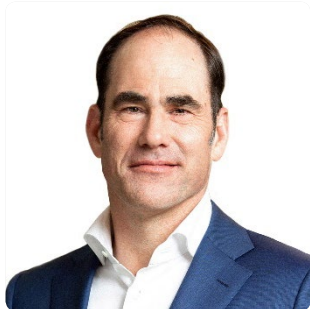


# ING Monthly

November 2023

Too early for optimism





## Too early for optimism

**With a less promising outlook on the horizon as we and many others had predicted, one major realisation has come to light for ING's Carsten Brzeski: being right isn't necessarily a good thing**

### **Boasting about being right in these circumstances would be wrong**

Cynics would say another month, another crisis. Tragic events in the Middle East amid the escalating Israel-Hamas conflict have once again shown us just how fragile the global economy currently is. They've also illustrated just how fragile geopolitics currently are, as well as how uncertain economic forecasts can be. This is a conflict with seemingly endless human tragedy, and it holds enormous potential to rock the global economy. As in the case of the ongoing war in Ukraine, the economic impact will not follow the traditional lines of trade flows, but rather via oil prices and ripples of increasing uncertainty. If the situation were to escalate further and if Iran becomes directly or indirectly involved, possible sanctions, further oil supply reductions or closure of the Strait of Hormuz could trigger a new surge in oil prices and consequently higher inflation. Recent demonstrations in the US and Europe – as well as individual terror attacks – could also bring the conflict to the Western world, weighing on economic sentiment at a time in which major economies are already weakening.

This brings me to the frustration of being right. Over the course of this year, we've rightly been challenged on our major calls of a slowing US economy and a eurozone economy being stuck in stagnation. Haven't both economies shown much stronger resilience than expected? In the case of the US, it did indeed. However, while we and many others might have been wrong on timing, the latest surge in bond yields and interest rates is very likely to push the US economy into a severe slowdown – only later than expected. In recent weeks, interest rates on credit cards surged to almost 30%, and mortgage and car loan interest rates jumped to 8%. It isn't unimaginable that the US economy could bow under this kind of interest rate pressure. We don't think it's a question of if, but when.

In Europe, stagnation has firmly become the new reality. The summer revival turned out to be weaker than hoped for and the latest sentiment indicators have dented any hopes of imminent improvement. Instead, new geopolitical uncertainties and the slowing of the US economy – together with the ongoing impact of ECB tightening so far – will once again test economic resilience over the winter months. It looks highly unlikely that the eurozone will be able to escape stagnation any time soon.

Major economies are now doing what they are supposed to do in the wake of aggressive monetary policy tightening: weakening. Some market participants may have simply forgotten that so far, the single most important driver of economic slowdown and recession since World War II has always been monetary policy tightening. With slowdowns on the rise, major central banks will eventually realise that their job of hiking rates is already done; but as long as headline inflation remains clearly above target, 'high for longer' will be the next stage of tightening. It could, however, very easily happen that this 'longer' period will be shorter than that of policy rate hikes. Interestingly, there seem to be first signs of central bankers preparing the ground for rate cuts even if inflation is not yet back on target. This would follow the principle of taking away some restrictiveness without moving again to accommodative monetary policies. We see actual and core headline inflation at around 3% as the magical level at which rate cuts could become a reality.

Kermit once sang that it's not easy being green. For us, with a less promising economic outlook on the horizon, it's not easy being right. And we don't take any pleasure from it.

### Our key calls this month:

- **United States:** With Treasury yields up around 5% and the dollar holding firm, financial conditions have undoubtedly tightened, reducing the need for another Fed rate hike. Consumer borrowing costs are moving rapidly higher, savings are being exhausted, and real household disposable incomes are falling. That means the risks to growth in 2024 remain to the downside.
- **Eurozone:** Growth turned negative in the third quarter and the next two quarters don't look very promising either. With inflation declining, the case for an additional rate hike is disappearing. However we don't expect any rate cuts before the summer of 2024.
- **United Kingdom:** The BoE is keeping the door open to further hikes, but we think the tightening cycle has finished. Higher mortgage rates will act as a growing drag on UK activity. Rate cuts are likely to start from next summer.
- **China:** It's been an eventful month in China. The economy has firmed up further, the government has pledged to expand the central government deficit. We've revised up our 2023 GDP forecast to 5.4%.
- **Central and Eastern Europe:** The story in the CEE region is becoming increasingly diversified due to varying economic outlooks, inflation profiles and reaction functions of central banks. We see more divergence looking forward than convergence, but some common themes remain that will temper the region's outlook in the year ahead.
- **Commodities:** Geopolitics will continue to dictate oil prices and the clear risk for the market is if an escalation in the Middle East leads to supply disruptions from some key producers in the region. We currently forecast ICE Brent to average \$90/bbl in 2024 and \$95/bbl in the second half of 2024.
- **FX:** November and December are normally soft months for the dollar. This year, however, the tailwind from strong US growth and hawkish Fed policy should keep the dollar bid through to year-end.
- **Market rates:** We're off recent highs for 10yr rates, but we think that the current momentum points to hitting those highs again, then likely breaking above. The Fed and the ECB may be done, but market rates are not. Despite geopolitics, market rates remain under upward pressure.

### Watch: Too early for optimism



[carsten.brzeski@ing.de](mailto:carsten.brzeski@ing.de)

## ING global forecasts

	2023				2024					2025				
	2Q23F	3Q23F	4Q23F	2023F	1Q24F	2Q24F	3Q24F	4Q24F	2024F	1Q25F	2Q25F	3Q25F	4Q25F	2025F
<b>United States</b>														
GDP (% QoQ, ann)	2.1	4.9	1.5	2.4	-0.3	-2.1	-1	1.3	0.5	1.5	1.9	2.2	2.0	1.1
CPI headline (% YoY)	4.1	3.6	3.4	4.1	3	2.6	2.2	1.7	2.4	1.9	2.0	2.2	2.3	2.1
Federal funds (% eop)	5.25	5.50	5.50	5.50	5.50	5.00	4.50	4.00	4.00	3.50	3.00	3.00	3.00	3.00
3-month interest rate (% eop)	5.20	5.40	5.40	5.40	5.40	4.90	4.40	3.90	3.90	3.50	3.00	3.00	3.00	3.00
10-year interest rate (% eop)	3.80	4.25	5.00	5.00	4.50	4.00	3.50	3.50	3.50	3.50	3.50	3.75	4.00	4.00
Fiscal balance (% of GDP)				-6.1					-6.3					-5.7
Gross public debt / GDP				97.2					100.7					103.2
<b>Eurozone</b>														
GDP (% QoQ, ann)	0.5	-0.3	-0.2	0.4	-0.2	0.6	1.2	1.1	0.2	1.6	1.6	1.4	1.4	1.4
CPI headline (% YoY)	6.9	5.0	3.7	5.9	3.4	3.3	3.0	2.4	3.0	1.9	2.0	2.1	2.1	2.0
Refi minimum bid rate (% eop)	4.00	4.50	4.50	4.50	4.50	4.50	4.25	3.75	3.75	3.50	3.25	3.25	3.25	3.25
3-month interest rate (% eop)	3.60	3.95	4.00	4.00	3.90	3.70	3.75	3.25	3.25	3.00	2.90	2.90	2.90	2.90
10-year interest rate (% eop)	2.40	2.80	2.80	2.80	2.70	2.60	2.60	2.70	2.70	2.70	2.70	2.90	3.00	3.00
Fiscal balance (% of GDP)				-4					-2.9					-2.6
Gross public debt/GDP				91.4					89.8					89.5
<b>Japan</b>														
GDP (% QoQ, ann)	4.8	-0.8	1.6	1.9	1.6	0.8	1.2	2.0	1.2	1.2	0.8	0.8	0.8	1.3
CPI headline (% YoY)	3.3	3.1	2.8	3.3	3.1	2.9	2.7	2.2	2.7	1.8	1.5	1.3	1.3	1.4
Interest rate on excess reserves (%)	-0.10	-0.10	-0.10	-0.10	-0.10	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25
3-month interest rate (% eop)	0.05	0.08	0.10	0.10	0.20	0.20	0.20	0.20	0.20	0.30	0.30	0.40	0.40	0.40
10-year interest rate (% eop)	0.40	0.70	1.00	1.00	1.00	1.00	1.20	1.20	1.20	1.20	1.20	1.25	1.25	1.25
Fiscal balance (% of GDP)				-8					-10					-8
Gross public debt/GDP				260.0					277.0					280.0
<b>China</b>														
GDP (% YoY)	6.3	4.9	5.8	5.4	4.2	4.2	5.1	6.1	5.0	5.8	5	4.1	5.20	5.0
CPI headline (% YoY)	0.1	-0.1	0.6	0.5	0.7	1.3	1.4	1.5	1.2	1.6	1.7	1.8	1.9	1.8
PBOC 7-day reverse repo rate (% eop)	1.90	1.80	1.80	1.80	1.80	1.80	1.80	1.80	1.80	1.90	2.00	2.00	2.00	2.00
3M SHIBOR (% eop)	2.17	2.30	2.30	1.90	2.15	2.15	2.15	2.15	2.15	2.15	2.25	2.30	2.30	2.30
10-year T-bond yield (% eop)	2.65	2.50	2.70	2.70	2.50	2.40	2.65	2.80	2.80	3.00	3.00	3.00	3.00	3.00
Fiscal balance (% of GDP)				-8.0					-6					-4
Public debt (% of GDP), incl. local govt.				131					132					129
<b>UK</b>														
GDP (% QoQ, ann)	0.8	-0.5	0.5	0.5	0.1	0.3	1.0	1.0	0.4	1.3	1.3	1.3	1.3	1.1
CPI headline (% YoY)	8.4	6.7	4.7	7.5	3.7	2.1	2.1	1.8	2.4	1.9	1.6	1.7	1.9	1.8
BoE official bank rate (% eop)	5.00	5.25	5.25	5.25	5.25	5.25	4.75	4.25	4.25	3.75	3.25	3.25	3.25	3.25
3-month interest rate (% eop)	5.40	5.40	5.25	5.25	5.25	5.05	4.65	4.15	4.15	3.60	3.20	3.20	3.20	3.20
10-year interest rate (% eop)	4.45	4.45	4.45	4.45	4.25	3.75	3.50	3.70	3.70	3.70	4.00	4.15	4.15	4.15
Fiscal balance (% of GDP)				4.1					2.9					2.4
Gross public debt/GDP				96.3					96.3					95.6
<b>EUR/USD (eop)</b>	1.08	1.06	1.06	1.06	1.08	1.10	1.12	1.15	1.15	1.15	1.14	1.13	1.12	1.12
<b>USD/JPY (eop)</b>	145	149	148	135	140	135	130	125	125	125	125	125	125	125
<b>USD/CNY (eop)</b>	7.24	7.30	7.30	7.30	7.25	7.15	7.00	6.90	6.90	6.80	6.70	6.60	6.50	6.50
<b>EUR/GBP (eop)</b>	0.87	0.87	0.87	0.87	0.88	0.89	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90
<b>ICE Brent -US\$/bbl (average)</b>	78	86	92	84	85	87	93	96	90	84	80	80	77	80
<b>Dutch TTF - EUR/MWh (average)</b>	35	34	50	43	55	44	40	45	46	50	40	30	40	40

Source: ING forecasts

# Geopolitics dominate commodity markets

**Warren Patterson**

Head of Commodities Strategy  
warren.patterson@asia.ing.com

**Geopolitics have rattled energy markets over the last month. And for oil, it's a theme which is likely to continue to dictate prices – at least in the short term**



There's no shortage of supply risks in the oil market at the moment, but for now, we're sticking to our base case

## Supply risks hang over the oil market

The oil market witnessed increased volatility over October, which shouldn't come as a surprise given the growing geopolitical risk in the Middle East over the last month. However, this increased volatility and strength in the market largely reflect supply risks rather than actual changes to supply and demand fundamentals. Up until now, the conflict between Israel and Hamas has not had an impact on oil supply from the region. Israel is a very marginal oil producer, so any disruptions to this output will not have an impact on the market.

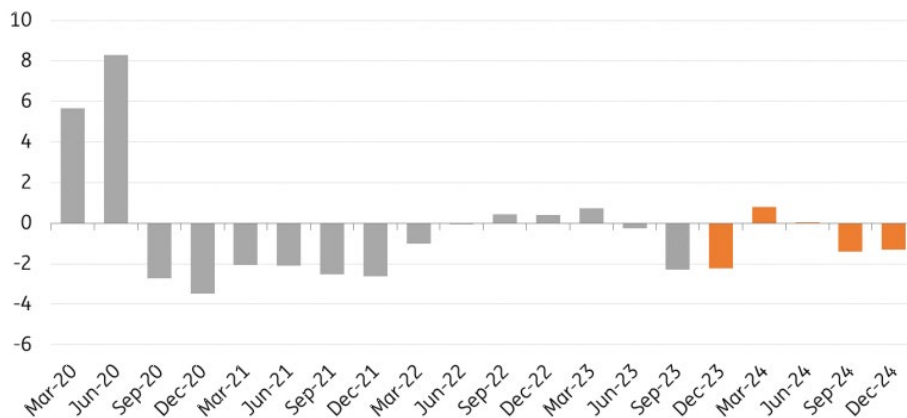
However, the clear risk for the market is if an escalation leads to supply disruptions from some key producers in the region. The most obvious supply risk in the current environment is Iran. While US sanctions against Iran remain in place, they have not been enforced strongly this year. As a result, we have seen Iranian oil supply growing from around 2.5m b/d at the start of the year to more than 3m b/d currently. Given concerns over higher energy prices, the US has decided not to strictly enforce these sanctions. However, if suggestions that Iran played a role in Hamas' attacks on Israel prove to be true – and if we continue to see attacks on US bases in the Middle East by Iranian-backed groups – the US could start enforcing sanctions more strictly once again. This could potentially remove anywhere in the region of 500k b/d to 1m b/d of Iranian supply.

Venezuela could partially offset potential supply losses from Iran. The US government recently reached a deal with the Venezuelan government whereby the US would ease sanctions in return for fairer elections in Venezuela in 2024. Expectations are that this could see an additional 200k b/d of supply over the course of 2024. However, there are risks to this. Since the deal, the Supreme Court in Venezuela has already suspended the results of the opposition's primaries. Clearly, the risk is that the US will reimpose sanctions if the Venezuelan government does not stick to its side of the deal.

While there are plenty of supply risks in the oil market at the moment, our base case remains unchanged. We assume Iranian oil supply will average 3m b/d over 2024. The oil

market should be in surplus in the first quarter of 2024, which should see a pullback in prices early next year. However, the market is then set to tighten for the remainder of 2024, particularly over the second half, which suggests further upside to prices. We currently forecast ICE Brent to average \$90/bbl in 2024 and \$95/bbl in the second half of 2024. However, the potential loss of Iranian barrels would leave the market in a deeper deficit and bring \$100/bbl oil back into play.

**Oil market returns to surplus in 1Q24 before tightening for the remainder of the year (m b/d)**



Source: ING Research, IEA, EIA, OPEC

**European gas storage full**

Geopolitics have also provided support to the European gas market in October with TTF breaking above EUR50/MWh. A leak found along the Balticconnector pipeline, which runs between Finland and Estonia was initially treated as a deliberate act of sabotage. While the pipeline is not significant in terms of wider European gas supply, the incident raised concerns over the vulnerability of European gas infrastructure as the region heads into the 2023-24 winter. More recently, however, it's less clear whether or not the damage was intentional.

Developments in the Middle East will also be providing support to the European gas market. While Israel is a very small oil producer, it does produce meaningful amounts of natural gas and exports some of this volume to Egypt. Following the Israel-Hamas conflict, Israeli gas flows to Egypt have stopped with Israel ordering the shutdown of one of its gas fields. Reduced pipeline flows to Egypt reduce its ability to export LNG to Europe through the winter. Although to be fair the volumes are relatively small – Egypt made up around 4% of total European LNG imports in 2022.

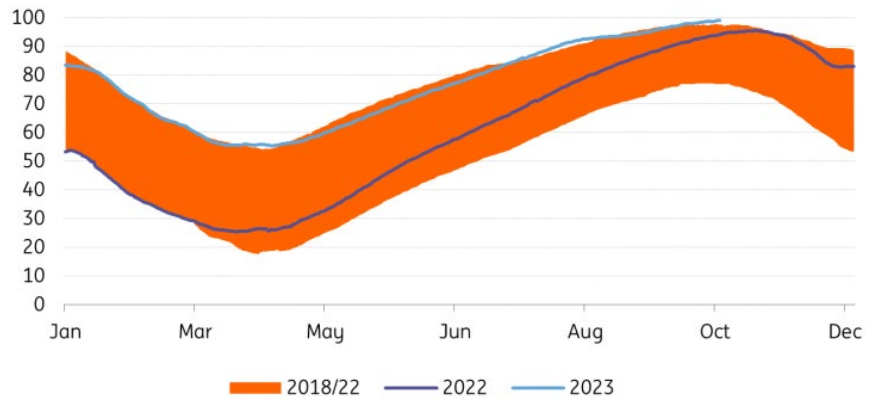
Despite some of the risks facing the European gas market, fundamentals in the short term remain bearish. European storage is now more than 99% full, which is record levels ahead of the start of the heating season.

The broader strength in the gas market means that for power generation it makes more sense to burn coal through the winter. Given that the region will want to ensure adequate gas storage at the end of the 2023-24 heating season (to make the injection season in 2024 more manageable), gas prices could remain relatively strong through the winter to ensure this trend continues.

In addition, European gas storage should start drawing over the coming weeks as the heating season gets underway. This should provide further support to the market. The risk to this view is if there is a late start to the heating season (as seen last year) when storage only started declining from mid-November.

However, assuming a normal winter, no significant supply disruptions and industrial demand remaining largely under pressure (at around 15% below the 5-year average), European gas storage should end the 2023-24 heating season with storage a little more than 40% full. While this is below the 56% seen at the end of the last heating season, it is still above the 5-year average of 34% full.

**European gas storage at record levels (% full)**



Source: GIE, ING Research

# Our view on the major central banks

We think that tightening cycles are now finished across the major economies, and we're expecting the first rate cuts from the likes of the Federal Reserve and the ECB by the middle of next year

## James Knightley

Chief International Economist, Americas  
james.knightley@ing.com

## Carsten Brzeski

Global Head of Macro and Chief Economist, Eurozone, Germany, Austria  
carsten.brzeski@ing.de

## Min Joo Kang

Senior Economist, South Korea and Japan  
min.joo.kang@asia.ing.com

## James Smith

Economist, Developed Markets  
james.smith@ing.com



Clockwise from top left: Bank of England Governor Andrew Bailey, Governor of the Bank of Japan Kazuo Ueda, US Federal Reserve Board Chairman Jerome Powell, European Central Bank President Christine Lagarde

## Federal Reserve

4.9% annualised third-quarter GDP, unemployment at 3.8% and inflation still well above target mean the Federal Reserve's 'higher for longer' narrative has gained increased traction, with Treasury yields hovering just below the 5% level. This has helped push mortgage rates above 8%, and with personal loan and credit card borrowing costs hitting multidecade highs, we are now seeing a clear tightening of financial conditions and the Fed regarding monetary policy as restrictive. This is giving us greater confidence that the Fed funds policy rate has now indeed peaked.

Consumer spending is key for the outlook for 2024 given it is 70% of economic activity. Real household disposable income has fallen in each of the past four months, savings are being run down, and consumer credit has turned negative with households repaying student loans. As such, the drivers of consumer spending are looking much less supportive and we expect economic activity to moderate. Inflation is moving in the right direction and we see this process continuing given the deteriorating consumer fundamentals. We acknowledge that we were too aggressive in expecting rate cuts – but we still see more scope for policy easing through 2024 than the market is currently pricing. We look for rate cuts to start in the second quarter, with the policy rate ending the year at 4%.

James Knightley

## European Central Bank

The European Central Bank has finally realised that its growth optimism might have been too much. While ECB officials had tried to talk up market expectations about further rate hikes after the September meeting, the message at the October meeting was a different one. The central bank has become much more cautious regarding the



eurozone’s growth outlook. Disappointing sentiment indicators – and most of all, the ongoing impact of the policy rate hikes so far – suggest a further weakening of the eurozone economy. As inflation should also continue to come down, there is very little need for the ECB to consider further rate hikes any time soon. Instead, we think that it has already reached peak interest rates and has now entered the next phase of its tightening cycle: high for longer.

**Carsten Brzeski**

### Bank of Japan

The Bank of Japan is expected to ditch its Yield Curve Control (YCC) policy in the next quarter once global rates stabilise. The BoJ recently decided to allow 10Y JGB to float above 1%, and continuing to ease the reference would make YCC policy meaningless. A weak yen will continue to add to inflationary pressures, and we believe next year’s wage growth could be strong enough to convince the BoJ to normalise its policies.

Our call is that we see YCC scrapped in the first quarter of next year and that a rate hike will follow in the second. The risk, however, is that the BoJ believes a sustainable return to the inflation target is not reachable, especially if we only see a slight growth in wages. That could see the central bank maintaining its policy easing for longer.

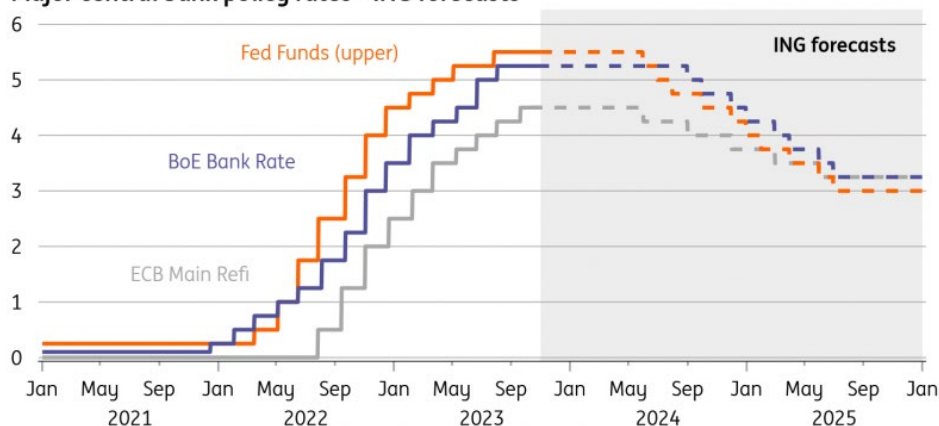
**Min Joo Kang**

### Bank of England

The Bank of England is keen not to shut the door to further rate hikes, and it would prefer the most recent on-hold decision to be viewed as a pause rather than a definite end to the rate hike cycle. It’s true that another hike can’t be totally ruled out, especially if we get some unpleasant surprises in either services inflation or private-sector wage growth over the next month or two. But we think that’s unlikely, and there are now clear signs of disinflation in the pipeline – not least because the jobs market is weakening. The battle is now keeping rate cut expectations at bay, and initial policy easing is now being priced for next summer. That’s our view too, especially if we’re right that core inflation will be back below 3% by then. We ultimately expect rate cuts to take us back to the 3% area by mid-2025.

**James Smith**

**Major central bank policy rates - ING forecasts**



Source: Macrobond, ING

## James Knightley

Chief International Economist, Americas  
james.knightley@ing.com

# Higher for longer means more headwinds for US growth

**With Treasury yields up at 5% and the dollar holding firm, financial conditions have undoubtedly tightened, reducing the need for another Fed rate hike. Consumer borrowing costs are moving rapidly higher, savings are being exhausted, and real household disposable incomes are falling. That means the risks to growth in 2024 remain to the downside**



Fed Chair, Jerome Powell

## The US continues to confound expectations

Twelve months ago, the consensus view was that rapid and aggressive monetary policy tightening coupled with a growing reluctance of the banks to lend would inevitably take its toll on the economy. Recession was the consensus call. Yet, in the third quarter, the economy expanded at a 4.9% annualised rate, unemployment was just 3.8%, and inflation remained closer to 4% than the 2% target.

Having confounded expectations, financial markets have embraced the Fed's higher-for-longer narrative on interest rates with 10Y Treasury yields up at 5% and the dollar strengthening to 12M highs on a trade-weighted basis. This is leading to a significant tightening of financial conditions in the US economy, helping to push mortgage and car loan interest rates above 8% and credit card interest rates to all-time highs. Given all that, Federal Reserve officials increasingly acknowledge that we are close to the end of the tightening cycle with policy widely regarded as restrictive. In our view, interest rates have peaked.

Nonetheless, with inflation still well above target, officials are refusing to close the door on possible extra rate hikes, if only to ensure the market doesn't move to the mindset that the next move is inevitably a cut and traders should start to price for that. We expect 10Y treasury yields to remain near 5% through the current quarter.

## Recent market moves intensify the challenges for 2024

The Federal Reserve wants to see clear evidence of slowing activity to be confident that inflation will return to 2% sustainably. We are now doubtful that there will be enough evidence for this to prompt an interest rate cut in 1Q 2024 and have subsequently pushed back the start point for Fed rate cuts to the second quarter. Recent upward

revisions to income data suggest that households may have more residual savings than previously thought, and this can keep positive growth momentum throughout 4Q and into early Q1.

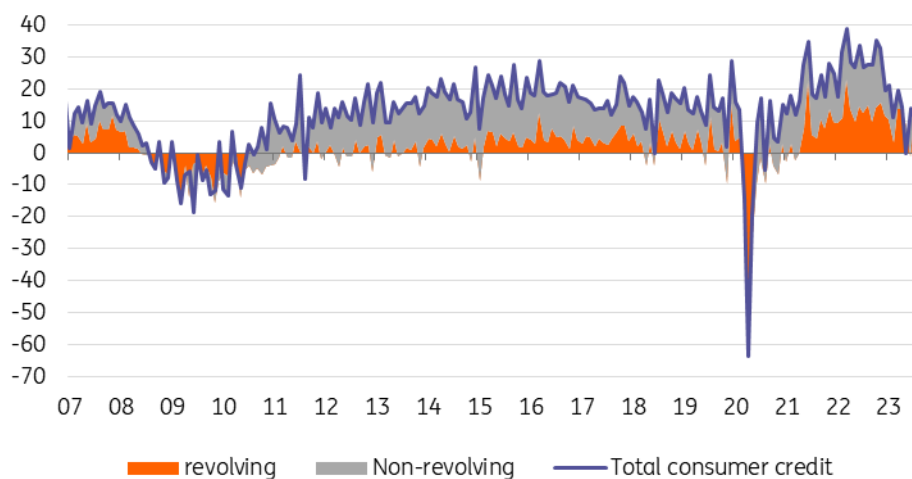
However, we remain more cautious about 2024's growth prospects relative to the consensus view, which should help to dampen inflation pressures more significantly than the Fed currently expects. In turn, we believe that this offers policymakers the room to cut interest rates more significantly than is currently priced by markets.

**Consumer spending is key and fundamentals are weakening**

Consumer spending is key for the outlook given it is 70% of economic activity. Real household disposable incomes have fallen in each of the past four months, savings have been run down, and the suspicion is many households have exhausted them, while consumer credit has turned negative with households repaying student loans. As such, the drivers of consumer spending are looking much less supportive. With loan delinquencies on the rise and banks' reluctance to lend pointing to credit growth turning negative in the coming months, the stresses in the household sector are becoming more apparent.

**Consumer credit has turned negative**

Monthly change in consumer credit (US\$bn)



Source: Macrobond, ING

Commercial real estate is another area of potential stress. There are lingering fears that low office occupancy, falling property prices and upwards of \$1.5tn of debt needing to be refinanced over the next couple of years could see landlords increasingly handing back the keys to lenders. This could see loan losses mount, particularly for small and regional banks which are responsible for two-thirds of the lending to the sector, compounding the problems for an economy where credit flow is so critical.

Given this situation, we need to see consumer fundamentals improve quickly. Real household disposable incomes are critical to the economy's prospects, and if they don't recover, we fear that the economy will experience a contraction in the middle quarters of 2024.

The one consolation is that inflation is slowing and we expect that process to continue as the housing rents slowdown story becomes more apparent in the data. This should give the Federal Reserve the opportunity to respond to economic weakness, with the Fed funds rate forecasted to end the year at 4% with the 10Y Treasury yield down at 3.5%.

# The eurozone is flirting with recession

## Peter Vanden Houte

Chief Economist, Belgium, Luxembourg,  
Eurozone  
peter.vandenhoute@ing.com

**Eurozone growth turned negative in the third quarter and the next two quarters don't look very promising either. With inflation declining, the case for an additional rate hike is disappearing**



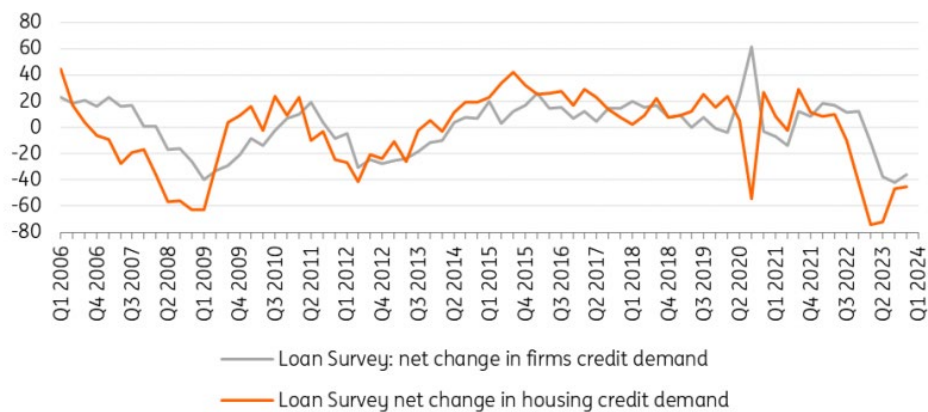
A bit like this loved-up couple in Paris, the eurozone economy is also flirting... with recession

## The economy has come to a standstill

It seems that not much has to happen to push the eurozone into recession. According to the flash estimates, the economy shrank by 0.1% in the third quarter, implying only 0.1% year-on-year growth. The fourth quarter has already started on a weak footing, with the composite PMI output index falling back to 46.5 in October, a 35-month low. Eurozone economic sentiment also lost ground in October and is now 0.6% below the third-quarter average.

Order books deteriorated in both industry and construction, an indication that further production cuts are to be expected. Some counterweight is offered by the services sector, where sentiment improved slightly, according to the European Commission. However, services sentiment also remains below its long-term average and in the Purchasing Managers Survey, there was even a deterioration in confidence.

### Loan demand has fallen to recession levels



Source: LSEG Datastream

### Geopolitical uncertainty could translate into weakening sentiment

The increased uncertainty on the back of the tensions in the Middle East might lead to more cautious behaviour from both businesses and households. At the same time, monetary tightening will be increasingly felt. Third-quarter bank lending surveys indicated that credit standards became tighter across the board, even more so than initially expected. And for the fourth quarter, further tightening is expected.

Not surprisingly, borrowing for fixed investment dwindled, indicating that investment in the eurozone economy is likely to soften in the quarters ahead. The fact that capacity utilisation in industry fell below its long-term average in the third quarter is a further indication of future weakness in business investment.

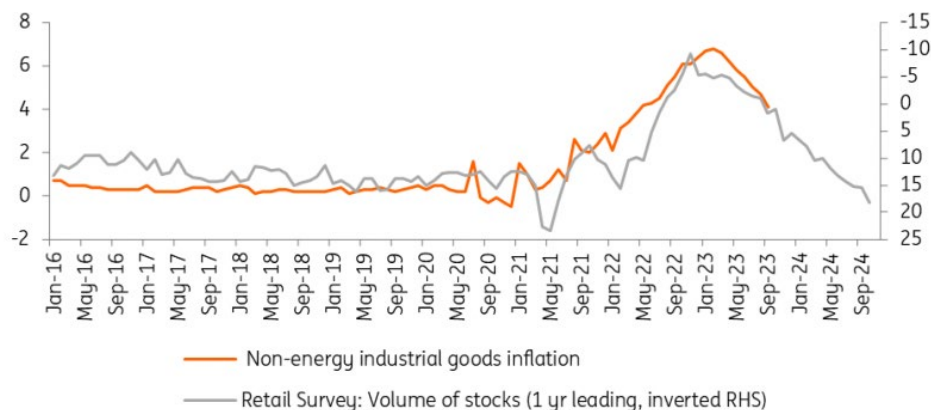
As for households, real income growth is certainly supportive of consumption, though the weakening labour market and higher interest rates will probably increase the savings ratio, thereby tempering consumption growth. All in all, we expect flat to slightly negative GDP growth over the next two quarters, followed by a timid recovery from the second quarter of 2024 onwards. By then, the impact of monetary tightening should gradually peter out. This results in 0.4% GDP growth for 2023 and – as a result of the weak base effect – only 0.2% growth for next year.

### Inflation downtrend continues

HICP inflation fell more than expected in October to 2.9%, the first sub-3% reading since July 2021. With retail inventories at unusually high levels, we expect disinflation in the goods sector to continue over the next 12 months. However, at 4.6%, services inflation remains high and selling price expectations in the services sector are still firmly above the pre-pandemic level. There is also an increase in both natural gas and oil prices over the last months that will contribute to headline inflation.

That said, with the economy coming to a standstill, second-round effects might be more muted this time. Overall, the downtrend in inflation is likely to continue, though not in a straight line, and we still expect inflation to average 3% in 2024.

### High inventories will push down goods inflation



Source: LSEG Datastream

### Case for additional rate hike is fading away

The European Central Bank (ECB) also acknowledges that growth is weaker than it pencilled in. At the same time, the increase in bond yields has further tightened monetary conditions. In that regard, additional rate hikes are no longer needed. But that doesn't mean that the ECB is in a hurry to cut rates. Both President Christine Lagarde and Chief Economist Philip Lane emphasised that they first need to have a good view of wage agreements in the first half of 2024 before giving the all-clear on inflation.

We don't expect any rate cuts before the summer of 2024. At the same time, a growing number of the members of the Governing Council want to stop the reinvestment of the pandemic emergency purchase programme holdings before the end of 2024. We think that this will indeed happen in the second half of next year, but since it will be accompanied by rate cuts, potential tensions in the bond market should remain limited.

# Policymakers in China look to the future after a crisis averted

**Rob Carnell**

Regional Head of Research, Asia- Pacific  
rob.carnell@ing.com

**It's been an eventful month in China. The economy has firmed up further, the government has pledged to expand the central government deficit, and President Xi Jinping has promised to open China to foreign investors ahead of major policy meetings**



China's president, Xi Jinping

## **Economy firms further, but questions remain**

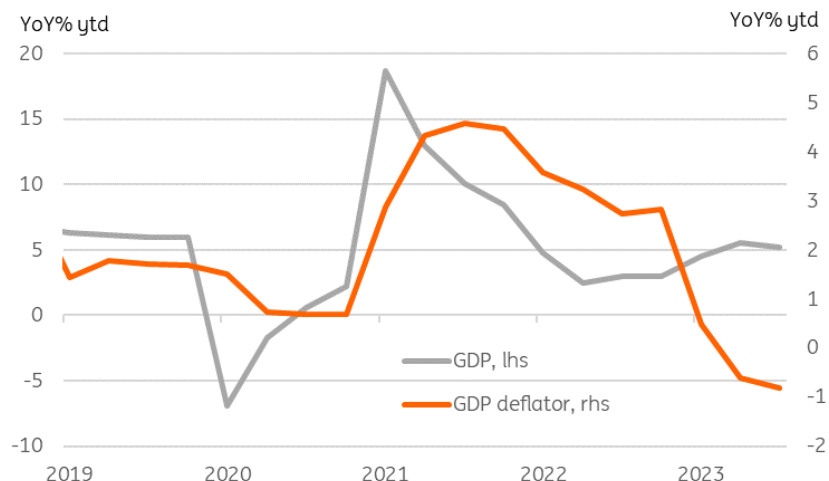
The last month has seen China reach some important milestones. August data had already begun to show that the economy was not in a downward spiral and was bottoming out. That was reinforced with third-quarter GDP data, which beat expectations with a 4.9% year-on-year growth rate. Together with some helpful historical revisions, this means that the hurdle for achieving 5% full-year growth is now very low.

Fourth-quarter GDP now only has to achieve a 4.2% YoY growth rate for full-year GDP to hit 5.0% (rounding up to one decimal place). Given all the distortions taking place last year, it may be more helpful to consider what needs to happen on an incremental basis to seasonally adjusted GDP. Measured like this, any positive growth at all in quarterly real GDP will ensure the 5% target is hit.

There are still some questions about the economy. Things don't seem to be getting worse, but after a decent bounce in August, the September retail sales increase was fairly marginal. Real GDP is also getting a substantial boost from a negative GDP deflator which in the third quarter recorded a year-to-date (YTD) rate of -0.82%, in contrast with consumer price inflation which is still hovering around zero. That looks a bit odd, but helps to lift real GDP figures while it persists.

Furthermore, the most recent purchasing manager indices (PMIs) showed that after September, the momentum of the economy slowed in October. While it will probably still be positive, incremental economic growth in the fourth quarter is likely to come in below that of the third quarter.

### Real GDP and GDP deflator



Source: CEIC, ING

### Growth forecasts for 2023 revised up to 5.3%

Monthly activity data for September tended to reinforce the message that the economy is bottoming, although there remain pockets of concern. Most notably, these include anything related to the property sector, which is still struggling – and by extension, infrastructure investment, where growth rates are still positive but slowing.

The net result of all this is that we have had to revise our full-year GDP forecast back up. We're placing it at 5.4%, comfortably above the 5% target rate. The same arithmetic that is proving helpful to the 2023 numbers isn't quite having the same effect for 2024, which we are struggling to push up above 5% even with some more optimistic underlying growth rates.

### Upcoming policy flashpoints

There are a number of important upcoming meetings in China in the near future. Perhaps the most important of these is the 3rd plenum of the 20th Central Committee (although there are also meetings of the Politburo and National Financial Work Conference).

The 3rd plenum will set the economic tone for the next five-year plan. In the past, these meetings have provided a forum for big economic reforms. Areas where we may expect to see strong policy commitment for development or restructuring could include:

- **Technology and innovation** (highlighted in February's Two Sessions meetings, with semi-conductor self-reliance a priority).
- **Foreign investment:** A possible taster for a more open Chinese economy came at the recent Belt and Road Forum, where President Xi Jinping suggested that all barriers to foreign investment in the manufacturing sector would be removed and talked up the goal to forge more free trade agreements.
- **Housing registration:** There have been many piecemeal changes at the city level to China's complicated housing registration (Hukou) system in the last year. However, a more coordinated approach to help reinvigorate the housing market may be a priority given the current problems with that sector and the associated problems with local government debt.

We may also hear more about plans to expand the central government's deficit, which has been strictly held at 3%. An outline of a plan to issue an additional CNY 1 trillion of sovereign debt has been put forward, and we could learn how that is to be funnelled; perhaps to restructure existing local government debt and financing vehicles, or to provide more support to construction during this adjustment phase.



# UK headed for stagnation as rate hikes start to bite

**James Smith**

Economist, Developed Markets  
james.smith@ing.com

**Higher savings rates have so far helped offset only modest increases in average mortgage rates. But that's set to change through 2024, and this means higher interest rates will act as a growing drag on UK activity. Rate cuts are likely to start from next summer**



Governor of the Bank of England Andrew Bailey

## **Higher savings rates have helped offset higher mortgage rates so far**

The Bank of England's rate hike cycle has almost certainly concluded, and the focus is now switching to rate cuts. Policymakers are adamant that these are a long way off, a view that markets have largely bought into. While we've seen a big repricing lower in UK rate expectations this summer, investors still expect Bank Rate to stay north of 4% for the next three years.

We're less convinced. Bank rate closer to 3% seems like a more sensible medium-term level, and cuts are likely from next summer. Part of that is a recognition that much of the impact of past rate hikes is yet to hit the economy.

So far, the average mortgage rate has risen from 2% to just above 3%, despite quoted rates on new lending surpassing 6% over recent months. By contrast, the rate paid on instant access savings has increased by almost 200 basis points in the same period – and fixed-rate saving rates by considerably more still. In other words, the impact of higher rates on household cashflows has thus far been relatively neutral.

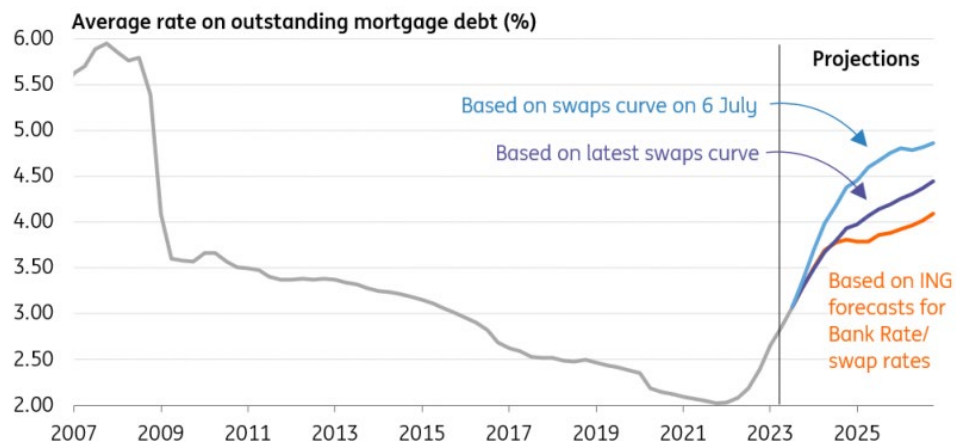
## **But that's set to change.**

The fact that the vast majority of mortgage lending is fixed for less than five years means a sizeable chunk of UK homeowners will refinance over the next year, much more so than in places like the US or parts of Europe where longer-term fixes are more prevalent.

Our estimates show that the average rate on UK mortgages will rise to close to 4% by the end of next year, even under our base case, which includes Fed rate cuts from the spring, BoE cuts from the summer and an accompanying slide in bond yields. And it's important to remember that the negative impact of higher lending rates is likely to be

much larger than the positive impulse we've had from higher deposit rates so far in this tightening cycle.

### Average rate on outstanding mortgages set to approach 4% in 2024



Projections are based on the split of mortgage lending by initial fixation period, and assume an even proportion of borrowers refinance each quarter (for example, one eighth of those with two-years fixes). We have also assumed that a recent bias towards shorter fixation periods for those refinancing persists such that the share of those with two-year fixes gradually climbs.

Source: Macrobond, ING calculations

### The impact rate hikes will be felt more heavily next year

Those benefitting from higher savings rates are typically higher earners who are less likely to spend the windfall. The same is unlikely to be true of higher mortgage rates, and we'd expect an ever-increasing drag on consumer spending as a result.

For businesses, the hit from higher rates has been more rapid. The higher prevalence of floating rate debt – especially for smaller businesses – appears to be taking its toll on cash holdings and margins. Unemployment does appear to be rising as a result, though issues with the data are making it difficult to be sure about how rapidly this is happening. Business surveys, including the PMIs, are weak too – but again, these also appear to be suffering from reliability issues.

Any hope that some of these pressures will be offset by the Treasury would be misguided. The Chancellor will unveil his latest budget later this month, but there's very little space for stimulus. Borrowing this year may have been roughly £20 billion lower than expected, but that windfall will be quickly eaten up by upward revisions to future debt repayments.

Put of all of this together, and it seems likely that the economy is headed for near-stagnation and possibly even recession, though the latter isn't our base case.

While it's true that higher mortgage rates are a challenge, remember that only around a quarter of households have a home loan these days, and a considerably higher proportion own their home outright. The backdrop for real wages is also improving, with inflation set to fall noticeably over coming months and private-sector nominal pay growth proving much stickier. Whether or not we do end up in recession will largely depend on whether the recent uptrend in unemployment persists through the winter months.

## One region but very different stories for CEE countries

**Frantisek Taborsky**  
EMEA FX&FI Strategist  
frantisek.taborsky@ing.com

The story in the CEE region is becoming increasingly diversified due to varying economic outlooks, inflation profiles and reaction functions of central banks. We see more divergence looking forward than convergence, but some common themes remain that will temper the region's outlook in the year ahead



A man at a recent election rally in Poland

### **Poland:** Shift in power should unlock Poland's investment potential

In Poland, the opposition has now secured a majority in the recent general elections. A new government should be formed this year, committed to restoring the rule of law and unlocking the Recovery and Resilience Facility (RRF) payments. In 2024, Poland could receive €8 billion in grants. A shift in priorities could raise growth potential and also help with funding high borrowing needs and pre-election pledges. Gradually, this should unlock Poland's investment potential. After lagging behind its CEE peers, EU funding and increased FDI confidence should enable the country to begin catching up.

The new coalition aims to deliver its fiscal pledges, potentially adding PLN 30-35 billion to the 2024 budget, and we expect to see expansionary fiscal policy over the coming years. In our view, extra borrowing needs may not increase POLGGB yields with foreign investors returning (foreign holding of 15% versus 25-30% in the rest of the region) and advances/loans from the RRF.

The third quarter of 2023 proved a turning point in the Polish economy. We estimate that GDP growth last quarter reached 0.5-0.7% year-on-year. Given a weak first half of the year, we expect full-year growth to come in at 0.4% YoY. Consumer spending should recover while EU-backed projects revive construction – both of which are likely to continue next year.

We forecast 2024 growth at 2.5% with risks to the upside, given improved investment prospects. Headline CPI moderated again in October, likely allowing for another 25bp rate cut from the National Bank of Poland (NBP) next month. However, the MPC may be less eager to ease in 2024. Extra fiscal risks still remain, and PLN gains may not last. NBP President Adam Glapiński's comments following the November meeting could also provide key insights.

The zloty rallied after the elections, and the rate has now stabilised around 4.46 as investors await the formation of the new government. In the short run, the MPC's stance should prove key as investors need clarity on NBP policy in the new political environment. The long end failed to rally alongside PLN as the fear of higher borrowing needs emerged. We expect some foreign inflows at the long end, allowing for tighter spreads against the German curve in the short run. Longer-term prospects are mixed at best, as extra fiscal stimulus looms for next year.

### **Czech Republic: Central bank within reach of inflation target**

The Czech economy disappointed again in the third quarter, and it's now confirmed that we will have to wait a little longer for a recovery. While we do not know the details, the monthly data suggests that the weakness in the economy is widespread. The only driver of the economy is essentially the auto sector, which is still benefiting from the recovery that followed the Covid-19 pandemic and problems with supply chains in the past.

Once again, it seems that the lowest unemployment level in the EU is a problem for the economy. On the other hand, however, we see great progress in the decline in inflation, which fell to 6.9% YoY in September. We believe this will be the lowest level this year. However, the main story here is that household energy prices are falling faster and earlier than expected. This should moderate the increase in the year-on-year rate over the coming months due to base effects from the previous year. We therefore expect growth to take us only slightly above 8% and fall back below that level by the end of the year. It should reach close to the central bank's 2% target in January.

The Czech National Bank (CNB) confirmed its readiness to discuss rate cuts in September, and we expect the cutting cycle to start by the end of this year. However, as a result of a fairly certain drop in inflation early next year, there is a possibility that the CNB could begin accelerating the pace soon. This leads us to the question of where the terminal rate is. We think it is 3% in the Czech Republic, as indicated by the central bank, which will be the target for the current board. In our forecast, we expect the rate to end at 4% next year – but it is clear that the main issue for the CNB will be maintaining the stability of inflation near the target, which will drive the cutting pace next year.

### **Hungary: The moment of truth approaches**

We are now at a critical juncture in Hungary. Firstly, there's an ongoing debate regarding EU funds. The Hungarian government has responded to the nine questions posed by the European Commission and the net 90-day review period is quickly nearing its end with less than 10 days to spare. A big part of the Cohesion Fund (EUR 13 billion) is at stake, and we anticipate a resolution soon. Another defining moment in the upcoming weeks will be the release of the third-quarter GDP figures. Our forecast indicates the end of the technical recession, due largely to both agriculture and industry. Despite this, we continue to maintain our full-year call, estimating a 0.5% reduction in this year's real GDP as compared to 2022.

The most significant problem in the economy (and for the budget) continues to be consumption. Even though real wage growth is expected to turn positive by September, we doubt that it will have a significant impact on consumption. Household purchasing power has plummeted to 2021 levels as a result of rampant inflation in the last two years, with consumer confidence hovering at a 10-year low in parallel.

However, this strain will ease in 2024 as disinflation and positive real wage growth come together. The September inflation reading was better than expected, leading us to lower our short-term inflation estimates. We expect the average annual figure to be at 17.8%, with a year-end reading of 7% year-on-year. Nonetheless, our 2024 prospects remain stable at 5.1% due to an increase in both global and domestic inflationary risks. Improved inflation dynamics and the HUF's surprising resilience provided the National

Bank of Hungary (NBH) with the ammunition to execute a 75bp rate cut in September. Consequently, we expect the central bank to maintain this momentum and cut rates further in the coming months, with the year-end base rate at 10.75%.

Nevertheless, the pace of cuts will decelerate in the first quarter as disinflation slows, and from there the anchor could be the ex-post real interest rate (around 200-300bp) in our view. As a result, we expect the forint to gain strength, subject to the situation regarding the EU deal. Our projection is for 375 EUR/HUF by year-end and 365 EUR/HUF in the middle of next year, bolstered by the region's most favourable positive real rate and carry.

### **Romania: Signs of bottoming in the economy**

The latest hard frequency data continues to point to a mixed sectorial picture in Romania, although overall, we see signs of a bottoming of the economy. Essentially, growth is dependent on one engine these days – the public infrastructure investments. This translates into a booming construction sector with civil engineering projects. Some help with GDP growth is likely to come from net exports as well and – while this is usually a large unknown – the agriculture sector. All of these factors are likely to keep the economy green in the third quarter of this year, offsetting the less overwhelming developments in industry and services. Our 1.5% GDP growth estimate for 2023 is looking rather conservative as it requires rather meagre 0.1-0.2% quarterly advances of the economy, which look reasonably within reach.

We continue to expect 150bp of rate cuts from the National Bank of Romania (NBR) in 2024, although we have shifted the starting point from the first to the second quarter – most likely at the April 2024 meeting. On-hold for longer seems to be considered by the NBR a safer choice than starting to ease as we're now seeing in Poland, Hungary and most likely the Czech Republic. Meanwhile, it remains likely that any upward pressure on the EUR/RON will be used as an opportunity to mop up some of the excess liquidity from the local market, leading to a stable FX rate. As for the outlook on the liquidity itself, as uncomfortable as the central bank might be with the situation, the latest numbers (+29bn RON in September) together with the higher budget deficit target announced by the Ministry of Finance make a return of liquidity levels to anywhere near the historical average quite unlikely for the foreseeable future. The liquidity surplus has most likely become a structural feature of the local banking system.

Relevant risks stem from the fiscal package recently adopted, which might be consistent with a higher for longer local rate environment, and possibly lower growth in the private sector. The upside of this is likely the fact the European Commission will allow for a deviation from the planned budget deficit reduction, with this year's target probably somewhere in the 5.5-5.7% of GDP range and next year in the 4.5-5.0% of GDP. While accumulating delays, the absorption of EU funds via the National Recovery and Resilience Plan (NRRP) and the multiannual financial frameworks (MFF) is likely to continue without any major hiccups.

# The Italian economy looks set to stagnate over the winter

**Paolo Pizzoli**

Senior Economist, Italy, Greece  
paolo.pizzoli@ing.com

Softening growth and rising debt servicing costs are re-awakening debt sustainability concerns, which call for a swift return to primary surpluses. How big these will have to be will also depend on whether the government will manage to effectively implement the Recovery and Resilience Plan



Italy's financial district in Milan

## Italian GDP stagnated in the third quarter as monetary tightening finally bites

The Italian economy is no exception. After a relatively quick post-Covid rebound, accommodated by the coexistence of expansionary monetary and fiscal policies, the economy has been cooling down since the second quarter of 2023, mainly on the back of softening domestic demand. After contracting by 0.6% quarter-on-quarter in the second quarter, Italian GDP was flat in the third – just about avoiding a technical recession.

With a notable delay since the start of the tightening cycle, the cumulated effect of past interest rate hikes has finally started showing up in credit data. In August, loans to non-financial corporations contracted by 7.9% year-on-year and loans to households for house purchases just expanded by 0.6% YoY. According to the latest Bank of Italy bank lending survey, loan demand is also expected to remain weak over the fourth quarter.

## Not the best environment for investments; consumption looking better

High interest rates, credit contraction and an increasingly uncertain geopolitical backdrop are a bad mix for investments. The ongoing phasing-out of very generous tax incentives (the so-called “super bonus”) should continue to act as a drag on the residential sector in the fourth quarter of 2023, whilst the non-residential component could potentially benefit from the recent payment of the third tranche of the Recovery and Resilience Facility, worth some €18.5bn, partially compensating.

Consumption, which had been a key growth driver during the re-opening wave, is likely holding up better, helped by a resilient labour market. In August, revamped employment and falling unemployment brought the unemployment rate down to 7.3%, a level not

seen since January 2009. Hiring intentions in recent business surveys continue to suggest that risks of a swift turnaround in employment remain low. Resilient employment and a progressive renewal of expired wage contracts at higher rates (hourly wage growth has stabilised at 3% YoY in the June-August period) should help support disposable income through the next winter, paving the way to a gradual recovery in consumption over 2024, and allowing for a gradual recovery of the savings ratio to pre-Covid levels (c.8%). Within the projected winter stagnation, private consumption should not be a drag on growth.

### **Disinflation should help, more likely in 2024**

The prospective growth profile will also be affected by developments on the inflation front, at least in 2024. The October CPI release marked a sharp fall in headline inflation to 1.8% (from 5.3% in September), thanks to a favourable base effect on energy products. Even though a return above 2.0% through the winter seems inevitable, the disinflationary wave should resume over 2024, creating a better growth environment via an improvement in households' purchasing power but also supporting a recovery in consumer confidence.

All in all, we expect the Italian economy to stagnate in the fourth quarter of this year and the first quarter of 2024, but see room for a gradual acceleration starting in the second quarter of next year. As 2023 will leave 2024 with a poor statistical carryover, it will be hard for average 2024 GDP growth to do better than 0.5% YoY.

### **Debt sustainability concerns re-awakened by a normalising environment...**

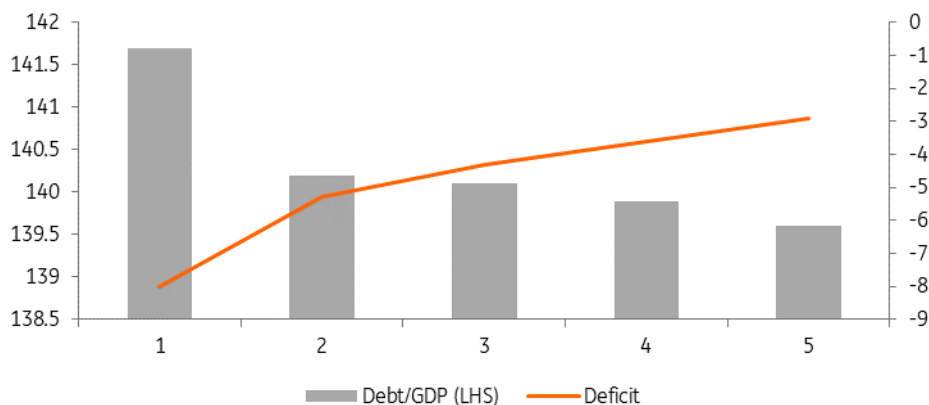
Softer growth and the rising cost of debt are resurrecting debt sustainability concerns, given the sheer size of the Italian public debt. The recent widening in the BTP-Bund spread (now hovering just below the 200bp level in the 10y tenor) has accompanied the genesis of the draft budgetary plan (DBP) recently submitted by the Italian government to the EU Commission. To be clear, the DBP, while projecting a deficit decline delayed with respect to the original plan (deficit at 5.3% in 2023 and 4.3% in 2024), is not a disruptive one.

The profile of deficit data is being affected by the impact of the new accounting rules adopted by Eurostat for tax credits, which tend to penalise 2023 with respect to 2024 (when part of the incentives will be phased out). In this context, the 1.1% correction in the structural budget foreseen for 2024 in the DBP, at face value a substantial one, should be treated with some caution. The tax credit accounting factor also shows up in public debt dynamics with a small delay, i.e. when the tax credit is actually cashed in.

The combined effect of slow adjustment, accounting rules and slowing inflation translates into an unpleasantly flat debt profile in the DBP, with the debt/GDP ratio down a whisker from 140.2% in 2023 to 139.6% in 2026. A flat profile with upside risks attached, given the underlying assumptions of 1.2% GDP growth in 2024 and optimistic expectations of (undefined) privatisations worth 1% of GDP over the 2024-2026 time span.

### The uncomfortable flat debt

GDP profile of Italy's Draft Budgetary Plan



Source: Italy's Draft Budgetary Plan 2024

### Calls for a return to sustained primary surpluses of around 1.5% of GDP

Looking beyond 2026, when the bulk of the tax credit noise should disappear from public finance data, a declining debt dynamic will almost inevitably call for a sustained return to solid sustained primary surpluses. In fact, in 2025, the Italian debt/GDP ratio dynamic will likely cease benefitting from the current positive 'snowball effect' (i.e. a negative difference between the average cost of debt and nominal GDP growth) driven by the solid post-Covid economic rebound and by the inflation surprise accentuated by the war in Ukraine. As expiring debt is refinanced at higher interest rates and inflation cools down, the snowball effect looks set to turn negative, as it has historically been when low growth-normal inflation environments prevailed.

How big should primary surpluses be to secure debt stabilisation under reasonable macro assumptions? To find out, we ran a simulation with our base case growth and rates forecasts, which foresee a temporary acceleration in GDP growth towards the 1% level in 2025 and 2026 (the last two years of the implementation of the National Recovery and Resilience plan) and assuming a subsequent stabilisation of growth at 0.6% and inflation at 2%. What we get is that a primary surplus of c.1.5% of GDP would be required to stabilise the debt/GDP in a normalised interest rates environment. While seemingly ambitious, this is a level that Italy has been able to sustain for prolonged periods in the past.

### Growth enhancing reforms and investments are key

As debt stabilisation would unlikely be deemed acceptable by any prospective fiscal rule (be it the old SGP or an amended version of the EU Commission proposal) a bigger effort would be required to secure a declining debt/GDP profile, the alternative being managing to sustainably increase the growth potential of the economy. The Italian government has a powerful tool to this end: the Recovery and Resilience Plan and its mix of reforms and investments. Its thorough implementation will likely become the single most important mission for the rest of the legislature, also for debt sustainability reasons.



## FX: Dollar to defy seasonal trends

### Chris Turner

Global Head of Markets and Regional  
Head of Research, UK & CEE  
chris.turner@ing.com

**November and December are normally soft months for the dollar. This year, however, the tailwind from strong US growth and hawkish Fed policy should keep the dollar bid through to year-end**



### **Fed-driven dollar weakness will be a story for 2024**

The dollar opens November close to the highs of the year. Normally, November and December are soft months for the dollar. This year, however, it is hard to see the dollar giving back its gains before year-end.

Driving that dollar strength continues to be US macro outperformance, which lends credibility to the Federal Reserve's hawkish position. The recent rise in US rates has largely come at the long end of the curve and has so far made little difference to the dollar. The view is that tighter US financial conditions are hardly good news for pro-cyclical currencies in Europe or Asia.

Equally, it seems too early for investors to view the sell-off in Treasuries as a dollar negative. There have been brief occasions in the past where the dollar has had a negative correlation with US yields – but these occasions have been few and far between. Instead, a disorderly rise in US yields is largely viewed as a risk-negative, dollar-positive event.

In fact, the most likely path to a weaker dollar will probably have to come from softer US macro data. The route to a weaker dollar through a re-rating of Chinese or European growth prospects looks unlikely. And even if high US rates prompted something to 'break' somewhere in the financial sector, the first move in the dollar would be higher as dollar funding conditions would invariably tighten – albeit temporarily.

Given our house view that a US slowdown is more likely in the next quarter rather than this one, we therefore expect EUR/USD to end the year around this 1.05/1.06 area and USD/JPY to end the year not far from 150. Into 2024, however, we expect the short end of the US curve to start moving lower ahead of Fed easing next summer and the dollar to turn lower.

We are also cognisant of the risk that Fed easing does not always deliver a higher EUR/USD. For example, the Fed cut rates nearly 500bp in 2001 and EUR/USD went nowhere. Our forecast for a eurozone recession, a difficult return of the Stability and Growth Pact, and the ongoing threat of a geopolitical spike in oil prices present downside risks to our view of a Fed-driven rise in EUR/USD to 1.10 next summer and 1.15 by year-end 2024.

## Rates: Still biased to rise

### Padhraic Garvey

Head of Global Debt and Rates Strategy/  
Regional Head of Research, Americas  
padhraic.garvey@ing.com

We're off recent highs for 10yr rates, but we think that the current momentum points to hitting those highs again, then likely breaking above. The Fed and the ECB may be done, but market rates are not. We risk reverting higher until or unless we see material labour market weakness, especially in the US



There are many good reasons to expect the upward pressure on market rates to be sustained

### Key levels have been hit, and there's more to come

In the past month, the US 10-year yield has touched 5%, and 10-year Euribor hit 3.5%, with the Bund practically hitting 3%. All key levels, and a clear manifestation of a prior pivot from the unnaturally low rates seen during the pandemic years. Even the 10-year Japanese Government Bond (JGB) is now belatedly journeying toward 1%, a level not seen in a decade. There are many good reasons to expect the upward pressure on market rates to be sustained, at least until we see a material change in the complex macro mix that continues to feature a tint of residual strength – or at a minimum, resilience. Inflation is down but not out, meaning the battle continues.

The Bank of Japan had been a hold-out for a long time, but the manifestation of this in yen weakness has been there for all to see for a prolonged period. The European Central Bank (ECB) was also relatively slow to kickstart hikes. Even the Federal Reserve was late to the rate hike process as inflation was allowed to take hold first. The ECB and the Fed are likely done at this point, but the bond market is not yet calling a halt to upward pressure on longer-dated rates. There are lots of reasons to worry, but also lots of reasons to expect a continuation formation where market yields remain elevated with ambitions to re-test higher. We are likely at or close to highs, but can also still march higher first.

In the past couple of days, there has been a material move lower in market yields, with the US 10yr down to 4.65% and the 10yr German bund yield down to 2.7%. This is below recent highs of 5% and almost 3% respectively. The key driver has been evidence of stress in expectation measures. There has also been continued success in getting inflation lower. On top of that, the US Treasury issued issuance plans that took some pressure off longer-dated maturities. We aren't convinced that this is the end of rises in long-dated market rates, though. For that to happen, we'd need to see material labour market weakness – especially in the US.

### **Higher real rates as a function of deficit and labour market pressure, with the BoJ only getting started**

Moving forward, we identify several factors that can pressure longer-dated yields even higher. First, there is the concern that JGBs finally have lift-off. While we are not convinced this is necessarily catastrophic for US Treasuries, it does, at the margin, pressure the spread to Treasuries tighter. Any hint of structural US dollar weakness would limit the protection in higher Treasury yields further from the point of view of the international investor. This can often become a self-fulfilling prophecy, where the marginal investor runs scared of the story, bringing higher yields with it.

Second, while Treasury Secretary Janet Yellen has suggested that higher real yields do not reflect the higher US deficit, it's tough to agree with this assertion. Higher deficits most definitely correlate with higher real yields, and the US is now staring down the barrel of a \$2 trillion refunding requirement. All other things being equal, such heavy supply pressure correlates with a steeper curve, primarily driven by higher real yields. The US 10-year real yield is now approaching 2.5%. It does not need to ratchet a whole lot higher, but there is also no immediate impulse for it to pull lower.

Third is the conundrum that is tight labour markets. We see this in the US front and centre. But even in the eurozone, there is no material generalised labour market angst. There is even an element of this apparent within many emerging markets and in other developed markets, like Australia. Something in the works is keeping the labour market ship afloat despite the tightening pressures coming from central banks. This won't last forever, as the pressure at a certain point will become too much. But for now, it remains a source of pressure for the maintenance of high market rates.

The latter point is important as there will be a tipping point ahead, but we are not at it now. For that reason, the highs hit in the past month for Treasury yields, Euribor rates and Bund yields are still liable to be seen again. That means above 5% for the US 10-year Treasury yield, and 3% for the German 10yr bund yield remain targets during bouts of bond market weakness.

We're on the eve of a pivotal payroll report too, which will have a material effect, either validating the recent fall in market rates, or causing a re-consideration of the better mood on bond markets this week; where a decent report puts renewed upward pressure on yields. For choice we're expecting the latter.

**GDP forecasts**

Developed Markets (QoQ% annualised growth)							
	3Q23F	4Q23F	1Q24F	2Q24F	2023F	2024F	2025F
US	4.9	1.5	-0.3	-2.1	2.4	0.5	1.1
Japan	-0.8	1.6	1.6	0.8	1.9	1.2	1.3
Germany	-0.4	-0.2	-0.4	0.6	-0.2	0.2	1.4
France	0.4	0.0	0.2	0.8	0.9	0.6	1.3
UK	-0.5	0.5	0.1	0.3	0.5	0.4	1.1
Italy	0.2	0.1	0.5	0.8	0.7	0.5	1.0
Canada	0.5	1.3	0.0	-0.5	1.2	0.2	1.6
Australia	1.2	0.8	0.8	2.4	1.9	1.6	2.9
Eurozone	-0.3	-0.2	-0.2	0.6	0.4	0.2	1.4
Austria	-2.4	0.0	0.6	0.8	-0.3	0.1	1.5
Spain	1.2	0.6	0.6	1.4	2.5	1.2	2.1
Netherlands	-0.1	1.1	0.9	0.2	0.3	0.9	1.5
Belgium	2.0	0.0	0.0	0.8	1.4	0.7	1.4
Greece	1.7	-0.4	1.1	1.8	2.3	1.5	1.9
Portugal	-0.8	-0.4	0.2	1.2	2.0	0.4	2.1
Switzerland	0.4	0.0	0.8	0.8	0.7	0.6	1.4
Sweden	0.0	-1.4	0.4	0.9	-0.5	0.0	1.3
Norway	0.9	0.8	1.5	1.5	1.3	1.2	1.7
Emerging Markets (YoY% growth)							
	3Q23F	4Q23F	1Q24F	2Q24F	2023F	2024F	2025F
Bulgaria	1.6	1.7	1.7	2.4	1.7	3.1	3.5
Croatia	3.5	3.5	2.8	2.4	3.1	2.6	2.7
Czech Republic	0.2	1.1	2.0	2.2	0.0	2.2	2.2
Hungary	-0.2	1.7	2.8	4.2	-0.5	3.4	3.8
Poland	0.7	1.8	2.1	3.5	0.4	2.5	3.5
Romania	3.0	2.3	2.4	3.3	1.5	2.8	3.5
Turkey	3.5	3.4	3.5	2.9	3.7	2.5	3.5
Serbia	1.7	2.1	2.9	4.3	2.1	3.0	3.7
Azerbaijan	1.7	2.0	4.0	2.5	1.2	2.5	2.7
Kazakhstan	5.0	4.7	4.2	4.0	5.0	4.5	4.0
Russia	5.3	3.5	3.0	1.5	3.0	1.5	1.0
Ukraine	3.5	3.5	-	-	5.9	5.5	-
China	4.9	5.8	4.2	4.2	5.4	5.0	5.0
India	7.8	7.2	6.8	3.4	6.9	6.6	7.5
Indonesia	5.2	5.0	5.6	5.1	5.2	5.0	5.1
Korea	1.2	1.6	1.6	1.3	1.2	1.8	2.4
Philippines	4.2	4.0	3.8	4.8	4.7	4.5	5.0
Singapore	0.7	1.9	2.8	2.6	0.9	2.7	2.8
Taiwan	2.0	3.6	3.9	3.2	0.9	2.9	2.6

Norway: Forecasts are mainland GDP  
 Source: ING estimates

**CPI Forecasts (pa)**

%YoY	3Q23F	4Q23F	1Q24F	2Q24F	2023F	2024F	2025F
US	3.6	3.4	3.0	2.6	4.1	2.4	2.1
Japan	3.1	2.8	3.1	2.9	3.3	2.7	1.4
Germany	5.8	3.6	3.2	3.1	6.1	3.0	2.1
France	5.5	4.5	4.4	3.7	5.8	3.5	2.2
UK	6.7	4.7	3.7	2.1	7.5	2.4	1.8
Italy	5.8	1.9	2.4	2.4	6.3	2.3	2.0
Canada	3.7	3.6	3.5	2.4	4.0	2.3	2.0
Australia	5.4	5.0	4.7	4.5	5.9	4.1	2.8
Eurozone	5.0	3.7	3.4	3.3	5.9	3.0	2.0
Austria	6.7	4.1	3.0	2.6	7.5	2.4	2.0
Spain	2.8	3.7	3.9	3.4	3.7	3.2	2.3
Netherlands	2.8	1.4	3.4	2.9	4.3	2.7	1.5
Belgium	3.2	2.4	4.0	3.7	4.4	3.5	2.1
Greece	3.2	3.3	2.8	2.3	4.2	2.4	2.0
Portugal	3.5	3.5	2.9	2.5	4.8	2.4	2.2
Switzerland	1.6	1.8	2.0	2.0	2.2	2.0	1.8
Sweden	5.0	3.5	2.4	2.2	5.5	2.0	2.0
Norway	4.5	3.2	2.9	1.5	5.2	2.2	2.5
Bulgaria	7.5	5.9	4.5	4.4	9.8	4.4	4.6
Croatia	7.3	5.5	5.2	5.2	8.2	4.8	3.4
Czech Republic	8.3	8.4	2.6	2.4	11.0	2.4	2.0
Hungary	15.4	8.6	5.0	5.2	17.8	5.1	3.7
Poland	9.7	6.4	4.7	4.2	11.5	4.9	5.0
Romania	9.2	7.3	6.5	5.4	10.6	5.2	4.2
Turkey	61.5	69.6	69.6	73.6	54.9	58.2	26.8
Serbia	11.4	8.2	6.4	5.2	12.5	5.2	4.8
Azerbaijan	7.5	3.4	6.6	3.1	9.1	5.5	5.6
Kazakhstan	13.0	10.5	9.3	8.8	14.8	8.5	6.7
Russia	5.1	7.3	7.6	7.6	6.0	6.8	4.3
Ukraine	15.5	15.0	15.0	-	16.7	12.6	-
China	-0.1	0.6	0.7	1.3	0.5	1.2	1.8
India	6.4	4.0	4.3	4.2	5.3	4.3	4.8
Indonesia	3.5	3.4	3.6	3.5	4.0	3.5	3.6
Korea	3.1	3.9	3.1	2.8	3.8	2.3	1.9
Philippines	5.5	4.7	3.6	3.9	6.0	4.3	3.5
Singapore	4.3	3.9	3.4	3.2	4.9	3.1	2.8
Taiwan	2.5	2.1	1.7	1.6	2.2	1.6	1.8

\*Quarterly forecasts are quarterly average; yearly forecasts are average over the year, HICP for Eurozone economies

Source: ING estimates

**Oil and natural gas price forecasts (avg)**

	4Q23F	1Q24F	2Q24F	2023F	2024F	2025F
Brent (\$/bbl)	92.00	85.00	87.00	84.00	90.00	80.00
Dutch TTF (EUR/MWh)	50.00	55.00	44.00	43.00	46.00	40.00
<b>Metals forecast</b>	<b>4Q23F</b>	<b>1Q24F</b>	<b>1Q24F</b>	<b>2023F</b>	<b>2024F</b>	<b>2025F</b>
Copper	8,500	8,600		8,582	8,750	9,000
Aluminium	2,250	2,350		2,283	2,500	2,700
Nickel	20,000	20,000		22,351	20,000	23,000
Zinc	2,650	2,700		2,695	2,800	2,900
Lead	2,150	2,200		2,125	2,150	2,100
Gold	1,950	2,000		1,929	2,050	2,000
Silver	24	23		23	24	23
Iron Ore	100	100		108	95	90

Source: ING estimates

## 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 <https://www.ing.com>.