The 2020 Aftermath

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2020 has been an extraordinary year that pushed us all into adapting as the pandemic shocked the global economy. We witnessed the drastic toll of the pandemic on economic activity, leading to historic job losses; crude oil prices dipping below zero for the first time ever; fiscal and monetary policy makers paranoidly stepping in to help the damaged economies recover; global markets volatilities skyrocketing and OTC hedge providers' trading risk appetite narrowing. There are many more metrics that can put the severity of the pandemic into context, but it's fair to say that the pandemic's hit has left the global ecosystem considerably injured. Nonetheless, just like any other crisis, it taught us all a lesson.

China

China, the second largest economy in terms of GDP and the world's largest manufacturer in terms of output, was already battling the consequences of the trade war it had with the United States. By the end of 2019, the country had already lowered its top tier Value Added Tax from 16% to 13%, raised personal tax threshold by $211 to $705, and allowed pre-tax deduction across various categories. Further depriving its tool kit, the country rolled out a massive $564 billion stimulus package to combat the global financial crises in 2008, leaving the country with a mountain of debt.

On 31-December-2019, the novel coronavirus was first identified after Wuhan Municipal Health Commission reported a cluster of cases of pneumonia. Since then, the country has been through multi-lockdowns, injected over $700 billion in stimulus packages including (but not limited to): bond buying, credit lines offering to SMEs, repo and reserve repo rates lowering, reducing Reserve Ratio Requirement (RRR) to its lowest since 2008, funding the construction of coronavirus hospitals, allowing budget deficit to exceed 3% of GDP, lowering electricity prices, and granting consumer vouchers to stimulate consumer spending. Ultimately, China managed to witness the best economic recovery among major economies. According to the latest International Monetary Fund (IMF) forecast, China is the only major economy to see a year-on-year economic growth in 2020. The expedited economic recovery helped the country's exports rapidly pick-up and even reach an all-time high on November-2020:

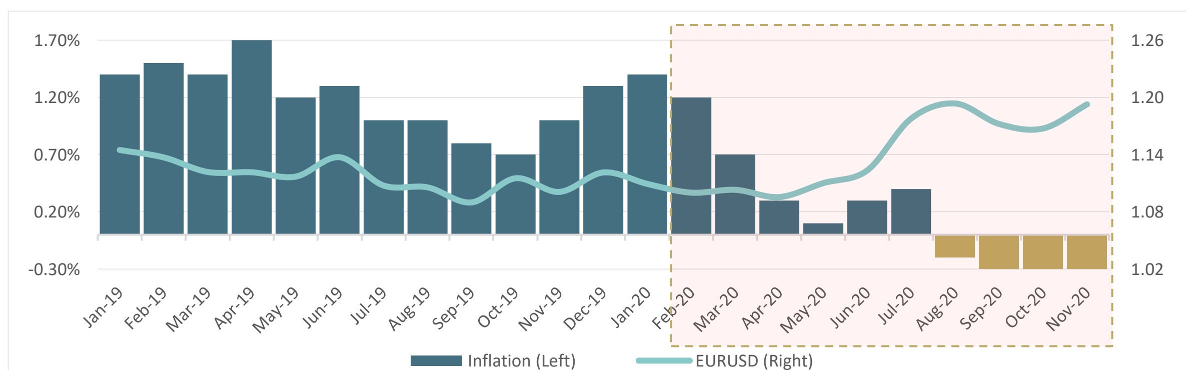
Source: Trading Economics

Europe

Late 2019, the European Central Bank (ECB) restarted its Quantitative Easing (QE) measures, which included: resuming eurozone government bond purchases starting from November 2019, lowering its policy rate to a new record low of -0.50%, and highlighting its plan to remain accommodative in its policies until it has seen the inflation outlook robustly converge to a level sufficiently close to, but below, 2%. At the time, the bloc was facing significant headwinds from the U.S-China trade war, Brexit uncertainty and signs that the German's economy, Europe's largest, is heading for recession.

On 24-January-2020, the Eurozone's first covid-19 case was reported to the World Health Organization (WHO) by France. The immediate reaction was what European Commission President Ursula von der Leyen described as the "My Nation First" approach. At first, member countries separately began fighting the health crisis through travel restrictions and local lockdowns. However, as the coronavirus outbreak posed the euro area outlook to downside risks, the ECB introduced what is called the "Pandemic Emergency Purchase Programme (PEPP)", a monetary package to counter the risks to liquidity and the outlook for the euro area. The PEPP was first introduced at a size of €750 billion by Mid-March before it was upgraded to €1,350 billion two and half months later. A wider European crisis response package followed. The European Commission (EC), European Investment Bank (EIB) and European Stability Mechanism (ESM) agreed to finance up to €540 billion to help people, businesses and countries throughout Europe, including liquidity support to companies, funding for development of treatments and vaccines, and financing for employment as well as direct and indirect healthcare costs related to the pandemic. Finally, European Heads of State and Government agreed on July a €750 billion European Fiscal Response, which consisted of €390 billion in grants and €360 billion in loans.

Last month revealed some hope for the region after the European Union reached a long-waited post-Brexit trade agreement with the United Kingdom while the European Commission concludes a "Comprehensive Agreement on Investment" with China. Nonetheless, euro area inflation continued trending downwards. The drop in inflation, trade agreements with the UK and China, and USD weakening led the EURUSD to tap levels that were last seen in 2018. In 2020, EURUSD appreciated by a tremendous 8.9%.



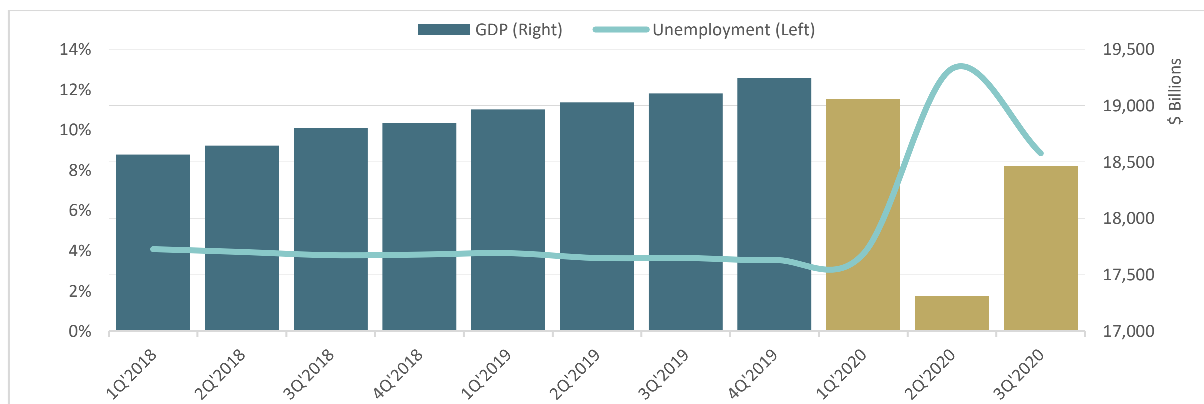
Source: Bloomberg

United States

The United States started the year on better ground compared to other major economies. The unemployment was at half-century low, a trade deal with China was on the verge of signing, the country's GDP marked its 14th consecutive quarterly growth, and the outlook was far more optimistic than other major economies. Yes, there was a raising concern around the accumulating US government debt, but it was not expected to have a material impact on the short-term outlook.

However, the combination of the pandemic hit, oil price war, political tension within the country, and the dramatic US election took the US economy through an unanticipated journey. A journey that even the most conservative financial risk models couldn't predict. The US economy lost a historic 22 million jobs between March-April (that is greater than the total jobs created since October 2010), unemployment rate sparked to the highest since the Great Depression, consumer spending dropped by a record 13.6% in May-2020, crude oil futures price dipped below zero level for the first time ever amid storage availability concerns, the Fed's benchmark rate dropped to its lowest level in history, the US economy contracted a massive 9.2% in the second quarter of this year.

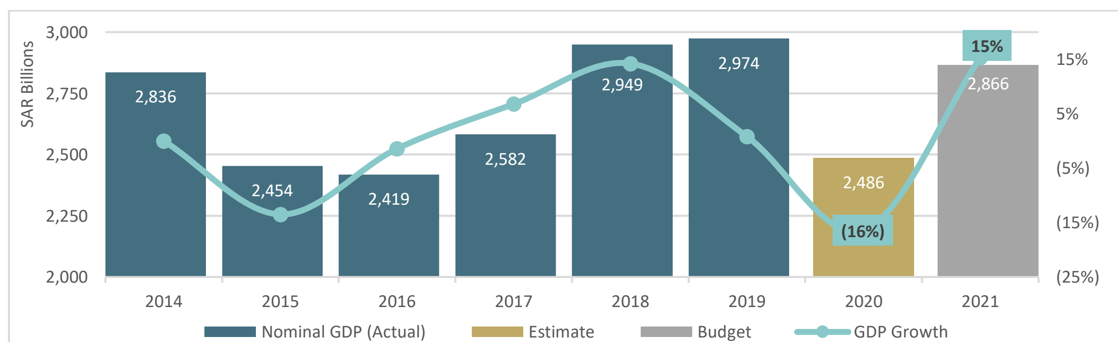
Fiscal and monetary policy makers immediately stepped in to revive a severely hit economy. The US government announced a USD 2 trillion stimulus package, the biggest ever in US history. In an emergency move, the Federal Reserve cut the target rate twice in March-2020, reaching to a range of 0% to 0.25% from a target rate range of 1.50% to 1.75% in February-2020. Moreover, the Fed also announced a USD 700bn quantitative easing program to help the economy and enhance the USD liquidity. Recently, the US congress reached a deal on a $900 billion coronavirus relief package.



Source: Bloomberg

Saudi Arabia

The Saudi economy witnessed a similar, yet more severe, stress amid the pandemic. Oil prices dropped significantly amid the twin-hit of reduced global demand for energy and oil price-war among major oil producers. In response to the pandemic, the Kingdom's authorities took various measures to fight the crises and maintain economic stability. The measures included SAR 120bn stimulus package, 5% reduction in 2020 budget, increased the debt ceiling from 30% to 50% of GDP. Furthermore, the Kingdom also raised Value Added Tax from 5% to 15% and stopped the cost-of-living allowance. Saudi Central Bank (SAMA) assets dropped significantly as the government continued to support the local economy. Nonetheless, despite the twin-hit, the Kingdom managed to breakthrough among the least impacted G-20 economies in 2Q-2020. The Ministry of Finance (MoF) now estimates 2020 GDP to contract by 16.4%.



Source: General Authority for Statistic (GASTAT), Ministry of Finance (MoF).

Although the Kingdom is now shifting away from the high reliance on oil revenues, the commodity still attributes the majority of the Kingdom's revenues. Hence, the local economy was severely impacted by the dispute among oil producers last year and the sever drop in the demand for energy. Nonetheless, as OPEC+ members resolved their disagreement, Brent oil barrel price started to stabilize above $50 level, and the global demand for energy showed decent signs of recovery, the MoF is now anticipating an expedited recovery that can get the Kingdom's GDP to surpass pre-pandemic levels by 2022.

Lessons Learned

The lessons learned can vary between one profession to another, one sector and another and even among individuals. For us as financial risk managers, we still have a great deal to learn from the 2020 pandemic, and we must do so. If history have taught us anything, it would be to never underestimate our risk management dashboards and to never time the market. In the meantime, we must seek to escape from the current disaster as quickly as possible. This will need a thorough review of our financial risk management framework, reforming our risk quantification models, defining the permissible means we use in managing our financial risks, and establishing a meticulous risk monitoring plan.

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