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MAKING SENSE OF *THIS* WORLD

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Central Banks Try To Avoid A Coronavirus-Induced Global Recession

The latest news from the COVID-19 front is a mixed bag. In China, following the draconian measures of containment the country adopted during the last few weeks, the official number of new cases is close to zero. A number of existing cases still need to be resolved, but there are not new infections occurring that would aggravate the situation. In the rest of the world, however, the situation is starting to become increasingly bad. In Italy, which has been the country with the second highest number fatalities (almost 370), the daily percentage increase of new cases is still around 20-25%, which means that the number of reported cases doubles every 4-5 days. Thus the diffusion of the infection is still in its exponential phase. And the number of cases is increasing in other countries too, including Germany and the UK and, of course, the US.

Albeit slowly, authorities in Germany, the UK and at EU level are awakening to the fact that COVID-19 is not going to remain a phenomenon limited to Italy, a conviction some European leaders have deluded themselves with for too long. This means that, in time, a larger response will be put in place. In the US, it seems that we are still in the delusional phase in which COVID-19 will remain primarily limited to China and Europe, with only a limited spread in the US. The response has therefore been limited and insufficient so far. The number of swab tests being carried out is still ridiculously low, and the official number of infected people is being kept artificially low by the fact that they are not being detected.

But the story of this virus always shows the same news cycle.

Initially, politicians delude themselves that the problem will remain limited to other countries. As soon as the first person dies in that country as a result of COVID-19, this delusion is no longer tenable, and so the initial timid admission and response occurs. When the number of deaths increases, one can easily infer the total number of infected people by knowing that the mortality rate at global level is around 3.4%. When the number of cases reaches the thousands, the response then becomes forceful. In Italy, the entire region of Lombardy has been quarantined, as have other provinces from neighbouring regions: people cannot get in or out.

As the disease spreads, the economic damage worsens. In our upcoming updated outlook, we will show how we expect global growth to be closer to 2% in 2020 than 3%. This means that in some countries, such as Italy and Japan, there will be a recession this year. Other countries could be equally badly affected – Germany might also fall into a recession, and US growth is likely to be around half of what was expected back in December. To prevent the economic downturn from becoming too large, policy makers are coming to the rescue. Fiscal authorities are trying to design targeted relief plans, in particular to support solvent but illiquid small and medium sized enterprises.

Central banks can also act faster to support market sentiment. A number of them have cut rates in the last few days: the Federal Reserve by 50bps to 1.00-1.25% (intra-meeting), the RBA by 25bps to 0.50%, the BoC by 50bps to 1.25%. Elsewhere, the central banks of Hong Kong and Malaysia cut their interest rates by 50bps (to 1.50%) and by 25bps (to 2.50%), respectively. These interventions are necessary to support market sentiment but will do little to solve the problem generally. The market understands all this, and therefore the selloff in equities continues. Equities will continue to adjust until market participants believe that the virus has been successfully contained at the global level. Even in the best-case scenario, this could take at least a couple of quarters. If the US delays its response to the virus in order to keep the economy strong during an electoral year, the process will be severely delayed, with the result being that immense damage to global health and economic activity could ensue.

Our Recent Publications

- UK Battling Over Brexit, Budget and Coronavirus, *by Nouriel Roubini and Brunello Rosa, 6 March 2020*
- EU Slowly Awakening To Covid-19 Reality, *by Brunello Rosa and Nouriel Roubini, 6 March 2020*
- BoC Follows The Fed (And Cuts Rates By 50bps) And Anticipates Other G10 Central Banks, *by Brunello Rosa, 4 March 2020*
- Flash Review: RBA Kicks Off The New Round Of Monetary Easing In G10, *By Brunello Rosa and Karmen Meneses, 3 March 2020*
- Germany Inching Towards Limited and Targeted Fiscal Stimulus, *by Brunello Rosa and Nouriel Roubini, 2 March 2020*
- **GEOPOLITICAL CORNER:** Brexit Painfully Illuminates Europe's Weakness, But Is There Light at the End of the Tunnel?, *John C. Hulsman, 11 February 2020*

Looking Ahead

The Week Ahead: US Expects Lower Demand And Lower Inflation, ECB To Ease Its Policy Stance

In the US, a 'preliminary March consumer-sentiment survey' is expected to hint at lower demand ahead (Michigan Consumer Sentiment Survey, c: 96.4; p: 101.0). Falling energy prices will slow inflation. February's core CPI is expected to remain flat at 2.3% y-o-y, while lower energy prices are expected to reduce the headline reading to 2.3% y-o-y (p: 2.5).

In the EZ, in the upcoming rate-setting meeting, the ECB will likely introduce a package of easing measures, including targeted measures to support corporate and SME lending (i.e. TLTROs targeting enterprises), a cut to the deposit rate and an increase in the monthly pace of asset purchases.

The Quarter Ahead: COVID-19 Worries Intensify, CBs To Follow The Fed's Lead.

The ***COVID-19 outbreak*** is: 1) likely to develop into a pandemic, spreading on a wide scale to all regions of the world; all major economies are likely to suffer thousands - rather than hundreds - of cases; and 2) is unlikely to be successfully contained before the end of Q2-2020. The WHO's warned against the 'false hope that the virus will disappear in the summer'. As the pandemic escalates most governments are set to announce fiscal stimuli to mitigate its impact.

However, ***in the US*** President Trump and White House officials said they 'do not see an immediate need to craft a broader fiscal-policy response'. Elizabeth Warren ended her presidential bid, limiting the Democratic contest to Joe Biden and Bernie Sanders. Fed Chair Powell hinted at further action in the next scheduled meeting on March 18; the market-implied probability of: a) a 75 bps rate cut rose to 61.5% (p: 0.0); and b) a 50 bps cut to 0.50-0.75% rose to 38.5% (p: 0.0).

In DMs, G7 finance ministers and CBs promised to 'use all appropriate policy tools to achieve strong, sustainable growth and safeguard against downside risks'.

Last Week's Review

Real Economy: Virus-Related Slowdown Prompts Central Banks, Led By The FED, To Support Growth

In the US, where data do not yet reflect the outbreak's impact: 1) manufacturing PMI fell slightly, but remained above 50 (ISM Manuf. PMI Feb., a: 50.1; c: 50.5; p: 50.9); and 2) February's labor market data showed strength as: i) nonfarm payrolls rose (a: 273k; c: 175k; p: 273k); ii) the unemployment rate declined to 3.5% (c: 3.6; p: 3.6); while iii) average hourly earnings stagnated at 3.0% y-o-y (c: 3.1; p: 3.0). The Fed announced a 50bps emergency cut, the first such move since the 2008 financial crisis. While the Fed reiterated that 'the fundamentals of the US economy remain strong', the vote for the rate cut was unanimous.

In China: 1) Jan/Feb's exports contracted by -17.2% (c: -14.0; p: +7.9), and imports fell by -4% (c: -15.0; p: +16.5); and 2) the services PMI collapsed to 26.5 (Caixin Feb., p: 51.8), due to the impact of quarantines and reduced travel.

In the EZ, January's core inflation rose to 1.2% y-o-y (c: 1.3; p: 1.4), while headline decelerated to 1.2% y-o-y, as COVID-19-related disruptions reduced energy prices (c: 1.2; p: 1.4).

In Canada, the BoC cut its key rate by 50 bps to 1.25%.

In Australia, the RBA cut its key rate by 25 bps to 0.50% and noted that the outbreak is having a 'significant effect' on the economy.

Central Banks in Hong Kong and Malaysia cut interest rates to 1.50% (p: 2.00) and 2.50% (p: 2.75), respectively.

Financial Markets: COVID-19's Rapid Spread Spurred Risk Aversion In Financial Markets

Market drivers: The Fed's emergency rate cut did not reduce volatility; global flight to safety continued as DM bond yields fell, credit spreads widened, and the USD depreciated.

Stocks: w-o-w, global indices rose marginally (MSCI ACWI, 0.4% to 513), supported by the US (S&P 500, +0.6% to 2,972) while other DMs (Eurostoxx 50, -2.9% to 3,232; Nikkei 225, -1.9% to 20,750). Volatility rose further (VIX S&P 500, +1.8pts to 41.9; 52w avg.: 15.6; 10y avg.: 16.8).

Bonds: w-o-w, global bond indices rose (BAML Global, +1.3% to 297.1), while the yields of safe-haven sovereign bonds plunged: i) 10y UST fell by 42 bps, to 0.71%; and ii) 10y German bunds fell by 12 bps, to -0.73%.

FX: w-o-w, the USD weakened against a basket of currencies (DXY, -2.2% to 95.951), while the EUR, JPY, and CHF strengthened (EUR/USD, +2.4% to 1.129; USD/JPY, +2.6% to 105.300; USD/CHF, +3.0% to 0.937).

Commodities: Oil prices continue to decline; Brent suffered its largest one-day drop in more than a decade (Brent, -10.4% to 45.3 USD/b) as, at a meeting of Opec and its allies, Saudi Arabia failed to convince Russia to agree to deeper production cuts to prop up prices in the face of weakening demand. Gold, a refuge in times of financial distress, rose w-o-w (Gold, +5.6% to 1,674 USD/Oz).

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The picture in the front page comes from this website

Abbreviations, Acronyms and Definitions

a	*Actual*	*LN*	*Northern League, Italy*
AKP	*Justice and Development Party, Turkey*	*M5S*	*Five Star Movement, Italy*
ann.	*annualized*	*m-o-m*	*Month-on-month*
ARS	*Argentinian Peso*	*mb*	*Million barrels*
avg.	*Average*	*mb/d*	*Million barrels per day*
bn	*Billion*	*MENA*	*Middle East and North Africa*
BoC	*Bank of Canada*	*MHP*	*Nationalist Movement Party, Turkey*
BoE	*Bank of England*	*mn*	*Million*
BoJ	*Bank of Japan*	*MPC*	*Monetary Policy Committee*
bpd	*Barrels per day*	*NAFTA*	*North-American Free Trade Agreement*
bps	*Basis points*	*NATO*	*North Atlantic Treaty Organization*
BS	*Balance sheet*	*OECD*	*Organization for Economic Cooperation and Development*
c	*Consensus*	*Opec*	*Organization of Petroleum Exporting Countries*
C/A	*Current account*	*p*	*Previous*
CB	*Central bank*	*P2P*	*Peer-to-peer*
CBB	*Central Bank of Bahrain*	*PBoC*	*People's Bank of China*
CBK	*Central Bank of Kuwait*	*PCE*	*Personal Consumption Expenditures*
CBT	*Central Bank of Turkey*	*PE*	*Price to earnings ratio*
CDU	*Christian Democratic Union, Germany*	*PM*	*Prime minister*
CNY	*Chinese Yuan*	*PMI*	*Purchasing managers' index*
CPI	*Consumer Price Index*	*pps*	*Percentage points*
DJIA	*Dow Jones Industrial Average Index*	*pw*	*Previous week*
DJEM	*Dow Jones Emerging Markets Index*	*QCB*	*Qatar Central Bank*
d-o-d	*Day-on-day*	*QAR*	*Qatari Riyal*
DXY	*US Dollar Index*	*QE*	*Quantitative easing*
EC	*European Commission*	*q-o-q*	*Quarter-on-quarter*
ECB	*European Central Bank*	*RE*	*Real estate*
ECJ	*European Court of Justice*	*RBA*	*Reserve Bank of Australia*
EIA	*US Energy Information Agency*	*RRR*	*Reserve Requirement Ratio*
EM	*Emerging Markets*	*RUB*	*Russian Rouble*
EP	*European Parliament*	*SWF*	*Sovereign Wealth Fund*
EPS	*Earnings per share*	*tn*	*Trillion*
EU	*European Union*	*TRY*	*Turkish Lira*
EUR	*Euro*	*UAE*	*United Arab Emirates*
EZ	*Eurozone*	*UK*	*United Kingdom*
Fed	*US Federal Reserve*	*US*	*United States*
FOMC	*US Federal Open Market Committee*	*USD*	*United States Dollar*
FRB	*US Federal Reserve Board*	*USD/b*	*USD per barrel*
FX	*Foreign exchange*	*UST*	*US Treasury bills/bonds*
FY	*Fiscal Year*	*VAT*	*Value added tax*
GCC	*Gulf Cooperation Council*	*VIX*	*Chicago Board Options Exchange Volatility Index*
GBP	*British pound*	*WTI*	*West Texas Intermediate*
GDP	*Gross domestic product*	*WTO*	*World Trade Organisation*
IMF	*International Monetary Fund*	*w*	*Week*
INR	*Indian Rupee*	*w-o-w*	*Week-on-week*
IPO	*Initial public offering*	*y*	*Year*
IRR	*Iranian Rial*	*y-o-y*	*Year-on-year*
JPY	*Japanese yen*	*y-t-d*	*Year-to-date*
k	thousand	*ZAR*	*South African Rand*
KSA	*Kingdom of Saudi Arabia*	*2y; 10y*	*2-year; 10-year*