

# Week Ahead

Focus: Covid-19 epidemic, EZ inflation

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## Market fears not subsiding, despite decreasing new Covid-19 infections

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The Covid-19 epidemic has probably passed its peak in China. Chinese authorities have been reporting a decrease in new infections for days. The bond markets, at least, have not yet jumped on this good news. Yields remain near this year's lows. There are two reasons for this. Firstly, data showed that the Eurozone economy was already weakening before the outbreak of the Covid-19 virus, and secondly, the economic damage of the epidemic to China and thus the world cannot yet be estimated. The World Health Organization continues to urge caution, despite the recent better data.

In the course of fighting the epidemic, China has implemented extensive quarantine measures that, among other things, have significantly restricted freedom of movement within the country. Some of these measures were recently withdrawn, but many are still in force and are placing a considerable burden on the economy. What is decisive is how long the quarantine measures in China will continue and thus how much damage will ultimately be done to the Chinese and the global economy. Of the approx. 300mn domestic migrants, less than a third have so far returned to their jobs. For Hubei province, which is by far the worst effected province, quarantine measures are currently scheduled until March 10. Globalized value chains make it difficult to assess the impact and increase the uncertainty. What damage will the production losses in China cause in other countries?

If the trend of declining infections is confirmed, this would make an end to quarantine measures foreseeable. Even then, however, it would take several weeks for the Chinese economy to return to normal, in our view. However, the aftermath of the epidemic will probably be felt longer, as Chinese companies will hardly be able to make up for the lost sales in the foreseeable future. The loss of sales poses a threat to the existence of smaller companies with lower financial buffers in particular. Wage losses will remain for hundreds of millions of workers.

For our forecasts, we assume that the peak of the epidemic has already been reached, but that China's economy will be slow to recover, due to the factors mentioned above. Upcoming Eurozone and US economic data is likely to show a deterioration. Overall, the Eurozone economy is likely to be under greater pressure, as the production of goods and international trade plays a lesser role in the US economy. This suggests that the Eurozone's economic data will improve only slowly, while we expect only relatively short-term negative effects for the US. For the bond markets, this means that yields will rise only slowly over the coming months, which should be stronger in the US than in the Eurozone. We are therefore reducing our yield forecasts.

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Note: Past performance is not necessarily indicative of future results

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## **EZ – Energy prices to weigh on inflation**

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Next week (28.02), a first flash estimate of Eurozone inflation for February will be released. Due to the weak oil price in February, we expect a slight decline in headline inflation in the Eurozone to around +1.3% y/y. For core inflation, after the decline in January to +1.1% y/y, we expect a slight increase. For 2020 as a whole, we expect average headline inflation in the Eurozone to be around +1.3% y/y.

## Economic calendar

Ctry	Date	Time	Release	Period	Consens	Prior
<b>Eurozone</b>						
DE	24-Feb	10:00	Ifo Index	Feb	94.7 Index	95.9 Index
DE	25-Feb	8:00	GDP y/y	4Q F	0.4%	0.4%
FR	28-Feb	8:45	GDP y/y	4Q F		0.8%
EA	28-Feb	11:00	CPI flash y/y	Feb	1.3%	1.4%
<b>USA</b>						
	27-Feb	14:30	GDP q/q	4Q S	2.1%	2.1%
	28-Feb	14:30	PCE Deflator	Jan		1.6%
<b>China</b>						

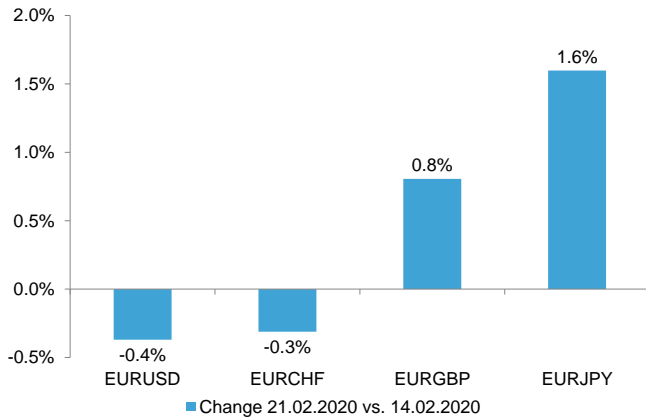
## Central bank events

	Date	Time	Event
<b>ECB</b>	27-Feb	11:05	Isabel Schnabel, speech, Barclays International Monetary Policy, London
	27-Feb	13:15	Philip Lane, panel discussion <i>Euro Area's Growth in a weakened Economic Outlook: Diagnosis and Responses</i> , Paris
	27-Feb	17:00	Luis de Guindos, speech, Grupo July and Cooperativas Agro-Alimentarias, Sevilla
	27-Feb	20:30	Philip Lane, speech, Center for European Reform, London
<b>Fed</b>	25-Feb	21:00	Richard Clarida, speech: <i>US Economic Outlook and Monetary Policy</i> , Annual National Association for Business Economics Economic Policy Conference, Washington D.C.

Source: Market Data Provider, Erste Group Research

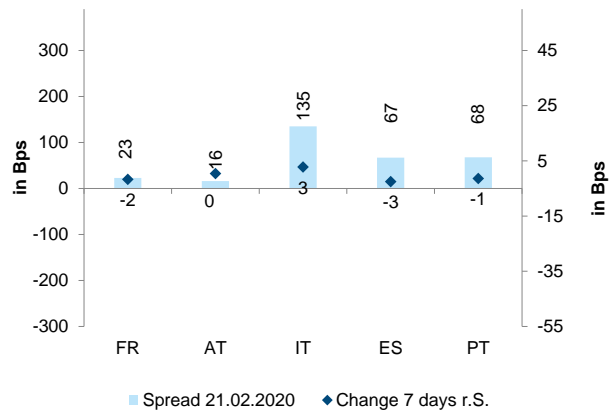
## Forex and government bond markets

**Exchange rates EUR: USD, CHF, GBP and JPY**  
 Changes compared to last week



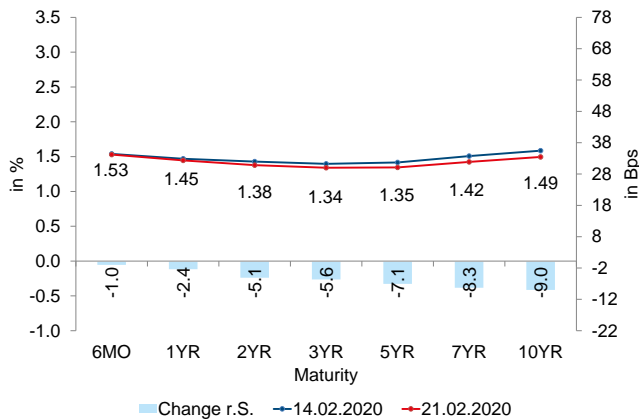
Source: Market Data Provider, Erste Group Research

**Eurozone spreads vs. Germany**  
 10Y government bonds



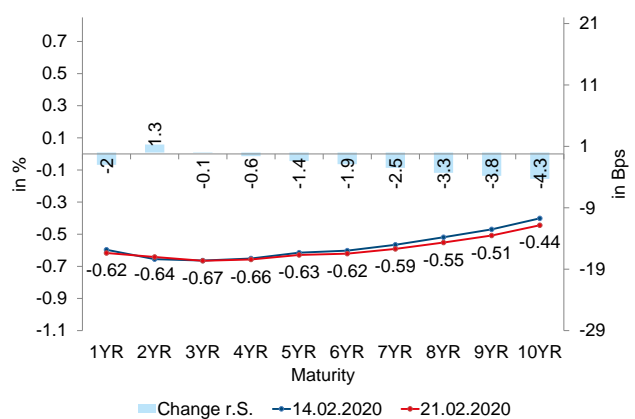
Source: Market Data Provider, Erste Group Research

**US Treasuries yield curve**  
 Changes compared to last week



Source: Market Data Provider, Erste Group Research

**DE Bund yield curve**  
 Changes compared to last week



Source: Market Data Provider, Erste Group Research

## Forecasts<sup>1</sup>

GDP	2018	2019	2020	2021
Eurozone	1.9	1.2	1.0 ↓	1.2
US	2.9	2.3	1.9	2.2

Inflation	2018	2019	2020	2021
Eurozone	1.7	1.2	1.3	1.5
US	2.4	1.8 ↓	2.1	2.0

Interest rates	current	Mar.20	Jun.20	Sep.20	Dec.20
ECB MRR	0.00	0.00	0.00	0.00	0.00
3M Euribor	-0.41	-0.40	-0.40	-0.40	-0.40
Germany Govt. 10Y	-0.45	-0.40 ↓	-0.30 ↓	-0.10 ↓	-0.10
Swap 10Y	-0.12	-0.10 ↓	0.00 ↓	0.20	0.20

Interest rates	current	Mar.20	Jun.20	Sep.20	Dec.20
Fed Funds Target Rate*	1.59	1.63	1.63	1.63	1.63
3M Libor	1.70	1.90	1.90	1.90	2.10
US Govt. 10Y	1.48	1.60 ↓	1.80 ↓	2.00 ↓	2.10
EURUSD	1.08	1.11	1.13	1.15	1.15

\*Mid of target range

In case of changes to our forecasts compared to the previous issue, arrows show the direction of the change.

Source: Market Data Provider, Erste Group Research

<sup>1</sup> Note: In accordance with regulations, we are obliged to issue the following statement:  
Forecasts are not a reliable indicator of future performance.

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**Published by:**

**Erste Group Bank AG**  
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**1100 Vienna, Austria, Am Belvedere 1**  
**Head Office: Wien**  
**Commercial Register No: FN 33209m**  
**Commercial Court of Vienna**

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