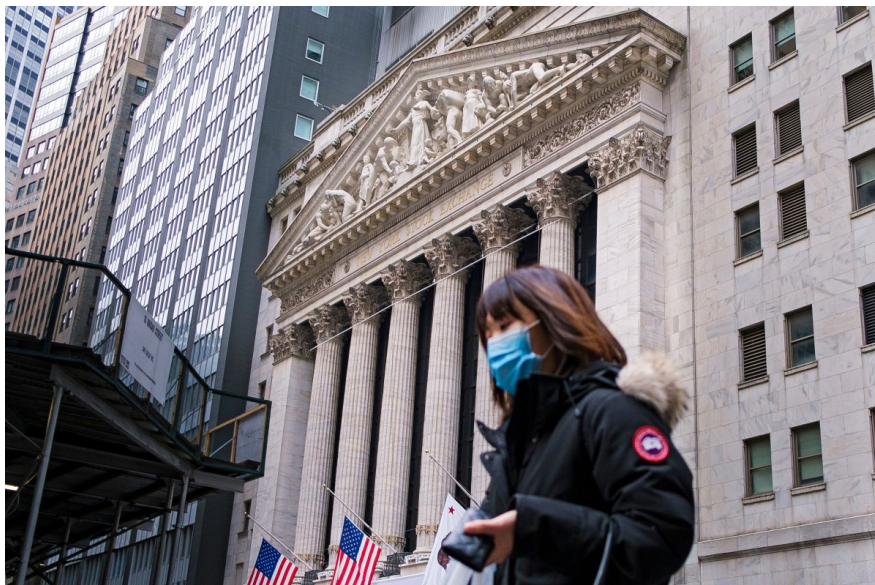


## Rates: Getting dumped

Risk assets were the darlings of 2019. Tainted now with virus risks, they are seriously stressed. Core bond markets are the ultimate safe haven. Even 3-month German bills at -0.7% are deemed an acceptable alternative versus the bigger risk implied in equity markets. It's very volatile out there though, and the net effect is low and likely even lower rates



### Lots of talk about zero rates

In a flash, we find the US 10-year below 1%, and the speed of the move from 1.8% was no doubt a factor behind the emergency 50bp cut delivered by the Federal Reserve. Ahead of delivery, the cut was fully discounted. The Fed just had to turn up and pull that rate cut lever. They did. And now the markets are gunning for at least another 50bp. That would bring the funds rate to the 50bp area. Then the debate starts as to whether the Fed is done, as if they are not, we are then staring down the barrel of the approach of zero rates.

---

*Rate cuts are no panacea for the flu, but they do help to lubricate the financial system*

---

Do zero rates make sense? Not based on what we know. Inflation is at 2% for starters. A -200bp real rate would paint a dire implied market discount for the US economy. What makes more sense to us is a quick dive into negative real rates due to exceptional circumstances that are expected to prove temporary. But as we can't say for sure, there are overshoots. Equity markets getting dumped is one. The exceptional flight into the safety of bonds is another. A rate-cutting Fed then chimes with both.

Think of the Fed cuts as a comfort blanket. Rate cuts are no panacea for the flu, but they do help to lubricate the financial system. As an evitable virus-panic-related-slowdown takes hold, high yield corporates would be the first to come under pressure. Company accounts in the black can quickly move into the red, elevating default risk. Easy access to liquidity is a first defence system. That's why loosening from the Fed is a sensible reaction.

And remember, they can be reversed just as quickly if needed.

## Identifying when the angst could end

In the meantime, exceptional volatility means we are never sure on a day-to-day basis whether we've seen the bottom for rates, or risk assets. The background noise on Covid-19 continues to darken though. It is still in expansion mode, especially outside of Asia. We are not yet at a point where we can look through the rise in infections to a macro recovery. Refuge from warmer months ahead offers the best glint of positivity. But we need to get there first, which likely keeps rates under downward pressure.

---

*We can envisage a series of Ws for risk assets in the coming weeks, more likely with a net slide further lower*

---

As we continue the overshoot to the downside, it is entirely conceivable that the US curve marks out at sub-50bp on the 2-year and the 75bp area in the 10-year. That's based off a comfort factor around the 1% area for the 10-year. A handle of one looks even better when compared with alternatives in risk-free space in deep negative territory. That said, even the German 3-month bill yield at -0.7% can be an acceptable safe haven relative to the downside that equity markets could suffer should things turn down again.

We can envisage a series of Ws for risk assets in the coming weeks, more likely with a net slide further lower, as a trend that will not become immediately obvious until we've had a run of weeks. That backdrop gels with the maintenance of low rates. German yields remain in the -75b area or lower. US yields trend in sub-1% territory, and increasingly closer to zero than 1% on the front end as the Fed continues to cut rates. And it's circular, as risk assets will worry about what that discount actually implies.

Causation so far is from the un-covering of Covid-19 cases to lockdown, and then to market angst in expectation of a pronounced macro hit. The SARS impact 20 years ago reversed when infections peaked after six months. Both interest rate and risk asset markets will be looking for a similar peak beyond which a recovery could be sensibly discounted. We're just

not there yet.

## Author

**Padhraic Garvey, CFA**

Regional Head of Research, Americas

[padhraic.garvey@ing.com](mailto:padhraic.garvey@ing.com)

## Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.