

Hopes fade for a synchronised global recovery

Better times are coming, though hopes of a synchronised global recovery are fading. That's the main thrust of our comprehensive Monthly Economic Update. We explain what this means for economies and markets around the world. James Smith tells us that it's not all bad news for the UK. And if credit markets are your thing, we've got you covered there too

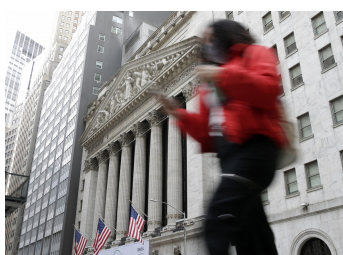
In this bundle



Monthly Economic update: Another sequel no one needed

Better times are coming, though hopes of a synchronised global recovery are fading. In our latest update, we explain what this means for economies and...

By Carsten Brzeski, James Knightley and 7 others



United States

US: Waiting for lift-off

The economy will likely continue struggling for the next month or two, but with vaccinations accelerating and households looking cash rich a reopening of...

By James Knightley



Eurozone: A delayed recovery

With more stringent lockdowns in the offing and a still underwhelming vaccination campaign, the eurozone economy is likely to shrink again in 1Q. A...

By Peter Vanden Houte

United Kingdom | Video

Smith on Britain, Brexit and better times?

ING's James Smith on three reasons to be vaguely cheerful about the UK economy despite the coronavirus and Brexit gloom

By James Smith



China

China: Impact of muted spring travel

The Chinese New Year is coming and this year is different, as new partial lockdowns reduce domestic travel. We discuss the impact of the change to this...



Asia: Covid catches up

Towards the end of last year, the relatively good performance of most Asian economies in terms of the Covid pandemic started to crack. The deterioration...

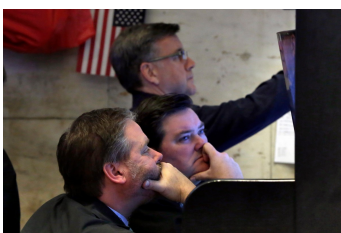
By Robert Carnell



FX

CEE: Delayed recovery but no fundamental change to the outlook

The recovery is delayed, but not derailed. Although coming later than expected, we still look for a meaningful rebound from the second quarter. Our...



Credit

Cross currency opportunities: EUR spreads to outperform USD counterparts

We expect USD spreads to underperform against EUR in 2021. Alongside this, we expect the cross-currency basis swap and 3m vs 6m roll to remain tight. In...

By Timothy Rahill and Jeroen van den Broek



Listen: Risky business - corporate bonds are 'very expensive'

Fed Chair Jerome Powell said this week that the Bank is monitoring the corporate bond market, where spreads have narrowed to levels seen before the...

By Jeroen van den Broek and Rebecca Byrne



Poland | Russia...

IMF World Economic Outlook: A diverging growth path for emerging markets

The IMF's latest World Economic Outlook update provides a glimmer of hope. After the 3.5% contraction in 2020, global growth is set to rise by 5.5%...

Report | 28 January 2021

Monthly Economic update: Another sequel no one needed

Better times are coming, though hopes of a synchronised global recovery are fading. In our latest update, we explain what this means for economies and...



Source: Shutterstock

Authors

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

James Knightley

Chief International Economist

james.knightley@ing.com

Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone

peter.vandenhoute@ing.com

Robert Carnell

Regional Head of Research, Asia-Pacific

robert.carnell@asia.ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

James Smith

Developed Markets Economist

james.smith@ing.com

Paolo Pizzoli

Senior Economist, Italy, Greece

paolo.pizzoli@ing.com

Marcel Klok

Senior Economist

marcel.klok@ing.com

US: Waiting for lift-off

The economy will likely continue struggling for the next month or two, but with vaccinations accelerating and households looking cash rich a reopening of...



Source: Shutterstock

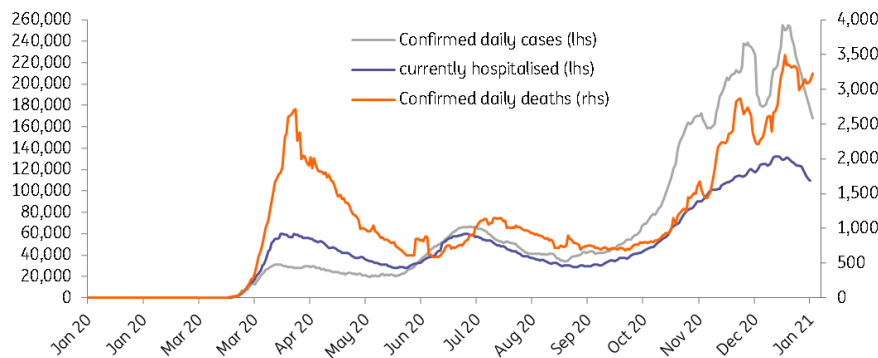
Pedestrians walk by the New York Stock Exchange after the opening bell at the NYSE on Wall Street in New York City

The quicker the vaccinations the sooner the reopening

The US economy started 2021 on a weak footing following three consecutive monthly falls in retail sales at the end of the year and news that 140,000 jobs were lost in December. With Covid containment measures continuing to weigh on sentiment and activity, we suspect that the economy will struggle through much of the first quarter.

However, the outlook thereafter is undoubtedly brightening. The US is getting close to averaging one million Covid vaccination doses a day with President Biden promising more resources to ramp up the process to 1.5 million and possibly even 2 million per day. With the warmer weather of spring approaching and hospitalisation numbers already falling, there is hope that a second quarter reopening of the economy is possible.

Covid cases and hospitalisations are falling. Deaths will follow



Source: Macrobond, ING

Consumer boom

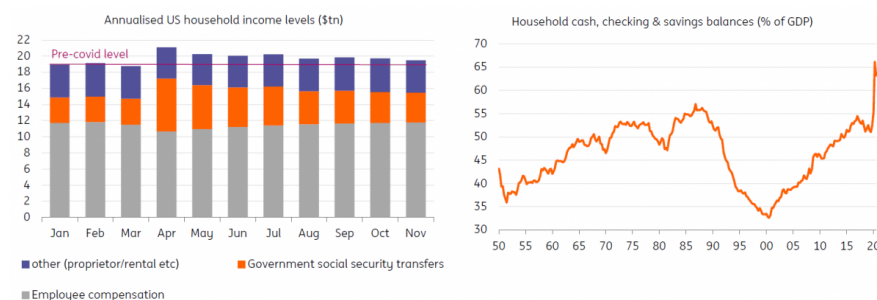
We expect to see consumer spending leading the charge with pent-up demand focused on the leisure, travel and entertainment sectors. Households are cash rich with government support programmes (extended unemployment benefits and individual cheques) helping lower income households. At the same time, the inability to travel and spend money on “experiences” has led to involuntary saving by higher income groups. The result is that savings in cash, checking and time deposits have surged \$2.4 trillion between the third quarter of 2019 and third quarter of 2020.

More support is proposed with a \$1.9tn fiscal plan set to make its way through Congress although some dilution and modifications will likely be required to get it [passed](#).

With credit card balances at four-year lows this means there is a huge amount of cash ammunition with which to propel spending higher. Add in the prospect of significant employment gains as the downtrodden service sector finds its feet and 2021 looks set to be the strongest year for economic growth in decades.

Elsewhere, the buoyant housing market is likely to keep residential construction activity robust while capex by US corporates is likely to recover after 12 months of flatlining. A pick-up in global trade and a more internationally-competitive US dollar following its recent declines will also support activity.

Higher household incomes have boosted savings



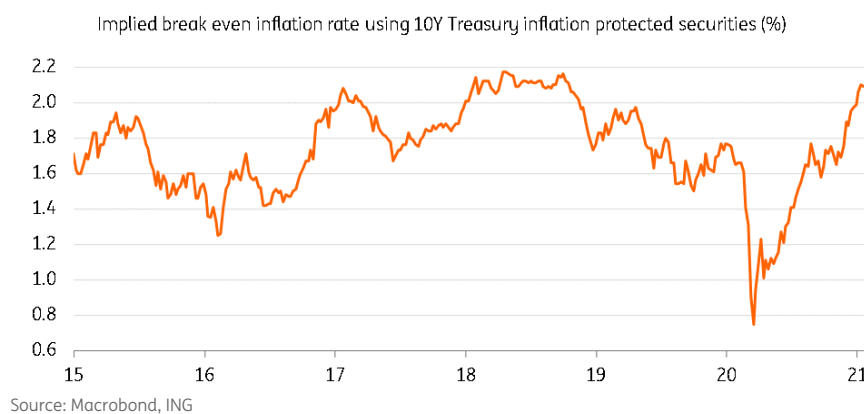
Source: Macrobond, ING

Inflation set to rise

Inflation will inevitably move higher. Much of it will be base effects as price levels in a vibrant, reopened economy will be higher than they were when companies were desperate for cash and were slashing prices in the depths of the pandemic in 2Q 2020. Moreover, higher fuel prices and some capacity constraints in heavily distressed sectors will add to upside inflation risks in the near-term.

Given this reflationary environment we expect to hear more talk of potential quantitative easing tapering this year with Federal Reserve interest rate hike expectations forecast to creep forward to 2023 from 2024.

Market inflation expectations have jumped



Can we avoid a taper tantrum?

This runs the risk of a taper tantrum 2.0 – similarly to when the Fed signalled it was going to slow its QE purchases in 2013 and the 10Y Treasury yield jumped from 1.6% to 3%. If repeated, this would lead to disruptive moves on the cost and availability of domestic credit, with implications for broader asset classes, including emerging markets.

We suspect that the tapering will be gradual and is likely to involve a twist operation to start – cutting the total purchases, but weighting more of those purchases towards the long end of the yield curve. Volatility could be further reduced if the Fed signals they are prepared to be flexible on this taper, such as by being willing to halt the taper and even temporarily increase purchases, depending on market circumstances. With more debt issuance coming this could be an important way of calming the market.

Fiscal optimism, but remember the mid-terms

The next move in fiscal policy will be an attempt to pass Joe Biden's \$3tn+ Build Back Better infrastructure and energy plan. This is going to be a major challenge given the Republican Party's re-discovered fiscal conservatism and the Democrats tiny majorities in the House and Senate.

The clock is already ticking given the mid-term elections in 2022. With all House seats and a third of the Senate up for re-election, legislation will have to be accelerated to give it time to be passed by Congress. Remember that through the 20th century, the incumbent President's party has on

average lost 26 House seats and 4 Senate seats at the mid-terms. If this were to be repeated, the Republicans would control Congress and Joe Biden would be a lame duck President in the final two years of his term, with little chance of getting any more of his proposals written into law.

Author

James Knightley

Chief International Economist

james.knightley@ing.com

Article | 28 January 2021

Eurozone: A delayed recovery

With more stringent lockdowns in the offing and a still underwhelming vaccination campaign, the eurozone economy is likely to shrink again in 1Q. A...

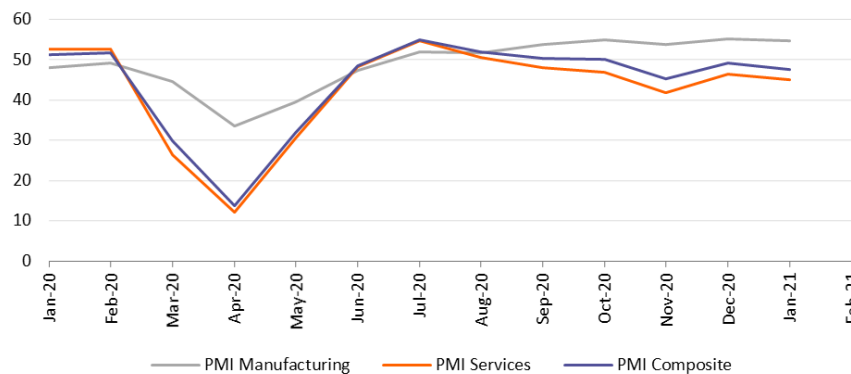


Source: Shutterstock
German Chancellor Angela Merkel

A weak January

The eurozone economy most probably shrank in the fourth quarter, though the contraction might be slightly smaller than we previously anticipated. According to provisional estimates, the German economy has apparently avoided recession, with strong exports providing important support. However, the build-up of inventories in the UK in the run-up to 2021, pushing up imports from the continent, is likely to reverse. Initial economic data for 1Q already signals some weakening. The German Ifo indicator dropped more than expected in January, with both the current conditions and the expectations component weakening. Eurozone consumer confidence also fell back in January, while the composite PMI slid to 47.5 from 49.1 in December.

PMIs soften in January



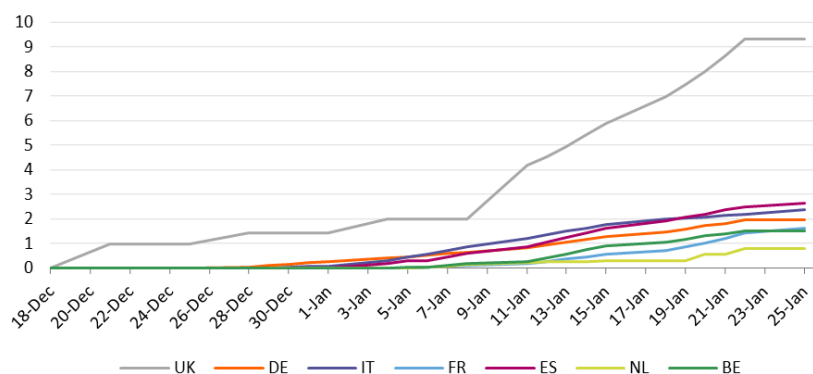
Source: Refinitiv Datastream

Underwhelming vaccination campaign

With the more contagious British and South-African Covid-19 strain spreading on the continent, lockdown measures have tightened again in several countries. The Netherlands introduced a curfew and France has tightened the existing one to 6pm. At the same time, the vaccine campaign continues to disappoint. While in the UK, around 11% of the population has been inoculated, in most eurozone countries, this was less than 2%. To make things even more painful, Pfizer had to reduce the deliveries of the vaccine to allow for changes in the production line. At the same time AstraZeneca, whose vaccine is not yet even approved, announced that it would deliver 60% fewer doses than promised in the first quarter. With these additional hurdles, it seems unlikely that herd immunity will be reached before the fourth quarter across the eurozone. That said, with the most vulnerable people probably inoculated by the end of April, some loosening of containment measures still looks likely. So after a difficult start of the year, we still stand by our recovery story from the second quarter onwards. However, the risk is that the number of infections remains high for some time to come. The political turmoil in Italy is not helping either, while the slow rollout of the plans to get money from the European Recovery Fund is also limiting the speed of the recovery. That is basically why we are looking at a sub-consensus 3.5% GDP growth rate in 2021 and 3.7% in 2022.

Slow vaccination pace

% of the population inoculated



Source: Refinitiv Datastream

Inflation might (temporarily) surprise

A VAT hike in Germany, higher energy prices and expected price hikes when some services reopen (see [here](#)) mean that inflation will come in higher this year. We expect an above-consensus average inflation rate of 1.3% for the year, with a 2% inflation rate at the start of the third quarter not out of reach. From the fourth quarter onwards, inflation should soften again and we expect it to settle around 1.3% in 2022. Given the fact that the inflation uplift is only temporary, the ECB is unlikely to react. What's more, by the summer months the ECB will probably have announced its new strategy. We expect the bank to go for an inflation target "around 2%", which allows for temporarily higher inflation without the need for a policy change.

Yield curve control by another name

For the time being, the ECB is certainly not thinking of tightening. Because of the huge negative output gap and the struggle to emerge from the pandemic-induced recession, loose monetary policy will still be required for some time to come. There is however a slight shift in the ECB's approach. The bank has now put the aim to preserve "favourable financing conditions" at the centre of its policy. While this sounds rather vague, it's obvious that long-term interest rates are an important determinant of financing conditions. As such, the ECB's Chief Economist Philip Lane declared that the Pandemic Emergency Purchase Programme has an important role to play in ensuring that the middle and long-end segments of the yield curve remain "appropriate". And that a premature steepening of the yield curve should be avoided. We read: yield curve control by another name. While we still expect long-term bond yields to rise somewhat during the year, the ECB bond purchases will probably limit the increase to 25bp by the end of this year.

Author

Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone

peter.vandenhoute@ing.com

Smith on Britain, Brexit and better times?

ING's James Smith on three reasons to be vaguely cheerful about the UK economy despite the coronavirus and Brexit gloom



Britain, Brexit and better times?

ING's James Smith on why we're looking for 5% growth in the UK this year but Brexit continues to bring significant disruption

[Watch video](#)

Author

James Smith

Developed Markets Economist

james.smith@ing.com

China: Impact of muted spring travel

The Chinese New Year is coming and this year is different, as new partial lockdowns reduce domestic travel. We discuss the impact of the change to this...



Source: Shutterstock

Chinese visit a normally bustling, international luxury shopping plaza in Beijing.

Lockdowns despite low numbers of Covid cases

For the first time since early 2020, there are once again partial lockdowns in Beijing city and Jilin province. Each lockdown has its own restrictions. This comes against a background of only around 100 cases per day nationally (though asymptomatic cases are often not reported in these numbers). The lockdown in Beijing suggests that a lockdown is possible anywhere in the country, even when the number of cases is very low.

We think partial lockdowns in specific locations will not adversely affect economic activity during the holidays.

Workers are now reluctant to buy train and domestic flight tickets to return to their hometowns for the Chinese New Year as they are concerned that they may not be able to return to work in time if

they are caught in lockdowns away from their workplaces. This reluctance to travel suggests that the disruptions to factory operations which took place in 2020 are unlikely to be repeated in 2021, which is positive for manufacturing and export-import activities.

Without travel to and from hometowns and work locations, money that would have been spent on transport may instead be spent celebrating the holiday in a different way. We expect shopping malls to remain open and online shopping as well as delivery to continue during the Chinese New Year, which is different from the past when many shops closed and delivery services stopped due to a lack of labour.

In short, we believe that partial lockdowns in specific locations will not adversely affect economic activity during the holidays.

A different Chinese New Year

A different Chinese New Year



40% reduction in cross city movements in January 2021, implying fewer workers going back to home town for Chinese New Year



300 cities would enjoy delivery service in the Chinese New Year holiday, a contrast with almost no delivery service in the past



37.2% will work during the Chinese New Year, according to a private HR survey. This number is usually much smaller.

Source: ING

Vaccination progress

China has 10 million people vaccinated with the first dose of vaccines developed by the country, which is still a small number compared to the whole population of 1.4 billion. Vaccination will continue after some pause over the Chinese New Year.

Deleveraging focuses on the property market

Over recent months, it has become obvious that deleveraging reform has resumed in China, and this time round, the focus of the reform is real estate property.

The government would like to lower the debt levels of these companies, most of which are private companies. Limits were set on debt-to-cash, debt-to-assets and debt-to-equity ratios in August 2020, and on bank lending ratios for property developers towards the end of 2020. More recently, additional constraints have been placed on property transactions and mortgages in some cities.

But the central government does not seem to be squeezing too hard on price and quantity restrictions for selling properties. It is giving some breathing space to the developers to sell existing properties (though not at higher prices) to get cash to repay debts. The whole process is finely managed.

This reduces our concern about a financial crunch caused by the property sector.

Article | 28 January 2021

Asia: Covid catches up

Towards the end of last year, the relatively good performance of most Asian economies in terms of the Covid pandemic started to crack. The deterioration...



Source: Shutterstock
Vaccine

Asia is not immune to Covid

In early December 2020, the very low prevailing daily case numbers in South Korea started to creep up, and at one stage topped 1,200 per day. Japan, which had inexplicably managed to be only mildly affected during earlier waves of the pandemic, started to see its numbers move higher even earlier, though the rise was slower and didn't really pick up aggressively until late December. Both Korea and Japan's daily Covid figures are beginning to ease down again now, but at their peak, Japan was registering close to 8000 cases per day.

Malaysia is now recording around 4,000 cases per day, Indonesia more than 10,000. China too has been seeing case numbers rise (see China section), though so far the numbers remain low relative to the millions who have been confined to their homes in response.

There are exceptions to this trend. In India, daily case numbers continue to fall but they still remain relatively high at around 14,000 a day if we accept the recorded figures at face value.

Rising Covid means rising restrictions

Even in Singapore, where the average number of community cases has risen from less than one to the occasional small cluster, the planned easing ahead of the Chinese New Year has been scaled back. Japan has been rolling out its regional states of emergency as caseloads have picked up in

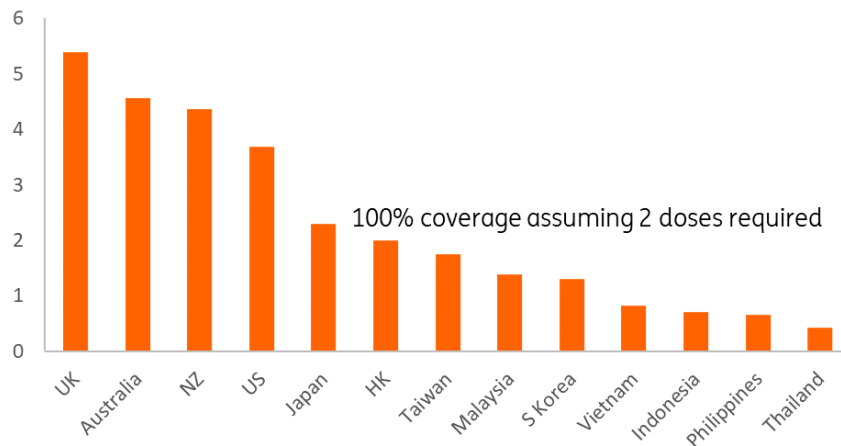
different parts of the country. Malaysia too has rolled out its movement restrictions. And in Indonesia, restrictions have been extended in Jakarta and Bali. The following table summarises what we believe to be the current situation in terms of restrictions around the region, against the recent seven-day moving average for daily cases.

Current Asian travel restrictions

Economy	Current Restrictions in place	7-day MAV *
Australia	➤ Some local hotspot related restrictions, some restrictions on interstate travel	8
New Zealand	➤ Limited to mask wearing on public transport	4
Japan	➤ States of Emergency until 7 Feb in Tokyo, Kanagawa, Chiba, Saitama, Osaka, Kyoto and Hyogo prefectures – limits on bar and restaurant opening hours and capacity, encouragement to work from home / stay home	5,217
South Korea	➤ Ban on gatherings of more than 4 persons ➤ Early closing for Cafes / restaurants. ➤ Clubs / Karaoke closed	398
Singapore	➤ Phase-3 reopening started on 28 Dec with up to 8 persons for social gathering and with higher operating capacity at retail outlets. ➤ Guidelines for restricted celebrations during the Chinese New Year festivities kicked in from 26 January.	32
Malaysia	➤ The government re-imposed Covid-19 Movement Control Orders (MCOs) in 5 Malaysian states and 3 Federal territories for two weeks on 13 Jan. ➤ It also declared a nationwide state of emergency lasting until 1 August. By 21 January most of the country under MCO 2.0 banning all social gatherings and dining out, limiting only two persons to do essential shopping locally , and restricting interstate travel.	3,587
Thailand	➤ On 3 January, the Thai Government declared 28 provinces, including Bangkok as high-risk zones , asking people to stay at home, avoid gathering, or travel across provinces. ➤ It is now considering easing some of the restrictions , including reopening schools in 20 out of 28 provinces from 1 February.	181
India	➤ Covid-19 restrictions have been relaxed as the country starts its vaccination drive. ➤ Strict controls on non-essential activity, including nightly curfews and a ban on public and private transport, will continue in hot-spots until at least end-January. ➤ Essential businesses are allowed to operate with minimum employees and bars and restaurants at 50% capacity.	13,580
Philippines	➤ Full (Enhanced Community quarantine) lockdown in Tuguegarao and Kalinga. ➤ General community quarantine (partial lockdown) for Capital region and surrounds. ➤ Restricted mall hours, restaurant capacity, movements for seniors and children. ➤ Firms, public transport at 50% capacity. ➤ Schools closed for in-person attendance.	1,753
Indonesia	➤ Java and Bali have enhanced lockdown – office capacity restricted to 75%, malls close at 7pm, restaurants dine-in limited to 25%. ➤ Worship services at 50% ➤ Schools closed for in-person attendance. ➤ Rest of country requirements on mask wearing and social distancing.	11,749
Taiwan	➤ Tightened international travel restrictions to SA requiring quarantine on arrival and additional testing.	4
Hong Kong	➤ Flight crew now need to quarantine for stays of over 2 hours. ➤ Restaurant hours and capacity limited. ➤ Selective lockdowns to conduct testing (part of Kowloon 22-24 Jan). ➤ Public mask wearing mandatory. ➤ Karaoke, facial, massage etc. banned.	71
<small>7-Day MAV is the 7-day moving average as of 25 January. International Travel restrictions not detailed – but generally bans for non-residents or quarantine plus testing if allowed. *Includes quarantined arrivals from overseas.</small>		

Confirmed vaccines secured* relative to population

multiples of population



Source: Duke University, ING

Vaccines secured by population

Case numbers low, but vaccine rollout is very slow

Covid case numbers in Asia may still look favourable relative to Europe or the US, even if their tolerance for very low case numbers is low. But the vaccination rollout speed has been very slow. China is probably in the lead here, but China has billions of vaccinations to disseminate, and vaccinations per 100 of the population (which is the appropriate metric for vaccinations) remain exceptionally low.

Many Asian countries will not even begin to roll out vaccines until February, and few countries have secured sufficient doses of reliable and efficient vaccines to be able to cover their entire population, at least not yet. Either that or local regulatory bodies have been slow to authorise the use of any of the new vaccines coming to the market. For many countries in the region, there are no physical stocks of vaccines, even if stocks have been "secured" on paper. This clearly prevents the rollout from proceeding at speed.

And until that happens, even though there are some good things happening in some sectors, for example, technology exports, which are important for the region, the broader recovery which will involve opening up the service sector, and international travel and hospitality can hardly be said to be gaining pace on a regional basis. With the exception of China, pre-Covid levels of activity remain a distant goal. A double-dip recession may be avoided, but we switched Asia (ex-China) to our second, less favourable scenario last month, and we are not going to change it back again this month and probably not next either.

With vaccine rollout likely to remain slow until 2Q 2021, Asia's recovery to pre-Covid levels is likely to remain subdued until later this year.

Author

Robert Carnell

Regional Head of Research, Asia-Pacific

robert.carnell@asia.ing.com

CEE: Delayed recovery but no fundamental change to the outlook

The recovery is delayed, but not derailed. Although coming later than expected, we still look for a meaningful rebound from the second quarter. Our...



Source: Shutterstock

Long queue of border commuters at Czech-Germany border-crossing in Fomava, Czech Republic - 25 Jan 2021

Covid-related restrictions delay the recovery...

As is the case in the eurozone, Covid restrictions will stay in place in the Central and Eastern European region for longer than initially expected. The pace of vaccination is similarly rather slow and as such, the expected rebound will come later than expected. But while the recovery has been delayed, the latest Covid restrictions will not derail the regional growth story and the outlook for local central banks and asset markets remains largely unchanged.

The Czech Republic provides a case in point. Although the country has suffered from one of the worst daily death rates in the world, this has not led to stricter lockdown measures in comparison to its European peers, thus not translating into a more pronounced fall in economic activity and in turn not warranting a material revision to the growth outlook relative to others.

The expected rebound in CEE economies from the second quarter onwards, as restrictions ease in the spring, should be driven by a mix of factors such as consumption, exports, and public

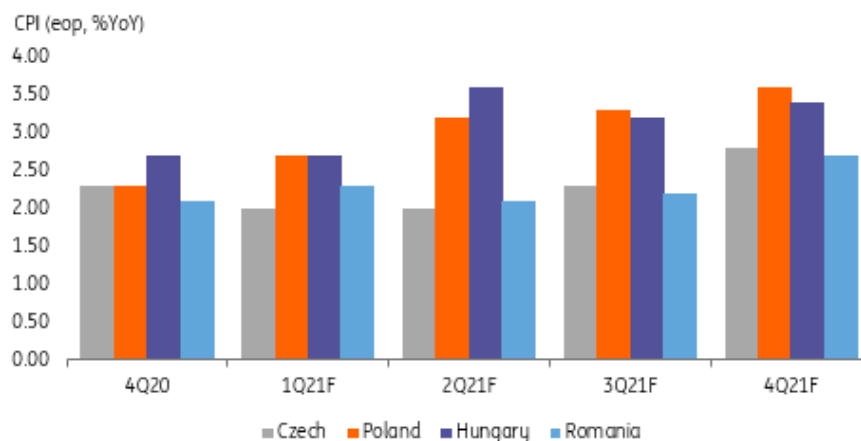
investment (with the strength of each varying among CEE countries).

... but this should have a limited impact on the stance of local central banks

On the inflation front, we will see some divergence in coming months (see the chart below). While in the Czech Republic, inflation will move temporarily lower, in Hungary and Poland, CPI should move above target, with Hungarian CPI likely to reach 4% in May (albeit temporarily and due to base effects). But the National Bank of Poland and Hungary are unlikely to react and should keep policy accommodative (both central banks should continue with QE and rule out rate hikes). The Czech National Bank should be a first mover in the region and Europe as whole, commencing a tightening cycle in the second half of the year as CPI picks up again.

Hence, and despite the delayed post-Covid recovery, the outlook for the region remains unchanged, with the CNB regaining its position as the hawkish outlier in Europe, while the NBP and the NBH leave their respective policies accommodative. In Romania, the central bank delivered a surprise 25bp rate cut in early January. Albeit a close call, we don't expect further rate cuts from here.

Diverging trends in CEE CPIs during the first half of the year



Source: ING

CZK still the top pick, HUF the least preferred

With the prolonged Covid restrictions having a largely non-differentiating impact on CEE economies and the outlook for local central banks remaining unchanged, our CEE FX view for 2021 has not changed either. We have a strong preference for the Czech koruna, a neutral view on Poland's zloty and the Romanian leu, and see Hungary's forint as the least attractive currency in the region.

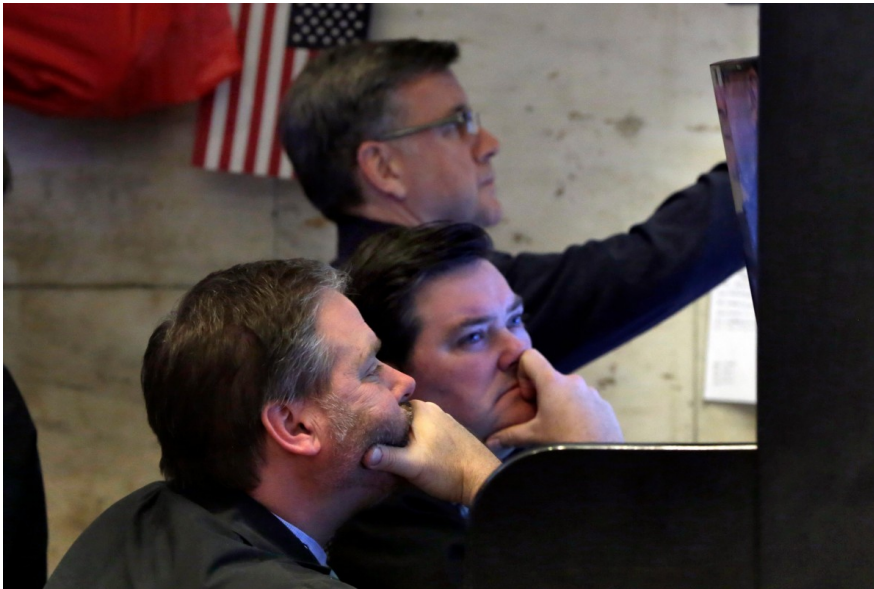
CZK should benefit from the most hawkish central bank in Europe. The 50bp tightening we forecast for this year should help EUR/CZK to move to 25.50, with a strong downside risk to 25.00. While the NBP continues to threaten FX intervention, this will be hard to justify from mid-year onwards once the economic recovery gains traction. Add to this the highest current account surplus in the region and EUR/PLN should dip below 4.40 in the second half of the year. In contrast, Hungary's non-tightening policy stance, less sound current account position (vs Poland) and preference for

gradual currency weakness all suggest that the forint should lag the koruna and zloty, with EUR/HUF likely moving higher in the second quarter as inflation starts to rise (albeit temporarily) towards 4%.

Cross currency opportunities: EUR spreads to outperform USD counterparts

We expect USD spreads to underperform against EUR in 2021.

Alongside this, we expect the cross-currency basis swap and 3m vs 6m roll to remain tight. In...

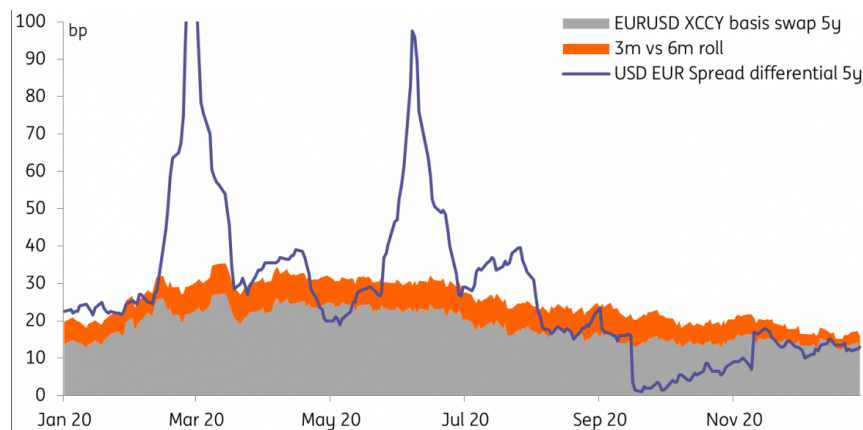


Corporate credit and Reverse Yankee supply implications

Following on from our report 'Cross Currency Swap Decomposition A rationale for swapping from USD into EUR', which you may be able to access [here](#) (under Developed Rates Strategy), we take a look at what this means for corporate credit and Reverse Yankee supply. As stated in the previous report, we find that swapping from USD to EUR is becoming more attractive in light of the widening of the spread in recent months. It will likely move wider, but even at current levels, there is opportunity to get cheaper funding.

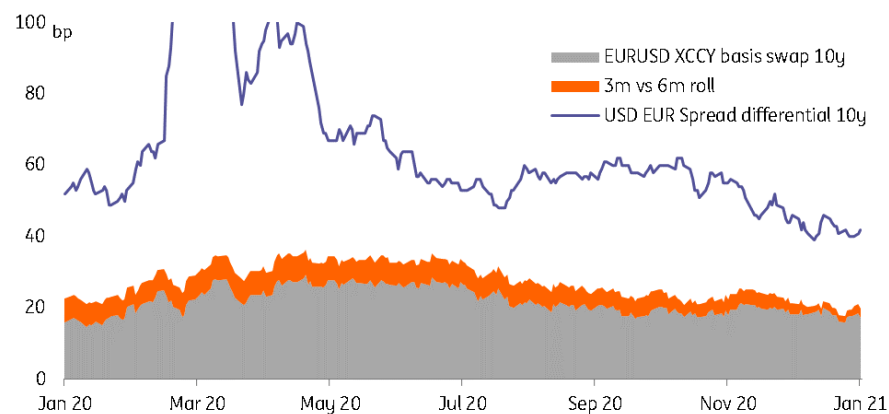
As seen in the two charts below, the cross-currency basis swap and the 3m vs 6m roll have tightened significantly. Furthermore, in the 10yr area, the USD EUR spread differential is notably wide. The 5yr spread differential on the other hand is significantly tight. At current levels, the long end of the curve offers an attractive cost-saving opportunity for US corporates to issue in EUR.

Cross currency basis swap 5yr & EUR USD spread differential 5yr



Source: ING, ICE, Refinitiv

Cross currency basis swap 10yr & EUR USD spread differential 10yr



Source: ING, ICE, Refinitiv

Examples indicate a similar picture

The table below illustrates the cost or saving for both European and US issuers to swap. As you can see, the 10yr+ area is very advantageous for US issuers to issue a EUR bond. Whereas the opposite can be said, but not to the full extent, for European corporates issuing in USD. As mentioned we expect the entire USD curve to underperform versus EUR and as a result, we will likely see the 5yr area also open up a cost-saving advantage for US corporates. However, this then eliminates any of the marginal cost saving seen for European corporates issuing in USD.

Swapping into home currency (bp)

European issuers	Tenor (yrs)	EUR	USD	USD Swapped	Saving/cost	US issuers	Tenor (yrs)	EUR	USD	EUR Swapped	Saving/cost
BMW	5	36	58	45	9	Pepsico	5	33	28	50	22
	10	40	77	58	18		10	36	58	59	1
							15	54	131	83	-48
Unilever	5	30	29	17	-13	IBM	5	34	40	50	10
	10	34	49	31	-3		10	48	88	78	-10
	15	39	71	49	10		15	72	153	104	-49
EDF	5	42	50	37	-5	General Electric	5	63	65	79	14
	10	55	114	95	40		10	84	126	107	-19
	15	117	216	170	53		15	145	234	185	-49
DT	5	37	68	53	16	AT&T	5	58	50	75	25
	10	95	160	125	30		10	81	125	105	-20
							15	149	237	192	-45

Source: ING

EUR spreads will outperform USD as ECB support remains across the curve

In 2021 we expect to see USD spreads underperform against EUR across the curve. Therefore, we will likely see the 5yr USD EUR spread differential also widen. USD curves have been particularly steep as a result of the short end limitation of the Fed support. The recent underperformance of USD is highlighted by the fact that the USD EUR spread differential is widening in the 5yr area of the curve, the exact area where both the US Federal Reserve and the European Central Bank were active. Naturally, the differential is much wider in the 10yr area where the FED was not directly purchasing. The cost-saving advantage in the 10yr is significantly higher and although these are indexed averages we can assume a funding advantage for almost all US corporates. Consequently, the majority of Reverse Yankee supply will be longer-dated bonds.

Many US corporates are likely waiting to issue multiple Reverse Yankee bonds in order to build their EUR curve

On saying that, we do still expect USD to underperform against EUR across the curve as the ECB remains active at roughly €5.5-6bn per month in EUR purchases. The Fed, on the other hand, has ended its purchasing programme for both corporates ETFs. Therefore, we may see a widening in the 5yr area of the spread differential, offering more Reverse Yankee likeliness. Many US corporates are likely waiting to be able to issue multiple Reverse Yankee bonds in order to build their EUR curve.

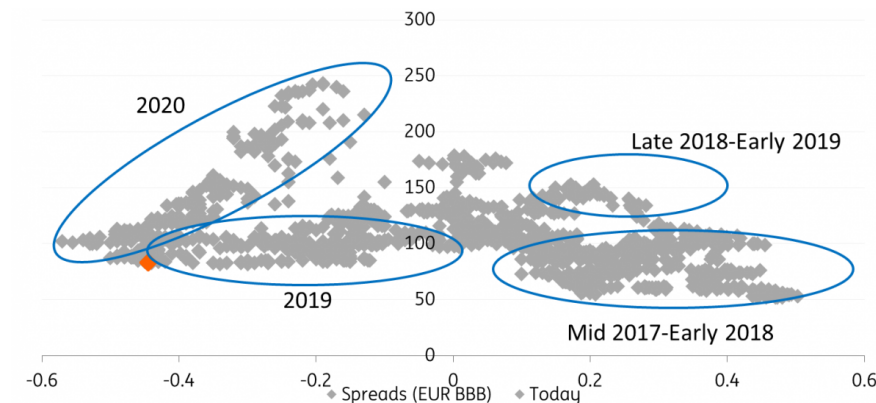
Apart from the ECB, other reasons we expect USD underperformance are;

The chart below illustrates the regression of yields to spreads, which shows constituents are currently deep in negative yield territory. Interestingly, 2019 also saw negative yields, but regardless of the direction that negative yields moved, spreads were locked in at or close to 100bp (in the case of a Euro BBB index). Essentially, negative underlying yields constrained further spread tightening, thus last year it seemed that in a negative rate yield environment there was no big movement in spreads.

In 2020, however, due to the substantial Covid 19 spread widening, this was no longer the case in terms of potential widening. Although, it is likely that the lack of tightening potential may hold

true, meaning that the squeeze from here will not occur whilst in negative yields. However, as we expect rates to rise this year the tightening potential for the short end of EUR spreads increases, and subsequently increasing the spread differential between EUR and USD on the short end.

Regression of euro yields to spreads over the past five years



Source: ING, ICE

The euro's strong and positive technical picture

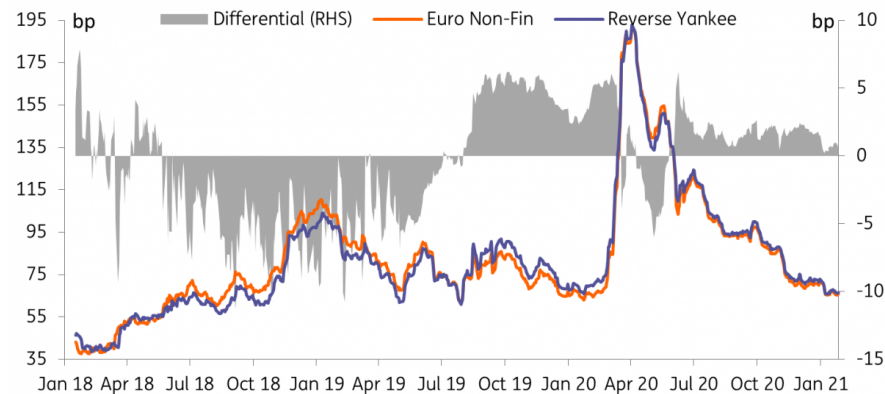
The technical situation in USD is not as positive as it is in EUR. The strong positive technical picture for EUR in 2021 will be a tightening driver for spreads. With a net corporate supply of just €270bn (€350bn supply expectation) as well as the increase in demand via continued ECB support and positive although limited mutual fund inflows. This results in just €50bn in positive EUR net supply for 2021. Indeed USD supply will substantially less than last year, with our expectation of around US\$800bn, combined with increased redemptions of US\$480bn, which is, of course, a positive technical swing. However, this is not as considerable as EUR.

The current low yields environment in Europe is credit tourism

The current low yields environment in Europe is credit tourism. Corporates will be attracted to the EUR credit markets and cheaper funding. Meantime, the search for yield will be very prevalent.

Interestingly, in the EUR credit market, US corporate EUR bonds only offer marginal spread premium versus European corporate EUR bonds as seen in the chart below. In saying that, it still holds true that Reverse Yankee issues tend to hold more premium in the primary market. Predominately, due to the US corporate bonds not being ECB eligible, we expect ECB eligible bonds to outperform in 2021, particularly in the second half of the year when we expect to see a slight widening in spreads.

Euro corporate non-financial versus Reverse Yankee corporate non-financial spreads



Source: ING, ICE

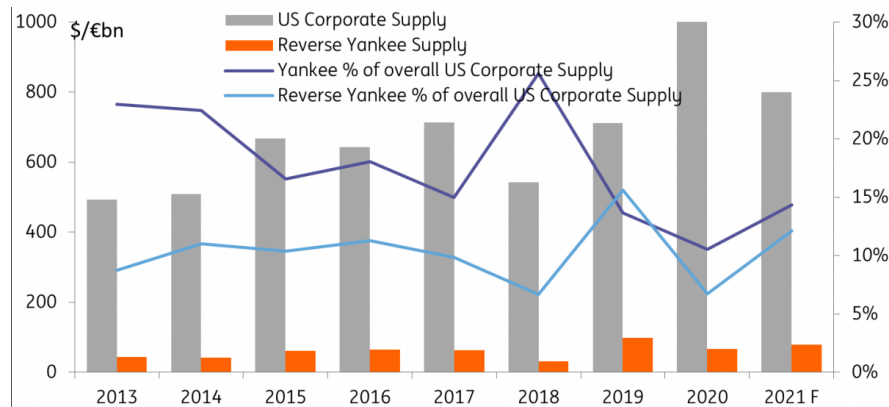
Reverse Yankee supply to return to 10% of US Corporates supply

2021 will continue to see the US issuer active in the European credit market driven by the fallen cross-currency basis swap, the need to diversify the funding mix after a USD focussed year, the current net funding advantage and the expected outperformance of EUR debt relative to USD. Supply as a whole is expected to return to normality after the substantial supply in 2020 but is likely to still be a sizeable amount of €350bn. Furthermore, we expect Reverse Yankee supply to play a role in this sizeable supply forecast. Our forecast for 2021 corporate reverse Yankee supply is €80bn. Hence last year reverse Yankee issuance at €65bn stood at 17% of total EUR IG issuance and only 7% of total US corporate (all currency) issuance.

We expect US corporate supply to fall from 2020's dizzying heights

We expect US corporate supply to fall from 2020's dizzying heights (given the coronavirus-related emergency liquidity needs) and we think US corporates will increase the share of euro funding and hit their trending average of 10% or more in the EUR currency. This is illustrated in the chart below, where we see the 2020 percentage of Reverse Yankee supply relative to domestic US corporate supply amounts to no more than 7%. For 2021, we expect US supply to return to the norm slightly, but still be a sizeable amount of \$800bn, marginally beating the previous records set in 2017 & 2019. Meantime the percentage of Reverse Yankee supply edges higher again to 10-12% of total USD supply like in 2017 and 2019. The means the total Reverse Yankee number is just over €80bn.

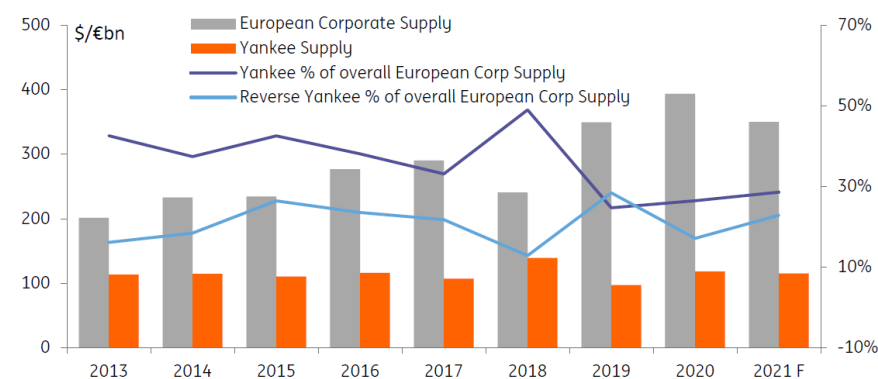
Corporate Yankee and Reverse Yankee Supply vs U.S. Corporate Supply



Source: ING, Dealogic

We also consider what percentage of EUR issuance is typically supplied by US corporates and see that the average here over the last few years (from 2014) stands at 25%. As seen in the chart below, we pencil in a forecast of €80bn, which will be roughly 23% of the €350bn we forecast for corporate supply. This is similar but slightly lower than 2019 when the arithmetic was also such that it offered a considerable cost-saving advantage.

Corporate Yankee and Reverse Yankee Supply vs European Corporate Supply



Source: ING, Dealogic

In conclusion, we expect the cross-currency basis swap to tighten further and remain tight for 2021. Alongside our expectation for USD spreads to underperform EUR, based on the lack of central bank support, EUR low yields environment being credit tourism, short end EUR outperformance and the stronger EUR technical picture. As a result, there will be a very attractive cost-saving opportunity for US corporates to issue EUR bonds and therefore we set our Reverse Yankee supply forecast at €80bn.

Authors

Timothy Rahill

Credit Strategist

timothy.rahill@ing.com

Jeroen van den Broek

Global Head of Sector Research

jeroen.van.den.broek@ing.com

Podcast | 29 January 2021

Listen: Risky business - corporate bonds are 'very expensive'

Fed Chair Jerome Powell said this week that the Bank is monitoring the corporate bond market, where spreads have narrowed to levels seen before the...



In this podcast, ING's Head of Sector Research Jeroen van den Broek tells Senior Editor Rebecca Byrne that very tight corporate bond spreads do not reflect the level of risk that investors are currently facing. The economic outlook is still uncertain, inflation is a growing concern and default rates are poised to stay elevated for a 'substantial' period of time.

Authors

Jeroen van den Broek

Global Head of Sector Research

jeroen.van.den.broek@ing.com

Rebecca Byrne

Senior Editor/Supervisory Analyst

rebecca.byrne@ing.com

IMF World Economic Outlook: A diverging growth path for emerging markets

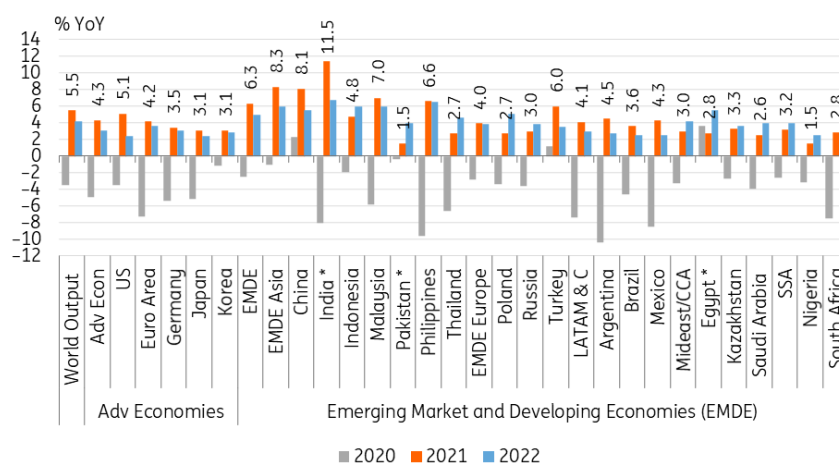
The IMF's latest World Economic Outlook update provides a glimmer of hope. After the 3.5% contraction in 2020, global growth is set to rise by 5.5%...



Source: Shutterstock

On an individual country level, there are substantial divergences, both in the growth outlook and in the revisions undertaken in the update.

IMF growth projections for 2020-22 across country groups and region (% YoY)



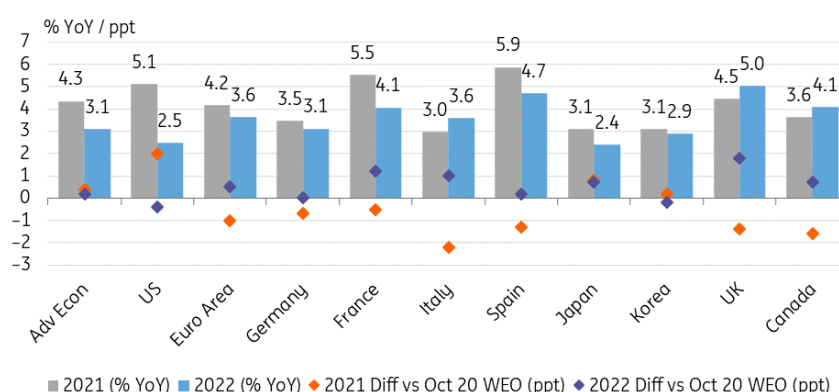
Source: IMF World Economic Outlook Update (January 2021), ING - * Fiscal year basis for Egypt, India and Pakistan

Fiscal stimulus and vaccine rollout give advanced economies a boost

The improved 2021 growth outlook is largely down to advanced economies which will grow by 4.3% (+0.4ppt vs October 2020 update), thanks to rapid vaccines rollout and supportive fiscal stimulus.

In particular, this has resulted in substantial upward revisions for the US (5.1% vs 3.1% in October 2020) and Japan (3.1% vs 2.3%), which make up for the lower projections for the Euro Area (4.2% vs 5.2%) and other advanced economies which are affected by rising infection cases and longer lockdowns.

Advanced Economies: Growth forecast for 2021 and 2022



Source: IMF World Economic Outlook Update (January 2021), ING

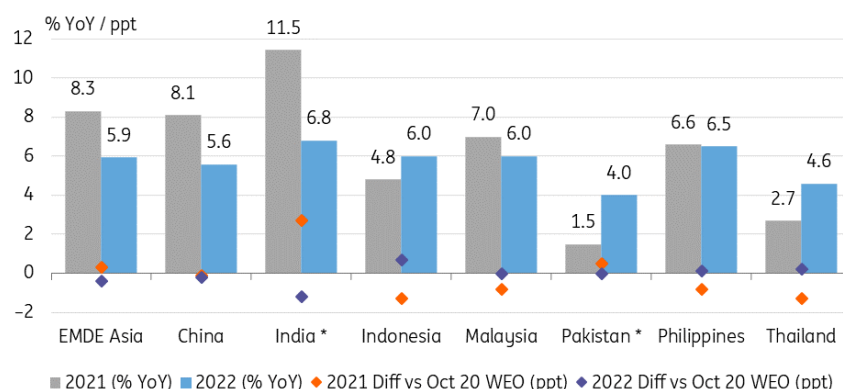
EM Asia runs ahead, Latin America recovery stands out

On aggregate, **emerging market and developing economies (EMDE)** have also seen upward revision to growth 6.3% (+0.3ppt), but the divergence in prospects remain. (regions sorted by

growth levels in 2021):

- **Emerging and Developing Asia** (+8.3% in 2021; +5.9% in 2022) remains the growth locomotive of the emerging and developing world in 2021, led by India (which saw a 2.7ppt upward revision to a whopping 11.5% for the fiscal year ending March 2022) and China (+8.1%).
- In contrast, most larger ASEAN economies are expected to see a delayed recovery, with downward revisions in the 0.8-1.3ppt area for Indonesia (+4.8% in 2021), Malaysia (+7.0%), the Philippines (+6.6%) and Thailand (+2.7%).

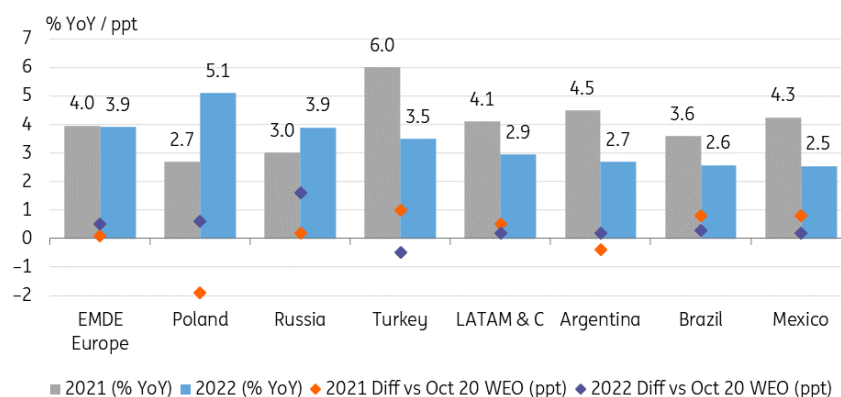
Emerging market and developing economies Asia: Growth forecast for 2021 and 2022



Source: IMF World Economic Outlook Update (January 2021), ING - * Fiscal year basis

- **Latin America and the Caribbean** (+4.1%; +2.9%) were hit by the deepest recession in 2020 across all regions (-7.4% vs -2.4% for EMDE on aggregate) but the IMF looks more optimistic for 2021, reflected by the 0.5ppt growth upward revision which is driven by Brazil (0.8ppt upward revision to +3.6%) and Mexico (0.8ppt upward revision to 4.3%). Both economies are also expected to fare a tad better in 2022 than previously assumed.
- In **Emerging and Developing Europe** (+4.0%; +3.9%), Turkey is seen growing by 6.0% (+1.0ppt vs October) after having already avoided a contraction in 2020 (+1.2%). However, Poland is only expected to grow by 2.7%, a 1.9ppt cut in comparison to the October 2020 forecasts.

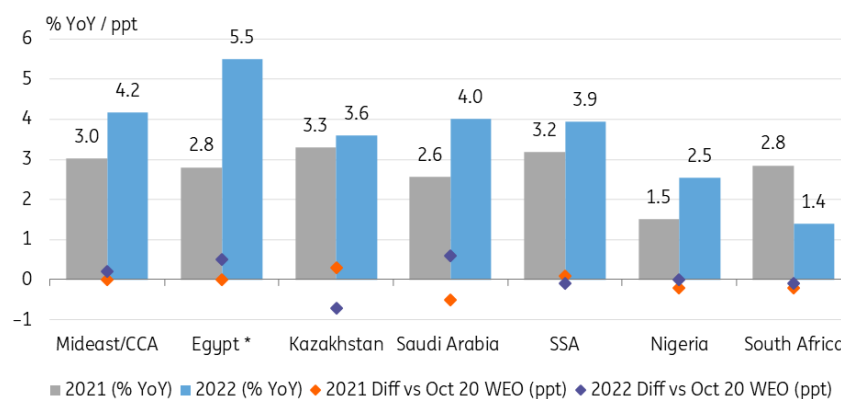
EMDE Europe / Latin America and the Caribbean: Growth forecast for 2021 and 2022



Source: IMF World Economic Outlook Update (January 2021), ING

- **Sub-Saharan Africa** (+3.2%; +3.9%) and **Middle East and Central Asia** (+3.0%; +4.2%) both see a muted recovery in 2021, with some of the lowlights found here: Saudi Arabia's growth forecast has been trimmed to 2.6% (-0.5ppt) while Nigeria (-0.2ppt to 1.5%) and South Africa (-0.2ppt to 2.8%) will also remain in low gear. South Africa also screens as the country with the lowest growth rate in 2022 (only +1.4%).

Middle East and Central Asia / Sub-Saharan Africa: Growth forecast for 2021 and 2022



Source: IMF World Economic Outlook Update (January 2021), ING - * Fiscal year basis

The IMF strikes a somewhat more optimistic tone thanks to vaccines and stimulus support which offset the weak near-term outlook in some parts of the world. Downside risks largely come from the pandemic (renewed virus surge possibly driven by new variants, extended lockdowns, vaccine rollout delays, unequal access to vaccines leading to inequality and unrest) and the risk of premature policy support withdrawal.

However, there are also upside risks thanks to vaccine prospects and spillover effects from supportive fiscal policies.

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>.