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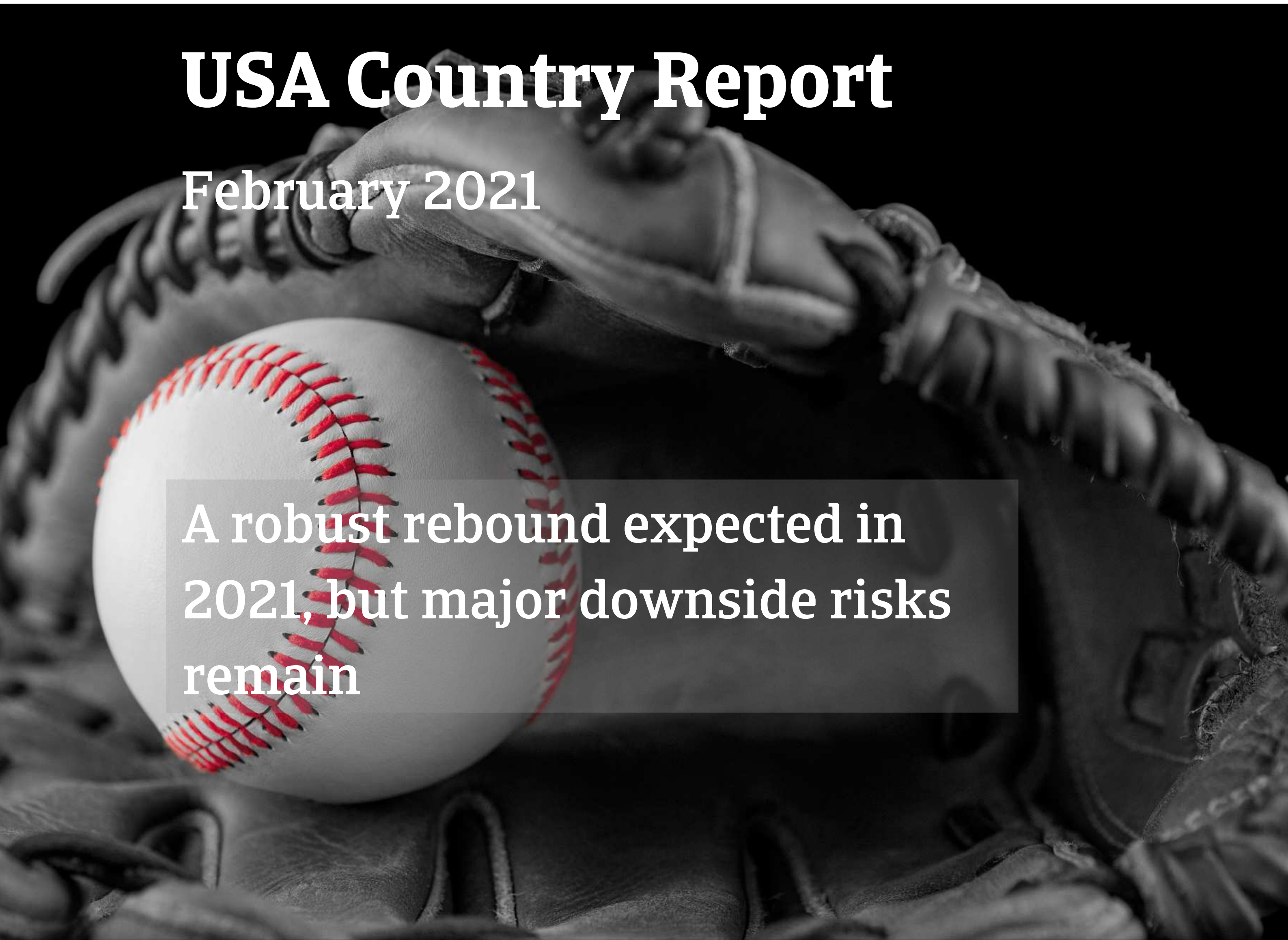
USA Country Report

February 2021



A robust rebound expected in 2021, but major downside risks remain

US industries performance forecast

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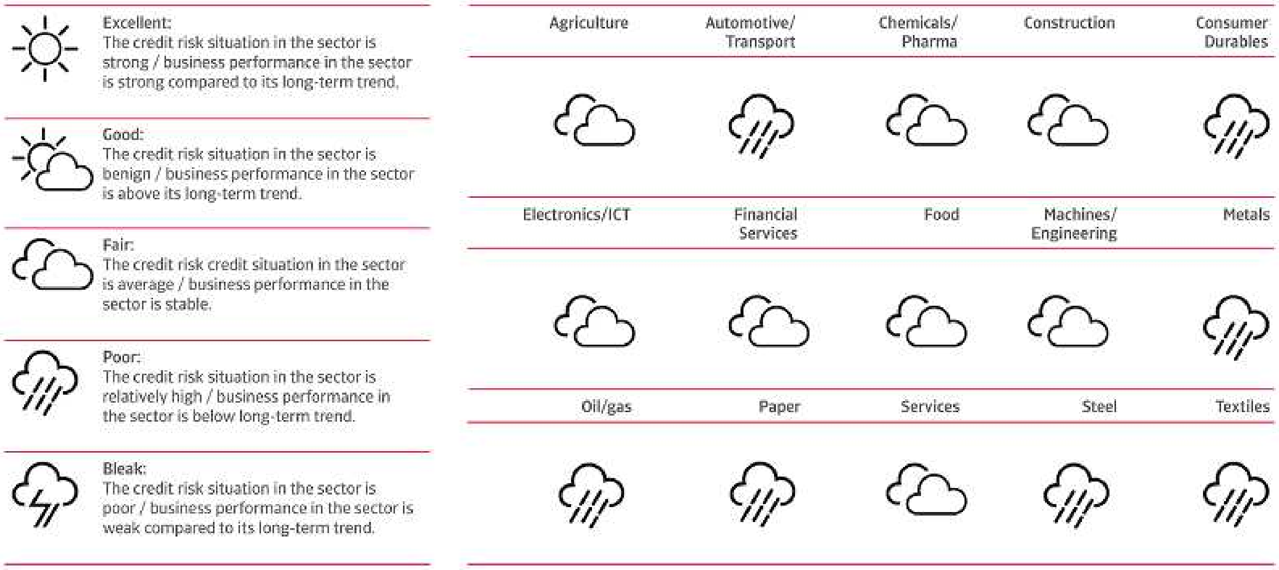


Political Situation

Policy uncertainty has decreased

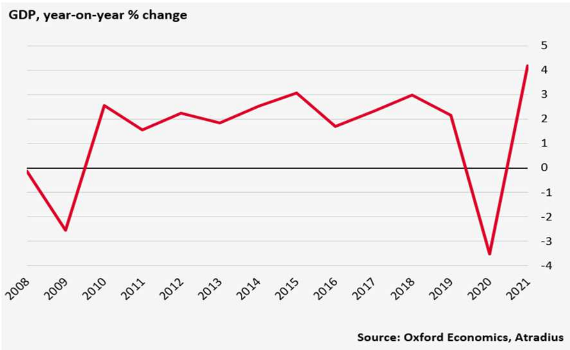
As a result of Joseph Biden's victory in the presidential election, policy uncertainty has decreased. While the Democrats have only narrow control in both chambers of Congress, the new administration should have some leeway through executive orders and lobbying moderate Republicans until the next mid-term elections in 2022.

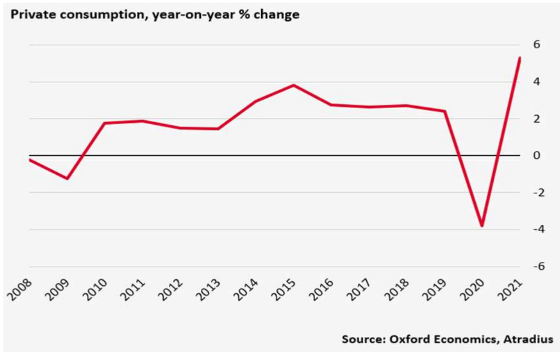
President Biden has announced another massive stimulus package worth USD 1.9 trillion, earmarked for higher spending on vaccines and health care, and intended to further support the economy. Additionally, he has taken several executive actions to address the pandemic more firmly, such as requiring masks in public transportation, increasing testing and accelerating the pace of vaccination.

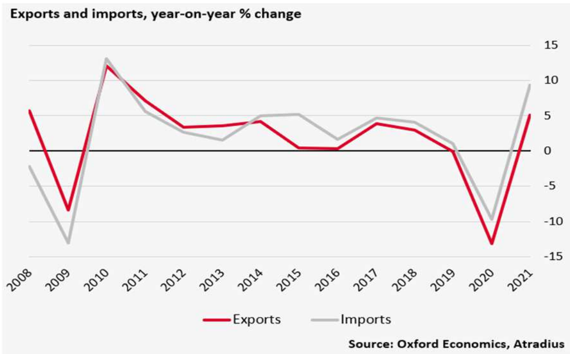
After the Capitol Hill riots, further civil unrest and potential violence against politicians cannot be fully ruled out in the current political climate. It is expected that the potential impact on business and trade will be limited. However, if civil unrest continues to a point that it temporarily impedes government acting, fiscal spending and stimulus planning could slow.

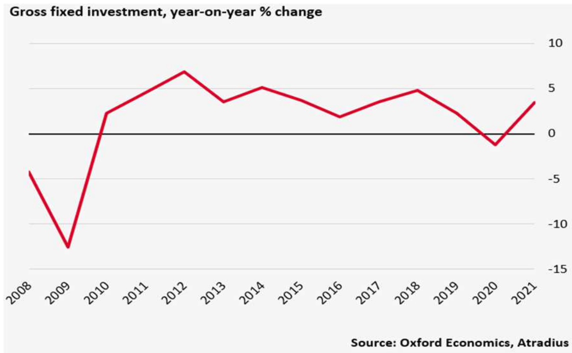
During Biden's term, growth should be supported by normalising trade relations and loosening the US immigration policy. However, in the mid-term, GDP growth gains could be partially offset by tighter environmental and tax policies.

Economic Situation









A robust economic rebound expected in 2021, but substantial downside risks remain

The spread of coronavirus has been rapid in the US, and it still registers the highest rate of infections among all countries in the world. The economic impact of the pandemic has compounded challenges created by the Sino-US trade war, which have weakened Chinese imports and caused disruptions in global supply chains.

After a 3.5% contraction in 2020, it is expected that an economic rebound will gain momentum as of Q2 of 2021. GDP is forecast to grow 4.2% this year, with private consumption increasing 5.3% (down 3.8% in 2020), while investments and exports are expected to grow 3.4% and 5.1% respectively.

However, this recovery expectation is based on the assumption that another major wave of infections is avoided, the vaccination process is rolled out in H1 of 2021 and massive stimulus measures are ongoing. Strict regional or even countrywide lockdowns over a longer term would severely hurt the fragile economic rebound, harming businesses and consumers alike. Under a prolonged slowdown, unemployment could sharply increase, and household finances could deteriorate significantly.

Currently, the US economy still remains on a weak footing. After a strong 41% rebound in Q3 of 2020, household consumption (which usually accounts for about 70% of GDP) grew only 2.5% in Q4 compared to the previous quarter, as the recovery of the labour market lost momentum towards the end of 2020. Next to rising long-term unemployment, initial job loss claims have increased again (up to 965,000 in the first week of 2021). The US unemployment rate was at 6.7% in December 2020, which was well above pre-pandemic levels of about 3.5%. The labour market situation is expected to remain strained until the pandemic is brought under control.

For the first time since 2009, household debt has increased again in Q4 of 2020. However, household finances are in much better shape than in the lead-up to the 2008 credit crisis (US households have been deleveraging, decreasing household debt as a percentage of GDP to 75% in 2019 from nearly 100%). Additionally, more short-term fiscal support for households and businesses is in the cards.

Comprehensive fiscal and monetary measures helped avoid a deeper recession

The estimated 3.5% contraction is milder than previously anticipated (in September 2020, the forecast included a 6.1% contraction). This is due to the fact that comprehensive fiscal stimulus boosted income growth, and historically low interest rates encouraged spending.

In order to counter the economic repercussions of the pandemic, the US government has launched massive fiscal stimulus programmes. In spring 2020, the Trump administration launched the Cares Act (amounting to around USD 2.3 trillion or 11% of GDP) to counter the downturn, addressing every segment of the economy. Measures included direct household support via the handout of cheques, an increase in unemployment benefits and wage subsidies to businesses, and emergency grants and loans for SMEs. This was followed by another relief package (worth USD 877 billion or 4.5% of GDP) in December. The Biden administration plans to launch another USD 1.9 trillion stimulus, providing further assistance to households of an additional USD 1,400 per individual, for a total value of USD 1 trillion. The rest of the package contains spending on vaccination, school reopening and aid for local and state governments, as well as for businesses. This package is still subject to approval by Congress, with some compromises most probable, as the Democrats have only a slim majority in the Senate.

The Federal Reserve has cut the policy rate by 1.5 percentage points since February 2020, down to 0.25%. In March the Fed began purchasing corporate bonds to ensure companies could secure emergency funding in the face of the economic downturn. Additionally, several liquidity enhancing measures have been taken. Facilities to keep credit markets functioning were extended until the end of Q1 of 2021. It is expected that there will be no tightening of the policy rate until 2023. Meanwhile, quantitative easing purchasing will continue through the year in order to support the labour market and to ensure a sustainable economic recovery and pace of inflation.

Business insolvencies decreased in 2020

Given the economic downturn, there were relatively few insolvencies in 2020, despite the fact that bankruptcy courts were still largely functioning. According to the Administrative Office of the US Courts, business bankruptcy filings decreased 4.9% year-on-year in 2020, to 21,655 cases. This decline was mainly due to the comprehensive fiscal and monetary measures and the strong rebound seen in Q3 of 2020.

Elevated credit risk in some industries

However, in certain industries, the credit risk situation of many businesses has deteriorated. In the automotive and steel/metals sectors, payment delays have increased due to rising pressure on businesses' cash flows. Payment delays and insolvencies increased in the brick-and-mortar retail segment, where permanent business closures amounted to more than 6,000 in 2020. In the service industry, subsectors like hotel and catering, restaurants, bars, entertainment and cultural events, travel agencies and tour operators have been heavily affected by sharply decreased footfall and closures resulting from the coronavirus pandemic.

In H1 of 2021, the risk of payment defaults will remain high for brick-and-mortar retailers and the above mentioned hospitality and entertainment-related service segments. The same accounts for airlines and cruise lines, where businesses continue to burn cash at a significant pace, given the sharp decrease in demand. A rebound of all those industries strongly depends on the vaccine rollout this year.

The risk of payment defaults is also elevated in the energy (oil/gas) sector and related OCTG businesses, which continue to suffer from a severe decline in investments and revenues. There has been strong pressure on profit margins of businesses, and low oil and gas prices continue to present significant challenges to businesses in H1 of 2021. Plans of the new administration to tighten environmental regulations could additionally affect the industry.

Despite the rebound, could there be a deteriorating insolvency environment in 2021?

Insolvencies historically lag economic downturns, and therefore, an increase in business failures is rather likely in 2021. While effective in the short run, direct spending and tax reduction measures are unlikely to prevent a rise in insolvencies in the mid-and long-term. Even if these packages cover costs incurred by companies, they will not cover persistent losses of profits. Companies with constrained liquidity following the lockdowns and demand shifts are particularly vulnerable.

Another issue is the high leverage of the US non-financial business sector. US corporate debt has been increasing again over the past couple of years, as businesses have had easy access to financing at low interest rates. There is evidence that many companies have taken advantage of the wide availability of capital to pay out larger sums to shareholders instead of investing in the real economy, increasing their vulnerability to economic and financial shocks. Corporate debt has risen further in 2020, and as a result, financial stress has increased.