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2020 Bilateral exports: The great variation

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- All German export markets will be hit hard by the COVID-19 crisis. However, we foresee great variation among key countries. Many markets that were already facing headwinds before the COVID-19 crisis – for instance, the UK and Italy – seem to have experienced a more a severe health crisis than others. Hence, we expect annual exports to both countries to decline by around 25% in 2020. Similarly, large contractions in German exports are also expected for France, Spain and the euro area as a whole.
- By contrast, exports to Asia may emerge relatively unscathed from the COVID-19 crisis. China, Japan and South Korea managed the crisis fairly well, and exports to these countries contracted only slightly in the first quarter. For these countries the relatively stable Asian demand might be less of a trade barrier than the shutdown of production facilities in Europe and the US. As these facilities increase their production capacity over the course of the year, annual exports to Asian countries may contract only marginally in 2020.
- Exports to the US are widely expected to shrink by around 10% in 2020. However, we consider this assessment highly uncertain. First, exports remained relatively stable in the first quarter. But the epidemiological crisis hit the country in late March and given the collapse of the US labor market, Q2 exports are set to nosedive. Second, in the US the corona crisis has not peaked yet, and the planned reopening of the economy might be riskier in the US than in other countries with flatter epi curves. Hence, the risk of a new wave of infections and new lockdown measures could be higher in the US than elsewhere.

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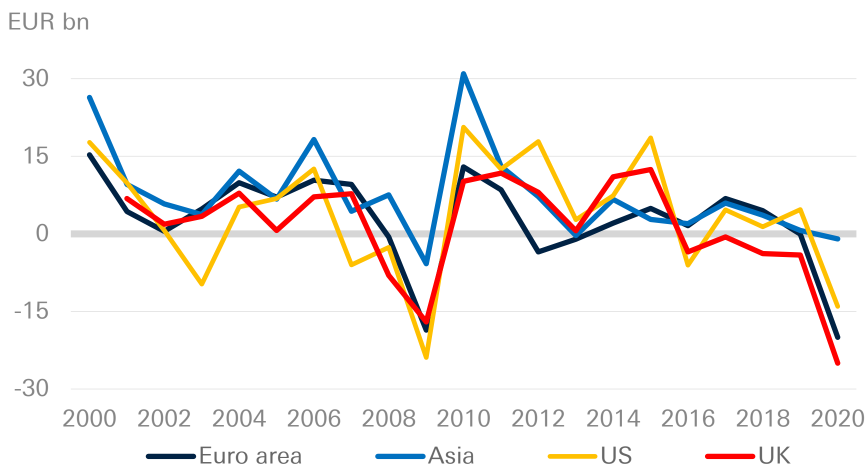
Rays of hope after heavy contraction in German exports

Strong COVID-19 headwinds led to a sharp slowdown in German industry and a collapse in global trade. In the second quarter German exports in year-on-year terms may contract more strongly than during the GFC in 2009, at least for some export markets. The anticipated GDP contraction of -9% in 2020 is clearly a negative record. But despite the deepest economic slump in over 70 years, there is a silver lining for exports. First, the recent reopening of major industrial plants in Germany. Second, the less restrictive lockdown measures in parts of northern Europe. And third, the low number of newly infected people in Asia provides the basis for a recovery of global value chains and global trade.

Figure 1: Bilateral exports to countries & regions



Source : Deutsche Bank Research, Federal Statistical Office

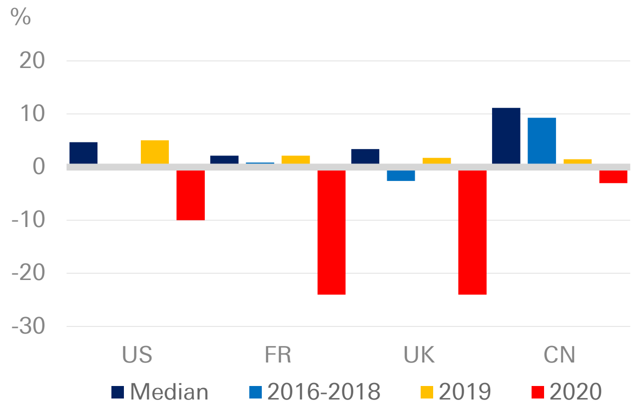
Asia: Exports to key countries might contract only slightly

Industrial heavyweights China, South Korea and Japan seem to have managed the crisis relatively well. So far, production indices have declined only mildly in these countries. In Korea, manufacturing production already recorded a marked improvement of 4.6% month on month in March. As a consequence German nominal exports to Asia – which account for one-sixth of total goods exports – were almost flat in the first quarter. Thus, the relatively stable demand in Asia could be less of a barrier than the collapse in production, at least in some sectors. As a result, the picture is expected to change in the second quarter due to the indirect effects of the lockdown in Europe and the US. However, economic activity in both regions is already gaining momentum. If the recovery continues and German production plants gradually increase their capacity utilization, exports to Asia could emerge relatively unscathed. So nominal exports to Asia, which grew by more than 3% p.a. from 2016 to 2019, could well contract only marginally in 2020.

Europe: Exports to some countries could drop by up to 25%

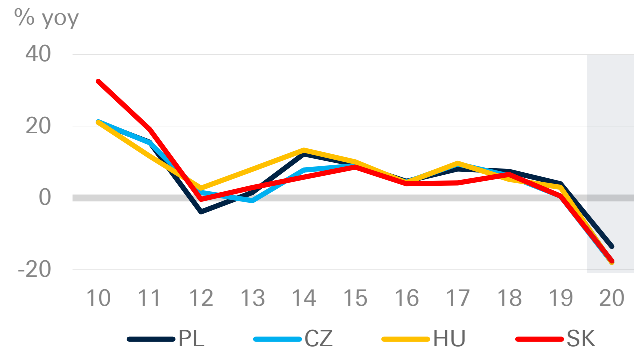
By contrast, it is almost certain that we will see a historical reduction in exports, at least to some European countries. In total they account for 68% of total goods exports. Exports to both the non-euro area (31% of total goods exports) and euro-area countries (37%) were already weak before the lockdown in March.

Figure 2: Top 4 countries: Bilateral nominal goods exports



Source : Deutsche Bank Research, Federal Statistical Office

Figure 3: Nominal goods exports to Visegrad countries



Source : Deutsche Bank Research, Federal Statistical Office

1. Exports to the euro area: It seems clear that the heavy GDP loss of 4% qoq in Q1 in the euro area will be followed by a double-digit contraction in Q2. We forecast -18% qoq. Despite an expected recovery in the second half of the year, 2020 GDP should shrink by 12% on annual average. In March 2020 exports to the euro area against the same month of 2019 dropped by 14% year on year. And April was likely much worse. The almost-complete collapse in German car production and very restrictive social distancing measures are expected to have led to a massive slump. We assume that exports in euro will be twice as low in April as in March. Subsequently, we foresee a gradual, muted recovery as many European value chains as well as aggregate demand will severely be hampered due to social distancing and the reorganization of production processes. Thus, we assume that it will take until December before the March export level is reached again. This would result in an annual contraction of exports to the euro area by 25% in 2020.

2. In our view, the impact of the crisis on non-euro area countries is very diverse. This seems to be true for both EU and non-EU countries. For instance, the Visegrad countries, which are deeply integrated into the production chains of German manufacturing, will be hard hit. Among these countries, Slovakia and Hungary are an integral part of the production line of the automobile sector. Hence, it comes as no surprise that among the four Visegrad countries, March exports to Hungary and Slovakia recorded particularly big declines of 12% and 16% in year-on-year terms, respectively. We expect annual exports to decline by up to 20% in 2020. By contrast, as we forecast contraction of Russian GDP of ~6% and Turkish GDP of ~5%, exports to both nations should fall by only 9% in 2020. A similar loss seems likely for exports to other Eastern European countries. A relatively moderate GDP loss is likely for Denmark, Sweden and Switzerland. They fairly quickly flattened the COVID-19 infection curve or had relatively moderate curfews. We assume exports to these countries will remain flat on annual average. A severe export loss is expected for the UK. Exports already plummeted by almost 15% year on year in the first quarter of 2020 due to a temporary increase in Q1 2019, i.e. anticipatory effects in the run-up to the first Brexit deadline (31 March 2019). The UK has also been particularly hard hit by the COVID-19 crisis. Hence, exports are likely to decline by more than 20% in 2020. In total, exports to non-euro area countries should shrink by roughly 12%.

As a result of factors (1.) and (2.) above, European exports in total are likely to decline by around 19%. This is the same level as during the GFC in 2009. An additional shock

– as covered in our protracted scenario[1] – with much deeper growth contractions, would result in new negative export collapses that might be comparable only to the Great Depression or WWII.

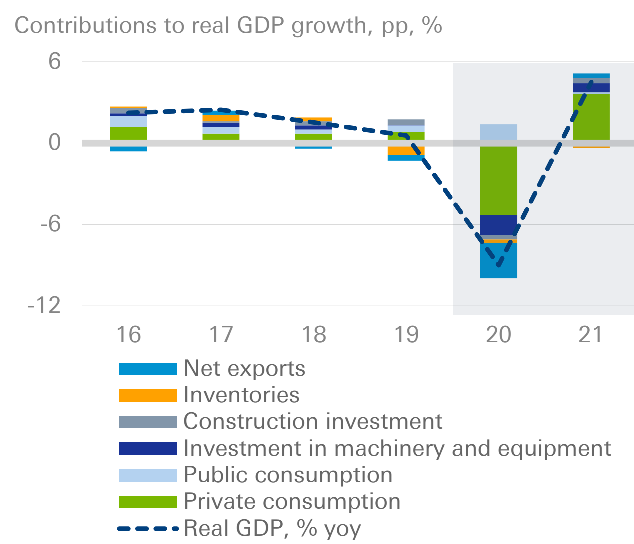
Americas: Exports to the US with extraordinary uncertainty

In our base scenario, we expect the US market to be less affected than many European countries. Exports to the US only marginally contracted until March in year-on-year terms. Yet, the epidemiological crisis does not seem to have reached its peak in the US. Moreover, the collapse of the labor market will leave its marks. We expect that the unemployment rate will peak above 15% in the second quarter and remain above 10% towards the end of 2020. We expect GDP contraction of ~7%. Based on our estimated GDP elasticity of 1.5, exports to the US may fall by around 10%. With the US accounting for more than 70% of exports to the Americas, we also assume a contraction by 10% for all other American countries. However, the US forecast is extremely uncertain as the future development of the corona crisis seems particularly vulnerable to a backlash. Some US states plan to reopen their economies despite still-precarious public health conditions. This raises the risk of further outbreaks requiring renewed further containment measures. It is an important downside risk for German exports.

Figure 4: Germany: Export prices

Source : Deutsche Bank Research, ECB, Federal Statistical Office

Figure 5: Germany: Real GDP growth and details



Source : Federal Statistical Office, Deutsche Bank Research

1 Peter Hooper et al. „Special report: World Outlook Update: Turning Gloomier", 7 May 2020

2020 export prices are expected to drop by 3%

Nominal global goods exports are forecast to decline by 17% in annual terms in 2020, roughly similar as during the GFC (2009: -18%). In the COVID-19 crisis, service exports should suffer a similar annual contraction as lockdowns have hit many service sectors. This is a notable difference to the GFC, where services were less affected and remained an element of stability. For our 2020 forecast we do not take into account any FX impact. First, changes in exchanges rates have been relatively limited. Second, their impact on exports relative to the large swings in economic activity is negligible. We expect export prices to decline by roughly 3%. First, our model based on commodity prices – the main structural input for export prices – implies a decline of only 1.2%. The model does not take into account the huge loss in aggregate demand. Therefore, we add the statistical error observed during the GFC in 2009. The result is a drop of 3% for 2020, which would be an all-time low in annual export prices. Accordingly, real annual exports should shrink by 14%, close to the contraction experienced during the GFC. As private consumption and investments are forecast to decline by around 10%, a similar contraction is expected for real imports in 2020. This should result in a net export contribution to GDP growth of -2.6pp.

Current account surplus: The never-ending story

Finally, we look at Germany's often-criticized current account surplus. In 2008 the annual surplus fell 16%, from EUR 172 by to EUR 145 bn. We take this as an indication for the current crisis, i.e. in 2020 the current account may also decline by roughly 16%. Assuming that the GDP deflator will increase by 1% results in nominal GDP contraction of 8%. As a consequence, the current account surplus should shrink to "only" 6.6% of GDP in 2020. So based on the 2019 surplus of 7.8%, we expect the largest annual contraction in over a decade. However, the ratio is still above the European Commission's 6% threshold, above which it interprets surpluses as potentially excessive. However, the COVID-19 crisis has the potential to rebalance German exports, including the debate about whether certain essential products such as key pharmaceuticals should be relocated back to Germany or at least Europe. To reach ambitious CO_2 targets and to reduce the carbon footprint, there are huge incentives to relocate more supply chains closer to the home market. If we see more continental supply chains, Germany's current account surplus with non-European countries may substantially fall, whereas surpluses to neighboring countries and Eastern European countries may increase even further.

Appendix 1

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