

## ING mid-year update: Reviewing our 2021 forecasts

Our economists review the predictions they made in our economic outlook last November and reflect on what the implications are for the rest of the year.



World leaders, clockwise from top left: Angela Merkel (Chancellor of Germany), Xi Jinping (China President), Lee Hsien Loong (Singapore Prime Minister), Joe Biden (US President), Boris Johnson (UK Prime minister).

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You can read our 2021 outlook from November 2020 [here](#)

### United States

Back in December, optimism surrounding the US economic outlook was on the rise as the effectiveness of vaccines was proven in clinical trials. Nonetheless, there was concern they wouldn't be distributed rapidly enough to head off another wave of Covid-19 cases.

There were also fears that Donald Trump's legal challenges to the election result would create such a toxic political atmosphere that it would limit President Joe Biden's ability to respond to the pandemic with additional fiscal stimulus.

These concerns didn't come to fruition and the US economy posted decent first-quarter growth versus the flat to modestly negative GDP print we anticipated. However, we were right to expect

that the second quarter would experience very strong growth on re-opening and eventual government stimulus. This will mean the economy fully recovering all the lost pandemic output when 2Q GDP figures are released later this month, versus the 3Q timeframe we anticipated in December.

While we were too cautious on 1H21 economic activity, we predicted healthy momentum through the second half of the year with most of the jobs lost during the pandemic recovered by the end of 2021 - and this still looks valid.

More successfully, we were worried the recovery “could be too good” in that demand would outstrip the supply capacity of the economy and inflation would be more of an issue than the Federal Reserve and most analysts expected.

Inflation has surpassed even our high expectations and reached 5% in May. This should mark the peak, but we were right to argue that Fed would gradually change its language to indicate that they wouldn't leave it as late as 2024 before implementing the first interest rate rise.

Nonetheless, the yield curve has confounded most forecasters expectations and not steepened, which either reflects the ample liquidity environment and/or bond market caution on the medium to longer-term outlook.

## Eurozone

Our growth outlook for the Eurozone at the end of 2020 was spot on. First, a double-dip in the eurozone and then a strong rebound on the back of an accelerating vaccination programme and the reopening of the economy.

When it comes to more structural developments, the eurozone is once again too late. Our calls for more digitalisation as a key driver for more convergence, a discussion on a fundamental reform of the fiscal rules and the ECB's move towards a symmetric inflation target are still valid there has been no movement on any of these topics.

The start of the NextGenerationEU programme and money paid out from the European Recovery Fund will, amongst other things, focus on investments in the digital economy and should at least limit further economic divergence. At the same time, another discussion on yet another overhaul of the fiscal rules has started but the outcome will very much depend on the results of the German elections. However, reading through the election manifestos, we think that the next German government is likely to approve more domestic investments rather than significant Eurozone fiscal rules reform.

Finally, the ECB's strategy review is close to a conclusion - and a more symmetric inflation target without explicitly calling it one seems to be on the cards. When it comes to more structural issues, the eurozone has once again taken a step back and slowed down any reform efforts, making our job of reviewing major calls for 2021 almost impossible.

## United Kingdom

The UK economy is in a better place than we expected when we wrote our 2021 outlook in November last year.

Businesses weathered the winter of restrictions better than expected, and the subsequent rebound in consumer spending appetite through the spring has been vigorous. We're now looking for 6.8% growth for 2021, a good couple of percentage points higher than in November. It now looks likely that the economy will be close to – or possibly back to – pre-virus levels by the end of the year, though the recovery is likely to be a little slower through the summer given the spread of the Delta variant.

Away from the forecasts, we made three calls. Firstly, that Brexit would put some pressure on the jobs market, but wouldn't cause a Covid-19 style GDP collapse. The latter has certainly been true, though the impact on trade is still clearly visible. Exports to the EU have recovered from January's disruption, but Eurostat data shows the UK's share of the EU's total imports has fallen. As for the impact on jobs, it's harder to say, though we'd expect the higher cost burden from customs processes to gradually take its toll – particularly for some SMEs.

Secondly, we suggested that unemployment would rise in 2021. So far the jobless rate has actually ticked lower, linked to business resilience through the Q1 lockdown. But we'd still expect a rise in unemployment when the furlough scheme ends, but the fact that this support extends a few months beyond the ending of restrictions suggests the peak will be much lower than it could have otherwise been. We're looking for roughly a one-percentage-point spike.

Finally, we predicted that the Bank of England would steer clear of negative rates. That's proven correct, partly because of the economic rebound, but also because there's clearly some reticence among committee members to go down this path. Attention now turns to the first-rate hike, which we expect in early 2023, a little later than markets are currently pricing.

## China

As the second half of the year arrives, were our views for 2021 still valid? Our [three convictions](#) for China 2021 at the end of 2020 were:

### **Economic growth upgraded from our earlier forecast**

We have seen China continue to grow fast at 18.3%YoY in 1Q21 and expect this to continue at 6.0%YoY for 2Q21. This has been partly due to the low base effect as well as a sign of some domestic and external demand recovery from Covid-19. Given the faster than expected growth in 1Q21, we have revised our GDP forecast upwards from 7.0% to 8.7% in 2021. But to keep this growth path, China, as well as the world, needs to re-open international borders but this seems to be some way off as the “delta” variant is spreading quickly.

### **Technology war is still the number one risk in 2021**

The risk of a technology war, or the realisation of this risk, has become even more obvious and imminent as the Biden government addresses China's rise as a high-risk competitor to the US and its allies. It is now even more difficult for companies in the US to do business related to technology with Chinese companies.

To react to this threat, China has assigned Liu He, Xi's economic czar, to lead the advancement of technology, and we expect this to induce a hostile reaction from the US.

### **Interest and exchange rate reform is both a risk and an opportunity**

Though we are correct that the central bank's monetary policies would remain stable in 2021, exchange rate reform has brought more volatility to the USD/CNY market. We have revised

our USD/CNY forecast from 6.3 to 6.45 for the end of 2021.

## Asia ex-China

Our 2021 forecast was supposed to be all about economic recovery in Asia. Despite relatively mild pandemics in 2020, the region's economic growth was hit hard by aggressive measures taken to slow the spread of the virus. A recovery in overseas export markets together with a re-opening of domestic economies should have delivered strong growth figures for 2021. That is the main gist of what we were forecasting. The rest was fluff.

What we didn't know back in January, was how feeble the Asian vaccine rollout would be. This has left many economies open to new variants and new waves of infection. As a result, we have had to slash many of our GDP growth forecasts which were too high.

India has been the hardest hit, though we were helped by starting with a much less upbeat view relative to the consensus.

Japan's GDP forecast also required some aggressive surgery. The timing of new waves in 2021 came early, resulting in a 1Q contraction. With more social distancing in 2Q21 ahead of the Olympics, the first half of the year will be a virtual write-off. Full-year 2021 will struggle to beat 2% growth. At the start of the year, 5% had looked plausible.

Elsewhere in North Asia, Taiwan has found the absence of vaccines a major handicap, as it suffered its first serious Covid-19 wave and has had to impose movement restrictions. South Korea has done better, though it too hasn't moved quickly on vaccinating its population, and a strong start to the year remains at risk of a downward revision until vaccination rates improve.

South-East Asia has had a torrid time amidst ineffective partial-rolling restrictions and a very slow vaccine rollout. We have cut back growth forecasts for most of the region since the start of the year. Singapore has been more resilient.

Australia has shown that tight border restrictions are an incomplete shield against new waves. Earlier choosiness over vaccine types is rapidly fading but it will take some time to protect their population given the slow start.

As the vaccine rollout continues, new waves will cause fewer problems. But as that is unlikely to happen either fully, or quickly anywhere in the region, the outlook for 2H21 is likely to be punctuated by renewed outbreaks and interruptions to recovery and perhaps further cuts to growth forecasts.

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