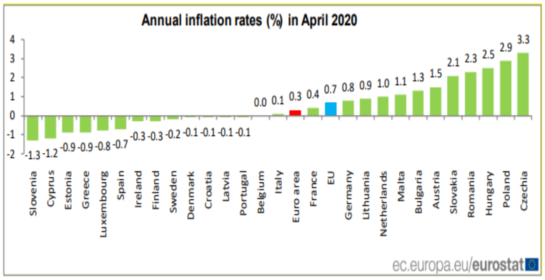


Source: Market and ECB Calculations

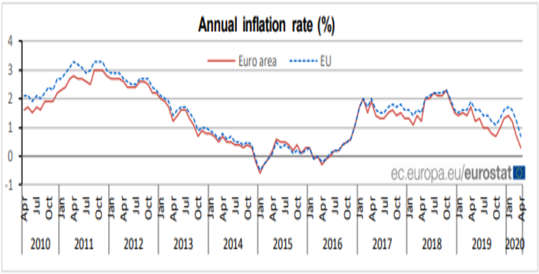


Subdued Inflation

Inflation has declined as a result of the sharp fall in oil prices and slightly lower HICP inflation excluding energy and food - In April 2020, containment measures in all countries, the euro area annual inflation rate was 0.3%, down from 0.7% in March; a year earlier, the rate was 1.7%. European Union annual inflation was 0.7% in April 2020, down from 1.2% in March. "Europe is experiencing an economic shock without precedent since the Great Depression," European Commissioner for Economic and Financial Affairs Paolo Gentiloni said adding, as the European economy contracts this year, consumer prices will almost stagnate, the Commission forecast. The inflation rate will slow to 0.2% in 2020, before accelerating to 1.1% next year. Samuel Tombs, chief UK economist at Pantheon Macroeconomics, said the figures indicated that inflation had taken a "big leap towards zero by the summer" with retailers already planning further, large price cuts.



Source: Eurostat



Source: Eurostat

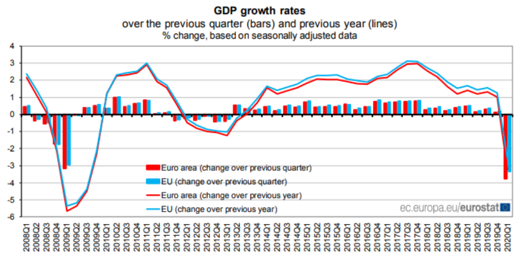
Costing Arm & Leg

The widespread increase of COVID-19 has shifted the world's hustle into varying degrees of uncertainty. One of the few things that seem fairly certain is that the current downturn is fundamentally different from the recessions of the past and not just another downturn in business cycle but a shakeup of world economic order. While nations and businesses comprehend the scale of this pandemic and how to respond, it is undeniable that we are staring at more permanent, structural changes in the way we live and work. The first question we need to ask is - how will we resolve the conflict between social isolation and economic recovery? The longer people stay at home, the more difficult it will be to bring the economy back to life. But the sooner they return to their daily lives, the harder it will be to get the disease under control.

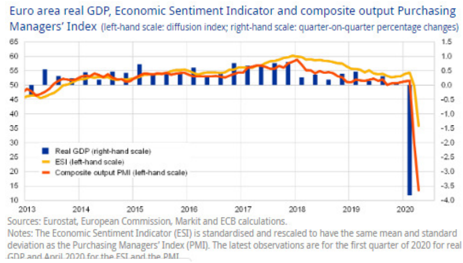
Seasonally adjusted GDP decreased by 3.8% in the euro area and by 3.3% in the EU during the first quarter of 2020, compared with the previous quarter, according to a flash estimate published by Eurostat, the statistical office of the European Union.

These were the sharpest declines observed since time series started in 1995. In the fourth quarter of 2019, GDP had grown by 0.1% in the euro area and by 0.2% in the EU. The shock to the EU economy is symmetric in that the pandemic has hit all Member States, but both the drop in output in 2020 (from -4¼% in Poland to -9¾% in Greece) and the strength of the rebound in 2021 are set to differ markedly.

Each Member State's economic recovery will depend not only on the evolution of the pandemic in that country, but also on the structure of their economies and their capacity to respond with stabilising policies. Valdis Dombrovskis, Executive Vice-President for 'An Economy that works for People', one of the six priorities for European Commission, said: "At this stage, we can only tentatively map out the scale and gravity of the coronavirus shock to our economies. While the immediate fallout will be far more severe for the global economy than the financial crisis, the depth of the impact will depend on the evolution of the pandemic, our ability to safely restart economic activity and to rebound thereafter." Given the interdependence of EU economies, the dynamics of the recovery in each Member State will also affect the strength of the recovery of other Member States.



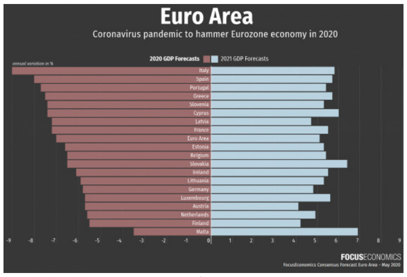
Source: Eurostat



Source: Eurostat

To overcome this pandemic, we need a global, coordinated health and economic policy effort. The IMF in collaboration with other partners—is doing everything it can to ensure rapid support is available to impacted countries through emergency financing, policy advice, and technical assistance. The rebound in 2021 depends critically on the pandemic fading in the second half of 2020, allowing containment efforts to be gradually scaled back and restoring consumer and investor confidence. Significant economic policy actions have already been taken across the world, focused on accommodating public health care requirements, while limiting the amplification to economic activity and the financial system. The level of GDP at the end of 2021 in both advanced and emerging market and developing economies is expected to remain below the pre-virus baseline.

Preliminary figures from Focus Economics published in May showed the economy suffered its worst contraction on record in the first quarter. The downturn came on the back of frozen business and household activity in the better part of March due to measures adopted by governments to contain the spread of the pandemic. According to data from national statistical institutes, Covid-19 wrecked havoc on both domestic and external demand in France, Italy and Spain, while contractions in smaller Eurozone economies were sizeable but less severe. Prospects for the second quarter are even bleaker, due to protracted lockdown measures, with a bigger blow to activity expected, as suggested by collapsing consumer and business confidence and a diving PMI reading in April. Focus Economics sees the economy contracting 7.0% in 2020, which is down 2.9 percentage points from last month's forecast. In 2021, GDP is seen increasing 5.1% as per their estimates. GlobalData, an independent agency estimated UK's economy to decline by 5.4%, France's by 6.0% and Germany's by 5.2% in 2020.



Source: Focus Economics

Disclosure & Disclaimer

CD Equisearch Private Limited (hereinafter referred to as **'CD Equi'**) is a Member registered with National Stock Exchange of India Limited, Bombay Stock Exchange Limited and Metropolitan Stock Exchange of India Limited (Formerly known as MCX Stock Exchange Limited). CD Equi is also registered as Depository Participant with CDSL and AMFI registered Mutual Fund Advisor. The associates of CD Equi are engaged in activities relating to NBFC-ND - Financing and Investment, Commodity Broking, Real Estate, etc.

CD Equi is registered under SEBI (Research Analysts) Regulations, 2014 with SEBI Registration no INH300002274. Further, CD Equi hereby declares that –

- No disciplinary action has been taken against CD Equi by any of the regulatory authorities.
- CD Equi/its associates/research analysts do not have any financial interest/beneficial interest of more than one percent/material conflict of interest in the subject company(s) **(*kindly disclose if otherwise*)**.
- CD Equi/its associates/research analysts have not received any compensation from the subject company(s) during the past twelve months.
- CD Equi/its research analysts has not served as an officer, director or employee of company covered by analysts and has not been engaged in market making activity of the company covered by analysts.

This document is solely for the personal information of the recipient and must not be singularly used as the basis of any investment decision. Nothing in this document should be construed as investment or financial advice. Each recipient of this document should make such investigations as they deem necessary to arrive at an independent evaluation of an investment in the securities of the companies referred to in this document (including the merits and risks involved) and should consult their own advisors to determine the merits and risks of such an investment.

Reports based on technical and derivative analysis center on studying charts of a stock's price movement, outstanding positions and trading volume, as opposed to focusing on a company's fundamentals and as such, may not match with a report on a company's fundamentals.

The information in this document has been printed on the basis of publicly available information, internal data and other reliable sources believed to be true but we do not represent that it is accurate or complete and it should not be relied on as such, as this document is for general guidance only. CD Equi or any of its affiliates/group companies shall not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. CD Equi has not independently verified all the information contained within this document. Accordingly, we cannot testify nor make any representation or warranty, express or implied, to the accuracy, contents or data contained within this document.

While, CD Equi endeavors to update on a reasonable basis the information discussed in this material, there may be regulatory compliance or other reasons that prevent us from doing so.

This document is being supplied to you solely for your information and its contents, information or data may not be reproduced, redistributed or passed on, directly or indirectly. Neither, CD Equi nor its directors, employees or affiliates shall be liable for any loss or damage that may arise from or in connection with the use of this information.

CD Equisearch Private Limited (CIN: U67120WB1995PTC071521)
Registered Office: 37, Shakespeare Sarani, 3rd Floor, Kolkata – 700 017; Phone: +91(33) 4488 0000; Fax: +91(33) 2289 2557 Corporate Office: 10, Vasawani Mansion, 5th Floor, DinshawWachha Road, Churchgate, Mumbai – 400 020. Phone: +91(22) 2283 0652/0653; Fax: +91(22) 2283, 2276
Website: www.cdequi.com; Email: research@cdequi.com