

# Global Macro Matters

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## Five Big Themes that Will Frame the Post-Virus Economy



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*The great American philosopher Yogi Berra once said, “It’s tough to make predictions, especially about the future.” If anything, Berra’s quip understates the challenges of figuring out where the global economy is headed at this unprecedented time. But taking a stand on such issues is the unavoidable task of economists and, more concretely, of investors as they look to put money to work.*

*In that spirit, we turn to the question of how global economic conditions—after the virus has receded (whenever and however that occurs)—will differ from those that prevailed before. While our crystal ball is admittedly cloudy, we see five big themes that are likely to characterize the post-virus economy and markets.*

**First**, the economy will be plagued by some painful hangovers. Workers who have lost their jobs are seeing their skills deteriorate. Some otherwise productive firms are being forced out of business by the extraordinary conditions. And, to fight the shock, enormous monetary and fiscal support is being implemented; this effort, while necessary, is likely to leave [government debt levels](#) and central bank balance sheets bloated.

In some respects, the situation will be reminiscent of the aftermath of the global financial crisis. Then, unemployment was high, bankruptcies were elevated, and monetary and fiscal tools were fully deployed. As the recovery progressed, the supply side and the demand side of the economy slowly normalized. This allowed workers to return to employment, existing firms to expand, and new firms to be created. However, central banks and governments, particularly in the advanced economies, made little progress getting policy settings back to their pre-crisis trajectories.

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How relevant is that experience? The answer depends on how quickly the pandemic abates and the recovery begins. On the favorable side of the ledger, the current downturn has been caused by a virus, rather than by accumulated economic and financial imbalances. As such, things may be less out of whack than after the GFC and bounce back more quickly. We may already be seeing some early signs of this as the stronger-than-expected May payroll report in the U.S. might attest. On the other side of the ledger, the depth of the global contraction has been unprecedentedly severe. And, in any event, we see little inclination to bring down bloated public debt levels in the years ahead and correspondingly little scope for central banks to normalize rates or reduce the size of their balance sheets. Concerningly, this may leave less scope to tackle subsequent periods of economic turbulence.

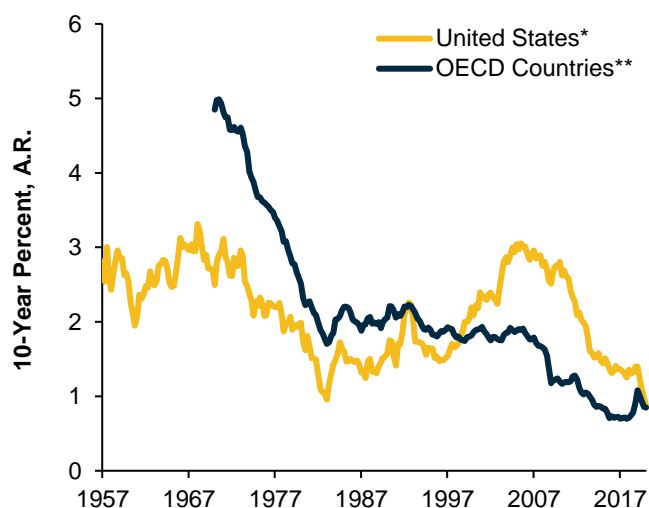
**Second**, the post-virus economy will bring [winners and losers across sectors](#). The virus-related shutdowns brought profound changes in the distribution of production and consumer spending. The resulting rebalancing of the economy will create an ongoing “relative value” trade for investors. The winners will likely be many virtual technologies that bring people together, provide entertainment, or that offer information, education, or services. Even more than before the virus, the tech sector will represent critical infrastructure that is central to the economy. Similarly, the experience in recent months has underscored that households have highly inelastic demand for certain staples, including food, paper products, cleaning supplies, and pharmaceuticals. These sectors are likely to continue to perform well.

The losers coming out of the crisis will be service providers that depend on face-to-face contact. This will reflect both lingering health concerns and, more fundamentally, that people are finding ways to interact and conduct business that require less physical contact. The losing sectors are likely to be airlines, sit-down restaurants, hotels, theme parks, and other industries that bring together large groups of people. Bricks-and-mortar retail will continue to lose ground to e-commerce, as consumers are increasingly attracted by the convenience.

**Third**, and more speculatively, this sectoral rebalancing may bring a resurgence in [productivity growth](#). We see this as a key upside risk to the outlook. Recent years have brought a proliferation of impressive technologies—smart

phones, accelerating computing power, big data, artificial intelligence, genomics, brain science, etc. Nevertheless, productivity growth over the past decade has been the slowest of the post-war era. As shown in Figure 1, this is true not only in the United States but in other OECD countries as well.

**Figure 1: Labor Productivity Growth**



\*Output per hour; \*\*Output per worker

Source: PGIM Fixed Income, U.S. Bureau of Labor Statistics, and OECD

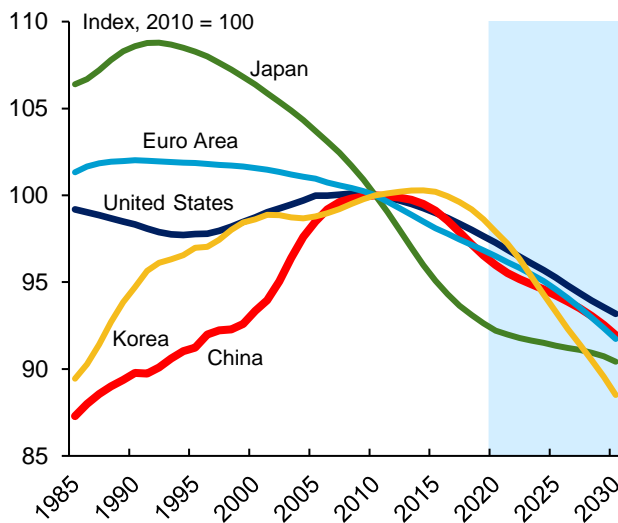
We hypothesize that the current episode may be driving a transition to a more productive economy. While working from home during the quarantines, people have paid the fixed costs of learning and applying new technologies to their work. Although these technologies will not fully replace face-to-face contact, they will remain in use once the virus has passed. In many cases, they will allow jobs to be done more efficiently and will raise levels of worker productivity. In short, the exigencies of the virus may have created massive network externalities by coordinating adoption of key technologies across the economy.

**Fourth**, at least in the United States, the unequal incidence of the virus across economic cohorts is likely to stoke [ongoing frustrations about inequality](#). The data clearly indicate that poorer communities have borne the brunt of the virus’ wrath—reflecting, for example, that these populations faced greater health challenges and sickness before the virus hit and, in many cases, lived in dense households or communities that aided the virus’ spread. Moreover, lower paid workers have been more likely to lose their jobs or hold positions that were deemed “essential” and, thus, more exposed to the risk of

infection. These realities are no doubt amplifying the frustrations expressed in the recent protests across the United States. These issues are likely to echo in the political theatre in the years ahead.

**Fifth**, deep [demographic trends](#) will continue to shape global economic performance. As highlighted in Figure 2, the growth rate of the working-age population (ages 16-64) will slow or contract across the advanced economies during the coming decade, and among the emerging markets, China and Korea will feel contractions as well. Many other EM economies will also see slower growth than in previous decades.

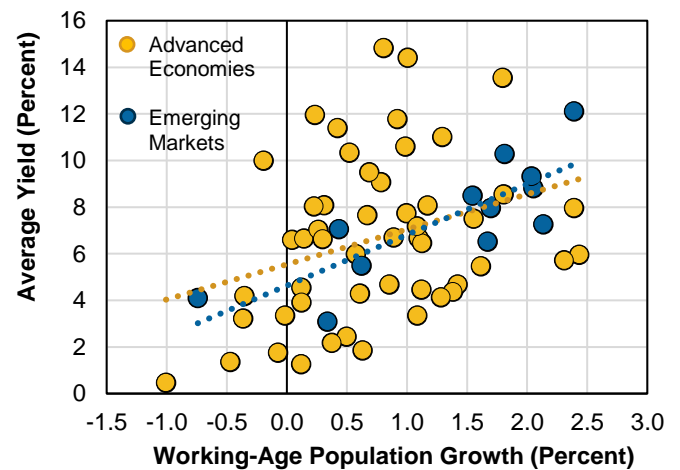
**Figure 2: Aging Demographics—Working Age Population\***



\*Share of total population ages 16-64 years. Source: United Nations

Notably, our previous research found that aging demographics are associated with weaker real GDP growth and lower inflation. Further, as shown in Figure 3, slower working-age population growth is also associated with lower long-term nominal bond yields, likely reflecting a softer economy and, particularly, reduced inflation and inflation expectations.

**Figure 3: 10-year Bond Yields and Population Growth**



Note: Decadal averages (1960s-2010s) for nine advanced and six emerging markets. Source: PGIM Fixed Income, United Nations, and Haver Analytics

Our view is that the aging of the global population was a powerful factor influencing the global economy and markets in the decade before the virus erupted, and that trend seems poised to continue. In this sense, we see the post-virus world as carrying forward many of the demographically-related themes that have characterized the past decade—restrained global growth, low inflation (which will require central banks to remain stimulative), and low long-term interest rates. This, in turn, should translate into a low volatility macro-financial environment, with many of the key uncertainties emanating—as in recent years—from political developments.

## Conclusion

Each of these five big themes is powerful taken individually. Occurring in tandem, these forces promise to create a global economy that differs in some important ways from before the virus. Navigating these shifting rapids will require investors to remain alert and to respond adroitly to the evolving circumstances.

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